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August 26, 2008

W. Thomas Reeder  
Benefits Tax Counsel  
Office of Tax Policy  
Department of the Treasury  
1500 Pennsylvania Avenue, NW  
Washington, DC 20220

Marty Pippins  
EP Technical Guidance and Quality Assurance  
Internal Revenue Service  
1750 Pennsylvania Avenue, NW  
Washington, DC 20006

Re: Code Section 414(s) Compensation Definition

Dear Mr. Reeder and Mr. Pippins:

The American Society of Pension Professionals & Actuaries (ASPPA) is writing to follow up on our meeting on June 23, 2008, with Internal Revenue Service (Service) and Treasury representatives where we requested guidance from the Service concerning the Code §414(s) definition of compensation.

ASPPA is a national organization of more than 6,000 retirement professionals who provide consulting and administrative services for qualified retirement plans covering millions of American workers. ASPPA members are retirement professionals of all disciplines, including consultants, investment professionals, administrators, actuaries, accountants and attorneys. Our large and broad-based membership gives ASPPA unique insight into practical applications of ERISA and qualified retirement plans, with a particular focus on the issues faced by small- to mid-sized employers. ASPPA's membership is diverse but united by a common dedication to the employer-sponsored retirement plan system.

### Summary of Recommendation

We request that the IRS issue a notice or similar guidance to modify the safe harbor definition of compensation provided in Internal Revenue Code (Code) Regulation §1.414(s)-1(c) to add a Code §414(s) safe harbor permitting plans to exclude either all post-severance payments or all post-severance payments other than the last-paycheck without discrimination testing. ASPPA's recommendation is discussed in greater detail in the section below.

### Discussion of Issue

Final regulation §1.415(c)-2(e)(3) provides that *compensation* includes amounts paid within certain time periods after severance from employment if the payment is regular compensation for services during the employee's regular working hours, or compensation for services outside the

employee's regular working hours (such as overtime or shift differential), commissions, bonuses or other similar payments and the payment would have been paid to the employee prior to a severance from employment if the employee had continued in employment with the employer. Plans may treat certain leave cashouts and deferred compensation payments as *compensation* if the leave or deferred compensation payment would have been available if employment continued. All other post-severance payments are excluded from *compensation* under the final Code §415 regulations.

Code §414(s) and Regulation §1.414(s)-1(c) provide "safe harbor" compensation definitions that can be used for certain purposes without additional discrimination testing. However, there is no safe harbor definition that permits a plan to exclude post-severance payments. As a result, it appears that plans choosing to exclude post-severance payments are required to test compensation for discrimination as provided in Regulation §1.414(s)-1(d)(3).

In our experience, it is a common practice among employers to include an employee's final paycheck as "compensation" for retirement plan purposes (even though the final check may be issued/processed after the employee's termination date) and to exclude other post-severance payments. The final paycheck may include some amount paid as severance. Providing an additional safe harbor under regulations §1.414(s)-1(c) to permit this practice without additional discrimination testing would significantly help to make plan administration more efficient, avoid confusion and ease the administrative burdens on employers. This approach is consistent with the approach taken in the final regulations under Code §403(b). Regulation §1.403(b)-3(b)(4)(i) provides that compensation is not treated as provided to a former employee if it is compensation for a pay period that began prior to the date of severance.

Defining compensation to include amounts paid in the employee's final paycheck and to exclude payments made after severance from employment is reasonable and would not be inherently discriminatory. There is support for the proposition that a definition of compensation that excludes post-severance compensation is not discriminatory in analogous regulations under Code §401(k). The compensation definition in regulations §1.401(k)-6 provides that "A plan may, however, limit the period taken into account under either method to that portion of the plan year or calendar year in which the employee was an eligible employee, provided that this limit is applied uniformly to all eligible employees under the plan for the plan year." In the case of a 401(k) safe harbor plan, regulation §1.401(k)-3(b)(2) refers to the above definition and specifically adds, "Thus, for example, the plan may limit the period used to determine safe harbor compensation to the eligible employee's period of participation."

Based on the foregoing analysis, **ASPPA requests and recommends** that the IRS issue guidance to add a Code §414(s) safe harbor permitting plans to exclude either all post-severance payments or all post-severance payments other than the last-paycheck without discrimination testing. Regulation §1.414(s)-1(i) provides:

*(i) Additional rules. --The Commissioner may in revenue rulings, notices, and other guidance of general applicability provide additional rules for defining compensation within the meaning of §414(s), including additional definitions of compensation that satisfy §414(s).*

Thus, the IRS can clarify this point by notice, revenue ruling or similar means, without the necessity of issuing additional regulations under Code §414(s).



These comments were prepared by ASPPA's IRS Subcommittee of the Government Affairs Committee, James C. Paul, APM, Chair and primary author. We would welcome the opportunity to meet with you to further discuss these issues. Please contact us if you have any comments or questions regarding the matters discussed above. Thank you for your consideration.

Sincerely,

/s/

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Executive Director/CEO

/s/

Teresa T. Bloom, Esq., APM  
Chief of Government Affairs

/s/

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