

Pension Benefit Guaranty Corporation

78-23

October 24, 1978

REFERENCE:

[\*1] 4021. Plans Covered

OPINION:

This is in response to your letter of September 6, 1978, to this Office concerning the coverage of Puerto Rico defined benefit plans under the insurance provisions of Title IV of the Employee Retirement Income Security Act of 1974 (ERISA). You point out that Puerto Rico situs trusts under certain Puerto Rican pension plans are treated, under § 1022(i)(1) of ERISA, as organizations described in § 401(a) of the Internal Revenue Code (the "Code"), and thus are exempt from U.S. income taxes under § 501(a) of the Code. You have asked whether, in the case of defined benefit plans, such a qualification for income tax exemption by reason of the application of § 1022(i)(1) satisfies the tax qualification requirements under § 4021 of ERISA.

Section 4021 of ERISA applies to a plan which "is, or has been determined by the Secretary of the Treasury to be, a plan described in section 401(a) of the Internal Revenue Code of 1954, or which meets . . . the requirements of section 404(a)(2) . . ." This section also applies to a plan "which has, in practice," met such tax qualification requirements for the past five plan years and which is maintained by an employer engaged in [\*2] interstate commerce.

Section 501(a) of the Code grants U.S. tax exemption to an "organization described in . . . section 401(a) of the Code."

Section 1022(i)(1) provides:

(i) Certain Puerto Rican Pension, Etc., Plans To Be Exempt From Tax Under Section 501(a). -

(1) General Rule. - Effective for taxable years beginning after December 31, 1973, for purposes of section 501(a) of the Internal Revenue Code of 1954 (relating to exemption from tax), any trust forming part of a pension, profit-sharing, or stock bonus plan all of the participants of which are residents of the Commonwealth of Puerto Rico shall be treated as an organization described in section 401(a) of such Code if such trust -

(A) forms part of a pension, profit-sharing, or stock bonus plan, and

(B) is exempt from income tax under the laws of the Commonwealth of Puerto Rico.

\* \* \* (Emphasis added)

Both the title and the underlined language of this subsection indicate that Puerto Rican pension trusts are treated as organizations described in § 401(a) of the Code only for purposes of § 501(a), and not for purposes of § 4021 of ERISA. The sole effect of § 1022(i)(1), therefore, is to give certain Puerto Rican [\*3] pension trusts the benefit of tax-exempt treatment accorded qualified U.S. trusts by § 501(a). An analysis of the legislative history of § 1022(i)(1) reveals that Congress wished to enable Puerto Rican plan administrators to diversify their investment portfolios through the purchase of U.S. securities without encountering the adverse tax consequences which they would have otherwise suffered because of their ineligibility for a § 501(a) exemption.

The language of § 4021 of ERISA indicates that compliance with the requirements of §§ 401(a) or 404(a)(2) of the Code is mandatory for Title IV coverage. The legislative history of § 4021 reveals that Congress regarded the tax qualification requirements of Title II as a prerequisite to Title IV coverage. See H.R. Rep. No. 93-1280, 93d Cong., 2d Sess., 367 (1974).

In conclusion, Puerto Rican pension plans whose trusts have qualified for tax exemption through § 1022(i)(1) of ERISA do not thereby satisfy the Title IV coverage requirements of § 4021. In order to meet the requirements of § 4021 Puerto Rican plans must either (1) meet, or have been determined by the Secretary of the Treasury to meet, the requirements of § 401(a) of the [\*4] Code, or (2) have met, in practice, the requirements of § 401(a) of the Code for

the past five plan years.

We hope this has been of assistance.

Henry Rose  
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