



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

200510042

DEC 14 2004

SE. T. EP. RA. T3

Uniform Issue List: 404.15-00

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Legend

Company P = * * *

Dear * * *:

This letter is in response to your ruling request dated September 30, 2004, in which your authorized representative requested a ruling on your behalf concerning the determination of the maximum amount of the deduction allowable under section 404(a)(7) of the Internal Revenue Code ("Code").

The following facts and representations have been submitted under penalty of perjury in support of the ruling requested:

Company P maintains defined benefit plans and defined contribution plans (qualified under section 401(a) of the Code) for the benefit of its eligible employees. Company P calculates the deduction limit for employer contributions to each plan under sections 404(a)(1) or 404(a)(3) of the Code whichever is applicable. In addition, because certain employees of Company P participate in both defined benefit plans and defined contribution plans, Company P's contributions to the plans are also subject to the combined plan deduction limit under section 404(a)(7) of the Code.

In determining the individual defined benefit plan deduction limit, Company P uses the special rule under section 404(a)(1)(D)(i) of the Code that increases the maximum amount deductible to the unfunded current liability under section 412(l) of the Code. Company P also elects under section 404(a)(1)(F) of the Code to disregard the modified interest rate under sections 412(b)(5)(B)(ii)(II) and 412(l)(7)(C)(i)(IV) of the Code and use interest rates based on 30-year U.S.

Treasury securities for purposes of determining unfunded current liability and, accordingly, the maximum amount deductible.

Company P's combined plan deduction limit under section 404(a)(7) is at least equal to the amount necessary to satisfy its unfunded current liability under section 412 of the Code to its defined benefit plans because Company P relies on section 404(a)(1)(D)(i) of the Code for each defined benefit plan deduction limit.

Company P proposes to calculate its unfunded current liability for purposes of the combined plan deduction limit under section 404(a)(7) of the Code using interest rates based on 30-year U.S. Treasury securities just as it calculates its unfunded current liability for purposes of the individual plan deduction limit for each of its defined benefit plans. Company P proposes to disregard sections 412(b)(5)(B)(ii)(II) and 412(l)(7)(C)(i)(IV) of the Code for purposes of determining the interest rate used in calculating the maximum amount of the deduction allowable under section 404(a)(7) of the Code to the same extent that it is expressly statutorily permitted under section 404(a)(1)(F) of the Code to disregard such subsections for purposes of determining the interest rate used in calculating the maximum amount of deduction allowable under section 404(a)(1) of the Code.

Based on the facts and representations, you request the following ruling:

If section 404(a)(1)(D)(i) of the Code applies to one of Company P's defined benefit plans for any plan year, Company P is allowed to disregard sections 412(b)(5)(B)(ii)(II) and 412(l)(7)(C)(i)(IV) of the Code for purposes of determining the interest rate used in calculating the maximum amount of deduction allowable under section 404(a)(7)(A) of the Code.

Section 404(a) of the Code provides, as a general rule, that if contributions paid by an employer on account of any employee to a pension, profit sharing or annuity plan would otherwise be deductible, they shall be deductible under section 404 of the Code, subject to certain limitations set forth therein on the amounts deductible in any year. Section 404(a)(1)(A) of the Code provides limits on the deductibility of contributions with respect to qualified defined benefit plans.

Section 404(a)(1)(D)(i) of the Code provides that, in the case of a defined benefit plan, the maximum amount deductible under the limitations of section 404(a)(1) shall not be less than the unfunded current liability determined under section 412(l). The term "unfunded current liability" is defined in section 412(l)(8)(A) of the Code, with respect to any plan year as the excess (if any) of - (i) the current liability under the plan, over (ii) the value of the plan's assets determined on the basis of any reasonable actuarial method of valuation which takes into account fair market value and which is permitted under the Treasury Regulations ("Regulations").

Section 404(a)(1)(F) of the Code provides that an employer can elect to disregard sections 412(b)(5)(B)(ii)(II) and 412(l)(7)(C)(i)(IV) of the Code for purposes of determining the interest rate used in calculating the maximum amount of the deduction allowable under section 404(a)(1) of the Code.

Section 404(a)(7)(A) of the Code provides that, if an employer maintains one or more defined benefit plans and one or more defined contribution plans, the maximum deductible contribution for all such plans of the employer for the taxable year is limited to the greater of: (1) 25% of the aggregate compensation paid or accrued during the taxable year to the beneficiaries under such plans; or (2) the amount of contributions made to or under the defined benefit plans to the extent such contributions do not exceed the amount of employer contributions necessary to satisfy the minimum funding standard of section 412 of the Code with respect to any such defined benefit plans for the plan year ending with or within such taxable year or for any prior plan year ("Minimum Funding Amount").

Section 404(a)(7)(A) of the Code also provides that, for purposes of calculating the Minimum Funding Amount, if section 404(a)(1)(D) of the Code applies to a defined benefit plan for any plan year, the amount necessary to satisfy the minimum funding standard provided by section 412 of the Code with respect to such plan for such plan year shall not be less than the unfunded current liability of such plan under section 412(l) of the Code.

Section 412(b)(5)(B) of the Code states that, for purposes of determining a plan's current liability and for purposes of determining a plan's required contribution under section 412(l) of the Code for any plan year, if any rate of interest used under the plan to determine cost is not within the permissible range, the plan shall establish a new rate of interest within the permissible range.

Section 412(b)(5)(B)(ii)(I) of the Code states that except as provided in sections 412(b)(5)(B)(ii)(II) and 412(b)(5)(B)(ii)(III) of the Code, the term "permissible range" means a rate of interest which is no more than 10% above, and not more than 10% below, the weighted average of the rates of interest on 30-year Treasury securities during the 4-year period ending on the last day before the beginning of the plan year. ("30-year Treasury Rate")

Section 412(b)(5)(B)(ii)(II) of the Code provides that, in the case of plans years beginning after December 31, 2003, and before January 1, 2006, the term "permissible range" means a rate of interest which is not above, and not more than 10% below, the weighted average of the rates of interest on amounts invested conservatively in long-term investment grade corporate bonds during the four-year period ending on the last day before the beginning of the plan year. ("Corporate Bond Rate")

Section 412(l)(7) of the Code provides additional rules for determining the current liability under subsection (l) of section 412 of the Code. The term "current liability" is defined in section 412(l)(7)(A) of the Code to mean all liabilities to employees and their beneficiaries under the plan.

Section 412(l)(7)(C)(i) of the Code sets forth the general rule for the interest rates to be used effective for plan years beginning after December 31, 1994. Under section 412(l)(7)(C)(i)(I) of the Code the rate of interest used to determine current liability shall be the rate of interest used under section 412(b)(5) of the Code, except that the highest rate in the permissible range under section 412(b)(5)(B)(ii) of the Code shall not exceed the specified percentage (as determined under section 412(l)(7)(C)(i)(II)) of the weighted average referred to in such subparagraph.

Section 412(l)(7)(C)(i)(IV) of the Code provides a special rule for determining the interest rate in plan years beginning in 2004 or 2005. For such plan years, the rate of interest used to determine current liability under section 412(l)(7) of the Code shall be the rate of interest under section 412(b)(5) of the Code.

In essence, Company P is requesting to use the 30-year Treasury Rate and not the Corporate Bond Rate for purposes of determining the unfunded current liability under section 404(a)(7) of the Code.

For each of its defined benefit plans, Company P uses the special rule under section 404(a)(1)(D)(i) of the Code to determine the deduction limit with respect to the plans, and is making the section 404(a)(1)(F) election to disregard the modified interest rate under sections 412(b)(5)(B)(ii)(II) and 412(l)(7)(C)(i)(IV) of the Code for purposes of the deduction allowable under section 404(a)(1) of the Code. This election allows Company P to use the 30-year Treasury Rate for purposes of determining the deduction limit under section 404(a)(1)(D)(i) of the Code.

Section 404(a)(7) of the Code applies because Company P maintains both defined benefit and defined contribution plans covering the same employees. Accordingly, the maximum deductible amount in a taxable year for such plans may not exceed the greater of (1) 25% of the aggregate compensation paid or accrued during the taxable year to the beneficiaries under such plans; or (2) the Minimum Funding Amount. Pursuant to section 404(a)(7)(A), the Minimum Funding Amount, for a plan to which section 404(a)(1)(D)(i) applies, is the unfunded current liability determined using section 412(l) of the Code. The reference to unfunded current liability in section 404(a)(7)(A) is identical to the reference in section 404(a)(1)(D)(i) and is applicable only to plans to which section 404(a)(1)(D)(i) applies. Given the statutory language and design, it would be inconsistent for a plan that is subject to both section 404(a)(1)(D)(i) and section 404(a)(7)(A) to compute the unfunded current liability differently for purposes of section 404(a)(1)(D)(i) and section 404(a)(7). Therefore, we rule

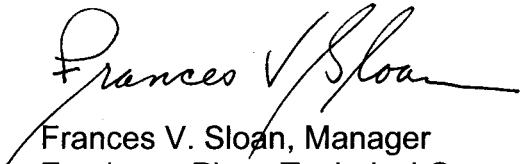
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that the calculation of unfunded current liability is the same for section 404(a)(7)(A) as it is for section 404(a)(1)(D)(i). Because of the section 404(a)(1)(F) of the Code election, the unfunded current liability is determined for section 404(a)(1)(D)(i) of the Code using the 30-year Treasury Rate. Accordingly, the 30-year Treasury Rate is used to determine unfunded current liability for section 404(a)(7) of the Code as well.

This ruling is directed only to the taxpayer that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent. A copy of this letter is being sent to your authorized representative in accordance with a power of attorney on file in this office.

If you wish to inquire about this ruling, please contact * * *, I.D. # * * *, at * * *. Please address all correspondence to SE:T:EP:RA:T3.

Sincerely yours,


Frances V. Sloan, Manager
Employee Plans Technical Group 3

Enclosures: Deleted copy of this letter
Notice of Intention to Disclose, Notice 437

cc: * * *

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