

SECTION 404

DB/DC Limit
Excise taxes

Single Employer Plans

404(n) ELECTIVE DEFERRALS

Handling of 402(g)(3) deferrals (see page 404(o)-15) in determining deduction limits:

- **Included in total compensation**
- **No longer considered employer contributions**

§404(a)(3)

PROFIT SHARING / STOCK BONUS PLANS

**Deductible limit is 25% of compensation,
which is limited under 404(l)**

§404(a)(3)(v) MONEY PURCHASE PLANS

DC plans subject to 412 Minimum Funding Standards are treated like Stock bonus and Profit Sharing plans

Deductible limit is 25% of compensation

412 minimum contribution equals percent of pay contribution stated in document

§404(a)(7)

DEDUCTION LIMIT - BOTH DB&DC PLANS

- 1. §404(a)(7) applies if one or more persons covered under both DB and DC plans**
- 2. This DB / DC limit no longer applies to single-employer plans, if plan is covered by PBGC**

**§404(a)(7) WRERA
DEDUCTION LIMIT - BOTH DB&DC PLANS**

Greater of

- 1. 25% of compensation, or**
- 2. Greater of §430 DB plan minimum, and**

Lesser of

- a) §430 Funding Target - AAV**
- b) DB contribution**

404(a)(7) DB/DC limit does not apply for these five cases

- (i) No employee is covered under both the DB and DC plans**
- (ii) DC plan contributions are solely §401(k) deferrals, and nothing else**
- (iii) DC plan contributions are 6% or less of compensation**
- (iv) Single-employer DB plan is covered by the PBGC**
- (v) Multiemployer plan**

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IRS NOTICE 87-37

10% excise tax on non-deductible contributions

If non-deductible contribution is carried forward many years, employer must pay 10% excise tax each year.

§4972(c)(6) EXCISE TAX EXEMPTION

WRERA

Exemption available if employer deductions limited by 404(a)(7) for combined DB/DC plans. Excise tax applies to non-deductible DC contributions in excess of the sum of

- 1. ER matching contributions §401(m)(4)**
- 2. Contributions under §402(g)(3)(A) CODA**

404(a)(7) limit first applies to DB plan contributions, then to DC plan contributions

NOTES

- 1. Under 404(a)(7)(C)(iii), only consider DC plan contributions in excess of 6%**
- 2. 404(a)(7) only applies to single-employer DB plans which are NOT covered by PBGC**

ASSUME 4972(c)(6) APPLIES

EXCISE TAX EXAMPLES

<u>Item description</u>	<u>CASE 1</u>	<u>CASE 2</u>	<u>CASE 3</u>
DB plan contribution	450,000	520,000	520,000
DB plan deductible limit	<u>450,000</u>	<u>450,000</u>	<u>450,000</u>
DB plan non-ded contribution	-0-	70,000	70,000
10% excise tax - DB plan	-0-	7,000	7,000
DB plan contribution	450,000	520,000	520,000
DC plan contribution	<u>130,000</u>	<u>130,000</u>	<u>300,000</u>
Total contribution	580,000	650,000	820,000
6% of compensation	132,000	132,000	132,000
Overall DB/DC 25% limit	N/A	N/A	550,000
404(a)(7) non-ded contribution	N/A	N/A	270,000
DB plan non-ded contribution	-0-	70,000	70,000
DC plan non-ded contribution	-0-	-0-	200,000
DC plan: excise tax exempt	N/A	N/A	132,000
DC plan: subject to excise tax	-0-	-0-	68,000
10% excise tax - DC plan	-0-	-0-	6,800
Total excise tax	-0-	7,000	13,800

Examples assume total compensation of 2,200,000

§4972(c)(7) EXCISE TAX EXEMPTION

PPA

Single employer plans may elect to ignore all contributions to a DB plan, in lieu of exemption under §4972(c)(6)

Now the 404(a)(7) limit applies to DC plan contributions first, then to DB plan contributions

Must be elected by employer for taxable year in lieu of §4972(c)(6)

NOTES

- 1. Under 404(a)(7)(C)(iii), only consider DC plan contributions in excess of 6%**
- 2. 404(a)(7) only applies to single-employer DB plans which are NOT covered by PBGC**

ASSUME 4972(c)(7) APPLIES

EXCISE TAX EXAMPLES

<u>Item description</u>	<u>CASE 1</u>	<u>CASE 2</u>	<u>CASE 3</u>
DC plan contribution	130,000	130,000	300,000
DC plan deductible limit (25%)	<u>550,000</u>	<u>550,000</u>	<u>550,000</u>
DC plan non-ded contribution	-0-	-0-	-0-
10% excise tax – DC plan	-0-	-0-	-0-
DB plan contribution	450,000	520,000	520,000
DC plan contribution	<u>130,000</u>	<u>130,000</u>	<u>300,000</u>
Total contribution	580,000	650,000	820,000
Overall DB/DC 25% limit	N/A	N/A	550,000
6% of compensation	132,000	132,000	132,000
404(a)(7) non-ded contribution	N/A	N/A	270,000
DC plan non-ded contribution	-0-	-0-	-0-
DB plan deductible limit	450,000	450,000	450,000
DB plan non-ded contribution	-0-	70,000	270,000
10% excise tax – DB plan	-0-	-0-	-0-
Total excise tax	-0-	-0-	-0-

Examples assume total compensation of 2,200,000

§4972(c)(7) EXCISE TAX EXEMPTION

PPA

**Must be elected by employer for taxable year
in lieu of §4972(c)(6)**

**In some cases, you should assume employer
has made this election:**

- **No DC plan**
- **Not subject to 404(a)(7) limitation**

EXCISE TAXES

§4971(a)-(e) Accumulated Funding Deficiency

	Non-multi	Multiemployer
Initial		
Ultimate		

4971(f) Unpaid Liquidity Shortfall

	Non-multi	Multiemployer
Initial		
Ultimate		

§4972 Non-deductible Contributions

	Non-multi	Multiemployer
DB plans		
DC plans		

EXCISE TAXES

54.4971(c)-1 regulation

Key points of examples in regulation

- **Determine unpaid MRC for year 20XX at valuation date**
- **Adjust unpaid MRC for year 20XX forward using EIR for year 20XX until it is eliminated**

EXCISE TAXES

54.4971(c)-1 regulation

EXAMPLE 1

- **2009 plan year**
- **MRC is 250,000**
- **2009 contribution paid at 07-01-2009 is 200,000**
- **EIR is 5.9%**

Unpaid MRC calculation:

$$55,651 = 250,000 - 200,000(1.059)^{-6/12}$$

Excise tax is 5,565

EXCISE TAXES

54.4971(c)-1 regulation

EXAMPLE 2

- **Add to Example 1**
- **2010 plan year**
- **2010 contribution paid at 12-31-2010 is 175,000**
- **Adjust unpaid MRC from 01-01-2009 to 12-31-2010**

Remaining contribution at 12-31-2010 to satisfy 2010 MRC:

$$112,588 = 175,000 - 55,651(1.059)^2$$

Must discount this back to 01-01-2010 with 2010 EIR, then compare to 2010 MRC