



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

OFFICE OF
CHIEF COUNSEL

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Reference: Self-directed Accounts in Public Retirement Systems

Dear :

This is in response to your request for information concerning whether participant self-directed accounts in a defined contribution public retirement system provide retirement benefits to employees that are comparable to the benefits provided under social security. We are unable to provide you with a letter ruling because your request did not satisfy the requirements for requesting a letter ruling contained in Revenue Procedure 2005-1, 2005-1 I.R.B. 1. However, we are able to provide you with the following general information which we hope will be helpful.

Internal Revenue Code (Code) section 3121(b)(7)(F) provides the general rule that service performed by an individual in the employ of a State, political subdivision thereof, or any wholly owned instrumentality of the foregoing will not be considered employment for Federal Insurance Contribution Act (FICA) purposes if such individual is a member of a public retirement system.

Employment Tax Regulation (regulation) section 31.3121(b)(7)-2(e)(2)(i) provides the general rule that a public retirement system within the meaning of Code section 3121(b)(7)(F) must provide "a retirement benefit to the employee that is comparable to the benefit provided under the Old-Age portion of the Old-Age, Survivor and Disability Insurance [OASDI] program of Social Security." The regulations provide that whether a retirement system satisfies this retirement benefit requirement is generally determined under the facts and circumstances of each case and on an individual-by-individual basis.

In order to be considered a public retirement system providing a retirement benefit comparable to the OASDI portion of Social Security, a plan must provide for an allocation to a participant's account equal to at least 7.5% of the participant's compensation during any period under consideration. Additionally, a plan must satisfy the reasonable interest rate requirement. A defined contribution retirement system satisfies the reasonable interest rate requirement if "the employee's account is credited

with earnings at a rate that is reasonable under all the facts and circumstances, or employees' accounts are held in a separate trust that is subject to general fiduciary standards and are credited with actual earnings on the trust fund."

Whether the interest rate with which an employee's account is credited is reasonable is determined after reducing the rate to adjust for the payment of any administrative expenses. If employees' accounts are held in a separate trust that is subject to general fiduciary standards and are credited with the actual earnings on the trust fund, the applicable interest rate requirements will be satisfied regardless of the actual rate of earnings on the accounts.

If you have any questions with regard to this matter, please contact
of my staff. can be reached at .

Sincerely,

Lynne Camillo
Chief, Employment Tax Branch 2
Office of the Associate Chief
Counsel/Division Counsel
(Tax Exempt & Government Entities)