CHAPTER 2, Overview of selected determination Worksheets

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INTERNAL REVENUE SERVICE
TAX EXEMPT AND GOVERNMENT ENTITIES

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MINIMUM PARTICIPATION STANDARDS-WORKSHEET 1 (OVERVIEW)

The purpose of this chapter is to provide a synopsis of the points noted at Alert Guidelines Worksheet Number 3 (Form 5622). For a detailed review of the items noted on that form, see Explanation Number 1, Minimum Participation Standards (Document 6388).

I. AGE AND SERVICE

I.a. does the plan provide an age or service requirement (including an entry date requirement) for participation?

If the plan provides for participation only on specified entry date(s), but no other age or service requirements are provided, complete only part I.c. of the worksheet.

If the plan does not otherwise specify an age requirement or a service requirement, then the rest of this worksheet is not needed. This is because such a plan provides for participation commencing upon employment.

I.b. does the plan meet the minimum age and service requirements of Internal Revenue Code (IRC) section 410(a)(1), as amended by the Tax Reform Act of 1986?

An employee who otherwise meets requirements to participate generally must be eligible to participate in the plan at age 21, or upon completion of 1 year of service, whichever is later.

If the plan provides for full and immediate vesting, an employee who otherwise meets requirements to participate must also be eligible to participate at age 21, or upon completion of 2 years of service, whichever is later.

Note that a plan cannot exclude an employee(s) based on service (for example, part-time employees) where the employee(s) meet(s) the age and service requirements imposed by the plan.

If the plan uses the elapsed time method of crediting service, substitute “period of service” for “year of service” above.

I. c. will a new employee, otherwise eligible, participate on the earlier of the first day of the plan year after meeting the minimum age and service requirements of IRC section 410(a)(1), or 6 months after satisfying the requirements?

The general rule is that a plan must provide that an employee who has satisfied the minimum age and service requirements, and who is otherwise eligible to participate in the plan, must participate in the plan no later than the **earlier** of the first day of the plan year after the date the age and service requirements were met, or the date 6 months after the day on which the employee first met the age and service requirements.

I.d. is an employee's eligibility to participate determined without regard to the attainment of any maximum age?

A plan cannot exclude an employee who meets the plan's age and service requirements from participation on the basis of age.

P.L. 99-509 repealed (for service performed on or after January 1, 1988) the provision allowing denial of entrance into a plan if an employee commenced employment within 5 years of the plan's normal retirement age.

II. YEARS OF SERVICE

(If the plan has no service requirement, do not complete section II. or section III. Also, section II. is to be completed only if years of service and breaks in service are based on hours of service (as opposed to elapsed time-if elapsed time, complete section III. instead of section II.))

II.a. does the plan designate an "eligibility computation period"?

An eligibility computation period is the 12 consecutive month period that a plan uses to determine a year of service for eligibility.

Any plan must designate an eligibility computation period, except a plan that uses an "elapsed time" method of counting service, or a plan that has no service requirement for eligibility to participate.

II.b. is an employee required to complete no more than H hours of service during the eligibility computation period to be credited with a year of service?

Depending on its definition of "hours of service" and the method used to count such hours, a plan must credit an employee with a year of service for eligibility if the employee completes at least 1000, 870, or 750 hours of service (H) in an eligibility computation period.

(H=1000) For a plan that counts all hours of service, or that uses an equivalency based on a period of employment (daily, weekly, semi-monthly, monthly, or shift), the completion of more than 1000 hours cannot be required in order to be credited with a year of service for purposes of eligibility.

(H=870) For a plan that counts "hours worked," or that uses an equivalency based on earnings for an employee who is compensated on an hourly rate, the completion of more than 870 hours cannot be required in order to be credited with a year of service for purposes of eligibility.

(H=750) For a plan that counts "regular time hours", or that uses an equivalency based on earnings for an employee who is compensated on a basis other than an hourly rate, the completion of more than 750 hours cannot be required in order to be credited with a year of service for purposes of eligibility.

II.c. does the plan credit hours of service in accordance with Department of Labor (DOL) Regulations?

If a plan counts all hours of service, credit each hour for which (1) an employee is paid or entitled to payment for performance of duties, (2) an employee is paid or entitled to payment because of a period of time during which no duties are performed, and (3) back pay is either awarded or agreed to by the employer.

If a plan credits hours of service by an equivalency based on a period of service, and an employee is required to be credited with at least 1 hours of service under the paragraph above, then, depending on the basis used, the plan must credit hours of service as follows:

Basis of Equivalency:	Number of Hours Credited:
Day	at least 10
Week	at least 45
Bi-weekly payroll period	at least 95

Month…….at least 190

If a plan counts "hours worked", credit each hour for which an employee is paid or entitled to payment for the performance of duties; also credit hours for which back pay is awarded, or agreed to, by the employer to the extent that the back pay covers a period in which the employee would have been employed in the performance of duties for the employer.

If a plan counts "regular time hours", credit each hour for which an employee is paid or entitled to payment for the performance of duties.

If a plan credits hours of service by an equivalency based on earnings for an employee who is compensated on an hourly rate, an employee must be credited during a computation period with at least the number of hours equal to either the employee's total earnings -

1) from time to time during the computation period, divided by the hourly rate of those times; or
2) for performance of duties during the computation period divided either by the employee's lowest hourly rate during that time, or by the lowest hourly rate payable to an employee in the same, or a similar, job classification.

If a plan credits hours of service by an equivalency based on earnings, and determines compensation other than on an hourly rate, an employee must be credited during a computation period with at least the number of hours equal to his total earnings for duties performed during that period, divided by the employee's lowest hourly rate of compensation during the same period. NOTE: If the same hourly rate of compensation if used for all employees, this method may result in discrimination in favor of highly compensated employees.

II.d. if the plan credits hours of service for period of time during which no duties are performed, does the plan incorporate, in its own words or by reference, the rules for determining or crediting those hours?

This question applies only if H (as noted at II.b. above) equals 1000.

If the plan credits hours of service in periods during which no duties are performed, the plan must designate the method of determining the number of hours to be credited and the method of crediting the hours to the computation periods.

The plan must conform to the requirements of DOL Regulations sections 2530.200-2(b) and (c). Section 2530.200-2(f) of the DOL Regulations, however, also indicates that a plan is not required to state these rules if they are incorporated by reference.

II.e. is the initial eligibility computation period used to determine if the participant has a year of service for eligibility purposes defined as the 12-consecutive-month period, figured with reference to the employee's employment commencement date?

Generally the plan must initially use an eligibility computation period of 12-consecutive-months, beginning with the employee's employment commencement date.

The employee's employment commencement date is the first day for which an employee is entitled to be credited with an hour of service for the performance of duties.

An alternative eligibility computation period may be used where employment commencement dates cannot be specifically determined. This alternative (based on payroll periods not exceeding 31 days) is detailed in DOL Regulations section 2530.202-2(e).

II.f.if the plan uses the plan year as the computation period to measure years of service for purposes of eligibility after the first computation period, does the first computation period include the first anniversary of the employment commencement date?

If eligibility computation periods under a plan are determined solely on the anniversary of employment, then this item is not applicable.

Where eligibility computation periods after the initial eligibility computation period are based on other than anniversaries of employment (i.e.-plan years), the plan should provide that the succeeding computation periods will begin with the plan year that includes the first anniversary of the employee's employment commencement date.

II.g. is a "break in service" defined as an eligibility computation period when the employee is not credited with more than B hours?

The break in service rules allow a plan to disregard certain service before the employee has a break in service. An employee who comes back to work after incurring a one year break in service may have to complete a year of service (as noted at II.b. above) in order to be eligible to participate in the plan.

Depending on the definition of "hours of service" and the method used to count these hours (as noted at II.b. above), a plan may charge an employee with a break in service for an eligibility computation period in

which the employee fails to complete **more than** B hours of service. Thus (again, based on II.b. above), where:

H = 1000; then B = 500
H = 870; then B = 435
H = 750; then B = 375

If all of an employee's service with an employer is counted for participation, the plan need not provide break in service rules. If the plan does not provide for a break in service, questions II.g. through II.k. are not applicable.

II.h. is the eligibility computation period for determining a break in service the same as is used to figure a year of service for eligibility?

To apply the break in service rules, the plan must use the same computation periods to measure breaks in service that it uses to measure service for eligibility to participate.

II.i. does the plan credit hours of service to the appropriate computation period to avoid a break in service for employees on maternity or paternity leave?

In order to avoid a break in service for employees on maternity or paternity leave, an individual is credited with certain hours of service if such individual is absent from work for any period by reason of 1) **pregnancy** of the individual, 2) **birth of a child** of the individual, 3) **placement of a child with the individual** in connection with an adoption or 4) **caring for a child** described in 2) or 3) immediately following such birth or placement.

During the period of absence, the individual is considered to have completed the number of hours that would have been credited but for the absence. If the number of hours that would have been credited but for the absence is not known, then eight hours of service per work day of such absence is credited.

Note that hours of service treated as completed for this purpose cannot exceed 501.

The so credited hours of service are credited in the year in which the absence from work begins, if the individual would be prevented from incurring a one year break in service in such year solely because of the application of this rule. Otherwise, the hours are credited to the immediately following year.

Credit for maternity or paternity leave is *only made* to avoid a break in service and *not to obtain a year of service.*

II.j. when an employee has a vested benefit, does the employee participate immediately upon returning to work after a break in service? and II.k.-when an employee who has satisfied the minimum service requirement and who has no vested benefit has a break in service, and the number of consecutive breaks in service is less than the greater of 5 or the number of years in which the employee attained a year of service, does the employee participate immediately upon returning to work?

In general, an employee's pre-break service does not have to be credited until the employee has completed 1 year of service after the break. This should not be confused with the following rule of parity. If a participant with no vested interest has a break in service under the rule of parity, service before the break need not be counted for participation if the number of consecutive 1- year breaks equals or exceeds the greater of 5 or the aggregate years of service completed before the break. The aggregate years of service completed before the break does not include years of service that need not be counted because of earlier breaks. In the case of a plan that provides for 100 percent vesting after 2 years of service, an employee who has not met the plan's service requirement and has a one year break in service need not have pre-break service taken into consideration for purposes of meeting the plan's service requirement.

When an employee's pre-break service must be taken into account after a year of service, an employee who meets the plan's eligibility requirements and has a break need to be credited with the pre-break service until completion of a year of service after returning. However, at that time the employee would be required to retroactively participate under the plan.

III. YEARS OF SERVICE AND BREAKS IN SERVICE BASED ON ELAPSED TIME

III.a. does the plan credit an employee with a period of service, beginning no later than the employment commencement date and ending no sooner than the severance from service date?

The employment commencement date is no later than the date an employee first performs an hour of service for the employer.

The severance from service date is the **earlier** of the date on which the employee quits, is discharged, retires, or dies **OR** the first anniversary of the first date of absence of an employee for any reason other than if the employee quits, is discharged, retires, or dies.

The employee must be credited with a period of service equal to at least the time between the employment commencement date and the severance from service date.

III.b. does the plan determine an employee's total period of service by aggregating all individual periods, unless the periods of service may be disregarded under the rule of parity?

A plan must generally aggregate all separate periods of service, except for those periods of service that may be disregarded because of the rule of parity (see III.h.).

Alternatively, instead of keeping separate periods of service, the plan may aggregate by adjusting the employment commencement date.

III.c. in determining an employee's period of service, does the plan take into account the service spanning rules?

A period of severance is the time between the employee's severance from service date and the date the employee again performs an hour of service for the same employer.

If an employee severs from service by quitting, being discharged, or retiring, and then performs an hour of service within 12 months of the severance from service date, the plan must consider the period of severance as a period of service.

Also, if an employee severs from service for any reason other than quitting, being discharged, or retiring, and within the next 12 months or less quits, is discharged, or retires and then performs an hour of service within 12 months of the date on which he or she was first absent from service, the plan must consider that period of severance as a period of service.

III.d. if a plan contains a service requirement for initial eligibility to participate, does an employee satisfy this service requirement as of the date the employee completes a period of service equal to the period required?

Where a plan has a service requirement and uses the elapsed time method of crediting service, an employee satisfies the requirement as of the date he or she has credit for a period of service equal to the requirement.

For this purpose, the period of service runs from the employment commencement date to the applicable anniversary of the employment

commencement date, as specified in the plan (usually this is one year, but a lesser period of time may be specified).

III.e. is a 1-year period of severance defined as a 12-consecutive-month period beginning on the severance from service date and during which the employee does not perform an hour of service for the employer?

A 1-year period of severance is a 12-consecutive-month period beginning on the severance from service date and ending on the first anniversary of the date, provided that within this period the employee does not perform an hour of service for the employer maintaining the plan.

This definition is needed in order to apply the break in service rules. The break in service rules allow a plan to disregard certain service before the employee has such a break.

If all of an employee's service with an employer is counted for participation, the plan need not provide break in service rules. If the plan does not provide for a break in service, questions III.e. through III.h. are not applicable.

III.f. is the first period of severance ignored to the extent that such period is attributable to maternity or paternity leave?

An individual shall not incur the first 12-month period of severance that would otherwise be counted if severance is due to maternity or paternity leave. Such 12-month period is neither counted as a year of service nor as a period of severance.

Maternity or paternity leave is a period an individual is absent from work by reason of 1) **pregnancy** of the individual, 2) **birth of a child** of the individual, 3) **placement of a child with the individual** in connection with an adoption or 4) **caring for a child** described in 2) or 3) immediately following such birth or placement.

III.g. when an employee has a vested benefit, does the employee participate immediately on returning to work after a 1-year period of severance?

And

III.h.-when an employee who has no vested benefit has a 1-year period of severance, and the period of severance is less than the greater of 5 years or the prior period of service, does the employee participate immediately on returning to work?

In general, an employee's service before a 1-year period of severance is not required to be credited until the employee completes a 1-year period of service after the period of severance. The rule of parity applies to employees who are not vested. If a participant with no vested interest has a 5-year or more period of severance, service before the severance need not be counted for participation if the period of severance equals or is more than the aggregate periods of service before the break. The period of service completed before the period of severance does not include service that need not be counted because of earlier periods of severance.

When service before a 5-year or more period of severance must be taken into account after a 1-year period of service, an employee who meets the plan's eligibility requirements and has a 1-year period of severance need not be credited with pre-break service until he completes a 1-year period of service after severance. However, at that time the employee would be required to participate under the plan retroactively.

JOINT AND SURVIVOR-WORKSHEET 3 (OVERVIEW)

The purpose of this chapter is to provide a synopsis of the points noted at Alert Guidelines Worksheet Number 3 (Form 5625). For a detailed review of the items noted on that form, see Explanation Number 3, Joint and Survivor Determination of Qualification (Document 6391).

I. APPLICABILITY

I.a.-is the plan a defined contribution plan (other than a money purchase or target benefit plan) that provides that the surviving spouse or, if the surviving spouse consents, a designated beneficiary, shall upon the participant's death receive the full nonforfeitable accrued benefit of the participant? (if "yes", answer I.b.; if "no", go to II.).

Defined benefit plans, money purchase plans and target benefit plans are subject to the survivor annuity requirements, per Internal Revenue Code (IRC) section 401(a)(11)(B).

Other defined contribution plans are not subject to the survivor annuity requirements if **all** the following conditions are met:

1) the plan provides that the participant's nonforfeitable accrued benefit is payable in full, on the participant's death, to the surviving spouse (unless the participant elects, with spousal consent, that the benefit instead be paid to a designated beneficiary);
2) the participant does not elect to receive benefits in the form of a life annuity (see I.b (i)); and
3) the plan is not a transferee (see I.b (ii)) or offset (see I.b.(iii)) plan with respect to the participant.

Note that the second and third requirements apply on a participant by participant basis. Thus a profit-sharing plan, for example, could be subject to the survivor annuity requirements with respect to some participants, but not others. However, if a plan offers a life annuity to any participant the plan must contain all language necessary to satisfy IRC 401(a)(11) and 417.

I.b.(i)-is this a plan that offers benefits in the form of a life annuity?

A life annuity is an annuity payable for the life of the participant.

If the plan contains a life annuity option, the terms of the plan must meet the requirements described in the remainder of the worksheet for those participants who elect the life annuity.

I. b.(ii)-is this a plan that is a transferee of benefits from a plan subject to IRC sections 401(a)(11) and 417?

A plan is a transferee plan if it is a direct or indirect transferee of a participant's benefits from a defined benefit plan or a defined contribution plan that was subject to the survivor annuity requirements with respect to a participant (as noted at I.a. above).

A plan that otherwise would be exempt from the survivor annuity requirements will have to meet these requirements if the plan is a transferee plan with respect to **any** participant.

I. b.(iii)-is this a plan that offsets benefits under a defined benefit plan?

An offset plan is an arrangement where an employer maintains both a defined contribution plan and a defined benefit plan, and the benefits under the defined benefit plan are reduced by the participant's account value of the defined contribution plan.

In such an arrangement, the defined contribution plan must meet the requirements specified in the rest of this worksheet, with respect to those participants whose benefits are offset.

A plan will not become subject to the survivor annuity requirements on account of the offset, however, unless the plans are maintained by the same employer or by affiliated employers.

IF THE ANSWER TO I.b.(i) OR I.b.(ii) OR I.b.(iii) IS "YES", PROCEED TO PART II. (JOINT & SURVIVOR BENEFITS); IF THE ANSWER TO I.b.(i) AND I.b.(ii) AND I.b.(iii) IS "NO", DO NOT COMPLETE THE BALANCE OF WORKSHEET NUMBER 3, AS THE JOINT AND SURVIVOR REQUIREMENTS DO NOT APPLY.

II. JOINT AND SURVIVOR BENEFITS

II.a.-does the plan provide for the payment of benefits in the form of a qualified joint and survivor annuity (QJSA) in the case of a vested participant who survives until the annuity starting date?

A plan subject to the survivor annuity requirements (as noted at I. above) must provide that a vested participant who is alive on the annuity starting date must receive his or her benefit in the form of a QJSA, unless there has been a proper election by the participant, with spousal consent, to waive the QJSA **and** written notice requirements (pursuant to IRC section 417(a)(3)(A)) have been met.

A QJSA is an annuity for the life of the participant with a survivor annuity for the life of the spouse which is not less than 50% or more than 100% of the annuity payable during the joint lives of the participant and the spouse.

In a defined contribution plan, the amount of the QJSA benefit is that which can be purchased with the participant's nonforfeitable account balance, including both the employer and employee contributions.

In a defined benefit plan, the entire vested accrued benefit (including any portion attributable to mandatory contributions) is subject to the QJSA requirements and the QJSA for a married participant must be at least as valuable as any other optional form of benefit that is payable under the plan at the same time.

A QJSA is the actuarial equivalent of a single life annuity for the life of the participant (IRC section 417(b)(2)); thus, in the case of an unmarried participant, a QJSA is an annuity for the life of the participant.

For benefits payable in the form of an annuity, the annuity starting date is the first day of the first period for which an amount is payable as an annuity (IRC section 417(f)(2)(A)(i)).

For benefits not payable in the form of an annuity, the annuity starting date is the first day on which all events have occurred which entitle the participant to the benefit (IRC section 417(f)(2)(A)(ii)).

II.b.-if the plan provides for disability benefits that are not auxiliary benefits, does the plan treat the first day of the first period for which these benefits are to be paid as the annuity starting date?

A disability benefit is an auxiliary benefit if the participant will receive, at early or normal retirement age, a benefit that meets the accrual and vesting requirements without taking the disability payments into account. Thus, if a participant receives a disability benefit under the plan and is also entitled to an annuity that is unreduced for the disability payments at normal retirement age, then the disability payments received are considered to be auxiliary. **In such case, the participant's annuity starting date is at normal retirement age.**

A disability benefit that reduces the benefit that would otherwise have been payable at early or normal retirement age is not an auxiliary benefit. Also, a disability benefit that reduces the number of optional forms of benefit available to the participant at early or normal retirement age is not an auxiliary benefit. **In such case, the annuity starting date is the first day of the first period for which a disability payment is received.**

II.c.-is the QJSA under the plan an annuity that commences immediately?

A plan cannot make a distribution at any time in a form other than a QJSA (except for the $5,000 cash out limit per IRC section 411(a)(11) and section 1.411(a)-11(a)(3) of the Income Tax Regulations (Regs.)), unless a QJSA that commences immediately is available at the same time and the participant has waived it (with spousal consent, as applicable).

No consent of the spouse is needed for distribution of a QJSA at any time.

No consent of the participant or spouse is needed for distribution of a QJSA **after** the benefit is no longer immediately distributable (after the participant attains the later of normal retirement age or age 62).

II.d.-is the QJSA for a married participant at least as valuable as any other optional form of benefit payable under the plan at the same time?

For an unmarried participant, the QJSA may be less valuable than other optional forms of a benefit payable under a plan. But for a married participant, the QJSA must be at least as valuable as any other optional form of benefit payable under the plan at the same time.

If a plan has two joint and survivor annuities that would satisfy the requirements for a QJSA, but one has a greater actuarial value, the more valuable joint and survivor annuity is the QJSA.

II.e.-if the plan provides for two or more actuarially equivalent annuities that satisfy the requirements for a QJSA, does it specify which is the automatic form?

If there are two or more actuarially equivalent joint and survivor annuities that satisfy the requirements for a QJSA, the plan must designate which one is the QJSA and, therefore, the automatic form of benefit payment.

II.f.-is the participant allowed to receive a QJSA distribution at earliest retirement age under the plan?

A plan must permit a participant to receive a distribution in the form of a QJSA when the participant attains the earliest retirement age under the plan.

Earliest retirement age for purposes of IRC sections 401(a)(11) (requirement of joint and survivor annuity and preretirement survivor annuity), 411(a)(11) (restrictions on certain mandatory distributions) and 417 (definitions and special rules for purposes of minimum survivor annuity requirements) are as follows:

1) Where a plan provides for voluntary distributions starting on the participant's separation from service, earliest retirement age is the earliest age at which a participant could separate from service and receive a distribution (participant death is considered a separation from service).
2) Where a plan provides for in-service distributions, earliest retirement age is the earliest age at which such distributions may be made.
3) Where a plan does not provide for voluntary distributions starting on the participant's separation from service or for in-service distributions, earliest retirement age is the early retirement age determined under the plan. If there is no early retirement age under the plan, then the earliest retirement age is the normal retirement age under the plan.

II.g.-does the plan provide that the participant can elect during the applicable election period not to take a QJSA only with the spouse's consent to a specific beneficiary and a particular optional form of benefit?

A participant's election to waive his or her spouse's survivorship rights in the participant's pension benefits is invalid unless the spouse of the participant consents in writing to such an election. The election must designate a beneficiary (or form of benefits) that can not be changed without spousal consent (unless the consent of the spouse expressly permits designations by the participant without any requirement of further consent by the spouse and this consent identifies the specific form of benefit). The spouse's consent must acknowledge the effect of the election and be witnessed by either a plan representative or a notary public.

The period for such election/consent begins on the first day of the 90-day period ending on the annuity starting date and ends on the later of the annuity starting date or the 30th day after the plan administrator provides the participant with a written explanation of the QJSA.

A plan must also provide participants with notice explaining the terms and conditions of a QJSA, their rights to waive the QJSA and to revoke a waiver, and their spouses' rights regarding consent. In general this written explanation must be provided no more than 90 nor less than 30 days prior to the annuity starting date and it must explain the terms and conditions of the QJSA; the participant's right to elect, in writing, not to receive the QJSA (with the consent of the participant's spouse, also in writing, if applicable), and the effect of such an election; the participant's right to revoke an election not to receive the QJSA, and the effect of such a revocation; and the eligibility conditions, material features, and relative values of available optional forms of benefit.

For plan years beginning after December 31, 1996, the plan may contain language that the annuity starting date could be a date prior to the time the participant received the written explanation if the participant's right to waive the QJSA does not end less than 30 days after such explanation is provided, subject to the participant's waiver of the 30 day period.

II.h.-does the plan provide that a participant who is to receive a QJSA may elect, with spousal consent, not to take the QJSA and may revoke the election, or choose again to take the QJSA, at any time and any number of times within the applicable election period?

A plan must allow a participant to revoke an election to waive the QJSA at any time (and any number of times) during the election period noted at II.g

If a participant's spouse consents to the participant's waiver of a survivor annuity form of benefit, a subsequent spouse of the participant is not bound by that consent. However, a waiver by the former spouse in the case of plan benefits securing plan loans does apply to any subsequent spouse.

II.i.-does the plan provide an automatic QJSA to a participant who is married on the annuity starting date, regardless of whether married throughout the one-year period ending on the annuity starting date?

A plan may provide that a QJSA does not apply if the participant and his/her spouse had not been married throughout the one year period ending on the earlier of the participant's annuity starting date or the date of the participant's death (IRC section 401(a)(11)(D).

However, a plan must treat a participant and spouse who are married on the annuity starting date as having been married during the one-year period ending on that date if they remain married for one year (IRC section 417(d)(2)).

Example: Plan A provides that participants who are married on the annuity starting date for less than one year are treated as unmarried participants. Plan A provides benefits in the form of a QJSA or an optional lump sum distribution.

Participant B was married six months prior to the annuity starting date (normal retirement age). Plan A must treat B as married and must commence payments in the form of a QJSA unless another form is selected (with spousal consent).

If a QJSA is paid and B is divorced from the spouse (C) within the first year of the marriage, C will no longer have any survivor rights under the annuity (unless a qualified domestic relations order provides otherwise).

If B stays married to C, and B dies within the one-year period, Plan A may treat B as unmarried and forfeit the QJSA benefit payable to C.

III. PRE-RETIREMENT SURVIVOR ANNUITIES

III.a.-does the plan provide the surviving spouse of a vested participant who dies before the annuity starting date with a qualified preretirement survivor annuity (QPSA)?

A plan that is subject to the qualified survivor annuity rules must provide that a QPSA be provided to the surviving spouse of a vested participant who dies before the annuity starting date (the first day of the first period for which an amount is payable).

This applies unless there has been a proper election to waive the QPSA and notice requirements have been met.

III.b.(i)-is the amount of the QPSA correctly defined in the case of a defined benefit plan?

A defined benefit plan should provide that the benefit to be paid to the surviving spouse of a participant who dies before the annuity starting date will be determined as follows:

If the participant dies **after** attaining the plan's earliest retirement age, the benefit will not be less than the benefit payable to the survivor if the participant had retired with an immediate QJSA on the day before the participant's death.

If the participant dies **on or before** attaining the plan's earliest retirement age, the benefit may not be less than the benefit that would be payable to the survivor if the participant had separated from service at the earlier of actual separation or death, survived until the plan's earliest retirement age, retired at that time with an immediate QJSA, and died on the day thereafter.

III.b.(ii)-is the amount of the QPSA correctly defined in the case of a defined contribution plan?

A defined contribution plan subject to the qualified survivor annuity requirements must provide that the annuity, to be provided to the surviving spouse of a participant who dies before the annuity starting date, must

have a value not less than 50 percent of the participant's nonforfeitable account balance as of the date of the participant's death.

If a contributory defined contribution plan has a forfeiture provision permitted by IRC section 411(a)(3)(A) (forfeiture on account of death), not more than a proportional percent of the account balance attributable to contributions that may not be forfeited at death (for example, employee and IRC section 401(k) contributions) may be used to satisfy the QPSA benefit. Thus, for example, if the QPSA benefit is to be provided from 50 percent of the account balance, not more than 50 percent of the nonforfeitable contributions may be used for the QPSA.

III.c.(i)-does the plan provide that the surviving spouse can begin receiving the QPSA, in a defined benefit plan, no later than the month the participant would have attained earliest retirement age (or within a reasonable time after death, if later)?

A defined benefit plan must permit the surviving spouse to direct the commencement of payments under a QPSA no later than the month in which the participant would have attained the earliest retirement age under the plan.

A plan may permit the commencement of payments at an earlier date.

III.c.(ii)-does the plan provide that the surviving spouse can begin receiving the QPSA, in a defined contribution plan, within a reasonable time after the participant's death?

A defined contribution plan subject to the qualified survivor annuity requirements must provide that the surviving spouse may direct the commencement of payments under the QPSA within a reasonable time after the participant's death.

For this purpose, availability within the 90-day period following the date of death is deemed to be reasonable; the reasonableness of a longer period is determined based on the particular facts and circumstances (section 1.401(a)-20, Q&A 3(b) of the Regs.).

III.d.-in a defined benefit plan that allows the QPSA to be paid earlier or later than the time described in III.c.(i), does the plan make actuarial adjustments to reflect the early or delayed payment?

A QPSA is calculated as of the earliest retirement age if the participant dies before such time, or at death if the participant dies after the earliest retirement age.

The plan must, therefore, make reasonable actuarial adjustments to reflect a payment earlier or later than the earliest retirement age.

III.e.-in a defined benefit plan that charges the participant for the cost of the QPSA, is the charge inapplicable prior to the later of the time the participant can waive the QPSA or when the participant is given notice of the right to waive the QPSA?

A defined benefit plan may charge a participant for the cost of providing the QPSA. However, for plan years beginning after 1988, the plan may not charge for the QPSA prior to the later of the time the participant can waive the QPSA or when the participant is given notice of the right to waive the QPSA.

A charge for the QPSA that reasonably reflects the cost of providing the QPSA will not fail to satisfy the IRC section 411 even if it reduces the accrued benefit.

III.f.-does the plan provide that the participant can elect during the applicable election period to waive the QPSA only with spousal consent to a specific nonspouse beneficiary?

In addition to providing an automatic QPSA, a plan that is subject to the survivor annuity rules must generally meet certain notice, election, and consent requirements that apply to a QJSA.

The plan (subject to IRC section 401(a)(11)) should provide that, on or after the first day of the plan year in which the participant attains age 35, a participant may waive the QPSA provided **all** the following conditions are satisfied:

1) The participant's spouse consents in writing to the election **and** the spouse's consent is witnessed by a plan representative or notary public;
2) The participant's waiver **and** the spouse's consent state the specific nonspouse beneficiary (including any class of beneficiaries or contingent beneficiaries), which may not be

modified (except back to a QPSA) without subsequent spousal consent (unless expressly permitted by the spouse);

3) The spouse's consent acknowledges the effect of the election.

Generally, the participant may not be allowed to waive the QPSA before first day of the plan year in which the participant attains age 35, although the plan may provide for an earlier waiver (with spousal consent) if written explanation of the QPSA is given to the participant and the waiver becomes invalid with the beginning of the plan year in which the participant attains age 35.

If the participant separates from service before the plan year in which he or she attains age 35, the foregoing election may be made on or after the date of separation, with respect to benefits accrued prior to separation.

A plan must also provide participants with notice explaining the QPSA that is comparable to the QJSA explanation. In the case of a participant who separates from service before age 35, the notice must be given within one year before or after the date of separation. In other cases, the notice must generally be given between the first day of the plan year in which the participant turns age 32 and the last day of the plan year before the participant turns 35.

The plan does not have to meet these notice, election and consent requirements if it fully subsidizes the QPSA and the participant is not allowed to waive the QPSA or to select a nonspouse beneficiary.

III.g.-does the plan provide that a participant may revoke a waiver of the QPSA at any time and any number of times during the applicable election period?

The plan should provide that a participant who has elected to waive the QPSA with spousal consent may revoke the election at any time and any number of times during the period between the first day of the plan year in which the participant attains age 35 and the date of the participant's death.

III.h.-does the plan limit any marriage requirement for the QPSA to no more than one year before the participant's death?

In the case of a QPSA, any marriage requirement must be limited to no more than one year before the participant's death.

IV. SPOUSAL CONSENTS AND PLAN LOANS

IV.a.-does the plan require the consent of the spouse (or surviving spouse) to any distribution in any form other than a QJSA (or QPSA), except where the present value of the nonforfeitable benefit does not exceed $5,000?

Generally plans may not commence the distribution of any portion of a participant's accrued benefit in any form unless the applicable consent requirements are satisfied (Treas. Reg. section 1.417(e)-1(b)).

A plan may provide, however, that the present value of a QJSA or a QPSA will be immediately distributed if such value does not exceed $5,000 (IRC section 417(e)(1)).

IV.b.-does the plan require the consent of the surviving spouse to the distribution of a QPSA while it is immediately distributable, except where the present value of the nonforfeitable benefit does not exceed $5,000?

A plan may not require a surviving spouse to begin receiving benefits under a QPSA while the benefit is immediately distributable.

A benefit is immediately distributable until such time as the participant would have attained the later of age 62 or normal retirement age (normal retirement age is the **earlier** of (a) the time a participant attains normal retirement age under the plan, or (b) the **later** of the time a plan participant attains age 65 or the 5th anniversary of the time a plan participant commenced participation in the plan).

The plan may distribute the QPSA without spousal consent once it is no longer immediately distributable.

IV.c.-if the plan provides for participant loans, does it require spousal consent to the use of the accrued benefit as security for the loan?

The plan that provides for participant loans should further provide that written spousal consent (pursuant to the requirements of IRC section 417(a)(2), as noted in the first paragraph of II.g., above) to the use of a participant's accrued benefit as security for a loan must be obtained within the 90-day period ending on the date on which the loan is to be secured.

Consent it not needed if the participant is not married at the time the loan is secured or if the participant's total accrued benefit does not exceed $5,000 ($3,500 for plan years beginning before August 6, 1997).

EMPLOYEE AND MATCHING CONTRIBUTIONS-WORKSHEET 11 (OVERVIEW)

The purpose of this chapter is to provide a synopsis of the points noted at Alert Guidelines Worksheet Number 11 (Form 8799). For a detailed review of the items noted on that form, see Explanation Number 11, Employee and Matching Contributions (Document 7334).

I. APPLICABILITY

I. a. (i)-does the plan provide for voluntary or mandatory employee contributions or matching employer contributions? (defined contribution plan)

Such employee contributions are "after-tax" (included in the employees' gross income). This is distinct from 401(k) deferrals, which are made on a before-tax basis.

A matching contribution is any employer contribution (including discretionary contributions) made on behalf of an employee on account of an employee contribution to the plan.

I. a. (ii)-does the plan include a section 401(k) cash or deferred arrangement (CODA) and does the plan provide for the allocation of matching contributions or forfeitures on the basis of a participant's elective contributions? (defined contribution plan)

The key feature of a 401(k) CODA is the employee's option to either have the employer contribute to the plan or receive such amounts in cash.

The match must be based on the participant's elective (401(k)) contribution. There is no required matching formula; however, the formula used cannot result in contributions in excess of statutory limits or discrimination in favor of highly compensated employees.

I. b.-does the plan provide for voluntary employee contributions? (defined benefit plan)

Defined contribution plans entail individual employee accounts, with separate account balance(s) for each individual. This is not generally the case for defined benefit plans. However, if a defined benefit plan calls for voluntary (after tax) employee contributions, such contributions must be allocated to a separate employee account.

II. DISCRIMINATION

II a. (i)-does the plan include the actual contribution percentage (ACP) test set forth in section 401(m)(2)(A) of the Code and provide that it will meet the ACP test or II a (ii) below?

The contribution percentage must be determined for each eligible employee, whether or not they participate in the CODA and related matching contribution arrangement.

The contribution percentage is calculated as follows: employee (after tax) contributions, plus matching contributions, plus qualified nonelective contributions, plus qualified matching contributions, divided by compensation.
(EC+Match+QNEC+QMAC/Comp)

For plan years beginning after December 31, 1996, the ACP test compares the average of the actual amounts contributed for the plan year, as a percentage of compensation, on behalf of the eligible highly compensated employees to the average of the actual amounts contributed, again as a percentage of compensation, on behalf of the eligible non-highly compensated employees for the prior year.

The ACP test is computed by first separately calculating the actual contribution ratios of each eligible employee and then averaging the ratios of all eligible employees in the highly compensated and non-highly compensated groups.

The percentage contributed for the HCEs can't be more than the greater of:

1) 1.1.25 times the percentage contributed for NHCEs, or
2) 2.the lesser of two **times** the percentage contributed for NHCEs or two **plus** the percentage contributed for NHCEs.

For calendar years beginning after December 31, 1996, a plan subject to section 401(m) is deemed to satisfy the ACP test if it contains, and complies in operation with, "SIMPLE" provisions or for plan years after December 31, 1998, "Safe Harbor CODA Provisions".

The testing method (prior year or current year, in calculating the NHCE average ratio) must be specified.

II a. (ii)-does the plan incorporate the ACP test by reference, including whether it is using the prior or current year testing method, and provide that it will meet the test?

In lieu of stating the ACP test (as previously noted), the plan may instead reference the provisions of Internal Revenue Code (IRC) section 401(m)(2), the regulations thereunder, Notices 97-2 and 98-1, and any subsequent superseding guidance.

The testing method (prior year or current year, in calculating the NHCE average ratio) must be specified.

II b. (i)-if the terms of the plan set forth the ACP test, instead of incorporating it by reference, does the plan take into account the actual contribution ratios of all eligible employees?

The actual contribution ratio for **all** eligible employees must be taken into account in determining whether a plan satisfies the ACP test.

An eligible employee is any employee who is directly or indirectly eligible to make an employee contribution or receive an allocation of matching contributions.

For plan years beginning after December 31, 1998, if the employer elects to apply IRC section 410(b)(4)(B) (exclusion of employees not meeting statutory age (21) and service (one year) requirements), in determining whether a CODA meets IRC section 410(b)(1) (70% minimum coverage or 70% average benefit requirement, as applicable), for ACP test purposes the plan may provide that all eligible employees (other than HCEs) not meeting the age and service requirements are excluded.

II b. (ii)-if the terms of the plan set forth the ACP test, instead of incorporating it by reference, does the plan take the proper contributions into account?

An employee (after-tax) contribution is to be paid to the trust during the plan year.

A matching contribution must:

1) be made on account of 401(k) deferrals or employee after-tax contributions for the plan year,
2) be allocated to the employee's account during the plan year, and
3) be paid to the trust by the end of the 12th month following the close of the plan year.

II b. (iii)-if the terms of the plan set forth the ACP test, instead of incorporating it by reference, does the plan treat contributions made under plans that are aggregated for purposes of IRC sections 401(a)(4) or 410(b) as made under a single plan?

When two or more plans are treated as one for purposes of IRC section 401(a)(4) or 410(b), all employee and matching contributions are considered as made under a single plan for purposes of the ACP test, also.

Two or more plans subject to section 401(m) may be permissively aggregated if the aggregated plans satisfy the ACP test. Plans may not be permissively aggregated unless they have the same plan year and use the same testing method (either all current or all prior).

II b. (iv)-if the terms of the plan set forth the ACP test, instead of incorporating it by reference, does the plan aggregate all plans under which an HCE is eligible to make employee contributions or receive matching contributions for purposes of the HCE's actual contribution ratio?

Whenever an HCE is eligible under more than one plan of the same employer subject to IRC section 401(m), this employee's actual contribution ratio is calculated by treating all the plans subject to IRC section 401(m) as one plan. This rule does not apply to employees who are not highly compensated.

II b. (v)-if the terms of the plan set forth the ACP test, instead of incorporating it by reference, does the plan determine the ACPs of the HCEs and of all other eligible employees using the relevant plan year?

If the plan is using the prior year testing method, the ACP of HCES for the testing year is determined using the current plan year data, while the ACP of NHCEs is determined using the prior plan year data.

If the plan is using the current year testing method, the ACP of both HCEs and NHCEs is determined using the current plan year data.

II C.-ARE EMPLOYEE AND MATCHING CONTRIBUTIONS AVAILABLE ON A NONDISCRIMINATORY BASIS?

A plan that provides for employee or matching contributions must make such contributions available to employees on a nondiscriminatory basis.

A plan is required to satisfy section 401(a)(4) with respect to the availability of benefits, rights, and features under the plan, including the right to make each level of employee contributions and to receive each level of matching contributions.

A benefit, right or feature must be available to a group of employees that satisfies IRC section 410(b) (minimum coverage requirements).

III. ELECTIVE CONTRIBUTIONS AND QNECS (FOR A PLAN PROVIDING THAT QNECS AND /OR ELECTIVE CONTRIBUTIONS ARE TREATED AS MATCHING CONTRIBUTIONS FOR ACP TEST PURPOSES)

III a. (i)-are QNECs immediately vested, without regard to a participant's age and service?

A QNEC **must** be fully vested when made, regardless of a participant's age, service, or whether the contribution is actually taken into account for the ACP test.

III a. (ii)-are QNECs distributed only under the distribution rules for elective contributions under qualified cash or deferred arrangements?

A QNEC must be distributable only under the following circumstances:

1) The employee's retirement, death, disability or separation from service;
2) The termination of the plan without establishment or maintenance of another defined contribution plan (other than an ESOP, SEP or SIMPLE IRA);
3) Attainment of age 59 1/2 (only profit sharing, stock bonus and for distributions made after August 20, 1996, rural cooperative plan;
4) The sale or other disposition by a corporation to an unrelated corporation of substantially all of the assets used in a trade or business, but only with respect to employees who continue employment with the acquiring corporation and the acquiring corporation does not maintain the plan after disposition; and
5) The sale or other disposition by a corporation of its interest in a subsidiary to an unrelated entity, but only with respect to employees

who continue employment with the subsidiary and the acquiring entity does not maintain the plan after disposition.

Paragraphs 2, 4 and 5 apply only if the distribution is in the form of a lump sum.

III b.-are QNECs and elective contributions treated as matching contributions only if the conditions described in section 1.401(m)-1(b)(5) of the Regulations are satisfied?

If the plan provides that QNECs and elective contributions are considered for purposes of the ACP test, then the QNECs and elective contributions that will be treated as matching contributions must be limited to only those contributions that are made with respect to those employees who are eligible employees under the 401(m) plan being tested.

The plan must either provide that such contributions are treated as matching contributions only if they meet the five additional requirements enumerated under section 1.401(m)-1(b)(5) of the Regulations, or incorporate these requirements by reference.

IV. CORRECTIONS

IV a.-if the plan is using the current year testing method, does it provide that in the event it would otherwise fail the ACP test the employer will make QNECs in order to satisfy the test? (if "yes", also complete section III).

If the plan is using the current year testing method, it may provide, that in order to satisfy the ACP test, the employer will make additional matching contributions or QNECs. If the plan so provides, further correction will not be required.

Note that if a plan contains provisions that ensure the ACP test is always satisfied, then it need not contain a method for correction.

IV b.-does the plan provide a mechanism by which employee and/or matching contributions of the HCEs in excess of the amount allowed in the test in II a. ("excess aggregate contributions") may be distributed or, if forfeitable, forfeited? (no = n/a; if yes, then complete IV c.)

A plan may provide that if the ACP limit is exceeded, the plan will distribute (or forfeit, if forfeitable) the excess aggregate contributions plus the income that is allocable to these contributions.

IV c. (i)-is the amount of the excess aggregate contributions to be distributed to HCEs (or, if forfeitable, forfeited) determined using the "ratio leveling method"?

For plan years beginning after December 31, 1996, the determination of the amount of excess contributions attributable to each HCE and the identity of the HCEs who will have excess contributions distributed from their accounts are performed in two separate steps.

Ratio leveling method: Determine how much the actual contribution ratio (ACR) of the HCE with the highest ADR would have to be reduced to satisfy the ACP test or cause such ratio to equal the ACR of the HCE with the next highest ratio. Repeat this process until the ACP test would be satisfied. The amount of excess contributions is equal to the sum of these hypothetical reductions multiplied, in each case, by the highly compensated employee's compensation.

IV c. (ii)-does the plan determine the amount of excess aggregate contributions only after first determining the amount of excess contributions to be treated as employee contributions due to a recharacterization under a CODA in this or any other plan of the employer?

The plan should provide that the amount of excess aggregate contributions for a plan year shall be determined only after first determining the excess contributions that are treated as employee contributions due to recharacterization.

IV c. (iii)-does the plan properly determine income to be distributed or forfeited?

The plan should provide that the distribution (or forfeiture, if applicable) of excess aggregate contributions will include the income allocable thereto. The income allocable to the excess aggregate contributions includes income for the plan year for which the excess aggregate contributions were made. The plan may also provide that it includes income for the period between the end of the plan year and the date of the distribution (or forfeiture).

IV c. (iv)-if the plan will distribute matched employee contributions, will it also forfeit the corresponding matching contributions?

A method of correcting excess aggregate contributions must meet the nondiscrimination requirements of IRC section 401(a)(4). A method under which employee contributions are distributed to HCEs to the extent necessary to meet the requirements of IRC section 401(m)(2) while matching contributions attributable to such employee contributions remain

allocated to the employee's account will not meet the requirements of IRC section 401(a)(4).

IV c. (v)-will the distribution be made after the end of the plan year for which the excess aggregate contributions were made and no later than the end of the following plan year?

Failure to correct excess aggregate contributions by the close of the plan year following the plan year for which they were made will cause the plan to fail to satisfy the requirements of IRC section 401(a)(4) (and thus be unqualified) for the plan year for which the excess aggregate contributions were made and for all subsequent plan years until corrected. Also, the employer will be liable for a 10% excise tax on the amount of excess aggregate contributions unless they are corrected within 2 ½ months after the close of the plan year for which they were made.

IV c. (vi)-are distributions or forfeitures of excess aggregate contributions determined using the "dollar leveling method"?

Dollar leveling method: Excess aggregate contributions are distributed (forfeited, if forfeitable) from the account(s) of the HCE with the highest dollar amount of contributions used in the ACP test for the plan year and continuing until the contributions remaining in such employee's account equals the plan-year contributions in the HCE account(s) with the next highest dollar amount.

Note that the ACP test is deemed passed after these corrections even though running the test then would not produce a passing average ACP for the HCEs.

IV d.-if the answer to a. and b. is n/a (no), does the plan contain provisions that will ensure that the ACP test is always satisfied?

The plan need not contain methods for correcting a failure of the ACP test if it contains a fail-safe formula (e.g.-employee contributions are limited to 2% and 2% QNECs are given to all employees) or a procedure for prospectively reducing the employee contributions of HCEs so that no excess contributions arise.

V. DEFINITION OF HIGHLY COMPENSATED EMPLOYEE (HCE) COMPENSATION

V a.-does the plan define highly compensated employee in accordance with IRC section 414(q)?

Effective for plan years beginning after December 31, 1996, the term "highly compensated employee" (HCE) means any employee who:

1) was a 5 percent owner at any time during the year (determination year)or the preceding year (look-back year), or

2) for the preceding year (look-back year) had compensation from the employer in excess of $80,000 (as adjusted pursuant to IRC section 415(d)) and, if the employer so elects by plan amendment, was in the top-paid group for the preceding year (look-back year).

V b. (i)-for the purpose of defining HCE, does the plan define determination year, look-back year, compensation, and, if applicable, top-paid group?

Determination year-the plan year for which the determination of who is highly compensated is being made.

Look-back year-the 12 month period immediately preceding the determination year or, if the employer so elects in the plan, the calendar year beginning with or within such 12 month period.

Compensation-compensation within the meaning of IRC section 415(c)(3). In general, this is the compensation of the participant from the employer for the plan year.

Top-paid group-if the employer has made a top-paid group election, the top-paid group consists of the top 20% of employees ranked on the basis of compensation received during the look-back year.

V b. (ii)-for the purpose of defining HCE, does the plan apply the aggregation rules of section 414?

Employers aggregated under IRC sections 414(b) (employees of controlled group of corporations), 414(c) (employees of partnerships, proprietorships, etc., which are under common control), 414(m) (employees of an affiliated service group), or 414(o) (regulations as necessary to prevent avoidance of aggregation through separate organizations, employee leasing, or other arrangements.

V c.-does the plan define compensation and specify the period used to determine an employee's compensation for purposes of the ACP test?

IRC section 414(s) sets forth the definition of compensation that must be used for the ACP test.

The following definitions of compensation automatically satisfy section 414(s):

1) Compensation within the meaning of IRC section 415(c)(3). This is generally compensation of the participant from the employer for the year.
2) Wages as defined in IRC section 3401(a). This is generally all remuneration for services performed by an employee for his employer, including the cash value of all remuneration (including benefits) paid in any medium other than cash. This also includes information at source (income for which form 1099 is required), receipts for which FICA or Federal Income Tax withholding are required, and tips.
3) A safe-harbor definition that starts with 1. or 2., but excludes: reimbursements or other expense allowances, fringe benefits, moving expenses, deferred compensation, and welfare benefits.
4) Other definitions of compensation if they are reasonable, not designed to favor HCEs, and if the facts and circumstances show that the average percentage of total compensation included for highly compensated employees as a group does not exceed the average percentage for NHCEs by more than a de minimis amount.

The period used to determine an employee's compensation must be the plan year, the calendar year ending in the plan year, or the portion of either during which the employee was eligible under the plan.

VI. MULTIPLE USE (REPEALED BY EGTRRA FOR PLAN YEARS BEGINNING IN 2002)

VI a.-does the plan include a CODA? (if yes, go to VI c.; if no, go to VI b.)

If the plan includes both a CODA subject to IRC section 401(k) and contributions subject to IRC section 401(m), the plan should provide the test for multiple use of the alternative limitation. For this purpose, the plan may incorporate by reference the provisions of Treas. Reg. section 1.401(m)-2(b).

The method of correction to be used if the limitation is exceeded must be designated.

VI b.-is any HCE eligible under the plan also eligible or potentially eligible under another CODA of the employer? (if yes, go to VI c.; if no, the remainder of worksheet #11 does not apply)

Such plan should provide that it will comply with the limitation on multiple use of the alternative limitation described in section 1.401(m)-2 of the Regulations and designate the method of correction of multiple use.

Alternatively information establishing that these requirements are satisfied in another plan of the employer, or that no HCE is eligible or potentially eligible in a CODA and in a plan maintained by the same employer subject to the requirements of IRC section 401(m) may be submitted.

VI c.-does the plan contain or incorporate by reference the test for determining whether there is multiple use of the alternative limitation?

The plan should either provide the test for multiple use of the alternative limitation, or incorporate this by reference to the provisions of section 1.401(m)-2(b) of the Regulations.

The limit is the greater of the following:

1) the sum of a) 1.25 times the greater of (i) the ADP for eligible NHCEs under the CODA for the prior plan year or (ii) the ACP for eligible NHCEs for the 401(m) plan for the plan year beginning with or within the prior plan year of the CODA, and b) two plus the lesser of (i) or (ii), above, but in no event more than twice the lesser of (i) or (ii), above; or
2) the sum of a) 1.25 times the lesser of (i) the ADP for eligible NHCEs under the CODA for the prior plan year or (ii) the ACP for eligible NHCEs for the 401(m) plan year beginning with or within the prior plan year of the CODA, and b) two plus the greater of (i) or (ii), above, but in no event more than twice the greater of (i) or (ii), above.

VI d.-does the plan provide that multiple use will be corrected and designate the manner of correction?

The plan should designate the method of correction of multiple use, whether:

(1) through reduction of the actual deferral percentage or the actual contribution percentage, and

(2) whether with respect to all HCEs or only those eligible under both the arrangement subject to IRC section 401(k) and the plan subject to IRC section 401(m).

VII. SAFE HARBOR CODA PROVISIONS

VII a.-does the plan provide for:

(i) a basic matching formula, and no other matching contributions, or

(ii) an enhanced matching formula and no other matching contributions, or

(iii) a safe harbor nonelective contribution formula and a contribution formula that satisfies (i) or (ii)?

The plan should provide the matching formula or nonelective contribution formula it is using to automatically satisfy IRC section 401(k)

VII b.-with respect to matching contributions, does the plan:

(i) meet the vesting requirements of IRC section 411 with respect to matching contributions that are not needed to satisfy the ADP test safe harbor?

(ii) provide that (1) matching contributions are not made with respect to after-tax employee contributions or elective contributions that in the aggregate exceed 6% of the employee's compensation, (2) the rate of matching contributions does not increase as the rate of employee contributions or elective contributions increases, (3) at any rate of employee contributions or elective contributions, the rate of matching contributions that would apply with respect to any HCE who is an eligible employee is no greater than the rate of matching contributions that would apply with respect to an NHCE who is an eligible employee and who has the same rate of employee contributions or elective contributions are limited to those permissible as described in Explanation #12, Section X, Line b? If not, the regular ACP test applies to these matching contributions.

(i) the plan should specify the applicable vesting schedule for matching contributions, if not immediately nonforfeitable.

(ii) as noted, pursuant to Notice 98-52, 1998-46 I.R.B. 16.

VII c.-if the plan provides for discretionary matching contributions, does the plan provide that such discretionary matching contributions may not, on behalf of any employee, in the aggregate exceed an amount equal to 4% of the employee's compensation (for plan years beginning on or after January 1, 2000?) If the answer to this is no, the plan fails to satisfy the ACP test safe harbor for a plan year, and the regular ACP test applies.

As stated.

VII d.-does the plan (i) permit after-tax employee contributions or (ii) permit matching contributions that fail to satisfy the ACP test safe harbor? If so, the plan must apply the regular ACP test to these employee contributions and matching contributions, taking into account the special rules for the ACP test described under Explanation #11, Part VII, Line d.

As stated.

VII e.-if the plan satisfies the ACP test safe harbor but permits one or more HCEs to make after-tax employee contributions and one or more of these HCEs are covered by a CODA of the employer that must perform the regular ADP test, does the plan meet the restrictions on multiple use under Treas. Reg. section 1.401(m)-2?

Such plan should provide for the restrictions on multiple use, as noted in section VI.

VII f.-are matching contributions taken into account for a plan year under the ACP test safe harbor in accordance with the allocation and timing rules of Treas. Reg. section 1.401(m)-1(b)(4)(ii)(A)?

Allocation and timing rules are as previously noted at II b. (ii).

VII g.-if the plan provides for a period of suspension when an employee makes a withdrawal of after-tax employee contributions, does the period of suspension of employee contributions last no longer than 12 months?

As stated.

VII h. (i)-are other requirements applicable to both the ADP and ACP test safe harbors met, including the aggregation and disaggregation rules, as described in Explanation 12?

Such safe harbor plan should provide for the aggregation and disaggregation rules described under IX.B of Notice 98-52.

SECTION 401(K) REQUIREMENTS-WORKSHEET 12 (OVERVIEW)

The purpose of this chapter is to provide a synopsis of the points noted at Alert Guidelines Worksheet Number 12 (Form 9002). For a detailed review of the items noted on that form, see Explanation Number 12, Section 401(k) Requirements (Document 7335).

I. APPLICABILITY

I.a.-does the plan have a cash or deferred arrangement (CODA)?

A CODA is an arrangement under which an employee may elect to have the employer either contribute an amount to an employee's account in a plan's trust, or pay the amount to the employee.

Internal Revenue Code (IRC) section 401(k) contributions are tax deferred 401(k) elections are made with respect to future amounts payable to the employee.

The two most common forms of CODAs are salary reduction arrangements and bonus arrangements. In a salary reduction arrangement the participant has a portion of their salary contributed to the plan rather than paid him or her in cash. In a bonus arrangement the participant has all or part of any bonus paid into the plan.

I.b.-is this plan a profit-sharing plan, a stock bonus plan, a pre-ERISA money purchase plan or a rural co-operative plan?

The only types of plans allowed to have CODAs are profit-sharing plans, stock bonus plans, rural cooperative plans, and money purchase plans that had a CODA feature in place on June 27, 1974.

A CODA of a state or local government is not a qualified CODA if such CODA was adopted after May 6, 1986.

A CODA adopted by a tax-exempt organization between July 2, 1986 and December 31, 1996 is not a qualified CODA.

II. CONTRIBUTIONS

II.a.-does the plan provide each participant with an option to elect to have a contribution made to the plan on his/her behalf instead of receiving cash and is such election made before the time at which the employee may receive the amount?

Elective contributions (401(k) deferrals) are contributions an employer makes to a plan pursuant to employees' elections to make such contributions, instead of paying them cash.

An election by the participant to defer compensation under a CODA must be in effect before such a deferral may be made.

II.b.-does the plan separately account for elective contributions?

A plan should provide for a separate accounting for the portion of each employee's benefit under the plan that is attributable to elective contributions (and any other amounts treated as elective contributions).

A CODA not providing such separate accounting is not a qualified CODA, unless all amounts held under the plan are nonforfeitable and subject to the same distribution limitations that apply to elective contributions.

II.c.-does the plan provide that elective contributions will not exceed the limit imposed by IRC section 402(g) under all the plans of the employer?

IRC section 401(a)(30) requires a plan that has elective contributions provide that such contributions for a participant's taxable year not exceed the limit imposed by IRC section 402(g).

The IRC section 402(g) limit applies to the total of such contributions made under the plan and all other plans, contracts and arrangements of the employer.

The limit is $10,500 for 2000 and 2001, and $11,000 for 2002.

III. COVERAGE AND PARTICIPATION

III.a.-do the employees eligible to benefit under the CODA satisfy the applicable coverage provisions of IRC section 410(b)?

Employees eligible under a CODA must satisfy either the percentage test of IRC section 410(b)(1)(A), the ratio test of IRC section 410(b)(1)(B), or the average benefits test of IRC section 410(b)(1)(C).

For this purpose, all employees eligible under the CODA are treated as benefiting under the CODA.

III.b.-does the plan allow employees to make elective contributions after no more than one year of service?

No service requirement greater than one year (or age requirement greater than age 21) may be imposed for participation in the CODA.

IV. VESTING

IV.a.-are elective contributions nonforfeitable when made, regardless of a participant's age or service?

The plan is to provide that each participant's right to the amount attributable to elective contributions is nonforfeitable, regardless of the participant's age or service.

V. DISCRIMINATION (V.A.(I) OR V.A.(II) OR V.A.(III) OR V.A.(IV) MUST APPLY)

V.a.(i)-does the plan include the actual deferral percentage (ADP) test set forth in IRC section 401(k)(3) and provide that it will meet the test?

A plan having a CODA must provide that it will meet the nondiscrimination (ADP) test set forth in IRC section 401(k)(3)(A).

The ADP test compares the average of the actual amounts deferred for the **current** plan year (as a percentage of compensation) by the eligible HCEs to the average of the actual amounts deferred (also as a percentage of compensation) by the eligible NHCEs for the **prior** plan year (prior year testing method).

Under this test, the ADP for the group of eligible HCEs for the current plan year may not exceed the **greater** of (a) 125% of the ADP of the eligible

NHCEs for the prior plan year, or (b) the lesser of: (i) two times the ADP of the eligible NHCEs for the prior plan year, or (ii) two plus the ADP of the eligible NHCEs for the prior plan year.

V.a.(ii)-does the plan incorporate the ADP test by reference, including whether it is using the prior or current year testing method, and provide that it will meet the test?

The ADP test provisions of IRC section 401(k)(3), Treas. Reg. section 1.401(k)-1(b) and Notices 97-2 and 98-1 may be incorporated by reference. If this is done, the testing method (current year or prior year) must be specified in the plan. If using prior year, it must be specified whether first year NHCE ADP is 3% or actual ADP.

The current year testing method is as noted at the explanation to V. a. (i) above, except that current plan year NHCE data is used.

V.a.(iii)-does the plan contain SIMPLE provisions? (if the plan contains SIMPLE provisions, do not complete V.b., VI., VII.d.-g. and VIII.)

SIMPLE provisions are as described in IRC sections 401(k)(11) and 401(m)(10). SIMPLE provisions are discussed in Part IX.

V.a.(iv)-does the plan contain safe harbor CODA provisions? (if the plan contains safe harbor CODA provisions, do not complete V.b.(i), VII.d.-g. and IX.)

Safe Harbor CODA provisions are as described in IRC sections 401(k)(12) and 401(m)(11). Safe Harbor CODA provisions are discussed in Part X.

V.b.(i)-if the terms of the plan set forth the ADP test rather than incorporate it by reference, does the plan take into account the actual deferral ratios of all eligible employees?

The plan should provide that the actual deferral ratios of **all** eligible employees will be taken into account for the purpose of the ADP test of IRC section 401(k).

An eligible employee is any employee who is directly or indirectly eligible to make a cash or deferred election under the plan for any portion of a plan year. An eligible employee includes: an employee who would be a plan participant but for the failure to make required contributions; an employee whose eligibility to make elective contributions has been suspended because of an election (other than certain one-time elections) not to participate, a distribution, or a loan; and an employee who cannot defer because of the IRC section 415 limits on annual additions.

Some plans have tried to base the ADP test only upon participants, rather than eligible employees. They then define "participant" as any employee who chooses to make an elective deferral. This definition inflates the deferral percentage by ignoring all the employees who should be counted in the ADP test as having deferral ratios of zero percent. This is **not** a permissible definition of participant for the purpose of calculation the actual deferral percentage.

For plan years beginning after December 31, 1998, if an employer elects to apply section 410(b)(4)(B) (relating to exclusion of employees not meeting the statutory minimum age and service requirements), in determining whether a CODA meets section 410(b)(1) the plan may provide that, in determining whether the CODA meets the ADP test, all eligible employees (other than HCEs) who have not meet the minimum age and service requirements of section 410(a)(1)(A) (age 21 or 1 year of service) are excluded.

V.b.(ii)-if the terms of the plan set forth the ADP test rather than incorporate it by reference, does the plan take elective contributions into account for a plan year only if attributable to compensation that would be received by the employee during the plan year or earned during the plan year and received within 2½ months after the end of the plan year?

In running the ADP test for a plan year, an elective contribution is to be taken into account only if it relates to compensation that either (a) would have been received by the employee in the plan year but for the deferral election, or (b) is attributable to services performed by the employee in the plan year and would have been received by the employee within 2½ months after the close of the plan year but for the deferral election.

V.b.(iii)-if the terms of the plan set forth the ADP test rather than incorporate it by reference, does the plan take a contribution into account for a plan year only if it is allocated to the participant's account on a day within the plan year?

An elective contribution is taken into account under the ADP test for a plan year only if it is allocated to the employee as of a date within the plan year.

An elective contribution is considered allocated as of a date within the plan year if the allocation is not contingent on the performance of services after that date and the contribution is actually paid to the trust by the last day of the 12th month after the end of the plan year.

Note that Department of Labor Regulations at 29 CFR 2510.3-102 require that money withheld from an employee's paycheck be deposited into the

plan as of the earliest date such money can be separated from the employer's general assets, but not later than the 15th business day after the month the money was withheld.

V.b.(iv)-if the terms of the plan set forth the ADP test rather than incorporate it by reference, does the plan treat contributions made under plans that are aggregated for purposes of IRC sections 401(a)(4) or 410(b) as made under a single plan?

When two or more plans are treated as a single plan for purposes of IRC sections 401(a)(4) (nondiscrimination) and 410(b) (coverage and participation-other than the average benefits test), all CODAs included in such plans are treated as a single CODA for purposes of the ADP test, as well as for the purposes of IRC sections 401(a)(4) and 410(b).

V.b.(v)-if the terms of the plan set forth the ADP test rather than incorporate it by reference, does the plan aggregate all arrangements under which an HCE is eligible to make elective contributions for purposes of the HCE's actual deferral ratio?

When an HCE is eligible under more than one CODA of the same employer, that HCE's actual deferral ratio is calculated by treating all the CODAs as one CODA. In this situation, the HCE's actual deferral ratio will be the same under all CODAs in which he or she is eligible to participate. This rule does not apply to NHCEs.

This rule does not apply to NHCEs.

V.b.(vi)-if the terms of the plan set forth the ADP test rather than incorporate it by reference, does the plan determine the ADPs of the HCEs and of all other eligible employees using the relevant plan year?

If the plan is using the prior year testing method, the ADP of HCEs is determined for the current plan year and the ADP of NHCEs is determined for the prior plan year. Whether an eligible employee is in the highly compensated or non-highly compensated group, or both, it based on his or her status in the current and prior plan years.

If the plan is using the current year testing method, the ADPs of both HCEs and NHCEs are determined for the current year.

V.c.-are elective contributions available to eligible employees on a nondiscriminatory basis?

Any limitation on the percentage of compensation (such as the definition of compensation subject to a deferral election) that may be deferred which favors highly compensated employees will cause both the CODA and the plan to fail to be qualified.

A CODA may not be integrated with Social Security.

A CODA will not be qualified if any other benefit is directly or indirectly conditioned on whether or not the employee chooses to defer.

VI. QUALIFIED NONELECTIVE CONTRIBUTIONS (QNECS) AND QUALIFIED MATCHING CONTRIBUTIONS (QMACS) (FOR A PLAN PROVIDING THAT QNECS OR QMACS ARE TO BE TREATED AS ELECTIVE CONTRIBUTIONS FOR ADP TEST PURPOSES)

VI.a.(i)-if the plan provides for QNECs or QMACs, are these contributions immediately vested, without regard to a participant's age and service?

QNECs and QMACs **must** be fully vested when made, regardless of a participant's age, service, or whether the contribution is actually taken into account for the ADP test.

VI.a.(ii)-if the plan provides for QNECs or QMACs, are these contributions distributed only under the distribution applicable for elective contributions?

Elective contributions, QNECs and QMACs are distributable only under the following circumstances

1) The earlier of the employee's retirement, death, disability or separation from service;
2) The termination of the plan without establishment or maintenance of another defined contribution plan (other than an ESOP, SEP or SIMPLE IRA);
3) In the case of a profit sharing, stock bonus or rural cooperative plan, the employee's attainment of age 59½ or the employee's hardship;
4) The sale or other disposition by a corporation to an unrelated corporation of substantially all of the assets used in a trade or business, but only with respect to employees who continue employment with the acquiring corporation and the acquiring corporation does not maintain the plan after disposition; and

5) The sale or other disposition by a corporation of its interest in a subsidiary to an unrelated entity, but only with respect to employees who continue employment with the subsidiary and the acquiring entity does not maintain the plan after disposition.

Paragraphs 2, 4 and 5 apply only if the distribution is in the form of a lump sum.

The plan may not allow distributions of contributions merely by reason of completion of a stated period of plan participation or the lapse of a fixed period of years.

For plan years beginning after 1988, amounts attributable to QNECs and QMACs may not be distributed on account of hardship, unless credited to the employee's account as of a date specified in the plan which may be no later than December 31, 1988, or, if later, the end of the last plan year ending before July 31, 1989.

Under the terms of the plan, QNECs and QMACs must be subject to these distribution limitations regardless of whether they are actually taken into account for the ADP test.

VI.b.-are QNECs and QMACs treated as elective contributions only if the conditions described in Treas. Reg. Section 1.401(k)-1(b)(5) are satisfied?

If the plan provides that QNECs and QMACs are considered for purposes of the ADP test, then the QNECs and QMACs that will be treated as elective contributions must be limited to only those contributions that are made with respect to those employees who are eligible employees under the CODA being tested.

The plan must either provide that such contributions are treated as elective contributions only if they meet the requirements enumerated under section 1.401(k)-1(b)(5) of the Regs., or incorporate these requirements by reference.

VII. DISTRIBUTIONS AND CORRECTIONS

VII.a.-does the plan allow distributions of elective contributions only if one of the following occurs:

(i) retirement, death, disability, or separation from service;

(ii) attainment of age 59½ (profit sharing, stock bonus, rural cooperative plans only)

(iii) participant hardship (profit sharing, stock bonus, rural cooperative plans only);

(iv) excess contributions (see VII.e. and f.) or participant allocation to the plan of excess deferrals (see VII.c.);

(v) termination of the plan without establishment or maintenance of another DC plan (other than an ESOP, SEP or SIMPLE IRA plan), or one of the events specified in IRC sections 401(k)(10)(A)(ii) and (iii), that is, the plan does not allow distributions of contributions merely by reason of completion of a stated period of plan participation or the lapse of a fixed period of years?

As noted at VI.a.(ii) above.

VII.b.-if the plan is a profit sharing, stock bonus, or rural cooperative plan which allows hardship distributions, are such distributions made only in accordance with objective standards, set forth in the plan, giving the criteria for determining whether:

(i) the participant has an immediate and heavy financial need, and

(ii) the distribution is needed to alleviate the hardship?

Profit sharing, stock bonus and after August 20, 1996, rural cooperative plans may make distributions of elective contributions on account of participant hardship. Such distributions must be in accordance with objective nondiscriminatory standards set forth in the plan. The plan must state criteria for determining whether: 1) the participant has an immediate and heavy financial need, and 2) the distribution is needed to satisfy the financial need.

Whether there is an immediate and heavy financial need is a question of facts and circumstances. However, a distribution made on account of **medical expenses** described in IRC section 213(d), the **purchase of a principal residence** of the employee, the **payment of college/graduate school tuition** (for the next 12 months) for the employee, spouse, children or other dependents, or the **need to prevent eviction or foreclosure of the employee's personal residence** is deemed to be on account of immediate and heavy financial need.

A distribution is not necessary to satisfy the need to the extent it exceeds the amount required or to the extent the need can be met from other resources reasonably available to the employee.

VII.c.-does the plan provide a mechanism by which the excess deferrals may be distributed to the participant?

Under IRC section 402(g)(1), a participant generally may not defer an amount greater than $7,000 (as adjusted for inflation-$10,500 for 2000 and 2001, $11,000 for 2002) in a taxable year, taking into account all of the plans in which the employee participates.

A plan must be written to preclude deferrals over the indexed amount. The plan may provide a mechanism by which a participant can ask that all or a portion of his or her excess deferrals, and the income allocable to that amount, will be returned to him or her no later than April 15 of the following year.

Such a mechanism, however, is not required as a condition of qualification.

A distinction should be made between an excess deferral, an amount in excess of an individual participant's $7,000 (section 402(g)(1)) elective deferral limit, and an excess contribution, a contribution on behalf of a highly compensated employee that is above the maximum deferral percentage allowed under the ADP test for a particular plan in a particular plan year.

VII.d.-if the plan is using the current year testing method, does it provide that, in the event it would otherwise fail the ADP test, the employer will or may make additional qualified nonelective contributions (QNECs) or additional qualified matching contributions (QMACs) in order to satisfy the test?

A plan may provide that the employer will make additional QNECs or QMACs in order to satisfy the ADP test. In this event, no further correction will be required.

The option of making additional QNECs or QMACs to pass the test is generally unavailable to plans using the prior year testing method.

VII.e.-does the plan provide a mechanism by which elective contributions by HCEs in excess of the amount allowed in the ADP test may be distributed or recharacterized or have an alternative method that ensures satisfaction of the ADP test?

If the deferral limits of the ADP test are exceeded and the employer is not making corrective contributions (QNECs or QMACs), then the plan must distribute or recharacterize the excess contributions, plus any income thereon (in the case of distributions) in order for the CODA to be qualified.

A plan may use a combination of additional QNECs or QMACs, distribution, and recharacterization, and may also permit or require a participant to designate which of the latter two methods will be used, and to what extent each of the latter two methods will be used, provided the method is described in the plan.

VII.f.(i)-if the plan provides that excess contributions will be distributed, is the amount of the excess contributions to be distributed to individual HCEs determined by using the "ratio leveling" method?

For plan years beginning after December 31, 1996, the determination of the amount of excess contributions attributable to each HCE and the identity of the HCEs who will have excess contributions distributed from their accounts is performed in two separate steps.

Ratio leveling method: Determine how much the actual deferral ratio (ADR) of the HCE with the highest ADR would have to be reduced to satisfy the ADP test or cause such ratio to equal the ADR of the HCE with the next highest ratio. Repeat this process until the ADP test would be satisfied. The amount of excess contributions is equal to the sum of these hypothetical reductions multiplied, in each case, by the highly compensated employee's compensation.

VII.f.(ii)-if the plan provides that excess contributions will be distributed, are distributions of excess contributions determined using the "dollar leveling" method?

Dollar leveling method: Excess contributions (calculated using the ratio leveling method) are distributed from the account(s) of the HCE with the highest dollar amount of contributions used in the ADP test for the plan year and continuing until the contributions remaining in such employee's account equals the plan-year contributions in the HCE's account(s) with the next highest dollar amount.

Note that the ADP test is deemed passed after these corrections even though running the test then would not produce a passing average ADP for the HCEs.

VII.f.(iii)-if the plan provides that excess contributions will be distributed, and the answer to VII.c. was "yes", does the plan reduce excess contributions to be distributed by excess deferrals previously distributed?

Any distribution of excess deferrals from the plan must be coordinated with the distribution or recharacterization of excess contributions.

If excess deferrals have previously been distributed for the employee's taxable year ending with or within the plan year, then the plan must offset such distribution from the amount of the employee's excess contributions to be distributed or recharacterized for than plan year.

The amount of excess deferrals that may be distributed by the plan for a taxable year of the employee must be reduced by the amount of excess contributions previously distributed or recharacterized for the plan year beginning with or within that taxable year.

VII.f.(iv)-if the plan provides that excess contributions will be distributed, does the plan properly determine income to be distributed?

The plan should provide that distribution of excess contributions will include the income allocable thereto. The income allocable to excess contributions includes income for the plan year for which the excess contributions were made. The plan may also provide that it includes income for the period between the end of the plan year and the date of distribution.

VII.f.(v)-if the plan provides that excess contributions will be distributed, will the distribution be made no later than the end of the following plan year?

Failure to correct excess contributions by the close of the plan year following the plan year for which they were made will cause the CODA to fail to satisfy the requirements of IRC section 401(k)(3) for the plan year for which the excess contributions were made and for all subsequent years they remain in the trust.

Also, the employer will be liable for a 10% excise tax on the amount of excess contributions unless they are corrected within 2½ months after the close of the plan year for which they were made.

VII.g.(i)-if the plan provides for recharacterization, does the plan permit employee contributions in addition to those resulting from recharacterization?

The amount recharacterized, when added to the other employee contributions for the HCEs, may not exceed the limits under the plan relating to employee contributions.

VII.g.(ii)-if the plan provides for recharacterization, is the amount to be recharacterized determined by using the "ratio leveling" method?

Ratio leveling method: Determine how much the actual deferral ratio (ADR) of the HCE with the highest ADR would have to be reduced to satisfy the ADP test or cause such ratio to equal the ADR of the HCE with the next highest ratio. Repeat this process until the ADP test would be satisfied. The amount of excess contributions is equal to the sum of these hypothetical reductions multiplied, in each case, by the highly compensated employee's compensation.

The amount to be recharacterized is offset by any amounts previously distributed as excess deferrals.

VII.g.(iii)-if the plan provides for recharacterization, are recharacterizations of excess contributions determined using the "dollar leveling" method?

Dollar leveling method: Excess contributions are recharacterized from the account(s) of the HCE with the highest dollar amount of contributions used in the ADP test for the plan year and continuing until the contributions remaining in such employee's account equals the plan-year contributions in the HCE's account(s) with the next highest dollar amount.

Note that the ADP test is deemed passed after these corrections even though running the test then would not produce a passing average ADP for the HCEs.

VII.g.(iv)-if the plan provides for recharacterization, and the answer to VII.c. was "yes", does the plan reduce excess contributions to be recharacterized by excess deferrals previously distributed?

As per VII.f.(iii) above.

VII.g.(v)-if the plan provides for recharacterization, will the recharacterization occur within 2½ months of the end of the plan year?

Recharacterization must take place within 2½ months of the end of the plan year to which the recharacterization relates.

Recharacterization will be deemed to occur on the date on which the last affected HCE is notified of the recharacterization and the tax consequences of such recharacterization.

VIIg.(vi)-if the plan provides for recharacterization, will recharacterized amounts remain subject to the distribution restrictions applicable to elective contributions?

Recharacterized excess contributions are nonforfeitable and subject to the distribution limitations of elective contributions.

VIII. DEFINITION OF HIGHLY COMPENSATED EMPLOYEE (HCE)/ COMPENSATION

VIII.a.-does the plan define highly compensated employee in accordance with IRC section 414(q)?

Effective for plan years beginning after December 31, 1996, the term "highly compensated employee" (HCE) means any employee who:

1) was a 5 percent owner at any time during the year (determination year) or the preceding year (look-back year), or
2) for the preceding year (look-back year) had compensation from the employer in excess of $80,000 (as adjusted pursuant to IRC section 415(d)) and, if the employer so elects, was in the top-paid group for the preceding year (look-back year).

VIII.b.(i)-for the purpose of defining HCE, does the plan define determination year, look-back year, compensation, and, if applicable, top-paid group?

Determination year - the plan year for which the determination of who is highly compensated is being made.

Look-back year - the 12 month period immediately preceding the determination year or, if the employer so elects in the plan, the calendar year beginning with or within such 12 month period.

Compensation - compensation within the meaning of IRC section 415(c)(3). In general, this is the compensation of the participant from the employer for the plan year.

Top-paid group - if the employer has made a top-paid group election, the top-paid group consists of the top 20% of employees ranked on the basis of compensation received during the look-back year.

VIII.b.(ii)-for the purpose of defining HCE, does the plan apply the aggregation rules of section 414?

The plan must take into account employees of all employers aggregated under Code sections 414(b) (employees of controlled group of corporations), 414(c) (employees of partnerships, proprietorships, etc., which are under common control), 414(m) (employees of an affiliated service group), and 414(o) (regulations as necessary to prevent avoidance of aggregation through separate organizations, employee leasing, or other arrangements).

VIII.c.-does the plan define compensation in accordance with 414(s) and specify the period used to determine an employee's compensation for purposes of the ADP test?

IRC section 414(s) sets forth the definition of compensation that must be used for the ADP test. Even if the plan incorporates the ADP test by reference the plan must still include this definition.

The following definitions of compensation automatically satisfy section 414(s):

1) Compensation within the meaning of IRC section 415(c)(3). This is generally compensation of the participant from the employer for the year.
2) Wages as defined in IRC section 3401(a) plus all other compensation required to be reported by the employer under sections 6041, 6051, and 6052, or wages as defined in 3401(a). This is generally all remuneration for services performed by an employee for his employer, including the cash value of all remuneration (including benefits) paid in any medium other than cash. This also includes information at source (income for which form 1099 is required), receipts for which FICA or Federal Income Tax withholding are required, and tips.
3) A safe-harbor definition that starts with 1. or 2., but excludes all of the following: reimbursements or other expense allowances, fringe benefits, moving expenses, deferred compensation, and welfare benefits.

4) Other definitions of compensation if they are reasonable, not designed to favor HCEs, and if the facts and circumstances show that the average percentage of total compensation included for HCEs as a group does not exceed the average percentage for NHCEs by more than a de minimis amount. NOTE: This definition may require a Demonstration 9 to verify that it is not discriminatory.

The period used to determine an employee's compensation must be the plan year, the calendar year ending in the plan year, or the portion of either during which the employee was eligible under the plan.

IX. SIMPLE PLAN PROVISIONS (IF THE PLAN HAS SIMPLE PROVISIONS)

IX.a.-does the plan prohibit eligible employees from participating in another plan of the employer?

A SIMPLE plan must provide that no contributions can be made, or benefits accrued for services during the year, on behalf of any eligible employee under any other plan, contract, pension, or trust described in IRC section 219(g)(5)(A) or (B) maintained by the employer.

IX.b.-is the plan year the calendar year?

The plan year of a SIMPLE 401(k) plan must be the calendar year.

IX.c.-does the plan define compensation properly?

For purposes of applying the 401(k) SIMPLE provisions, compensation means the sum of wages, tips, and other compensation from the employer subject to federal income tax withholding and as limited by the Code section 401(a)(17) amount.

IX.d.-with respect to contributions under the plan:

(i) are elective contributions limited to $6,000, as adjusted?

(ii) is the employer required to either match employees' elective contributions (limited to 3% of compensation) or contribute 2% of compensation to all eligible employees?

(iii) are no other contributions permitted under the plan?

(iv) are all contributions under the plan nonforfeitable when

(v) made?

Each eligible employee must be allowed to have up to $6,000 (as adjusted for inflation) of compensation contributed to the plan for a calendar year.

Each year, the employer must contribute a matching contribution to the plan for each employee who made elective contributions. The amount of matching contributions that must be made for each employee is equal to the employee's elective contributions for the calendar year; but the matching contributions cannot exceed 3 percent of the employee's compensation.

For any year, instead of a matching contribution, the employer may elect to contribute a nonelective contribution equal to 2 percent of compensation for the entire calendar year for each eligible employee who had compensation of at least $5,000(a lesser amount may be used, but such lesser amount must be specified in the plan and communicated to employees).

Only the contributions specified in the two preceding paragraphs may be made to the plan, together with rollover contributions described in Treas. Reg. section 1.402(c)-2, Q&A-1(a).

All benefits attributable to contributions made under the plan are nonforfeitable at all times.

IX.e.-are employees allowed to make, amend or terminate deferral elections at the proper times?

During the 60-day period immediately preceding each January 1, and during any additional periods specified in the plan, each eligible employee must be permitted to make or modify an election to defer compensation. Employee elections must be given effect as soon as practical after the employee becomes eligible.

Each employee may terminate an election to defer compensation at any time during the year.

IX.f.-is the employer required to give proper notice of the plan to employees?

The employer must notify each eligible employee prior to the 60-day election period.

The notification must indicate whether the employer will provide a 3-percent matching contribution or a 2-percent nonelective contribution.

X. SAFE HARBOR CODA PROVISIONS (IF THE PLAN HAS SAFE HARBOR CODA PROVISIONS)

X.a.-does the plan provide for one of the following:

(i) a safe harbor basic matching formula, or

(ii) an safe harbor enhanced matching formula, or

(iii) safe harbor nonelective contributions, or

(iv) an amendment that changes from the current year ADP (and, if applicable, ACP) testing method to a safe harbor nonelective contribution method for the plan year, or

(v) an amendment that changes from a safe harbor matching contribution method to the current year ADP (and, if applicable, ACP) testing method during the plan year?

(i) The safe harbor basic matching formula:

The plan must provide for a plan year that a safe harbor matching contribution is required to be made on behalf of each eligible employee who is a NHCE equal to: (1) 100% of the amount of the employee's elective contributions that do not exceed 3% of the employee's compensation for the plan year, plus (2) 50% of the amount of the employee's elective contributions that exceed 3% of the employee's compensation but that do not exceed 5% of the employee's compensation.

(ii) The safe harbor enhanced matching formula:

The plan must provide that an enhanced matching contribution is required to be made to the plan on behalf of each eligible NHCE under a formula that, at any rate of elective contributions, provides an aggregate amount of matching contributions at least equal to the aggregate amount of matching contributions that would have been provided under the basic matching formula. The rate of matching contributions may not increase as an employee's rate of elective contributions increases.

(iii) The safe harbor nonelective contribution:

The plan must provide for a plan year that a safe harbor nonelective contribution is required to be made to the plan on behalf of each eligible NHCE who is an eligible employee equal to at least 3% of the employee's compensation.

(iv) Amendment from ADP

Amendment from ADP (and, if applicable, ACP) testing to safe harbor nonelective contribution ((iii) above). To be made not later than 30 days before the last day of the plan year.

(v) Amendment from safe harbor matching formula

Amendment from safe harbor matching formula to ADP (and, if applicable, ACP) testing. To be effective no earlier than the later of 30 days after eligible employees are given supplemental notice, or the date the amendment is adopted.

X.b.-if the plan contains a safe harbor matching contribution formula, does the plan contain only permissible restrictions on elective contributions by NHCEs?

The safe harbor matching contribution requirement (under X.a.) is not satisfied if elective contributions by NHCEs are restricted, except as follows:

(i) restrictions on the frequency and duration of election periods in which eligible employees may make or change cash or deferred elections under a plan are allowed, provided that after receipt of the required notice, an employee has a reasonable opportunity to make or change a cash or deferred election for the plan year.

(ii) restrictions on the amount of elective contributions are allowed, provided that each NHCE who is an eligible employee is permitted to make elective contributions in an amount that is at least sufficient to receive the maximum amount of matching contributions available under the plan for the plan year, and the employee is permitted to elect any lesser amount of elective contributions.

(iii) Restrictions on the types of compensation that may be deferred are allowed, provided that each NHCE who is an eligible employee is permitted to make elective contributions under a reasonable definition of compensation under Treas. Reg. section 1.414(s)-1(d)(2).

(iv) A plan does not fail to satisfy the ADP test safe harbor contribution requirement (or the ACP test safe harbor requirements) merely because employees are required to make CODA elections in whole percentages of compensation or whole dollar amounts.

X.c.-does the plan provide that safe harbor matching contributions or nonelective contributions are immediately nonforfeitable?

Safe harbor matching and nonelective contributions must be immediately nonforfeitable.

X.d.-does the plan contain the appropriate restrictions on distributions of safe harbor matching and nonelective contributions and earnings?

Safe harbor matching and nonelective contributions (and earnings thereon) must not be distributable earlier than separation from service, death, disability, upon termination of plan or disposition of assets or subsidiary, or, in the case of a profit-sharing or stock bonus plan, age 59½.

Hardship is not a distributable event for safe harbor matching and nonelective contributions.

X.e.-is the plan year 12 months long, or a permissible shorter length if it is a newly established plan, or, if applicable, does the plan meet the special requirements applicable to a CODA that is added to an existing profit-sharing, stock bonus or pre-ERISA money purchase pension plan for the first time during a plan year (and the similar rules for matching contributions added to a defined contribution plan for the first time, if applicable)?

The plan should provide that the plan year is 12 months long (unless it is the first plan year of a newly established plan).

If a CODA is added to an existing plan, the plan should be amended to provide that the CODA (and the addition of matching contributions, if applicable) is effective not later than 3 months prior to the end of the plan year.

X.f.-does the plan use the correct definition of compensation?

The plan should define compensation in accordance with Treas. Reg. section 1.401(k)-1(g)(2) (which incorporates by reference the definition of compensation in IRC section 414(s)).

Also, it should be provided that compensation in excess of a certain amount may not be excluded in this definition, except that the limit of IRC section 401(a)(17) applies.

X.g.-does the plan provide that safe harbor matching contributions must be made on behalf of all NHCEs who are eligible employees and who make elective contributions or that safe harbor nonelective contributions must be made on behalf of all NHCEs who are eligible employees?

An eligible employee is an employee eligible to make elective deferrals under the plan for any part of the plan year, or who would be eligible to make elective deferrals but for a suspension due to a hardship distribution described in the plan, or due to statutory limitations, such as the section 402(g) and 415 of the Code.

X.h.-does the plan provide that proper notice is given (satisfying content and timing requirements), including the additional plan provisions applicable to plans that change their testing methods during the plan year as described in X.a. (iv) and (v) above?

The plan should provide that the employer must distribute a notice to each eligible employee that comprehensively describes the types of safe harbor contributions made, the plan to which they are made, the type and amount of compensation that may be deferred, how to make elections and the period for making elections, and the withdrawal and vesting provisions.

The notice must be provided within a reasonable period before the beginning of the plan year (or, in the year an employee becomes eligible, within a reasonable period before the employee become eligible). The timing requirement is deemed to be satisfied if, at least 30 days (and no more than 90 days) before the beginning of each plan year, the notice is given to each eligible employee for the plan year.

If a plan changes from a current year ADP (and if applicable ACP) testing method to use the 401(k) safe harbor nonelective contribution method, the plan will only satisfy applicable requirements if the notice given to employees before the beginning of the plan year provides that the plan may be amended during the plan year to provide that the employer will make a safe harbor nonelective contribution of at least 3 percent to the plan for the plan year, and if the plan is so amended, a supplemental notice will be given and is given to all eligible employees no later than 30 days prior to the last day of the plan year, stating that this 3 percent contribution will be made for the plan year.

X.i.-if safe harbor contributions will be made to another defined contribution plan, (i) is the name of the other plan specified in this plan, (ii) does the other plan meet the same requirements in satisfying the safe harbor contribution requirements, and (iii) does the plan have the same plan year (for plan years beginning on or after January 1, 2000)?

The plan should specify the name of the other plan to which safe harbor contributions will be made.

The requirements applicable to the safe harbor contributions also apply to the other plan, and each employee eligible under the plan containing the CODA must be eligible under the same conditions under the other plan.

The plan must have the same plan year as the plan containing the CODA, except for plan years beginning before January 1, 2000.

X.j.-does the plan comply with all other applicable requirements of IRC section 401(k) and other sections of the Internal Revenue Code? (Complete other applicable portions of Worksheet #12 for the CODA requirements, and if section 401(m) applies, see Worksheet #11.

Benefits (other than matching contributions) must not be contingent on an election to defer.

Elective contributions must satisfy allocation and timing rules applicable to section 401(k) plans.

There must be nondiscriminatory availability of benefits, rights and features, pursuant to IRC section 401(a)(4).

Limitations on compensation, elective deferrals, and contributions (pursuant to IRC sections 401(a)(17), 401(a)(30) and 415, respectively) must be met.

Section 410(b) of the Code also applies to a CODA that is treated as satisfying the ADP test safe harbor.