

NEWS & Highlights

401(K) NONDISCRIMINATION TESTS— *JUST THE FACTS*

INTRODUCTION TO THE WORLD OF NONDISCRIMINATION TESTING

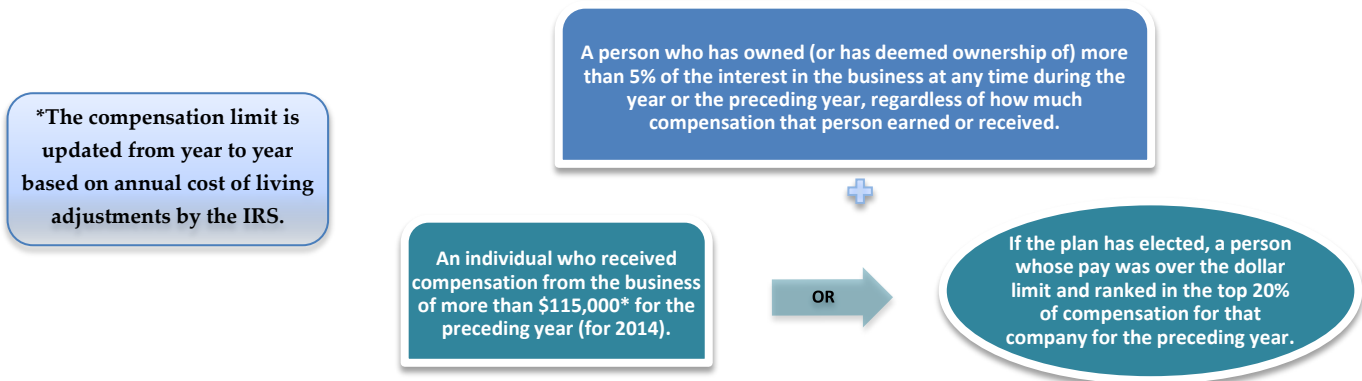
As third-party administrators, ensuring that our clients' retirement plans remain in compliance with ERISA (Employee Retirement Income Security Act) rules is crucial. INTAC's experienced pension consultants accomplish this by performing 401(k) plan nondiscrimination tests, along with providing the other annual administrative services. As a plan sponsor, it's important to understand what information goes into this type of testing, how it is evaluated and what happens if a plan fails.

The most common nondiscrimination tests include the following: classifying who are the NHCEs (non-highly compensated employees) and HCEs (highly compensated employees), 410(b) coverage, ADP (actual deferral percentage), ACP (actual contribution percentage) and Top Heavy determination. In this edition of *INTAC's News and Highlights*, we will cover the important FAQs about these tests and help you navigate through the process.

TEST COMPARISON

ERISA put several tests in place to protect employees' future retirement benefits. For some nondiscrimination tests in an employer sponsored qualified retirement plan, employees are divided into two groups: **non-highly (NHCEs)** and **highly compensated employees (HCEs)**. First, it's important to understand the criteria in determining NHCEs and HCEs, since this has a significant impact on nondiscrimination testing for a retirement plan.

In an employer-sponsored qualified retirement plan, a highly compensated employee (HCE) fits one or more of the following descriptions:



The **410(b) coverage test** ensures that the plan benefits a nondiscriminatory cross-section of employees and ensures that it does not favor HCEs. The test compares the percentage of eligible HCE to eligible NHCE participants benefiting from the plan. If a ratio amount of 70% or greater is determined, then the plan passes the coverage test. If the ratio falls below 70%, then a comparison of the average benefits of the two groups is calculated. A plan must satisfy one of these two tests.

If the plan fails the 410(b) coverage test, the plan sponsor must take corrective measures and bring the plan into compliance (to avoid penalties or even plan disqualification). This can be achieved by either extending coverage to more NHCEs or by modifying contribution applications or benefit accruals.

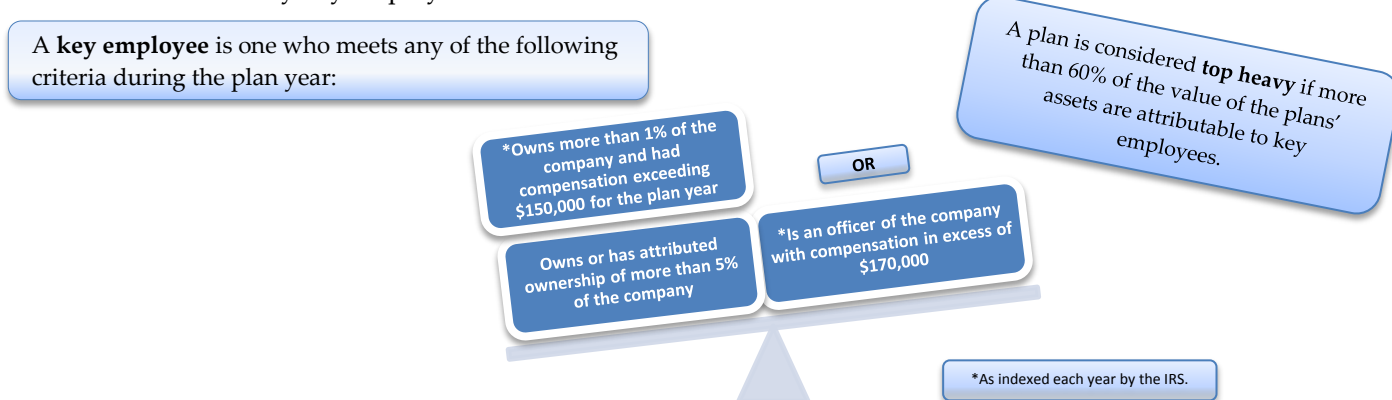
Once it is determined that a sufficient amount of NHCEs are indeed covered, the plan benefits and design are tested. **ADP (actual deferral percentage)** and **ACP (actual contribution percentage)** tests weigh and analyze the benefits and features of the plan.

The ADP test is designed to ensure that all participants, meaning both NHCEs and HCEs, are benefiting fairly from the plan. It compares the average salary deferral percentage for the highly compensated to the average salary deferral percentage for the non-highly compensated employees (pre-tax and Roth elective deferrals).

Charles Rosenberg, INTAC Vice President adds, "HCEs may not be able to defer as much as they would like to their 401(k) retirement plan during any given year due to inadequate NHCE participation. So it's a common incentive to provide minimum contributions to non-highly compensated employees - this ensures the plan passes testing as well."

The ACP test compares the average of the percentage of matching contributions and after-tax employee contributions for HCEs compared to NHCEs. It ensures that the plan design benefits all participants and does not only benefit the HCEs.

Since many plan sponsors base their contributions largely on the employees' salaries, those with larger compensations often receive greater benefits from their employer's retirement plan. Therefore the **top heavy** test ensures that the overall benefits accumulated by key employees do not exceed certain rules.



If the plan is found to be top-heavy, the plan sponsor may be required to make a minimum contribution (generally 3% of compensation) to non-key employees.

OTHER PLAN OPTIONS

Rosenberg adds, "There are other plan design options available that may be presented to the employer. A safe harbor 401(k) plan meets the IRS's requirements when a plan may have difficulty satisfying nondiscrimination testing. This type of plan eliminates various nondiscrimination tests allowing key employees to contribute and keep more money in the plan."

KEEPING A PLAN IN COMPLIANCE

As IRS rules and regulations often change year to year, it is important to communicate with your plan consultant and provide the necessary, complete census data and other required information in a timely manner. INTAC pension consultants are always available to help plan sponsors navigate through these complicated testing requirements smoothly and efficiently. They are well-versed in plan design and actively involved in the on-going administration of our retirement plans. INTAC integrates the most cutting edge plan design and administration strategies to help keep testing failure, top-heavy liabilities and plan audits at a record low. To learn more about Highly Compensated, Non-Highly Compensated and Key Employees, as well as a host of other important industry topics, check out our *Just the Facts* page at www.intacinc.com.

ABOUT INTAC

Intac Actuarial Services has been providing complete administration and consulting to employer sponsored retirement plans since 1977. INTAC's professional staff of experienced and innovative plan consultants and actuaries designs, creates and continually refines a wide range of qualified retirement plans. We are committed to meeting our clients' needs by providing these services in a timely, accurate and cost-effective manner. INTAC has been recognized by NJBIZ as one of the Best Places to Work in New Jersey in 2014, as well as New Jersey's Top Defined Contribution Provider for five consecutive years. For more information, visit www.intacinc.com.



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INTAC ACTUARIAL SERVICES, INC.

Design • Implementation • Administration • Consultation

545 Route 17 South • Ridgewood, NJ 07450 201.447.2525 • 800.221.3563