SECTION 401(a)(4)

Non-discrimination in Benefit amounts

401(a)(4) SUMMARY

1.401(a)(4)-1 Nondiscrimination requirements

1.401(a)(4)-2 Nondiscrimination - DC plans

1.401(a)(4)-3 Nondiscrimination - DB plans

1.401(a)(4)-4 Benefits, rights and features

1.401(a)(4)-5 Plan amendments, and pre-termination restrictions

1.401(a)(4)-6 Contributory DB plans

1.401(a)(4)-7 Imputing permitted disparity

1.401(a)(4)-8 Cross Testing

1.401(a)(4)-9 Plan aggregation, restructuring

1.401(a)(4)-10 Testing former employees

1.401(a)(4)-11 Additional rules

1.401(a)(4)-12 Definitions

1.401(a)(4)-13 Effective dates, Fresh start rule

§401(a)(4) NONDISCRIMINATION OVERVIEW

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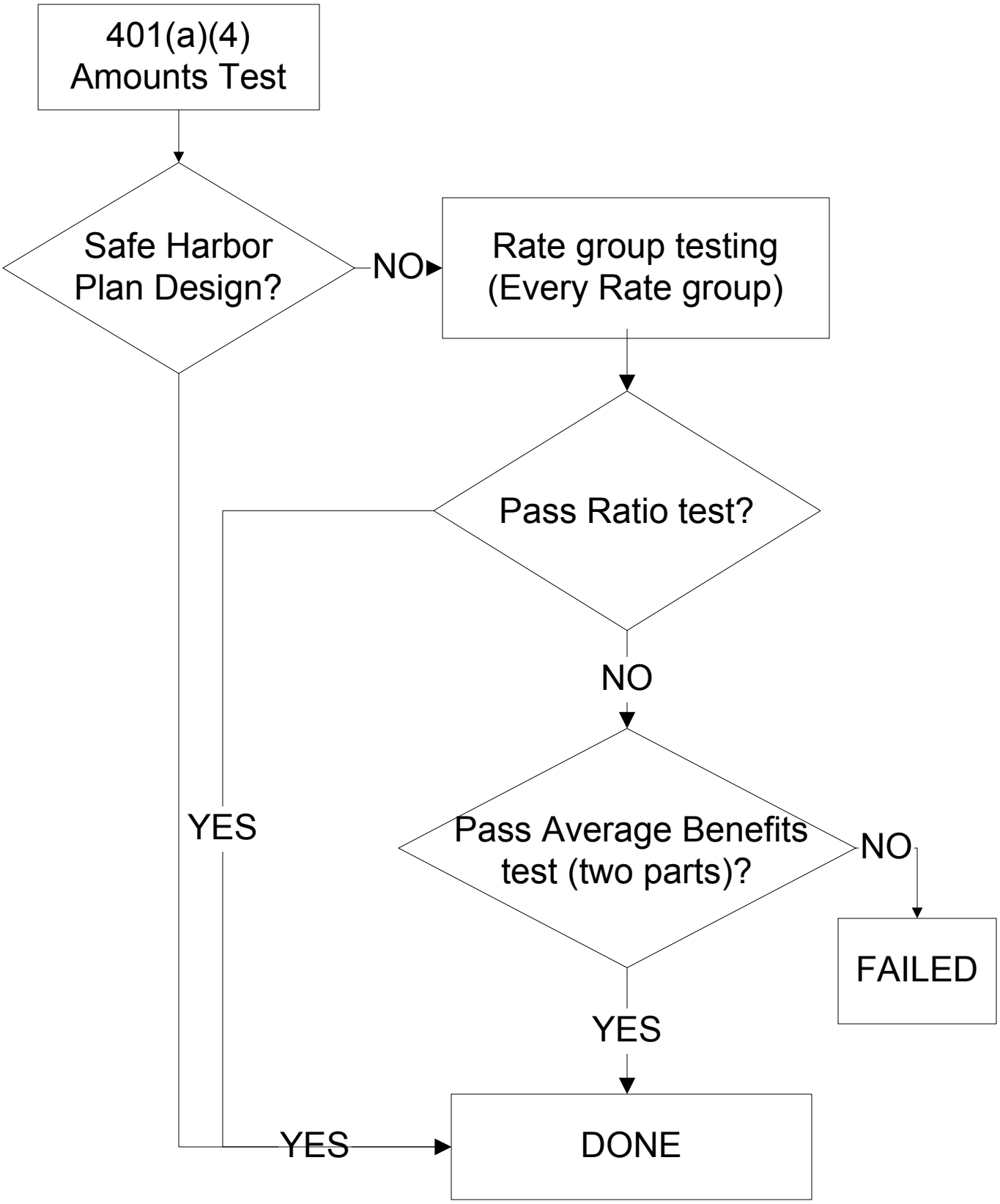
§401(a)(4) states that a qualified plan can't discriminate in favor of HCEs:

- **Plan coverage must be nondiscriminatory (410(b) testing)**
- **Plan benefits must be nondiscriminatory in amount (401(a)(4) testing)**
- **Coverage also includes benefits, rights, and features**
- **Timing of plan amendments must not discriminate in favor of HCEs**

NOTE: Text above from page 410(b)-3

401(a)(4) TESTING FLOWCHART



1.401(a)(4)-12 DEFINITIONS
TESTING AGE

- If uniform NRA definition for all employees in plan, then testing age = uniform NRA
- If uniform NRA for ees in various groups, then testing age = latest uniform NRA
- If no uniform NRA, then testing age = 65
- If current age > testing age for an employee, then testing age = current age

1.401(a)(4)-12 DEFINITIONS
UNIFORM NORMAL RETIREMENT AGE

- Single NRA definition, same for all ees in a group
- Can't exceed age 65 (in general)
- If all ees in group have same SSRA, and NRA = SSRA, then uniform NRA = SSRA

Allowable plan provisions

- Plan can define NRA as later of age 65 and anniversary of participation or service
- Plan can define NRA based on date, but uniform NRA can't be more than 6 months away from NR date

1.401(a)(4)-12 DEFINITIONS

Normalize
Convert benefit to actuarially equivalent straight life annuity at employee's testing age
Apply assumptions on a gender-neutral basis

Standard interest rate
7.5% to 8.5%

Standard mortality table
UP-1984, or
1983 GAM / IAM for M / F, or
1971 GAM / IAM for M / F
Applicable mortality under 417(e)(3)

1.401(a)(4)-3(d)(1)(i)
ACCRUAL RATE CALCULATION METHODS

Three different calculation methods

METHOD	Testing service
Annual	Current plan year
Accrued to date	Current + prior plan years
Projected	ALL plan years

Testing service definition:

- Benefit service under the plan
- Must include years employee is benefiting under plan, even if no benefit accrual (see page 410(b)-27)
- For annual method, always = 1.0

1.401(a)(4)-3(d)(1)(i) CALCULATION METHODS

Take increase in accrued benefit during the measurement period, divide by the testing service, and express as dollar amount, or percent of average annual compensation.

Normal Accrual Rate calculation methods

ANNUAL METHOD:

$$\frac{\text{Accd Ben}_1 - \text{Accd Ben}_0}{\text{Comp}_1}$$

ACCD TO DATE METHOD:

$$\frac{\text{Accrued Ben}_1}{\text{Comp}_1 * \text{Past Ben Service}_1}$$

PROJECTED METHOD:

$$\frac{\text{Projected Ben}_1}{\text{Comp}_1 * \text{All Ben Service}_1}$$

1.401(a)(4)-3(d)(2) RULES OF APPLICATION

1) Determine rates in consistent manner for all ees for plan year

2) If benefits not defined based on life annuity at testing age, they must be normalized

3) Projected benefits can NOT assume increases in compensation, or that ee will terminate prior to testing age

4) Section 415 limits are usually ignored

5) Future years
   a) Can not include future years if projected benefits for HCEs are relatively front loaded compared to non-HCEs
   b) Can NOT include years > testing age

1.401(a)(4)-3(d)(1)(ii)
MOST VALUABLE ACCRUAL RATE (MVAR)

Take increase in "most valuable optional form of payment of the accrued benefit" during the measurement period, divide by the testing service, and express as dollar amount, or percent of average annual compensation.

This requires a very complex calculation, as shown in the seminar handouts. You won't find details in the 1993 regulation! They are in the 1991 regulation at 1.401(a)(4)-5(d)(2)(iii)(F).

In regulation, "most valuable optional form of payment of the accrued benefit" == QJSA

1.401(a)(4)-3(e) "TESTING COMPENSATION"

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1) **General rule**
   Average of 414(s) comp over ANY averaging period in comp. history ➔ highest average

2) **Averaging period**
   a) **At least 3 consecutive 12 mo. periods**
   b) **Not greater than employment period**

3) **Compensation history**
   a) **May begin at any time**
   b) **Must be continuous**
   c) **Must be no shorter than averaging period**
   d) **Must end in current plan year**

Apply 401(a)(17) limit to each year's comp, produces higher benefit % for HCEs

NOTE: Same definition shown on page 401(l)-6

EXAMPLE - NAR + MVAR

Early retirement eligibility	55
Early retirement reduction	4% per year
Normal form of payment	10 year C & L
Optional form of payment	100% J & S
Optional form reduction	5%

Testing assumptions

Date	12/31/2016
Measurement period	Prior service
Interest	8% per year

12/31/16 Data for Smith

Age	50
Hire Date	12/31/2011
Compensation:	60,000
Accrued benefit:	3,000

EXAMPLE - NAR + MVAR

Selected annuity factors for testing

x	$\ddot{a}_{x}^{(12)}$	$\ddot{a}_{\overline{x:x}}^{(12)}$	$\ddot{a}_{\overline{x:\overline{10}\vert}}^{(12)}$
55	10.0	11.5	10.5
60	9.5	11.0	10.0
65	8.5	10.0	9.0

What are Smith's normal and most valuable accrual rates as of 12/31/2016?

Normal accrual rates

Smith's testing service = 5 years

Age	Accrued Benefit (1)	ERF (2)	10 C&C Benefit (3) = (1)(2)	10 C&C Annuity (4)	Life Annuity (5)	Normalized Benefit (6) = (3)(4)/(5)
65	3,000	1.00	3,000	9.00	8.50	3,176

Age	Svc (7)	Testing Comp (8)	NAR (9) = (6)/[(7)(8)]
65	5	60,000	1.06%

Most valuable accrual rates

Age	Accrued Benefit (1)	ERF (2)	J&S (3)	Early ret 100% J&S Benefit (4) = (1)(2)(3)	100% J&S Annuity (5)	Interest (6)	Normalized Benefit (7) (4)(5)(6)/$ä_{65}$
55	3,000	0.60	0.95	1,710	11.50	2.16	4,995
60	3,000	0.80	0.95	2,280	11.00	1.47	4,335
65	3,000	1.00	0.95	2,850	10.00	1.00	3,353

$ä_{65}$ is the life annuity at 65 = 8.5

Age	Svc (8)	Testing Comp (9)	MVAR (10) = (7)/[(8)(9)]
55	5	60,000	1.66%
60	5	60,000	1.45%
65	5	60,000	1.12%

Most valuable accrual rates

4% early retirement reductions
Interpolated annuity values from 55 to 65

Age	Accrued Benefit (1)	ERF (2)	J&S (3)	Early ret 100% J&S Benefit (4) = (1)(2)(3)	100% J&S Annuity (5)	Interest (6)	Normalized Benefit (7) (4)(5)(6)/$ä_{65}$
55	3,000	0.60	0.95	1,710	11.50	2.16	4,995
56	3,000	0.64	0.95	1,824	11.40	2.00	4,890
57	3,000	0.68	0.95	1,938	11.30	1.85	4,769
58	3,000	0.72	0.95	2,052	11.20	1.71	4,634
59	3,000	0.76	0.95	2,166	11.10	1.59	4,489
60	3,000	0.80	0.95	2,280	11.00	1.47	4,335
61	3,000	0.84	0.95	2,394	10.80	1.36	4,138
62	3,000	0.88	0.95	2,508	10.60	1.26	3,940
63	3,000	0.92	0.95	2,622	10.40	1.17	3,742
64	3,000	0.96	0.95	2,736	10.20	1.08	3,546
65	3,000	1.00	0.95	2,850	10.00	1.00	3,353

Normalized benefit decreases at each age

Most valuable accrual rates

6% early retirement reductions
Interpolated annuity values from 55 to 65

Age	Accrued Benefit (1)	ERF (2)	J&S (3)	Early ret 100% J&S Benefit (4) = (1)(2)(3)	100% J&S Annuity (5)	Interest (6)	Normalized Benefit (7) (4)(5)(6)/$ä_{65}$
55	3,000	0.40	0.95	1,140	11.50	2.16	3,330
56	3,000	0.46	0.95	1,311	11.40	2.00	3,515
57	3,000	0.52	0.95	1,482	11.30	1.85	3,647
58	3,000	0.58	0.95	1,653	11.20	1.71	3,733
59	3,000	0.64	0.95	1,824	11.10	1.59	3,780
60	3,000	0.70	0.95	1,995	11.00	1.47	3,793
61	3,000	0.76	0.95	2,166	10.80	1.36	3,744
62	3,000	0.82	0.95	2,337	10.60	1.26	3,671
63	3,000	0.88	0.95	2,508	10.40	1.17	3,579
64	3,000	0.94	0.95	2,679	10.20	1.08	3,472
65	3,000	1.00	0.95	2,850	10.00	1.00	3,353

Normalized benefit increases, then decreases

410(b) REVIEW

Which plans are included?

	410(b) Ratio test		410(b) ABPT	
	Permissive Aggregation 1.410(b)-7(d)	Mandatory Disaggreg. 1.410(b)-7(c)	Mandatory Aggregation 1.410(b)-7(e)	Mandatory Disaggreg. 1.410(b)-7(e)
Profit Sharing Plan				
401(k) Plan				
ESOP				
DB plan – for non-CBA				
DB plan – for CBA only				
Restriction re: different plan years?				

1.401(a)(4)-3(c)(1) TESTING - RATE GROUPS

Rate group:
Includes all employees with both MVAR and NAR ñ those rates for any HCE

Perform test for each rate group of population, similar to 410(b) ratio % test

May have separate rate group for each HCE, unless grouping options are used

1.401(a)(4)-3(d)(3) OPTIONAL RULES

1) Can impute permitted disparity

2) Grouping of rates
   a) HCE accrual rates in range must not be significantly higher than non-HCE rates
   b) Treat all ees with rate near midpoint of range as having rate = midpoint of range
   c) For NAR, range can use midpoint * 1.05 and midpoint * .95
   d) For MVAR, range can use midpoint * 1.15 and midpoint * .85
   e) If using rates as % of average annual comp, can use midpoint +- .05%, if that gives wider range (also for annual method using plan year compensation)

3) Fresh start alternative – complicated

4) MVAR floor

§401(a)(4)-2(c)(3) SATISFY 410(b) TEST

Ratio % test:

$$\frac{\dfrac{\text{Non HCEs in rate group}}{\text{Total Non-excludable non HCEs}}}{\dfrac{\text{HCEs in rate group}}{\text{Total Non-excludable HCEs}}}$$

If ratio ñ 70%, rate group passes §401(a)(4)

If ratio < 70%, rate group fails ratio test. Must pass both non-discriminatory classification reqt and the ABPT (next page)

1.401(a)(4)-2(c)(3)(ii)
Non-discriminatory classification requirement

Each rate group is deemed to have a reasonable classification of employees

Each rate group's ratio % must be ñ lesser of

- **Ratio % for the plan, or**
- **Midpoint between Safe harbor percentage and Unsafe harbor percentage for entire testing group**

NOTE: For rate groups that fail Ratio % test, must pass both the NDCR and the ABPT (next page).

1.401(a)(4)-2(c)(3)(iii)
Average Benefit Percentage test (ABPT)

Each rate group passes ABPT if entire testing group passed ABPT

Otherwise, each rate group fails the ABPT

NOTES:
For rate groups that fail Ratio % test, must pass both the NDCR (prior page) and the ABPT

For CBA plans which pass ABPT using 1.410(b)-5(f) (see page 410(b)-38), each rate group must separately satisfy 1.410(b)-5(f)

§401(a)(4) GENERAL TEST – SUMMARY

Define ANB as lesser of (A) and (B):

(A) The ratio percentage for the plan
(B) The midpoint between the safe and unsafe harbor percentages for the testing group

Calculated Ratio % for a single rate group	Testing group passed the ABPT?	
	YES ABPTñ70%	NO ABPT<70%
Ratio % ñ 70%	PASS	PASS
70% > Ratio % ñ ANB	PASS	FAIL
ANB > Ratio %	FAIL	FAIL

For plan to pass the general test, <u>every</u> rate group must pass

EXAMPLE - 401(a)(4) TEST

Data for all employees:

Rate Group	NHCEs	HCEs
1	100	50
2	150	50
3	100	50
4	150	50

	NHCEs	HCEs
Non-Excludable	1,200	300

What must the ABPT result be in order for the plan to pass both 410(b) and 401(a)(4)?

Satisfy 401(a)(4) without general test:

1) Uniformity requirements
2) Design based
3) Non-design based
4) Insurance contract plans

Pay related safe harbor plans must determine <u>plan benefits</u> as a percentage of Average Annual Compensation (1.401(a)(4)-3(e)(2))

1.401(a)(4)-3(b)(2) DB PLAN SAFE HARBORS

Uniformity requirements

- Same benefit formula for all ees, payable in same form at same uniform NRA
- Benefit must be same % of compensation (or same dollar amount) for ees with the same service at NRA. Benefit after NRA must be same % of compensation or dollar amount for any ee with same years of service at NRA.
- Each subsidized optional form must be available to substantially all ees
- No employee contributions
- Benefit must accrue over same years of service used in applying the benefit formula

Safe harbor for “unit credit plans”

- Plan must satisfy the 133 1/3% accrual rule under 411(b)(1)(B)
- Accrued benefit must be calculated using the plan’s benefit formula and the employee’s service and compensation determined for that plan year

Safe harbor for fractional rule plans - plan must satisfy (A), (B) and (C) below

(A) The plan must satisfy the fractional rule of 411(b)(1)(C).

(B) The employee's accrued benefit for any plan year before NRA must equal the product of the employee's "fractional rule benefit" (under 1.411(b)-1(b)(3)(ii)(A)) and the ratio:

$$\frac{\text{years of service}}{\text{total projected years of service}}$$

If the plan has an eligibility requirement and the benefit accrues over years of participation, the plan benefit can <u>not</u> satisfy this safe harbor.

Safe harbor for fractional rule plans
(C) Plan must satisfy one of three requirements

1. It must be impossible for an ee to accrue a benefit for a year of service that is more than 33 1/3% greater than that accrued in any year by any other ee. This is based on actual and potential ees, but none with > 33 years at NRA.

2. The benefit at NRA must be defined under the plan as a flat benefit that requires a minimum of 25 years of service at NRA to receive the unreduced flat benefit. The accrued benefit must be reduced on a pro-rata basis for participants with less than the minimum years of service.

3. Average Normal accrual rate (NAR) for non-excludable non-HCEs is ≥ 70% * (Average NAR for non-excludable HCEs). This test is based on all non-excludable employees, even if NOT benefiting under the plan. All other plans are excluded for this test.

1.401(a)(4)-4
BENEFITS, RIGHTS AND FEATURES

EXAMPLES

- Optional forms of payment, including subsidized forms
- Early retirement eligibility
- Ancillary benefits: death, disability
- Many features for DC plans, including loan provisions, investment options, etc.

1.401(a)(4)-4
BENEFITS, RIGHTS AND FEATURES

Each BRF must satisfy both CA <u>and</u> EA reqt

1) **Early ret windows ignored after 1st year**

2) **Effective Availability Requirement**
   a) **Satisfied if ees to whom BRF is EA does not substantially favor HCEs**
   b) **Based on relevant facts / circumstance**
   c) **Implicitly reflects <u>all</u> eligibility conditions, based on example: age 55 and 30 yrs svc**

3) **Current Availability (CA) Requirement**
   a) **Satisfied if ees to whom BRF is CA passes 410(b), excluding ABPT**
   b) **For 410(b), ee is treated as benefiting only if BRF is CA**
   c) **CA <u>ignores</u> any age or service eligibility conditions, or if ee could ever satisfy**
   d) **Exception to (c) is a time-limited eligibility**
   e) **BRF eliminated prospectively deemed CA**

Determination of whether plan amendment(s) discriminate in favor of HCEs is based on all relevant facts and circumstances

Safe harbor for grants of up to five years of service immediately prior to the effective date of an amendment

1.401(a)(4)-5(b)
PRE-TERMINATION RESTRICTIONS

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1) Plan must limit benefits of HCEs (or former HCEs) upon termination from service Otherwise, at plan termination, may be discriminatory under 401(a)(4)

2) Plan won't fail to satisfy 411(a) and 411(d)

3) Distribution restrictions

   a) Restricted ees: include HCE (or former) if also one of 25 highest paid EVER non-excl.

   b) Benefit for restricted ee can't exceed
      i) Straight life annuity act'l equivalent of plan benefits (excl. Soc. Sec. supp.),
      ii) Plus Soc. Sec. Supp.

   c) Benefit includes some loans, periodic income, active W/D, non-ins death ben

1.401(a)(4)-5(b)
PRE-TERMINATION RESTRICTIONS

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d) Exceptions to distribution restrictions
   i) After payment, plan assets greater than or equal to 110%*(Current Liability)
   ii) Distribution < 1%*(Current Liability)
   iii) Distribution < 411(a)(11)(A)

PRACTICAL NOTES

- Current Liability similar to Funding Target
- Revenue Ruling 92-76 requires use of market value for plan assets

1.401(a)(4)-7
IMPUTING PERMITTED DISPARITY

Attempt to allow for effect of Social Security benefits, which are higher % of pay for ees with lower compensation levels

For 401(a)(4) general test, adjust allocation rate (DC plans) or accrual rate (DB plans)

Safe Harbor Plans

- **Design DC plans based on 1.401(l)-2**
- **Design DB plans based on 1.401(l)-3**
- **No need for 401(a)(4) general test, don't need to impute permitted disparity**

1.401(a)(4)-7(b) DC IMPUTE PERM. DISPARITY

1) Plan year comp á taxable wage base
   A) 2 * unadjusted allocation rate
   B) Unadjusted allocation rate
      plus permitted disparity rate

   - Use lesser of A rate and B rate

   - Unadjusted allocation rate =
     allocation / compensation
     (without imputing permitted disparity)

2) Plan year comp > taxable wage base
   C) $$\frac{\text{Allocations}}{[\text{plan year comp} - \tfrac{1}{2}\,(\text{taxable wage base})]}$$

   D) $$\frac{[\text{Allocations} + (\text{permitted disparity rate})*(\text{taxable wage base})]}{(\text{plan year compensation})}$$

   - Use lesser of C rate and D rate

3) Permitted disparity rate

A) Current year 401(l)(2)(A)(ii): 5.7%

B) If covered under any DB plan, and imputing permitted disparity under DC plan causes cumulative disparity fraction > 35, then DC permitted disparity rate = zero

1.401(a)(4)-7(c) DB IMPUTE PERM. DISPARITY

1) Average annual comp. á covered comp.
   A) 2 * unadjusted accrual rate

   B) Unadjusted accrual rate
      plus permitted disparity factor

   - Use lesser of A rate and B rate

   - Unadjusted accrual rate = NAR or MVAR
     (without imputing permitted disparity)

2) Average annual comp. > covered comp.
   C) $\dfrac{\text{ER provided accrual}}{[\text{avg. annual comp} - \frac{1}{2}\,(\text{covered comp.})]}$

   D) $\dfrac{[\text{ER provided accrual} + \text{PDF} * \text{covered comp.}]}{(\text{Average annual compensation})}$

   - Use lesser of C rate and D rate

1.401(a)(4)-7(c) DB IMPUTE PERM. DISPARITY

3) Permitted disparity factor (PDF)

   A) Sum of annual PDF values divided by testing service in measurement period

   B) Annual PDF is .75% (if testing age = SSRA)

   C) Annual PDF = 0 for testing service > 35 yrs

   D) Reduce 35 years in (C) by cumulative disparity fraction based on other plans

DC PLAN - IMPUTE PERMITTED DISPARITY

Assume employee comp á taxable wage base

Unadjusted Rate	A rate	B rate	Lesser
X%	2X	X+5.7%	
3%			
6%			
9%			

DB PLAN - IMPUTE PERMITTED DISPARITY

Assume avg annual comp > covered comp
(100,000) (60,000)

SSRA is 65

Unadjusted Accrual	C rate	D rate	Lesser
X	$\frac{X}{AAC - ½\ CC}$	$\frac{X + PDF*CC}{AAC}$	
500			
1,500			

1.401(a)(4)-8 CROSS-TESTING

Can test DB plan on contributions basis, or DC plan on benefits basis. If DB and DC plans were aggregated, then must test entire group on either benefits OR contributions basis (see page 50).

Cross-testing rules require use of standard interest rate / mortality to normalize benefits (see page 7)

To cross test DC plan on DB basis, must meet gateway criteria (see pages 44 & 52)

1.401(a)(4)-8(c)(2) CONTRIBUTIONS BASIS

1) Must use annual method

2) Determine increase in accrued benefit for the plan year

3) May have different benefit for MVAR / NAR

4) Multiply by <u>straight life annuity</u> at testing age

5) Discount from testing age (interest only)

6) Express as dollar amount, or % of comp

7) Allowable options
   - A) May impute permitted disparity
   - B) May apply grouping of rates
   - C) Allowable subset of 1.401(a)(4)-3 options
     - i) 415 limits may be taken into account
     - ii) Use qualified disability benefits

1.401(a)(4)-8(b)(2) BENEFITS BASIS

1) Determine increase in account balance during the measurement period
   A) Measurement period can be current year or all prior service
   B) MUST exclude income, expenses, G/L during measurement period attributed to balance at start of measurement period
   C) Item (B) is "optional" for annual method

2) Bring forward to testing age (interest only)

3) Divide by <u>straight life annuity</u> at testing age

4) Divide by # years ee benefited during measurement period

5) Express as dollar amount, or % of comp

6) Use plan year comp for annual method, average annual comp for accrued to date

EXAMPLE - CROSS TESTING

Testing assumptions

Date	12/31/2016
Interest	8% per year

12/31/16 Data for Smith

Age	50
Hire Date	12/31/2011
Compensation:	60,000
Accrued benefit:	3,000

Selected annuity factors for testing

x	$\ddot{a}_x^{(12)}$	$\ddot{a}_{\overline{x:x}}^{(12)}$	$\ddot{a}_{\overline{x:\overline{10}\rvert}}^{(12)}$
55	10.0	11.5	10.5
60	9.5	11.0	10.0
65	8.5	10.0	9.0

If the plan is tested on a contributions basis, what is Smith's normal allocation rate?

1.401(a)(4)-8(b)(1)(i)
DC PLAN CROSS TESTING GATEWAYS

DC plan must satisfy <u>one</u> of several gateway criteria to be cross-tested on benefits basis. Plan can not be restructured to meet reqt.

- **Minimum allocation gateway - have to give minimum allocation to benefiting NHCEs**
- **Broadly available allocation rates**
- **Gradual age or service schedule of allocation rates**
- **Uniform target benefit allocation**

1.401(a)(4)-8(b)(1)(iii)
BROADLY AVAILABLE ALLOCATION RATES

Test similar to BRF (see page 29)

- **Satisfied if group of employees to whom each allocation rate is available passes 410(b)**
- **Allowed to assume ABPT is satisfied**
- **Unlike BRF, can NOT ignore any age or service eligibility conditions**
- **Ignore differences in allocation rates due to imputed permitted disparity**

1.401(a)(4)-8(b)(1)(iv)
GRADUAL AGE OR SERVICE SCHEDULE

- Not allowed to impute permitted disparity
- Define bands based on age, service, A+S
- Smoothly increasing
  - Allocation rate must increase by band
  - Increase can't exceed 5% (not 1.05)
  - Ratio of rates can't exceed 2.00 (compared to preceding rate band)
  - Ratios of ratios can't exceed 1.0
- Regular intervals
  - Bands should be same length
  - Highest band can have different length
  - First band
    - Can treat 1 yr service as 0-1 yr
    - Can treat start age as 25 or less, if band ends after age 25
    - Can treat as same length, if ends á 25

1.401(a)(4)-8(b)(1)(iv)
GRADUAL AGE OR SERVICE SCHEDULE

Which of these passes "smooth & regular"

Age	Alloc Rate
<25	1
25-35	2
35-45	4
45-55	8
55-65	14
> 65	18

Svc	Alloc Rate
<1	2
1-2	4
2-4	7
4-6	10
6-8	14
8-10	19

1.401(a)(4)-8(b)(1)(iv)
GRADUAL AGE OR SERVICE SCHEDULE

Can have minimum allocation rate, if meet additional criteria (1) and either (2) or (3)

1) Minimum allocation %
   A) Can be uniform for all employees
   B) Can provide T-H minimum 416(c)(2) to non-key ees, plan doesn't have to be T-H

2) Schedule ignoring minimum % starts ñ 1%

3) Steepness requirement - very complex, based on hypothetical employees

1.401(a)(4)-8(b)(1)(vi)
MINIMUM ALLOCATION GATEWAY

- **Not allowed to impute permitted disparity**

- **Each NHCE allocation rate ñ 1/3 highest HCE**

- **Deemed satisfaction alternative**
  - **Each NHCE allocation rate ñ 5%**
  - **Must use**
    plan year compensation,
    pay defined under 415(c)(3) (not 414(s)),
    and annual method to calculate rate

1.401(a)(4)-9(b) PLAN AGGREGATION

- Assume you have DB and DC plans, and one plan can not pass 401(a)(4) or 410(b)
- If plan can only pass 410(b) when aggregated, must also aggregate the same way for 401(a)(4) testing (and vice versa)
- Whether aggregated DB/DC plans satisfy 401(a)(4) or 410(b) is based on rules for the "deemed single plan"
- All DB/DC plans must be cross-tested, either on benefits basis OR on contributions basis
- Option - Aggregate all DB plans, treat as single DB plan (similar for DC plans)

1.401(a)(4)-9(b)(2) PLAN AGGREGATION

1. Assume aggregated DB/DC plans

2. Assume 401(a)(4) testing on Benefits basis

3. Determine MVAR and NAR for single DB plan, and equivalent NAR for single DC plan

4. Aggregate NAR for DB/DC is sum of NAR for single DB and equivalent NAR for DC plan

5. Aggregate MVAR for DB/DC is sum of MVAR for single DB and equivalent NAR for DC plan

6. Use Aggregate MVAR and NAR for testing of DB/DC under 401(a)(4)

1.401(a)(4)-9(b)(2)(v)
PLAN AGGREGATION - DB/DC GATEWAY

Aggregated plan must satisfy one of several gateway criteria to be cross-tested on benefits basis. Plan can not be restructured to meet requirement.

- **Primarily DB in character**
- **Broadly available separate plans**
- **Minimum aggregate allocation gateway - only have to give minimum allocation to benefiting NHCEs**

If aggregating DB/DC is required for ABPT calculations, do NOT have to meet DB/DC Gateway

1.401(a)(4)-9(b)(2)(v)(B)
PRIMARILY DB IN CHARACTER

- Not allowed to impute permitted disparity
- More than 50% of NHCEs benefiting have NAR from DB plans that exceeds equivalent accrual rate from DC plans

1.401(a)(4)-9(b)(2)(v)(C)
BROADLY AVAILABLE SEPARATE PLANS

- Treat all DB plans as single plan (also for DC)
- Single DB plan (and DC plan) must pass 410(b), and amounts test 401(a)(4)
- Allowed to assume ABPT is satisfied
- May use imputed permitted disparity for an employee only under one type of plan

NOTE:
ONLY useful when a plan fails the ABPT

1.401(a)(4)-9(b)(2)(v)(D)
MINIMUM AGGREGATE ALLOCATION GATEWAY

- Not allowed to impute permitted disparity
- General rule: "HCE rate" = aggregate normal allocation rate for HCE with highest rate

"HCE rate"	NHCE min. rate
15% or less	1/3 of "HCE rate"
15% to 25%	5%
>25% up to 30%	6%
>30% up to 35%	7%
>35% up to 40%	8%
And so on …	

- Can use average of equivalent allocation rates under DB for all NHCEs (vs actual)

1.401(a)(4)-9(b)(2)(v)(D)
MINIMUM AGGREGATE ALLOCATION GATEWAY

- **Deemed satisfaction alternative**
  - **Each NHCE aggregate normal allocation rate ñ 7.5%**
  - **Must use plan year compensation, pay defined under 415(c)(3) (not 414(s)), and annual method to calculate rate**
- **Can use average of equivalent allocation rates under DB for all NHCEs (vs actual)**

1.401(a)(4)-9(c) PLAN RESTRUCTURING

- You can restructure a plan into any number of component plans, any way you prefer
- If each component plan passes 401(a)(4) and 410(b), as defined in the regulation, then the plan satisfies 401(a)(4)
- Methods of restructuring and composition of groups can change every year
- Each employee must be included in only one component plan for a plan for the plan year

1.401(a)(4)-9(c)(3) COMPONENTS + 401(a)(4)

- Each component plan must pass all the 401(a)(4) requirements
- Any reference to “plan” in 401(a)(4) applies to “component plan”
- Exception - safe harbor for plans with uniform points allocation formulas is not available to test contributions under component plans

1.401(a)(4)-9(c)(3) COMPONENTS + 410(b)

Relationship between Components and total plan is almost independent

- **Entire plan must satisfy 410(b)**
- **Each component must also satisfy 410(b)**
- **Example – total plan passes ratio % test, but component plan does not, component plan must also pass ABP test**

<u>Exception – ABP test</u>
If entire plan passes ABP test, each component plan also deemed to pass

1.401(a)(4)-9(c)(3) COMPONENTS + 401(a)(4)

Cross testing exceptions - can not use component plans to determine when a plan passes new gateway tests:

- **1.401(a)(4)-8(b)(1) for DC plans**
  - **Has broadly available allocation rates**
  - **Has gradual age or service schedule**
  - **Has allocation rates based on uniform target benefit allocation**
  - **Satisfies minimum allocation gateway**

- **1.401(a)(4)-9(b)(2)(v) for DB/DC plans**
  - **Is primarily DB in character**
  - **Broadly available separate plans**
  - **Satisfies minimum aggregate allocation gateway**

401(a)(4) SUMMARY

1.401(a)(4)-1 Nondiscrimination requirements

1.401(a)(4)-2 Nondiscrimination - DC plans

1.401(a)(4)-3 Nondiscrimination - DB plans

1.401(a)(4)-4 Benefits, rights and features

1.401(a)(4)-5 Plan amendments, and pre-termination restrictions

1.401(a)(4)-6 Contributory DB plans

1.401(a)(4)-7 Imputing permitted disparity

1.401(a)(4)-8 Cross Testing

1.401(a)(4)-9 Plan aggregation, restructuring

1.401(a)(4)-10 Testing former employees

1.401(a)(4)-11 Additional rules

1.401(a)(4)-12 Definitions

1.401(a)(4)-13 Effective dates, Fresh start rule

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