SECTION 401(a)
SECTION 414(q)
SECTION 414(s)

Overview to Non-discrimination

INTERNAL REVENUE CODE §401(a)

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§401(a) has a "laundry list" of items that are required for a plan to be qualified:

§401(a)(3)	§410 minimum participation
§401(a)(4)	Nondiscrimination
§401(a)(5)	Special rules - Nondiscrimination
§401(a)(6)	Quarterly test for §401(a)(3)
§401(a)(7)	§411 minimum vesting
§401(a)(9)	Required distributions
§401(a)(10)	Owner ees / Top Heavy
§401(a)(11)	Joint and Survivor annuity
§401(a)(12)	Merger / consolidation / transfer
§401(a)(13)	Assignment and alienation
§401(a)(14)	Benefit commencement
§401(a)(15)	Social Security increase can not decrease benefit
§401(a)(16)	§415 limits
§401(a)(17)	Compensation limit

§401(a)(25)	Actuarial assumptions for benefits preclude employer discretion
§401(a)(26)	Minimum participation reqts
§401(a)(27)	Profit sharing plans
§401(a)(28)	ESOP requirements
§401(a)(29)	Benefit limitations
§401(a)(30)	Elective deferrals - limitations
§401(a)(31)	Direct transfer of rollover
§401(a)(32)	Liquidity shortfall – No effect if certain payments not made
§401(a)(33)	No benefit increase in bankruptcy
§401(a)(34)	Benefits of missing participants at Plan termination
§401(a)(35)	Diversification requirements for certain DC plans
§401(a)(36)	Distributions during working retirement

§401(b) Retroactive changes in plan
§401(c) Self-employed + owner-employees
§401(d) Contribution limit: owner-employees
§401(h) Medical benefits for retirees
§401(k) Cash or deferred arrangements
§401(l) Permitted disparity

§401(a)(5)(F)
Can treat SSRA as uniform retirement age for nondiscrimination testing

§401(a)(9)(C)
Required beginning date for distributions is April 1 of calendar year following later of calendar year of (i) attain age 70 ½, or (ii) retirement. Note: 5% owners: old 70 ½ reqt

§401(a)(13)(C)
Exception to assignment and alienation reqt for offset against benefit due to certain judgment or settlement

RECENT LAW CHANGES – IRC §401

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§401(a)(26)(A)
Defined benefit plan must benefit at least lesser of 50, or greater of (40%, or 2 employees [or 1])

§401(a)(36) PPA 06
Plans may provide distributions to employees at age 62 even though not separated from service

MANY more minor changes in PPA 06

§4974 Minimum Required Distributions

- Tax is 50% of the difference between required and actual distribution
- Tax is paid by the participant

§4975 Prohibited Transactions

- Tax is 15%
- IRS can increase to 100% if not corrected
- Usually entire amount is subject to tax

Revenue Ruling 2002-43

- If PT spans multiple years, new PT occurs at start of each taxable year
- Loans have special rules
  - Amount subject to tax is loan interest
  - Produces increasing excise taxes

Year	Loan int	Excise tax
200X	A	.15(A)
200Y	B	.15(A+B)
200Z	C	.15(A+B+C)

§401(a)(17) COMPENSATION LIMIT

§401(a)(17) defines includable compensation. DB plan benefits (or DC allocations) can't use pay over this amount:

2014	260,000
2015	265,000
2016	265,000

For non-calendar year plan year, use value for calendar year in which plan year <u>begins</u>

§414(q) HIGHLY COMPENSATED EES (HCE)

Can be HCE solely based on stock ownership, or based on pay

§414(q)(1)(A)	"5% owner" during current or prior year, OR
§414(q)(1)(B)(i)	Employee with prior year compensation in excess of 120,000, AND
§414(q)(1)(B)(ii)	If the employer elected this clause in prior year, was in top-paid group in prior year

§414(q) HIGHLY COMPENSATED EES (HCE)

§414(q)(1)(A)

- IRC §318 Constructive ownership rules apply - see page 14
- IRC §416 defines this as "greater than 5%"

§414(q)(1)(B)(i)

HISTORICAL VALUES

2014	115,000
2015	120,000
2016	120,000

- For non-calendar year plan year, use value for calendar year in which plan year starts

§414(q)(1)(B)(ii)

- The top-paid group is the highest 20% of employees, ranked by compensation

§414(q)(1)(B)(ii) HIGHLY COMPENSATED EES TOP-PAID GROUP EXCLUSIONS

Election to use top-paid group can reduce number of employees considered HCEs

414(q)(5) defines exclusions that apply to the total employee head count. 20%*(head count) gives maximum employees included in paid group.

A. **Ees with less than 6 months of service**
B. **Ees who work less than 17 ½ hours per week**
C. **Ees who work less than 6 months during a year**
D. **Ees who are less than age 21**
E. **Ees covered by a collective bargaining agreement (CBA)**

Calculate age and service at end of prior plan year

Employer may elect to use shorter service, smaller hours / months, or lower age

1.414(q)-1T HIGHLY COMPENSATED EES TOP-PAID GROUP EXCLUSIONS

E. Employees covered by a collective bargaining agreement (CBA):

i. 90 percent or more of all employees are covered under a CBA, AND
ii. Plan being tested only covers employees who are <u>not</u> covered under a CBA

These details are in the regulation, not in IRC §414

Tested numerous times on the exam!

§318 - CONSTRUCTIVE OWNERSHIP

Individuals are considered as owning the stock owned directly by their:

- **Children**
- **Grandchildren**
- **Parents**
- **Spouse**

"Spouse" does <u>not</u> include a legally separated spouse

"Children" does include a legally adopted child

More complex rules for attribution to / from partnerships, estates, trusts, corporations

§414(s) COMPENSATION

401(k) and other deferrals are <u>included</u> by default

- **Plan definition of compensation for testing purposes can override 414(s) defaults**
- **Compensation for testing purposes can be different than that used for plan benefits**
- **An alternative definition is NOT allowed if it discriminates in favor of the HCEs**

§414(s) COMPENSATION – DISCRIMINATORY?

1.414(s)-1(d)(3)(i) defines the test for an alternative 414(s) compensation definition:

1. **Calculate ratio of 414(s) comp to total comp for each employee.**

2. **1.414(s)-1(d)(3)(ii) states that the total compensation must be limited by 401(a)(17)**

3. **Compare average of ratios for HCEs versus non-HCEs**

4. **414(s) comp definition is nondiscriminatory if difference does not exceed de minimis amount**

5. **The de minimis amount is based on facts and circumstances**