

Administrative and Qualification Issues of Retirement Plans

E&E Course: C-1

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Part I

Plan Qualification Requirements

In order to receive favorable tax treatment, qualified plans must meet the requirements set forth in Internal Revenue Code §401(a). Failure to satisfy these requirements in both form and operation will result in plan disqualification. The Employer would lose the tax deduction for contributions made and trust earnings would become taxable. Participants would be taxed on their vested account balances or vested accrued benefits under the plan.

List of Requirements:

1. The plan must be in writing.
2. A plan must have a trust.
3. The plan must be communicated to employees.
4. The plan must be a permanent arrangement.
5. The plan must be for the employees of the employer.
6. The plan must be for the exclusive benefit of the company's employees and their beneficiaries.
7. The plan must satisfy minimum age and service requirements.
8. The benefits or contributions provided by the plan must not discriminate in favor of highly compensated employees.
9. The plan must satisfy the minimum coverage requirements of IRC §410(b).
10. The plan must satisfy the minimum vesting standards.
11. Benefits provided by pension plans must be definitely determinable.
12. The plan must satisfy the minimum distribution rules.
13. The plan must contain provisions that will take effect if the plan becomes top-heavy.
14. The pension plan must generally pay benefits in the form of a joint and survivor annuity, and death benefits in the form of a pre-retirement survivor annuity.

15. The plan must provide that, upon merger or consolidation of the plan, each participant shall be entitled to a benefit after the merger or consolidation that is no less than the benefit before the merger or consolidation.
16. The plan must generally prohibit the assignment and alienation of any benefits.
17. The plan must satisfy the rules concerning the timing and amount of benefit payments.
18. The plan must provide that benefits shall not be reduced because of changes in Social Security benefits or the Social Security wage base after a participant starts receiving benefits or is separated from service.
19. The plan must satisfy the IRC §415 limits.
20. The plan must limit the amount of compensation used in determining contributions or benefits for a participant to \$150,000 (adjusted for inflation); \$200,000 effective in 2002 and then increasing in \$500 increments.
21. The plan must provide for the direct transfer of eligible rollover distributions to another qualified plan or Individual Retirement Account.

Submission for an IRS Determination Letter:

- A retirement plan must be qualified both in form and in operation.
- Although not required, an employer may choose to request a determination letter for plan document qualification.
- Generally, must be filed by the due date for the plan sponsor's tax return for the first plan year.
- Some plans are drafted to require that the employer contribution will be returned in the event the plan is determined not to be qualified by the IRS.
- Timely filing allows the employer to make corrective amendments to the document retroactively.

Part II

Highly Compensated Employees

One of the basic qualification requirements listed in IRC §401(a)(4) states that benefits or contributions must not discriminate in favor of highly compensated employees. This section deals with defining and being able to identify highly compensated employees.

Definitions:

Highly Compensated Employee – Taking into consideration the stock attribution rules of IRC §318, an employee is considered highly compensated if either of the following two tests are met:

1. In either the determination year or the look-back year, the employee is a “5% owner.”

2. In either the determination year or the look-back year, the stock attribution rules of IRC §318 apply.
3. In the look-back year, the employee has compensation of more than \$80,000 (as indexed) (\$90,000 in 2003) A top paid group election may be made with respect to the compensation test.

Determination Year – The current plan year.

Look-Back Year – The 12-month period preceding the current plan year.

Attribution Rules of IRC §318 – An individual is treated as owning the interest owned by a spouse, child, grandchild, or parent.

Top Paid Group Election – This election limits the number of employees under the compensation test to those who are in the top 20 percent of employees (ranked by compensation) whose compensation exceeds the dollar limit.

Calendar Year Election – The plan sponsor of a fiscal year plan may elect to use the calendar year that begins within the look-back year as the “look-back year.” If this election is made, it applies to all subsequent determination years unless the plan is amended to change the election.

Part III

Requirements for Eligibility & Participation

In order for a retirement plan to be qualified, certain minimum standards for coverage of employees must be met. Failure to satisfy these requirements will result in plan disqualification. The Employer would lose the tax deduction for contributions made and trust earnings would become taxable. However, only highly compensated employees would be taxed on their vested account balances or vested accrued benefits under the plan.

Requirements for Eligibility and Participation:

Before becoming eligible to participate in the plan, a qualified retirement plan may require an employee to:

1. Reach age 21, and/or
2. Complete one year of service or
3. Complete two years of service (if full and immediate vesting is provided)

A qualified retirement plan *may not* exclude from participation employees who are hired after reaching a specified maximum age.

A plan that requires two years of service may provide that service prior to a break in service be disregarded if the participant has not met the service eligibility criterion. However, the plan cannot require that the two years of service be consecutive.

Example: Joan worked for ABC Company and completed the following hours of service. ABC established a calendar year profit sharing plan in 1999 with entry dates of January 1 and July 1. Joan's date of hire was January 1, 1999.

<u>Plan Year</u>	<u>Hours of Service</u>
1999	1,000
2000	500
2001	1,000
2002	700
2003	1,000

Joan's entry date is January 1, 2004.

An employee who has satisfied the statutory minimum age and service requirements must enter the plan (*statutory entry date*) by the earlier of:

1. The first day of the plan year after satisfying the requirements, or
2. Six months after satisfying the requirements.

The following employees are permitted to be excluded from participation by statute (*statutory exclusions*):

1. Employees who don't satisfy the minimum age and service requirements.
2. Employees who are nonresident aliens, without any earned income from sources within the United States.
3. Union employees who are members of a collective bargaining unit where retirement benefits are the subject of good faith bargaining.

Special Rule for Leased Employees – Leased employees are considered the employees of the recipient employer's plan unless:

1. The leased employees do not make up more than 20% of the employer's non-highly compensated work force; and
2. Each leased employee is covered by a *safe harbor money purchase plan* maintained by the leasing organization.

Definitions:

Safe Harbor Money Purchase Plan – A 10% money purchase pension plan with immediate entry and 100% immediate vesting.

Year of Service – A year of service of eligibility purposes is a twelve consecutive month period beginning on the date of hire during which an employee has at least 1,000 hours of service. The plan may define a year of service as less than 1,000 hours of service.

Hours of Service – Hours of service may be defined in the plan as actual hours or by using equivalencies. An alternative to the 1,000 hours method is the elapsed time method.

IRC §410(b) Minimum Coverage Test:

In order for a retirement plan to be qualified, it must satisfy one of two tests: the Ratio Percentage Test or the Average Benefits Test. Each plan of the employer is usually tested separately; however, the employer may elect to treat two or more plans as a single plan for testing purposes.

The coverage rules must be satisfied on either:

1. Each day of the plan year,
2. The last day of the plan year, or
3. At least one day of each quarter of the plan year.

Correction of a failed test must be made retroactively within 9 months following the close of the plan year by either increasing benefit levels or including more employees in the plan.

In addition to the statutorily excluded employees, participants who terminate employment during the plan year with less than 501 hours of service and who did not benefit for the year may be excluded when performing the test.

Ratio Percentage Test – The percentage of nonexcludable nonhighly compensated employees benefiting under the plan must equal at least 70% of the percentage of nonexcludable highly compensated employees who benefit under the plan.

Average Benefits Test – The plan must satisfy both the *nondiscriminatory classification test* and the *average benefit ratio test*. The nondiscriminatory classification test requires that the plan benefit a classification of employees set by the employer which the IRS deems not to be discriminatory in favor of highly compensated employees. Under the average benefit ratio test, the average benefit percentage for nonhighly compensated employees must equal or exceed the average benefit percentage for highly compensated employees.

Classroom Example

Highly Compensated Employees

Based on the following information, who is a highly compensated employee (HCE) for the plan year ending December 31, 2002?

- Assume that all employees are at least age 21 with at least one year of service
- Assume that the employee population is identical in 2001 and 2002
- Assume that ownership and officer status is identical in 2001 and 2002
- Assume that the employer elects not to use the top paid group rule

Employee	2001 Salary	2002 Salary	Officer	Ownership
Smith	\$200,000	\$170,000	Yes	85%
Brown	\$100,000	\$75,000	No	2%
Green	\$75,000	\$100,000	No	5%
White	\$30,000	\$30,000	No	8%
Jones	\$70,000	\$80,000	Yes	0%

- What would the solution be if the top paid group option were used?

Classroom Example

Ratio Percentage Test

You are given the following information about the employees covered in Plan A of the Employer.

	HCE	NHCE
Total employees	20	50
Nonexcludable employees	19	40
Employees benefiting	18	30

1. What is the ratio percentage for this plan?
2. What is the maximum number of NHCEs that could be considered as not benefiting for the plan to still pass the ratio percentage test?

Question 1.

All of the following statements regarding plan qualification are **TRUE, EXCEPT:**

- A. The plan must not discriminate in favor of highly compensated employees.
- B. The plan must be maintained for the exclusive benefit of the employees.
- C. The plan must reduce benefits for increases in Social Security benefits once benefits have begun.
- D. The plan must provide for direct transfer of eligible rollover distributions to another qualified plan or individual retirement account.
- E. The plan must be a written instrument.

Question 2.

Based on the following information, what is the latest date that a plan must designate as Employee A's entry date into the plan?

- Employee A was born on March 31, 1982.
- Employee A was hired on May 15, 2000.
- Employee A is a full-time employee.
- The plan year is April 1 to March 31.
- The eligibility requirements are age 21 and completion of one year of service.

- F. May 15, 2001
- G. October 1, 2001
- H. November 15, 2001
- I. April 1, 2003
- J. October 1, 2003

Question 3.

Based on the following information, what is the total number of employees that must be included in the coverage testing under IRC §410(b)?

Total employees during the year	60
Employees who have not met the minimum age and service requirements included in the total	14
Employees who have met the minimum age and service requirements, but are excluded by job description, included in the total	5
Participants who terminated with less than 500 hours of service included in the total	8
Active participants who have completed less than 1,000 hours of service included in the total	4

- A. 33
- B. 38
- C. 46
- D. 52
- E. 60

Question 4.

All of the following plans automatically satisfy the minimum coverage requirements under IRC §410(b), **EXCEPT**:

- F. Plans that benefit only highly compensated employees and exclude nonhighly compensated employees.
- G. Plans that satisfy the ratio percentage test.
- H. Plans that benefit 10 percent of the nonhighly compensated employees and exclude highly compensated employees.
- I. Plans that benefit only collectively bargained employees.
- J. Plans that benefit all nonhighly compensated employees and exclude highly compensated employees.

Part IV

Vesting & Protected Benefits

One of the requirements for a retirement plan to be qualified is that it provide for the vesting of benefits according to one of the schedules allowed by law. Vesting represents the nonforfeitable interest of a participant's account balance or accrued benefit and is directly related to the participant's length of employment.

When is an Employee Vested:

1. Employee contributions whether pre-tax or post-tax are always 100% vested.
2. Employer contributions must be 100% vested no later than permitted under the statutory vesting schedules.
3. A participant is 100% vested upon attainment of normal retirement age.
4. All participants vest at the termination of a plan.
5. Affected participants vest upon partial termination of a plan.
6. Immediate vesting is required if the plan's minimum service requirement is greater than one year.

Calculating a Participant's Length of Employment:

7. Generally, all years of service with the employer must be counted when determining a participant's vested percentage.
8. For purposes of determining a participant's vested benefits, IRC §411(a)(5) defines a year of service as a 12-consecutive-month period specified in the retirement plan during which the participant completes at least 1,000 hours of service.
9. If specified in the retirement plan, the following years of service with the employer may be disregarded:
 - a. Years of service before age 18,
 - b. Years of service before the effective date of the plan, provided there is no predecessor plan within the last five years.
 - c. Years of service in which the participant declined to make mandatory contributions, and
 - d. Years of service excluded under the break in service rules.

Calculating a Rehired Participant's Length of Employment:

A one-year break in service is a vesting year with fewer than 501 hours.

1. A non-vested participant who has a one year break in service and is rehired is subject to the “rule of parity.” The “rule of parity” permits the exclusion of years of service prior to a break in service when calculating vesting if the number of consecutive one-year breaks in service equals or exceeds the greater of:
 - a. Five years, or
 - b. The number of pre-break years of service.
2. Years of service before a break in service may not be excluded when calculating vesting for a partially or fully vested participant who is rehired.

Minimum Vesting Schedules:

1. 5-Year Cliff

<u>Years of Service</u>	<u>Vested %</u>
1	0%
2	0%
3	0%
4	0%
5	100%

2. 7-Year Graded

<u>Years of Service</u>	<u>Vested %</u>
1	0%
2	0%
3	20%
4	40%
5	60%
6	80%
7	100%

3. For plan years beginning in 2002, employer matching contributions must satisfy one of the top heavy matching contributions (3-Year Cliff or 6-Year Graded).
4. If the retirement plan is amended to change the vesting schedule, no participant’s vested percentage may be reduced. Additionally, any participant who has three or more years of service may elect to continue under the former vesting schedule.

Forfeitures:

A *forfeiture* is the non-vested portion of a participant’s accrued benefit.

5. The timing of a forfeiture depends on the provisions of the plan and when the vested benefit is distributed.

- a. Five-year break in service rule - A forfeiture made after a 5-year break in service will prevent any future service from being taken into account in determining the vested percentage of benefits accrued before the 5-year break in service. In this case, the participant need not receive a distribution for the forfeiture to occur.
- b. Cash-out distribution rule – Forfeitures may occur at the time a participant receives distribution; however QJSA rules, if applicable, and repayment rules must be satisfied.

Protected Benefits under IRC §411(d)(6):

1. Protected Benefits – The accrued benefit of the participant, optional forms of benefits, early retirement subsidies and other retirement subsidies.
2. Benefits that are not Protected – Ancillary life insurance, availability of loans, right to make employee contributions (pre or post tax), right to direct investments, the plan’s allocation dates.
3. A retirement plan will not violate the anti-cutback rules if:
 - a. It is a defined contribution plan and is amended to eliminate all periodic payment options, unless the QJSA option is an IRC §411(a)(11) requirement.
 - b. It is a defined contribution plan and is amended to eliminate certain in-kind distribution options.
 - c. The plan does not protect the optional forms of benefit that were previously available to benefits received as an elective transfer.

Part V

General Nondiscrimination Rules

IRC §401(a)(4) state that a qualified plan may not discriminate in favor of highly compensated employees. A plan may not discriminate in either form or operation.

The three areas tested for discrimination are:

1. Benefits or contributions provided under the plan must be nondiscriminatory in amount,
2. Benefits, rights and features must be available to all in a nondiscriminatory manner, and
3. The effect of plan amendments or terminations must be nondiscriminatory.

Benefits or Contributions – This test may be met by either adopting a safe harbor formula or by rate group testing.

- A safe harbor formula can be either design-based or non-design based.
- A design-based safe harbor formula for a defined contribution plan is a uniform allocation formula.
- A design-based safe harbor formula for a defined benefit plan must satisfy one of the following accrual methods: (1) the 133-1/3 percent accrual method (2) the fractional accrual method, or (3) and IRC §412(i) plan.
- A non-design-based safe harbor defined contribution plan is a uniform allocation formula based on compensation **and** age and/or service.
- A non-design-based safe harbor defined benefit plan meets all the requirements of a design-based safe harbor plan using the fractional accrual method except that it may permit less than 25 years for an unreduced benefit.
- A plan not meeting the safe harbors must meet the general test which requires that rate groups be determined for each highly compensated employee benefiting under the plan. Each rate group must satisfy IRC §410(b).

Benefits, Rights and Features – Each optional form of benefit and ancillary benefit provided by the plan must separately satisfy both the current availability test and the effective availability test.

- Under the Current Availability Test each group of employees eligibility for a benefit must satisfy either the ratio percentage test or the nondiscriminatory classification test of IRC §410(b).
- Under the Effective Availability Test the group of employees to whom the benefit is effectively available must not substantially favor HCEs.

Plan Amendments –

- Corrective amendments may not reduce benefits.
- Corrective amendment for 410(b) or 401(a)(4) may be adopted within 9-1/2 months after the plan year-end.
- A plan failing to satisfy IRC §401(a)(4) with regard to contributions, benefits or coverage may be amended retroactively to add dollars or include more participants.
- A plan failing to satisfy IRC §401(a)(4) may be amended prospectively to eliminate discrimination with regard to benefits, rights and features if not protected by IRC §411(d)(6).

Part VI

Compensation

Varying definitions of compensation exist for qualified retirement plans.

Plan Compensation:

Compensation as defined by the plan which is used in calculating the amount of contributions or benefits provided. Need not satisfy IRC §414(s); however, IRC §414(s) compensation must be used to determine whether contributions or benefits are discriminatory.

IRC §415 Compensation:

Compensation used to determine a participant's maximum contribution or benefit is defined in IRC §415(c)(3). One of three alternate safe harbor definitions must be elected in the plan document.

1. The basic definition includes all amounts received for services rendered in the course of employment to the extent includible in taxable gross income.
 - Including employer-provided accident or health benefits, reimbursement for moving expenses, the value of non-qualified stock options, transfer of property in connection with performance of services, (all to the extent includible in gross income); and elective deferrals (even though not includible in gross income).
 - Excluding premiums for group-term life insurance (to the extent not includible in gross income), amounts realized from the exercise of a non-qualified stock option plan, and amounts realized from the disposition of stock acquired under a qualified stock option.
2. Wages from Income Tax Withholding – IRC §3401(a)
3. Form W-2 Wages – Amounts for purposes of federal tax withholding. IRC §6041(d) and §6051(a)(3).

IRC §414(s) Compensation:

Compensation used for testing under IRC §§ 401(a)(4), 410(b), 401(l), 401(k) and 401(m) is defined in IRC §414(s). One of three safe harbor definitions may be used.

1. All three definitions above under IRC §415(c)(3).
2. IRC §415(c)(3) compensation excluding *all* of the following:
 - Moving expenses,
 - Fringe benefits,
 - Welfare benefits,
 - Deferred compensation, and

- Reimbursements or other expense allowances.
3. All types of elective deferrals may be excluded.

An alternate definition of compensation may be used provided it satisfies three conditions.

1. The definition must not favor highly compensated employees.
2. The definition must be reasonable.
 - It may exclude certain forms of compensation, such as overtime or bonuses.
 - It may limit compensation to a certain dollar limit.
3. The average of the HCE's plan compensation to total compensation may not exceed the average for NHCE's by more than a *de minimis* amount (compensation ratio test). This can be tested on an individual or an aggregate basis.

IRC §404 Compensation

To determine whether contributions are deductible under IRC §404, the following must be considered:

1. In determining compensation, elective deferrals must be included for plan years beginning after 12/31/01.
2. In determining the deductible amount, only compensation of participants who are eligible to make elective deferrals or to receive an employer contribution may be taken into account.
3. Contributions must be deductible under IRC §162 (for compensation paid if it is ordinary, necessary and reasonable) or IRC §212 (for expenses involved in the production of income).

IRC §414(q) HCE Compensation and IRC §416(c) Key Employee Compensation

Compensation used to determine highly compensated and key employees is defined in IRC §415(c)(3), including elective deferrals.

IRC §401(a)(17) Compensation

A qualified plan may not take into account for any participant annual compensation greater than \$150,000 (as indexed). For plan years beginning after 2001, the limit was raised to \$200,000 (as indexed).

This limit applies to the following:

1. Allocation of contribution or benefits.
2. Application of the nondiscrimination rules.
3. Determination of the maximum deductible contribution to the plan.

Compensation for Self-Employed Individuals

Compensation for self-employed individuals is defined as earned income derived from personal services which are a material income-producing factor. Earned income is the net earnings from self-employment minus:

1. One-half of the self-employment tax,
2. Contributions for common-law employees,
3. Contributions for the self-employed individual.

Classroom Example

401(a)(4) Safe Harbor Formulas

Which of the following are safe harbor plans in regard to the allocation or benefit formulas under 401(a)(4)?

1. A profit sharing plan with contributions allocated in proportion to compensation for all participants.
2. A money purchase pension plan integrated with social security that satisfies the integration rules of IRC §401(l).
3. A money purchase pension plan that provides an allocation of 5% of salary to all NHCEs and 10% of salary to all HCEs.
4. An age-weighted plan.
5. A defined benefit plan that provides a benefit of 2% of salary per year of service.
6. A defined benefit plan that provides a benefit of 2% of salary per year of service for all employees below age 60.
7. A defined benefit plan that provides a benefit of 2% of salary per year of service up to a maximum of 20 years.

Classroom Example

Forfeitures

You are given the following participant data as of 12/31/2002.

Name	Date of Birth	Date of Hire	Date of Termination	Account Balance
Smith	3/7/53	5/6/99	9/30/02	\$20,000
Brown	4/5/34	9/3/97	4/15/02	\$70,000
Green	1/8/84	1/7/00	3/15/02	\$6,000

- The plan effective date is 1/1/93.
- The normal retirement age is 65.
- Service before age 18 is disregarded for vesting.
- All employees are full time.
- The calendar year is to be used as the computation period for years of vesting service.

What is the total plan forfeiture amount under each of the following vesting schedules?

1. 3 to 7 year graded schedule
2. 20% per year of service
3. 5-year cliff schedule

Classroom Example

401(a)(4) General Test

Consider the following plan data.

	Accrual Rate
HCE 1	10.00%
HCE 2	11.00%
NHCE 1	6.00%
NHCE 2	10.00%
NHCE 3	10.40%

1. Which employees are in the rate group determined by HCE 1?
2. What is the ratio percentage of the rate group determined by HCE 1?
3. Which employees are in the rate group determined by HCE 2?
4. What is the ratio percentage of the rate group determined by HCE 2?

Classroom Example

Compensation Issues

Determine the average percentage of total compensation being used for both the highly compensated and non-highly compensated groups using each of the aggregate and individual methods.

Name	HCE	Eligible Compensation	Total Compensation
Smith	Yes	\$ 130,000	\$ 140,000
Brown	Yes	\$ 90,000	\$ 98,000
Green	No	\$ 35,000	\$ 35,000
White	No	\$ 25,000	\$ 30,000
Jones	No	\$ 17,000	\$ 18,000

Question 1.

Which of the following vesting schedules does not comply with the minimum vesting requirements of IRC §411 for a single employer plan?

- A. 10 percent per year with full vesting after seven years.
- B. 20 percent per year starting with the third year.
- C. 100 percent after five years of service.
- D. 25 percent per year of service.
- E. 33 1/3 percent per year starting with the second year.

Question 2.

Which of the following years of service may be disregarded for vesting purposes?

- I. Years of service before the employee reached age 18.
 - II. Years of service before the effective date of the plan.
 - III. Years of service before the employee's date of participation.
-
- A. I only
 - B. III only
 - C. I and II only
 - D. II and III only
 - E. I, II and III

Question 3.

Which of the following is a protected benefit under IRC §411(d)(6)?

- A. Ancillary life insurance protection.
- B. The right to a lump sum form of distribution.
- C. The right to direct investments.
- D. The availability of loans.
- E. The allocation dates for contributions.

Part VII

Top Heavy & Accrued Benefits

The Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) created §416 of the Internal Revenue Code, thus adding the concept of top heavy plans. Top heavy plans must meet additional qualification requirements which include minimum vesting and minimum benefits or contributions. This class will cover the determination of whether a plan is top heavy and the minimum vesting requirement.

The Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) altered certain definitions and rules that affect the determination of top heavy status for plan years beginning after December 31, 2001.

Steps to Determine Top Heavy Status:

1. Who is the employer?
2. What is the determination date?
3. Identify the participants to be considered.
4. Who are the *key employees*?
5. Is there a required or permissive aggregation group?
6. Determine the present value of accrued benefits or account balances of all participants.
7. Determine any distributions made in the prior year and in the five previous years. Distributions to participants identified in step three must be included in the test.
8. Determine the ratio of the accrued benefits for the key employees to the accrued benefits for all participants (be sure to include all participants identified in step 3).

If the ratio exceeds 60%, the plan is top heavy. If the ratio exceeds 90%, the plan is super top heavy. (For limitation years beginning after December 31, 1999, it is no longer necessary to test if a plan is super top heavy.)

Definitions:

(For Plan Years Beginning before January 1, 2002)

Key Employee – Taking into consideration the stock attribution rules of IRC §318, a key employee is an employee who at any time during the five year period ending on the determination date is:

1. A “five percent owner,”
2. A “one percent owner” who earned more than \$150,000,

3. A top ten owner who owns more than ½ percent of the employer and earns more than the defined contribution §415 dollar limitation, or
4. An officer who earned more than 50 percent of the defined benefit IRC §415 dollar limit. The number of employees who can be considered an officer is equal to 10 percent or all employees, or three whichever is greater. In no case, however, can the number of officers exceed 50.

Participants to be considered – In addition to all eligible employees, any former employee who has completed one hour of service in the five-year period ending on the determination date, and any participants receiving distributions in the five-year period ending on the determination date are participants to be considered.

Required Aggregation Group – This plan and any plans of the employer in which a key employee participates in the five-year period ending on the determination date, or any plan aggregated for IRC §410(b) coverage or for IRC§401(a)(4)nondiscrimination.

Definitions:

(For Plan Years Beginning after December 31, 2001)

Key Employee – Taking into consideration the stock attribution rules of IRC §318, a key employee is an employee who at any time during the one year period ending on the determination date is:

1. A “five percent owner,”
2. A “one percent owner” who earned more than \$150,000, or
3. An officer who earned more than \$130,000 (subject to COLAs in \$5,000 increments.) The number of employees who can be considered an officer is equal to 10 percent or all employees, or three whichever is greater. In no case, however, can the number of officers exceed 50.

Participants to be considered – In addition to all eligible employees, any former employee who has completed one hour of service in the one-year period ending on the determination date, any participants receiving distributions in the one-year period ending on the determination date, and any participants receiving certain in-service distributions in the five-year period ending on the determination date are participants to be considered.

Required Aggregation Group – This plan and any plans of the employer in which a key employee participates in the one-year period ending on the determination date, or any plan aggregated for IRC §410(b) coverage or for IRC§401(a)(4)nondiscrimination.

(For All Plan Years)

Determination Date – The last day of the previous plan year or the last day of the current plan year for the initial plan year.

Employer – If the employer that maintains the plan is related to another employer under the controlled group of businesses definition in IRC §414(b) or (c) or under the affiliated service group definition in IRC §414(m), then the related employer is also treated as an employer of the employees covered by the plan.

Account Balance – In a defined contribution plan, the account balance is the total value of a participant's share of the investments in the trust.

Present Value of Accrued Benefits – The PVAB is the current actuarial value of an accrued benefit expressed as a lump sum.

Accrued Benefits – In a defined contribution plan, the account balance. In a defined benefit plan, the benefit payable at normal retirement date that has been earned up to a particular point of employment.

Permissive Aggregation Group – A permissive aggregation group includes the required aggregation group and any other plans that satisfy IRC §410(b) and IRC §401(a)(4) when aggregated.

Aggregation Groups:

1. If a *required aggregation group* is top heavy, then all plans of the group are top heavy.
2. If a *required aggregation group* is not top heavy, then all plans of the group are not top heavy.
3. If the *required aggregation group* is top heavy, and a *permissive aggregation group* exists, then test the *permissive aggregation group*. If it is not top heavy, then all plans of the group are not top heavy.

Exception:

For plan years beginning after December 31, 2001, safe harbor 401(k) plans under IRC §401(k)(12) which provide the safe harbor matching contributions are NOT top heavy plans even if the top heavy ratio exceeds 60%.

Top Heavy Vesting:

The top heavy vesting schedules are a three-year cliff schedule or a six-year graded schedule. The rules for determining an employee's years of service for vesting are the same that apply for non-top heavy plans.

Rollover Contributions:

1. Rollovers between related plans are included in the testing of the recipient employer's plan.

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2. Rollovers between unrelated plans are included in the testing of the distributing employer's plan.

Part VIII

Special Rules Relating to Certain Business Entities

Sole Proprietorships and Partnerships:

1. ERISA does not apply to plans covering only sole proprietors, partners and their spouses.
2. Special lump-sum tax treatment is only available upon separation from service if due to disability.
3. Contributions on behalf of self-employed individuals to pay pure life insurance (PS-58 costs) are not deductible.
4. For plan years beginning prior to 1/1/02, participant loans to an owner-employee (*a greater than 10% owner*) were not exempt from the prohibited transaction rules.

S Corporations and Limited Liability Companies (LLCs):

1. For plan years beginning prior to 1/1/02, participant loans to a shareholder-employee of an S Corporation (*a greater than 5% shareholder*) were not exempt from the prohibited transaction rules.
2. LLCs may elect to be treated as either a corporation or a partnership.

Multiple Employer Plans:

1. A plan maintained by two or more unrelated employers is a multiple employer plan.
2. Each employer must individually meet requirements for the following:
 - Deductibility
 - Minimum Funding
 - Minimum Coverage
 - Top Heavy (although the entire plan would be disqualified if one employer fails to meet the top heavy requirements)
3. All employees are treated as employed by a single employer with regard to the following:
 - Participation
 - Exclusive Benefit Rules
 - Vesting

Multiemployer Plans:

1. A multiemployer plan is a plan maintained pursuant to a collective bargaining agreement by two or more unrelated employers.
2. Only the employees in the collective bargaining unit are taken into account in applying testing and other qualification rules.

3. PBGC rates are significantly less than for other qualified plans.
4. Generally, more time is granted to adopt law changes than for other qualified plans.

Controlled Groups:

1. A controlled group is treated as a single employer for qualified plan purposes.
2. A parent-subsiary controlled group exists if at least one business owns 80% or more of another business.
3. A brother-sister controlled group exists if:
 - Five or fewer individuals own 80% or more of each business, *and*
 - The same five or fewer individuals together own *more than 50%* of each business, taking into account only ownership that is identical.
4. A combined group is a controlled group which contains both a parent-subsiary and a brother-sister controlled group.
5. In determining controlled group status, attribution rules of IRC §1563 apply. The rules are applied differently when determining a parent-subsiary than when determining a brother-sister controlled group. Unlike, IRC §318, the level of ownership interest and type of family relationship may affect how attribution works.

Affiliated Service Groups:

1. An affiliated service group is treated as a single employer for qualified plan purposes.
2. An affiliated service group consists of one of the following:
 - A service organization (FSO) and a service organization (A-ORG) that is a shareholder or partner in the FSO and that either regularly performs services for the FSO or is regularly associated with the FSO in performing services for third persons.
 - A service organization (FSO) (and possibly an A-ORG) and any other organization (B-ORG) if a significant portion of the business of the B-ORG is performance of services for the FSO or the A-ORG (or for both) of a type historically performed in the service field of the FSO or the A-ORG employees, and 10 percent or more of the interests in the B-ORG is held by individuals who are highly compensated employees of the FSO or A-ORG.
 - A management organization and a recipient organization can form a management affiliation.

Part IX

Distributions & Taxation

Distribution from a qualified retirement plan may only be made upon retirement, death, disability, age 70 ½ or termination of employment. A plan may also provide for distribution upon attainment of a certain age or financial hardship. Generally, benefits become taxable upon distribution.

Benefits:

- Normal Retirement – Normal retirement benefits are payable upon attainment of the Normal Retirement Age stated in the plan. The NRA must be no later than the later of attainment of age 65 or the fifth anniversary of participation. The participant's benefits must be nonforfeitable upon attainment of the NRA.
- Early Retirement – A plan is not required to provide an early retirement benefit. If an early retirement benefit is provided, full vesting is not required.
- Postponed Retirement – A retirement plan *must* include a provision allowing a participant to defer retirement past the normal retirement age.
- Death Benefits – Most retirement plans and some profit sharing plans are subject to the qualified joint and survivor annuity rules and, therefore, have mandatory death benefits. Death benefits are not required to be fully vested.
- Disability Benefits – Disability benefits are not required to be fully vested.
- Termination Benefits – Upon termination of employment, a participant may be eligible to receive a distribution of the participant's vested benefits. If the participant's vested benefit is \$5,000 or less, the plan may allow for an involuntary cash out. Amounts above \$5,000 may not be distributed without the participant's written consent.
- In-service Distributions (profit sharing plans) – If provided for in the plan, an in-service distribution may be made from a profit sharing plan in either of these events:
 - Attainment of a stated age or completion of a specific number of years of service, or
 - Financial hardship.

Forms of Benefits:

1. Lump-sum payment.
2. Installment payments.
3. Annuity.
 - a. Qualified Joint & Survivor Annuity (QJSA) – An annuity payable for the life of the participant with a 50% to 100% annuity payable to the participant's spouse upon the death of the participant.
 - b. Qualified Pre-retirement Survivor Annuity (QPSA) – An annuity payable to the participant's spouse if the participant dies prior to receiving the QJSA (50% to 100% payable over the life of the spouse).
 - c. Single life annuity – A life annuity payable over the lifetime of the participant which ceases upon death.
 - d. Period certain and life annuity – Monthly payments are guaranteed to the participant for a certain period but continue for the life of the participant.

Minimum Distributions under IRC §401(a)(9):

1. When must distributions begin? – A participant must begin receiving distributions from the plan when the participant reaches age 70 ½.
2. Who must receive minimum distributions? –
 - a. 5% owners – The first distribution must be received by the April 1st following the calendar year in which the participant reaches age 70 ½.
 - b. All other participants – The first distribution must be received by the later of the April 1st following the calendar year in which the participant reaches age 70 ½ or the April 1st following the calendar year in which the participant retires.
3. The rules for calculating the minimum distribution amounts have been simplified for distributions made in 2002. Plans may take advantage of this simplified method in 2001 if amended to do so.

Taxation of Distributions:

1. Lump sum distributions – A lump sum distribution must be as the result of the participant's death, disability, separation from service or attainment of age 59 ½ and must be the total value of the participant's account paid within a single tax year. All like plans must be combined to determine whether the total value of the participant's account was paid.

- a. The participant's cost basis is recovered income tax free.
 - b. Distributions attributable to pre-1974 participation are eligible for long term capital gains treatment.
 - c. Participants born prior to 1936 continue to be eligible for favorable 10-year forward averaging.
 - d. All other distributions subject to ordinary income.
2. Rollovers – An eligible distribution may be rolled over into an IRA or another qualified plan and avoid current taxation.
- a. An IRA may serve as a conduit to transfer distributions from one qualified plan to another.
 - b. Effective for distributions made after December 31, 2001 an eligible rollover made within 60 days may be rolled to an IRA, a qualified plan, a 403(b) plan or a 457 plan.
 - c. Minimum distributions under IRC §401(a)(9) may not be rolled over.
 - d. Effective after December 31, 2001, hardship withdrawals may not be rolled over.
 - e. A qualified plan *must* provide for the direct transfer of an eligible rollover distribution to an eligible retirement plan, but need not provide for the receipt a direct transfer.
3. Cost basis – A participant's cost basis is the portion of the participant's distribution which is not subject to taxation. If the form of distribution is an annuity or installment payment, the participant's cost basis will be recovered over the number of anticipated payments from the plan. The cost basis may include:
- a. P.S. 58 costs.
 - b. After-tax employee contributions.
 - c. Participant loans that have already been taxed.
4. Ordinary income tax – Distribution of the following forms of benefit are taxed as ordinary income: single distributions, hardship withdrawals, installments, and annuity payments.
5. Death benefits – The beneficiary is generally entitled to the same tax treatment as is available to the participant. Death benefits are generally included in the participant's gross estate.
6. Excise taxes –
- a. Early withdrawal (pre-59 ½) – To discourage participants from taking their retirement benefit prior to NRA, certain participants must pay an

additional 10% penalty tax on distributions. The penalty is imposed unless the distribution is:

- i. Made on or after age 59 ½.
 - ii. Made to a beneficiary.
 - iii. Due to disability.
 - iv. Part of a series of substantially equal payments over the lifetime of the participant or the joint life of the participant and beneficiary.
 - v. Made after separation from service and attainment of age 55.
 - vi. Made on account of an IRS levy.
 - vii. An amount not in excess of the total medical expenses deductible under IRC §213.
 - viii. Made to an alternate payee pursuant to a QDRO.
 - ix. A corrective distribution, or
 - x. A dividend paid with respect to certain stock held by an ESOP.
- b. Although the Early Withdrawal Penalty does not apply to the following distributions from IRAs, it *DOES APPLY* to distributions from qualified plans.
- i. Made to an unemployed individual for health insurance premiums.
 - ii. Made to a qualified first-time home buyer.
 - iii. Made for qualified higher education.
- c. Age 70 ½ Required Minimum Distribution Excise Tax – 50% of the amount not distributed.
7. Income Tax Withholding – Federal income tax must automatically be withheld from *eligible rollover distributions* from qualified plans.
- 20% of the taxable amount is automatically withheld.
 - Hardship withdrawals are not eligible for rollover and, therefore are not subject to the mandatory withholding.
 - Required minimum distributions at age 70 ½ are not eligible for rollover and are, therefore, not subject to the mandatory withholding.

Classroom Example

Controlled Groups

Which of the following corporations are members of a brother-sister controlled group, assuming none of the individuals are related?

Name	Corporation X	Corporation Y	Corporation Z
Smith	100%	60%	20%
Brown	0%	30%	40%
Green	0%	0%	10%
White	0%	10%	30%

Classroom Example

Minimum Distributions under IRC §401(a)(9)

Determine the 2002 minimum distribution for Smith and the date by which the distribution must be made, based upon the following information.

- Smith's date of birth is November 23, 1931.
- Smith is not married and has no beneficiaries.
- Smith owns 10% of the corporation.
- Smith has the following account balances:

12/31/01	\$200,000
12/31/02	\$220,000

- You are given the following life expectancies:

Age	Uniform Lifetime Table
70	27.4 Years
71	22.9 Years

Classroom Example

Top Heavy

Background Information:

Determine who are the key employees and whether the plan is top heavy for the calendar year 2002.

- The employees listed in the table are the only employees of the employer.
- All employees received a 5% salary increase in 2002.
- The only plan maintained by the employer is a profit sharing plan.
- Only participant A has been a key employee before 2002.

Participant	2001 Salary	Ownership	Officer	12/31/01 Account	12/31/02 Account
A	\$180,000	80%	Yes	\$80,000	\$100,000
B	\$160,000	½%	No	\$60,000	\$70,000
C	\$155,000	13%	No	\$50,000	\$60,000
D	\$70,000	0%	Yes	\$20,000	\$25,000
E	\$50,000	1 ½%	No	\$15,000	\$18,000
F	\$25,000	5%	Yes	\$2,000	\$5,000

Question 1.

All of the following statements regarding top heavy plans are **TRUE, EXCEPT:**

- A. For plan years beginning after December 31, 2001, the top ten owner test is eliminated.
- B. Employee voluntary after-tax contributions are considered in the determination of whether a plan is top heavy.
- C. The rules for determining a participant's years of service for vesting are the same for non-top heavy plans and top heavy plans.
- D. All employers of a controlled group are considered in determining key employees.
- E. A terminated plan is always disregarded for purposes of determining whether another plan is top heavy.

Question 2.

Which of the following plans are part of a required aggregation group for purposes of determining top heavy status?

- Each plan satisfies the coverage requirements of IRC §410(b) by passing the ratio percentage test on its own.
- I. ABC Corporation Salaried Employees Profit Sharing Plan in which A, the 100% owner, participates.
 - II. ABC Corporation Defined Benefit Plan which covers only its union employees and no key employees.
 - III. ABC Corporation Salaried Employees Money Purchase Plan which terminated two years ago in which A was a participant.
- A. I only
 - B. II only
 - C. III only
 - D. I & III only
 - E. I, II & III

Question 3.

Based upon the following data, who are the key employees for determining the top heavy status of a plan for the year ending December 31, 2001?

Name	2000 Salary	Ownership	Officer
Smith	\$130,000	98%	Yes
Brown	\$100,000	0%	Yes
Green	\$80,000	1.75%	No
White	\$70,000	.25%	No
Jones	\$40,000	0%	No

- There are no other active employees of the employer.
 - There are no other plans sponsored by the employer.
 - None of the employees are related.
 - Only Smith was a key employee before 2000
- A. Smith only.
- B. Smith & Brown
- C. Smith, Brown & Green
- D. Smith, Green & White
- E. Smith, Brown Green & White

Question 4.

Which of the following statements regarding death benefits from a qualified plan is/are **TRUE**?

- I. All defined contribution plans must have a pre-retirement death benefit at least equal to the participant's vested account balance.
 - II. A participant needs to obtain his new spouse's consent if he designates the children of his first marriage as beneficiaries of his retirement benefits.
 - III. Death benefits paid from a qualified plan are distributed to the beneficiary income tax free.
-
- A. I only
 - B. II only
 - C. III only
 - D. I & II only
 - E. I, II & III

Question 5.

Which of the following plans must provide a qualified joint and survivor annuity (QJSA) for married participants?

- I. Defined benefit plans.
 - II. Target benefit plans.
 - III. Profit sharing plans that only provide lump sum distributions.
-
- A. I only
 - B. III only
 - C. I & II only
 - D. II & III only
 - E. I, II & III

Question 6.

All of the following distributions are exempt from the 10% early distribution tax, **EXCEPT:**

- A. A distribution made on account of the participant's death.
- B. A distribution made to an alternate payee under a QDRO.
- C. A distribution made to a 55 year old participant upon separation from service.
- D. A hardship distribution to prevent foreclosure on a participant's principal residence.
- E. A distribution due to disability.

Part X

Fiduciary Responsibility

A qualified plan must provide for one or more Named Fiduciaries; however, the actions or responsibilities of an individual could make them a fiduciary without being named as such.

The following actions would cause an individual to be deemed a fiduciary:

1. rendering investment advice with respect to plan funds for a fee,
2. having discretionary authority or responsibility over the administration of the plan,
3. exercising discretionary authority over the management or disposition of the plan's assets, or
4. exercising discretionary authority over the management of the plan.

Fiduciaries must carry out their responsibilities in accordance with the plan document. Three general rules that must be followed are:

1. Exclusive Purpose Rule – Fiduciaries must discharge their duties for the exclusive purpose of providing plan benefits and not for their own benefit.
2. Prudence Rule – Fiduciaries must carry out all duties with the care and skill that a prudent person in a like capacity and familiar with such matters would use.
3. Diversification Rule – Fiduciaries must diversify plan investments to minimize risk.

Fiduciaries may be held personally liable for any breach of responsibilities as well as be subject to sanctions such as excise taxes, removal as plan fiduciary, or even criminal sanctions. Although liability cannot be limited through plan document language, it can be somewhat limited by:

1. Purchasing insurance to protect the plan from losses resulting from a breach in fiduciary duty.
2. Allowing participant directed-accounts under ERISA §404(c).
3. Dividing responsibilities with co-fiduciaries; however, would not be protected if
 - Also participated in the breach
 - Knew of breach and failed to notify plan sponsor and DOL, file a lawsuit on behalf of plan participants, or attempt to correct the breach

Part XI

Prohibited Transactions

Plan Fiduciaries cannot receive money in connection with plan transactions or deal with the assets of the plan on their own behalf. They cannot act on behalf of a party whose interests are adverse to the interests of the plan.

In addition, the plan cannot enter into certain transactions with a party in interest or disqualified person:

1. Sale, exchange, lease of any property
2. Lending of money or other extension of credit
3. Furnishing of goods, services or facilities
4. Transfer to or use of plan assets;
5. Acquisition of qualifying employer securities and real property in excess of allowable limits.
6. Failure to timely deposit employee contributions
 - DOL requires deposits as soon as they can be segregated from the employer's general assets, but in no case later than the 15th business day of the month following the month in which they were withheld from the employee's check.

If the plan engages in a prohibited transaction, the IRS will impose a nondeductible tax of 15% of the amount involved. An additional 100% tax may be imposed if the transaction is not corrected in a timely manner.

1. The plan is not disqualified unless the prohibited transaction violates a qualification requirement.
2. The penalty does not relieve a party in interest from the obligation of correcting the prohibited transaction.
3. The tax is payable on IRS form 5330.

Individual requests can be made to the Department of Labor for a prohibited transaction exemption. Additionally, ERISA §408(b) and IRC §4975(d) list prohibited transaction exemptions, some of which are listed below:

1. The furnishing of office space and services for reasonable compensation,
2. Investment of not more than 10 percent of the fair market value of plan assets in a non-individual account plan in qualifying employer securities or real property,
3. Investment of plan assets in a bank or similar financial institution when the bank or institution is a fiduciary,
4. Loans to a leveraged ESOP,
5. Participant Loans.
 - Must bear a reasonable rate of interest

- Must be adequately secured
- Must not exceed the statutory limit
- Generally must be repaid within 5 years
- Payment must be levelly amortized and at least quarterly
- Interest only deductible if loan is not to a key employee, is otherwise deductible (such as a home loan actually secured by the home), and is not secured by 401(k) elective deferrals.

Part XII

Reporting Requirements

IRS Reporting Requirements:

1. Form 1099R – Distributions from Pensions, Annuities, Retirement or Profit Sharing Plans, IRAs, Insurance Contracts, etc.
 - Must be given to participant by January 31st of year following year of distribution.
 - Must be filed with IRS by last day of February of year following year of distribution
 - Used to report lump-sum distributions, periodic payments of \$10 or more and PS-58 costs.
2. Form 945 – Annual Return of Withholding of Federal Income Tax
 - Generally, must be filed with IRS by January 31st of year following year of distributions.
 - Reports income tax withholding from any non-payroll payments, such as the mandatory 20% withholding on eligible rollover distributions.
3. Form 5330 – Return of Excise Taxes
 - Due date depends on the reason for filing
 - Used to report and pay taxes for prohibited transactions, excess contributions, nondeductible employer contributions, failure to meet minimum funding standards, and reversion of plan assets to the employer.
4. Form 5310-A – Notice of Merger, Consolidation or Transfer of Plan Assets or Liabilities
 - Required to be filed 30 days in advance of only certain mergers or consolidations of plan assets with another plan.
 - Also used to notify the IRS if an employer is electing to be treated as a qualified separate line of business.

DOL Reporting Requirements:

The Form 5500 Series is filed with both the DOL and the IRS. It is actually filed with the DOL and the DOL sends a copy to the IRS.

1. Form 5500-EZ, Annual Return of One-Participant Pension Benefit Plan
 - Filed for plans covering only owners, partners and their spouses.
 - Only must be filed for years in which plan assets exceed \$100,000 and for the final year plan is in operation (regardless of assets).
2. Form 5500, Annual Return/Report of Employee Benefit Plan
 - Filed for plans with two or more participants.
 - One or more schedules may need to also be filed based on whether the plan is a “large plan filer” or small plan filer”

A large plan filer is a plan that covers 100 or more participants at the beginning of the plan year.

A small plan filer is a plan that covers less than 100 participants at the beginning of the plan year.

Schedules:

Schedule A – Insurance Information

Schedule B – Actuarial Information

Schedule C – Service Provider Information, This schedule only applies to large plan filers. It contains a list of terminated actuaries and accountants as well as fees paid to service providers.

Schedule D – DFE/Participating Plan Information, This schedule is filed by Direct Filing Entities (DFEs) and all plans that participate in DFE assets. DFEs are Master Trust Investment Accounts, Pooled Separate Accounts, Common/Collective Trusts, 103-12 Investment Entities, and Group Insurance Arrangements.

Schedule E – ESOP Annual Information, This schedule contains stock type, loan and dividend information for ESOPs.

Schedule F – Fringe benefit Plan Annual Information Return, This schedule is no longer required after 4/1/02.

Schedule G – Financial Transaction Schedules, This schedule only applies to large plan filers. It reports any loans, fixed income obligations or leases in default or classified as uncollectible.

Schedule H – Financial Information – This schedule only applies to large plans filers.

Schedule I – Financial Information – This schedule only applies to small plan filers.

Schedule P – Annual Return of Fiduciary of Employee Benefit Trust – This schedule starts the statute of limitations under IRC §6501(a). Filing is voluntary.

Schedule R – Retirement Plan Information, This schedule is required for any plan subject to IRC §412 minimum funding requirements and for any plan that had distributions during the year.

Schedule SSA – Annual Registration Statement – This schedule notifies the Social Security Administration of any terminating participants with deferred vested benefits so that these participants can be notified that they have money due when they apply for their Social Security benefits.

Schedule T – Qualified Pension Plan Coverage Information

Audit Report – A written opinion of an independent auditor must be attached for all large plan filers. For plan years beginning after April 17, 2001, small plan filers who do not meet specific exemptions may also be required to attach an audit report.

Due date for filing 5500 Series:

1. 5500 Return must be filed by 7 ½ months after the end of the plan year.
2. A 2 ½ month extension can be granted by filing a Form 5558 with the IRS.
3. If the plan year and corporate fiscal year are the same, an automatic extension to the corporation's extension deadline can be granted by filing a corporate extension.
4. If there is a short plan year, the filing deadline is 7 ½ months after the end of the short plan year.
5. If the plan is terminated, the final 5500 is due 7 ½ months after the final distribution of assets.

Penalties for Non-Compliance:

1. Form 1099R – If the plan fails to furnish a correct statement to a participant, the penalty is \$50 per statement, with a maximum of \$100,000 per year. If the plan fails to file correct information by the due date, a penalty of \$15 to \$50 per day per return is imposed.
2. Form 5330 – Interest is charged on the taxes not paid even if an extension of time is granted to file the form.
3. Form 5310-A – IRS imposes a \$25 a day penalty up to a maximum of \$15,000.
4. Form 5500 – DOL –
 - Can impose a civil penalty of up to \$1,100 per day for failure or refusal to file.
 - Can impose a penalty of up to \$5,000 plus up to one year imprisonment if the plan administrator willfully violates reporting requirements.
 - Can impose a penalty of up to \$10,000 plus up to five years imprisonment if false statements or representations are made or facts are concealed.
5. Form 5500 – IRS –
 - Imposes \$25 per day up to \$15,000 for late filings.

Both DOL and IRS penalties can be reduced if the Delinquent Filer Voluntary Compliance Program (DFVCP) is used.

6. Schedule B – If not filed, the IRS will require that it be filed and can assess a penalty of \$1,000.
7. Schedule SSA – The IRS penalty is \$1 per day, up to a maximum of \$5,000 for each terminated participant required to be, but not reported.

Classroom Example

Participant Loans

What is the maximum amount that Smith can borrow from the plan on December 30, 2002?

Summary of Smith's Existing Loans:

Date of Loan	Amount of Loan	Outstanding Balance on 1/1/02	Outstanding Balance on 7/1/02	Outstanding Balance on 12/31/02
August 1, 2001	8,000	7,000	6,100	5,000
January 1, 2002	10,000		8,500	6,000
July 1, 2002	5,000			4,000

- Smith's vested account balance on December 31, 2002 is \$60,000
- Smith is not a participant in any other plan
- All required loan payments have been made timely

Question 1.

Which of the following is **NOT** a responsibility of a fiduciary?

- A. A fiduciary must follow the terms of the plan document.
- B. A fiduciary must diversify plan investments.
- C. A fiduciary must determine the amount of benefit payable to a retiring participant.
- D. A fiduciary must invest the assets in such a manner as to benefit the plan participants.
- E. A fiduciary must attempt to keep administrative expenses to a minimum.

Question 2.

Provided certain conditions are met, all of the following are statutory exemptions from the prohibited transaction rules, **EXCEPT**:

- A. Services or office space provided for reasonable compensation
- B. A guaranteed loan to a pension plan by a disqualified person
- C. Ancillary services provided by a bank that is also the trustee
- D. The purchase of qualifying employer securities by the plan
- E. Loans made by an employer to an ESOP

Question 3.

All of the following are requirements for a participant loan to be exempt from the prohibited transactions rules, **EXCEPT**:

- A. The loan must be adequately secured.
- B. The loan must bear a reasonable rate of interest.
- C. The loan must be repaid through payroll deduction.
- D. The loan must be made according to specific written procedures.
- E. Loans must be available to all participants on a reasonably equivalent basis.

Question 4.

The excise tax for all of the following are reported on Form 5330, **EXCEPT**:

- A. Failure to meet minimum funding standards in a pension plan.
- B. Engaging in a prohibited transaction.
- C. Reversion of excess assets to the employer.
- D. Nondeductible contributions.
- E. Distributions prior to age 59 ½.