



Agenda

1. Document Failures
2. Notice Failures
3. Missed Deferral Opportunity
4. Funding with Forfeitures (or not)
5. When is testing required
6. Other "watch outs"



Document Failures

- You are either a SH plan or not
 - Cannot condition on giving notice
 - Must be in place for full PY (except first year)
 - First year must be in place by 3 months before end of PY (Oct. 1st for calendar year plans)



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Document Failures

- Current tested 401(k) must be converted as of first day of next PY
- Profit Sharing plan (no deferral feature) can be converted with at least 3 months left in PY



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Document Failures

- So what to do if document does not have proper language?
- EPCRS - VCP



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Document Failures

- What if plan uses all the correct provisions (fully vested contributions at the correct levels, etc.) and even gave notices out, but does not contain actual SH language?
 - Not a SH
 - Will IRS allow amendment to be a SH under VCP?
 - Bob's suggestion – run; not walk – to an ERISA attorney



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IRS Position on Mid-Year Amendments

- Plan provisions that satisfy the safe harbor requirements must be adopted before the first day of the plan year and remain in effect for an entire 12-month plan year
- If plan is amended, then plan will not satisfy the safe harbor rules
- There are limited exceptions



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IRS Position on Mid-Year Amendments

- IRS feels that a mid-year change is only OK if the IRS says you can make it
 - Can a plan sponsor make a change to a provision not reflected in the SH notice?
- Final regulations authorize IRS to issue guidance to allow other mid-year amendments
 - Revenue rulings, notices, announcements, etc.
 - On IRS priority plan - see next slide



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IRS Position on Mid-Year Amendments

- ASPPA GAC has asked that IRS look at items that do not affect SH or the notice first,
- Then look at items that are in notice or may affect SH



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Allowable Changes

- Roth Deferral option
- Roth Conversion option (expired 12/31/14)
- Adding beneficiary events to hardship provisions
- Spousal definition to conform with *Windsor* decision
- Cease or terminate SH
- Change of plan year, so long as preceded by SH PY and followed by 12-month SH



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Allowable Changes (non binding verbal guidance)?????

- Expand coverage to include employees previously not included (so long as existing participants are not affected)
- Change of investment vendor
- A retroactive corrective amendment to address a coverage failure
- Change of trustees



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PPA Restatements

- We are in a restatement period
- Can I restate in middle of year – restatement is retroactive anyway?
 - Yes
 - Issue is what effective date can be used for the restatement
 - If no discretionary changes being made then can have a retroactive effective date of restatement
- **Bob's suggestion** – amend as of 1st day of next PY is always safest approach (1/1/16)



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Impermissible Change

- What happens if an impermissible change is made mid-year?
- Would require VCP
- 3 options:
 - Amendment doesn't affect SH status so no problem
 - Amendment is void and SH status retained
 - Plan is not a SH



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Annual Notice - Content

- SH formula (match or nonelective)
- Other contributions or potential contributions
- Plan to which SH contribution made (if employer sponsors another plan)
- Compensation that may be deferred (type and amount)
- How to make deferral elections
- Periods available to make deferrals
- Vesting and withdrawal provisions of all sources of funds
- How to obtain other plan information



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Documentation and Disclosure

- Annual notice requirement - “reasonable period before each plan year”
- Deemed to be reasonable if distributed 30-90 days prior to plan year (safe harbor period for the Safe Harbor Notice)
- If less than 30 days before plan year still may be okay if it is deemed reasonable under a facts and circumstances test



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Documentation and Disclosure

- Newly Eligible employee – no sooner than 90 days before eligibility date and no later than eligibility date
- For a newly established SH plan, all eligible employees are “newly eligible,” therefore plans can be established during last month of prior year



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Bob's Opinion - FWIW

- Closer to 30 days the better
- 3% nonelective does not really affect deferrals so you have a better argument if this is very close to first day of plan year
- SH match – deferral amounts may be affected so you will want to show IRS if the timing of the distribution of notice affected deferral elections



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Failure to Provide Safe Harbor Notice

- Previously, IRS recommended VCP
- ER unlikely to incur costs of VCP for what it considers a harmless error
- IRS newsletter suggests correction by way of example (Fall 2008)
 - Not official but an indication of what the IRS probably would accept



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Failure To Provide Notice

- BLM maintains safe harbor 401(k) plan with basic safe harbor match
- BLM fails to provide notice to all participants
 - Ann became eligible on 1/1/15
 - In addition to not providing her with the notice, BLM failed to inform her of her right to make elective deferrals
 - Earns \$30,000/year
 - Bob (existing participant) defers at a 2% rate and earns \$50K/year
 - Although BLM did not provide him a notice, he was aware that:
 - he could change his deferral rate, and
 - the plan's matching formula did not change for 2015



Correction Options - SCP

- Ann receives \$1,350 (plus earnings)
 - $50\% \times (3\% \times \$30,000)$ – deferrals
 - $100\% \times \$900$ – match
- No correction for Bob – not affected by failure
- Not guaranteed (facts and circumstances)
- Document determination in case of audit
- Late notice reduces correction
- **Note: see 2015 update to EPCRS for new corrective options that might apply**



Correction Options - VCP

- Sanction payment
- Attorney cost
- Who knows what the correction may be



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Administrative Procedures

- IRS requires the ER to reform its administrative procedures to ensure that future failures do not occur
- For example, the ER could establish a calendar identifying due dates by which it must complete certain plan tasks
- The ER should commit to writing (*e.g.*, memorandum for the file) the reforms it is adopting
- The written description of the implemented changes is particularly important if the ER's correction does not involve a corrective contribution
- The ER also should document why the failure to provide the notice did not affect certain EEs
 - *Comment: IRS examiners are more persuaded by documents created at the time of correction than a verbal explanation given at an audit*



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Safe Harbor Nonelective

- The IRS does not discuss the correction for a plan providing the SH nonelective contribution rather than the SH match
- IRS officials have stated several times that:
 - ER maintaining such a plan probably could correct simply by providing the notice late (even if it were after the beginning of the plan year), and
 - Correcting its administrative procedures to prevent further failures



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Missed Deferral Opportunity

- Missed deferral opportunity = 50% of “missed deferrals”
- “Missed deferrals”
 - For SH match = greater of 3% of compensation or maximum % at which the employer matches at 100%
 - For nonelective = 3% of compensation



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Missed Match Opportunity

- When correcting for a missed deferral opportunity you calculate the match at the total missed amount (not the 50% corrective contribution amount)



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Example: Improper Exclusion

- Bob (NHCE) was improperly excluded from plan during 2014
 - 2014 compensation = \$50,000
- ADP SH plan with basic match (100% on first 3)
- Missed deferral = 3%
- Missed deferral opportunity = \$750 (50% x [3% x \$50,000])
- Missed match = \$1,500 (3% x \$50,000 x 100%)



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Defective Notice

- What if notice was given out timely but was defective
- Presumably same approach as failure to timely provide the notice
 - Is the missing information something that would affect a participant's decision to defer?



Compensation

- Safe harbor contribution must be based on definition of compensation that satisfies IRC §414(s)
- What if definition does not satisfy §414(s) (e.g., if plan excludes bonuses)?
 - Plan is no longer SH and amendment needed to add ADP tests
 - Corrective amendment to use total comp can be made



Creative Plan Design

- Top Heavy Exemption
- Cross-testing
- Maximizing match



Creative Plan Design – Top Heavy Exemption

- Plans that allow only elective deferrals and contributions that satisfy the safe harbor are exempt from TH



Creative Plan Design – Top Heavy Exemption

Exemption does NOT apply if:

- Forfeitures are allocated to the accounts
- Nonelective discretionary contributions are allocated
- Longer eligibility is required for the SH contribution than for elective deferrals



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Creative Plan Design – Top Heavy Exemption

- If the plan is not exempt from TH rules, remember that the SH contributions can be applied to satisfy TH
- Example – if an employee defers 2% and receives a 2% match; then only an additional 1% is needed to satisfy TH



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Creative Plan Design – Cross Testing

- The 3% nonelective may be used to satisfy 401(a)(4) testing.
- It can be applied as part of the Gateway that needs to be satisfied prior to cross-testing
- But watch out for....



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Creative Plan Design – Cross Testing

- Note: that if any nonelective is received; then the total gateway must be satisfied
- So if an employee receives 3% nonelective SH but is not entitled to additional nonelective a problem may occur (see next slide)



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Creative Plan Design – Cross Testing

Example:

- Plan is a 3% nonelective SH plan
- Plan is cross-tested and needs a 5% gateway
- Profit Sharing nonelective is discretionary and subject to 1000 hours or last day rule
- If a participant leaves....must make sure somehow gets the full 5% (document should specify)



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Creative Plan Design – Cross Testing

Triple Duty Nonelectives

- Satisfy SH
- Satisfy TH
- Apply towards Gateway

- Effective use of Employer \$



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Creative Plan Design – Maximizing Match

- Remember the rules
- Still satisfy SH if do not match deferrals in excess of 6% OR make a discretionary match of 4%
- Soooooo....How about an enhanced match of dollar for dollar on the first 4% and an additional match of 1% discretionary on the first 4%.
(Reward those that defer and stay within rules)



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Creative Plan Design – “Triple Stacked Match “

- Basic Match, plus
- Additional Fixed match*
- Additional Discretionary match*

* Note: as long as you do not match on deferrals in excess of 6% or the discretionary match is more than 4% you are good to go



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Creative Plan Design – Employer profile

- Many NHCEs are not deferring – so most employer contributions are directed to HCEs (**but watch out once you commit to match formulas just in case the NHCEs decide to contribute**)
- Employers that may not want to use a cross-tested or permitted disparity plan due to cost of gateway or disparity in age of HCEs



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The QACA

- How it differs from a traditional SH plan
- Auto enroll feature
- Specific range of auto enroll
- SH contributions do not have to be vested immediately but rather after two years of service



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The QACA

- Default contribution % must be uniform, except:
- Varies based on years of service
- Limited by 402(g) - \$18,000
- Suspension due to hardship withdrawal
- Deferral rate effective prior to effective date of QACA is not reduced
- See next slide for specific ranges



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The QACA

- Default deferral 1st period = at least 3% but no more than 10%
- 2nd Period = at least 4% but no more than 10%
- 3rd Period = at least 5% but no more than 10%
- 4th and later periods = at least 6% but no more than 10%
- 1st period can last until end of year following plan entry
- See next slide for example
- Note: Periods do not have to end on last day of PY
- May use anniversary or bonus date



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The QACA

- DoH = 1/16/14
- DOE = 2/01/14
- Calendar year plan

- Initial period may end as late as 12/31/15



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The QACA

- Match

- Dollar for Dollar on the first 1%
- 50 Cents on the Dollar for the next 5%
- Defer 6% = 3.5% Match

- Less expensive per participant but probably have more participants due to automatic enrollment feature



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Funding SH contributions with Forfeitures

- If your document currently says that you can – then you are okay
- If your document is silent – be aware that IRS is auditing and not allowing
- New documents will not allow



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Don't forget to test when...

- There are after-tax contributions (not Roth)
- Match on deferrals in excess of 6%
- Discretionary match greater than 4%
- Higher rate of match for HCEs than NHCEs



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“Watch Outs” for all SH Plans

- SH required to only be given to the NHCEs
- However, need to follow document and accrual requirements
- Example – if calendar year plan states that all participants get the SH, employer cannot decide after the PYE that the HCEs (even the owners) will not get the SH amounts!!!



“Watch Outs” for all SH Plans

- SH nonelective contributions may not be used to satisfy the permitted disparity (SS integration under 401(I))
- If a plan wants to use permitted disparity it must ignore the SH and start the nonelective from scratch
- Not so with cross testing gateways!!



Questions

