THE EMPLOYEE BENEFIT
Forum
current issues in retirement benefit planning

The Paragon Alliance Group LLC
Modeling Excellence In Benefits Solutions

When a Plan Is Top Heavy

SITUATION: Our company has to make an additional contribution to our 401(k) plan for nonkey employees because the plan is considered "top heavy."

QUESTION: How can we avoid having our 401(k) plan classified as top heavy in the future?

ANSWER: Adopting a "safe harbor" plan design is one option you may want to consider. Safe harbor 401(k) plans that meet certain conditions avoid the top-heavy rules *and* annual nondiscrimination testing.

DISCUSSION: Under the tax law, 401(k) and other defined contribution plans generally are considered top heavy when the aggregate value of the accounts of "key employees" as of the last day of the preceding plan year represents more than 60% of the aggregate value of all employee accounts.

For purposes of these rules, key employees include:

- Owners of more than 5% of the business
- Company officers with compensation greater than $170,000 (for 2015; subject to future inflation adjustment)
- Individuals who own more than 1% of the business and earn more than $150,000 a year

Ownership by certain family members and entities is considered in determining whether a participant has a 1% or 5% ownership in the business. Any employee who is not a key employee is a nonkey employee.

When a plan becomes top heavy, the employer sponsoring the plan generally must contribute at least 3% of compensation on behalf of each nonkey employee. All nonkey employees who are participants at the end of the plan year (and haven't separated from service) must receive the minimum contribution. Additionally, the plan must have a minimum vesting schedule. Failure to satisfy these requirements can jeopardize a plan's tax-qualified status.

As noted, a safe harbor 401(k) plan can automatically satisfy the top-heavy plan rules. With a safe harbor plan, the employer is required to make nonelective employer contributions of at least 3% of compensation *or* matching contributions under a specified formula (100% of a participant's deferrals up to 3% of compensation and 50% of deferrals between 3% and 5% of compensation). Only plans that consist solely of elective deferrals and safe harbor employer contributions qualify for the top-heavy exemption.

Ready for RMD Time?

With year-end getting closer, you may want to review your plan's procedures in preparation for making required minimum distributions (RMDs) to retired employees and beneficiaries.

Generally, plans must make RMDs to *retired* participants who have reached age 70½ and to any *current employees* who own 5% or more of the company and are age 70½ or older. (Alternatively, a plan may provide for RMDs to all participants after age 70½, including retirees and current employees regardless of their company ownership status.) RMDs also must be paid to beneficiaries of a deceased employee's qualified plan account.

Under the general rule, retirees and more than 5% owner/employees must take their first RMD by April 1 of the year following the year they turn age 70½. Your plan must make subsequent RMDs by December 31 of each year. Other rules apply to beneficiaries.

Please contact us if you have questions about making your plan's 2015 RMDs.

Supreme Court Confirms Duty To Monitor Investments

Plan sponsors and other fiduciaries will want to take note of a recent U.S. Supreme Court decision, *Tibble v. Edison International*,* in which the Court held that plan fiduciaries have a continuing duty to monitor the investment choices offered in a 401(k) plan.

In *Tibble*, participants in a company's 401(k) plan alleged that the plan fiduciaries had breached their duties by adding to the plan certain mutual funds with unnecessarily high administrative fees. In response, the defendants asserted that any claims related to three of the funds were time-barred because the participants failed to bring their lawsuit within the required time frame after the funds had been added to the plan.

The Court held that under trust law (and therefore ERISA pension law) a "trustee has a continuing duty to monitor trust investments and remove imprudent ones." The Court further held that the *duty to monitor* is separate from the *duty to prudently select* investments, and that for claims based on the former, the statute of limitations runs from the date of the breach, rather than the date of selection.

Though declining to speak further to the specific scope of the defendants' duty to monitor, the Court did state that "under trust law, a fiduciary is required to perform a regular review of its investment with the nature and timing of the review contingent on the circumstances."

As a result, plan fiduciaries may want to establish a procedure to make sure they are regularly reviewing plan investment options, diligently following up on any recommendations, and documenting any actions taken.

* 135 S. Ct. 1823 (2015)

. . . the *duty to monitor* is separate from the *duty to prudently select* investments . . . .

Encouraging Greater Plan Participation

If your work force includes employees who aren't taking full advantage of your 401(k) retirement plan, you may want to look for ways to increase plan participation. Below, we answer some commonly asked questions.

Why is it better to have more employees fully participating in a 401(k) plan? Increasing employee participation can help plans pass nondiscrimination testing. If a plan does not have a 401(k) safe harbor provision, low participation rates among non-highly compensated employees (NHCEs) could cause the plan to fail the actual deferral percentage (ADP) and actual contribution percentage (ACP) tests. Sponsors of plans that fail may have to either make contributions to NHCEs or make corrective distributions from the 401(k) plan to highly compensated employees (HCEs). Neither option is desirable.

Are there any other benefits to increasing employee participation? Yes. Employees who don't take full advantage of a 401(k) plan are at risk of not having enough savings to retire comfortably. Increasing employee participation can help employers make sure their employees are better prepared financially for retirement.

How can employers increase 401(k) plan participation? To increase employee participation, employers can implement plan design changes and provide financial education to employees.

What plan design changes can an employer make to help increase employee participation? Implementing programs such as automatic enrollment, automatic contribution escalation, and matching, as well as instituting a shortened enrollment waiting period, can help increase employee participation in a 401(k) plan.

How does automatic enrollment work? With automatic enrollment, employees are enrolled in the plan at a preset contribution rate. Employees can elect not to contribute or to contribute a different percentage of their pay. Since many employees choose not to opt out of automatic enrollment, automatic enrollment tends to increase participation rates.

Can you explain automatic contribution escalation? Generally, the default deferral rate for 401(k) plans is too low for many employees to accumulate enough money to meet their retirement income needs. With automatic contribution escalation, an employee's deferral rate is gradually increased over time and according to a specified schedule. An employee may opt out of the increases.

How do matching contributions increase participation? When an employer matches all or a percentage of an employee's contribution amount, employees are more motivated to contribute because the employer's contribution is viewed as potentially "free money" for the employee. Though such a program would create a direct expense for the employer, it can be an effective way to increase participation.

What is a shortened enrollment waiting period? Some plans require a new employee to wait a period of time before starting to make deferrals to the 401(k) plan. Shortening or even eliminating this waiting period would make it possible for more employees to become eligible to participate. If employer contributions are not accelerated, employers incur no additional contribution costs with this approach. However, if a company has a high rate of employee turnover, this strategy may result in a high number of 401(k) accounts with small balances, which could increase plan administration costs.

How will providing financial education to employees increase participation? A knowledgeable employee is more likely to understand the value of participating in his or her 401(k) plan. So the education materials should clearly communicate both the importance of saving for retirement and the benefits of participating in a 401(k) plan. Several different types of education materials can be used. Employers also may want to consider providing one-on-one meetings with financial advisors.

Designing retirement plans to meet your business needs…

Combining our knowledge, experience, and integrity with the services of the industry's leading record keepers and investment providers to offer personal, customized plan designs and administration solutions.

The Paragon Alliance Group LLC
Modeling Excellence In Benefits Solutions

300 Harleysville Pike
Souderton, PA 18964

215-703-0844

401(k), 403(b) & 457 Plans	Consulting	Retirement Plan Audits
Profit Sharing Plans Safe Harbor New Comparability	Employee Communications	Payroll
	Plan Administration	Human Resource Consulting
Prevailing Wage Plans	Compliance Services	
Section 125 Cafeteria Plans	Governmental Filings	Strategic Planning

RECENT DEVELOPMENTS
In Benefit Plans

Average Retirement Age. In 2013, the average retirement age was approximately 64 for men and 62 for women, about the same as a decade earlier, according to a report from the Center for Retirement Research at Boston College. The researchers define average retirement age as the age at which the rate of labor force participation drops below 50%.

Automatic Enrollment Error Corrections. The IRS has provided new safe harbor correction methods for errors related to 401(k) plan automatic enrollment (Revenue Procedure 2015-28). Generally, if an employer fails to automatically enroll an employee, the employer will not have to make a qualified nonelective contribution (QNEC) for the missed elective deferrals if the error is detected within 9½ months after the end of the plan year of the failure and certain conditions are met. Correct deferrals must begin no later than the first payment of compensation made on or after the last day of the 9½-month period (or earlier, if the employee notifies the employer of the mistake). Additional requirements and correction methods are also provided in the guidance.

New Lump-sum Prohibition. The IRS is amending the tax law's required minimum distribution regulations to provide that qualified defined benefit plans generally are not permitted to replace any joint and survivor, single life, or other annuity currently being paid with a lump-sum payment or other accelerated form of distribution. With limited exceptions, the amendments apply as of July 9, 2015.