Questions and Answers
Learn about Top-Heavy Plans with ftwilliam.com Industry Experts
Webinar January 29, 2013

Below are written Q&As from our January 29, 2013 webinar. You can find other webinar materials, upcoming webinars and recordings at www.ftwilliam.com/webinars.html. The Q&As listed below are arranged according to topics covered during the webinar

Housekeeping

Q. Do you know if this counts towards CE credits with ASPPA? If so, how do I get a certificate of completion?

A. The webinar was designed to be eligible for 1 ASPPA, NIPA, or ERPA credit. Certificates of attendance will be sent to participants who are logged in to the live webcast. We cannot provide certificates for attendees of the phone-only session or for recorded webcasts.

Q. I do have a PTIN and am interested in receiving credit. How exactly do I do that?

A. If you have not already provided your PTIN, or are not sure, please call us at 1-800-596-0714 to verify.

Q. How do you print the power point?

A. The slides are available at the following link - https://www.ftwilliam.com/Docs/Top_Heavy_Plans_Webinar.pdf.
You can print them by clicking 'File' then 'Print', or from your keyboard 'Ctrl' and 'P'.

The Top-Heavy Test

Q. Are outstanding loan balances included in the market value used in the top-heavy Ratio?

A. Yes. Loans are considered to be plan assets.

Q. Regarding related vs. unrelated rollovers, are the examples spoken of during the webinar available, or analogous examples available? Specifically I'm interested in examples including the closure of, say, a money purchase plan & the employee's decision to roll that money into the company's (or a related company's) 401(k) plan.

A. Some examples of related rollovers would be:

- Where an employer terminates one of its plan, such as a money purchase plan, and some employees elect roll to their accounts over to another plan maintained by that employer.

- Where a plan is frozen and merged into another plan sponsored by the same employer.

- Where an employer acquires the assets of another company, and as part of the sale, the acquirer agrees to allow the account balances of the acquired company's plan be transferred into the acquirer's plan.

A very common example of an unrelated rollover would be where an employee leaves one employer for another employer, and elects to roll his or her account from the prior employer's plan to the new employer's plan. In this case, the rollover will be disregarded by the new employer's plan when determining top-heavy status. However, the prior employer will include the rollover amount for top-heavy purposes for the length of the add-back period we discussed in the webinar.

Q. Regarding the suggestion of including employee deferrals on an accrual basis for the top-heavy test, using the DOL's 'as soon as separation is as administratively feasible', how does the new(er) deposit safe-harbor rule for small plans (7 business days from payday) fit? Soon enough?

A. Unfortunately, we do not know the answer to this. It may be acceptable to use the 7-day threshold, but without any guidance on this issue from the IRS, we cannot confirm that.

Top-Heavy Minimum Contributions

Q. Plan Sponsor has a DB and a DC plan. DB plan excludes Non-Key HCEs. DC plan has no exclusion. TH Min is provided by the DC plan. What should the Non-Key HCEs get for TH Min? 3% or 5%?

A. If a non-key is only participating in the DC plan, then he or she would be entitled to the 3% allocation.

Q. We have a plan that excludes HCEs from the Safe Harbor contribution portion of the plan. Have a non-key HCE and the plan is top-heavy. This non key HCE is also excluded from the Profit Sharing Portion of the plan, but allowed to participate in the deferral portion. Is a top-heavy minimum contribution required for this participant?

A. Yes.

Q. How are frozen plans treated for purposes of the top-heavy rules?

A. For purposes of section 416, a frozen plan is one in which benefit accruals have ceased but all assets have not been distributed to participants or their beneficiaries. Such plans are treated, for purposes of the top-heavy rules, as any non-frozen plan. That is, such plans must provide minimum contributions or benefit accruals, limit the amount of compensation which can be taken into account in providing benefits, and provide top-heavy vesting. Note that a frozen defined contribution plan may not be required to provide additional contributions because of the rule in section 416(c)(2)(B).

Q. An employer sponsors both a DB and DC Plan and the TH minimum is provided in the DC Plan. If the DB Plan accruals are frozen, what is the TH minimum % required in the DC Plan?

A. Frozen plans continue to be subject to the top-heavy rules (typically, top heavy minimum of 5% of compensation is provided by the defined contribution plan - see slide 35).

Q. In a 401(k) plan that provides a safe harbor matching contribution, can that matching contribution be used towards the top-heavy minimum benefit if a profit sharing contribution is made?

A. Yes, the safe harbor match may be used to satisfy the top-heavy requirement.

Q. For 401k SH plans with early eligibility for deferrals, can statutory eligibility be used for determining who is eligible for SH?

A. Safe harbor plans may exclude the otherwise excludable employees from the safe harbor (when drafted that way) but that will not eliminate the need to make the top-heavy minimum contributions to all of those otherwise excludable employees. You may want to look at your plan design to avoid the issue.

Q. Can you touch on the topic of using an additional match above the safe harbor match that has an allocation requirement, thus possibly making top-heavy come into play.

A. If the safe harbor match does not satisfy ACP safe harbor provisions, (e.g. it requires service for an additional match and only satisfies ADP safe harbor), the top-heavy minimum contribution requirements will have to be satisfied. The plan can use the safe harbor match to help satisfy the minimum, but any participant who did not make any deferral will need the full top-heavy minimum, and any participant who did not defer enough to receive the full top-heavy minimum as a safe harbor match, will need to receive an additional contribution until the top-heavy minimum is satisfied. You may want to take another look at that plan design. If there is any chance the plan may become top-heavy, you may find administration much simpler if you satisfy both ADP and ACP safe harbors.

Miscellaneous

Q. On Slide 28, if the former owner is still working does it change anything (even though she is not an owner)?

A. The example provided in slide 28 does not indicate that the former owner terminated employment; nothing changes.

Q. Can you talk about what the determination date is when you add a new DB plan to an existing DC plan? The DC plan began in 2010 say, but the DB plan is new for 2012

A. Unfortunately, the rule on this is not 100% clear. Many practitioners believe the reasonable approach would be to use December 31, 2011 as the determination date for the DC plan, and December 31, 2012 for the new plan.

However, it is our understanding that the IRS informally stated during a conference a few years ago that in this situation only the December 31, 2011 determination date should be used for both plans. At this point, we are under the impression that using approach discussed above instead of the IRS approach is more appropriate. With that said, we do not know whether using that approach would create any issues under audit.

Q. If the DB Plan is a cash balance plan, how is the TH required contribution determined since there is no PVAB?

A. The accrued benefit under a cash balance plan was defined, prior to the PPA, as an annual benefit (generally meaning a single life annuity) commencing at normal retirement age. However, the PPA expressly permits that, for periods after August 17, 2006, the accrued benefit under a cash balance plan (or pension equity plan) may be expressed as the balance of a hypothetical account or the current value of the accumulated percentage of the participant's final average compensation, as well as an annuity payable to the participant at normal retirement age, for purposes of the present value requirements under Code Section 417(e). It would seem that this PPA change should carry over to determining present value for purposes of the top-heavy requirements. Presumably, the actuarial assumptions required under the top-heavy rules, as described in the next paragraph and provided in Treasury regulations written prior to the PPA, could be modified to take this PPA change into account and the Treasury regulations may eventually be revised. Perhaps rules similar to the rules for defined contribution plans, described in Q 12:10, will apply to cash balance plans. In fact, informal IRS guidance does suggest that a cash balance plan can generally define the present value of accrued benefits for participants not yet in receipt of benefits as the value of participants' cash balance accounts for purposes of determining whether the plan is top-heavy. However, this may not be appropriate if a plan provides annuity benefits with non-proportional subsidies. If a plan is amended to apply this basis for determining the present value of accrued benefits for purposes of the top-heavy determination, and this change is expected to eliminate future top-heavy benefit accruals, the plan sponsor may need to issue an ERISA Section 204(h) notice. [2012 Gray Book Q&A 37]

Current Treasury top-heavy regulations provide that the actuarial assumptions used to determine the present value of accrued benefits must be reasonable, but need not relate to the actual plan and investment experience. An interest rate assumption not less than 5 percent, nor greater than 6 percent, is deemed reasonable, but does not have to be used. The actuarial assumptions can be different from those used for minimum funding purposes or determining actuarial equivalence of optional forms of benefit under the plan. Interest and post-retirement mortality assumptions must be used, and pre-retirement and future cost of living increases may be assumed (except for the maximum dollar amount permitted by Code Section 415). Assumptions about future pay increases or withdrawals may not be used. The participant and spouse may be assumed to be the same age for purposes of determining the

present value of a qualified joint-and-survivor annuity (see Q 9:4). The present value should reflect the normal retirement benefit (or benefit at actual age, if later), without regard to pre-retirement death, disability, and post-retirement medical benefits, or subsidized early retirement benefits or benefit

options, unless the plan provides for a non-proportional subsidy. If the plan provides for a non-proportional subsidy, the benefit commencing at the age when the benefit is most valuable must be used. [Treas. Reg. § 1.416-1]

Q. When determining the 2012 top-heavy minimum do you use the key determination based on 2011 or 2012? More specifically: John Smith is an officer and earned $200,000 in 2011. He is considered a key employee for the top-heavy determination date of 12/31/2011. The top-heavy test ran with the determination date of 12/31/2011, and shows that the plan is top-heavy for 2012. John Smith is still an officer for 2012 but his compensation dropped to $100,000 for 2012 making him a former key employee for the 2012 plan year. Knowing that former keys are entitled to a top-heavy minimum and we review 2012 compensation and contribution amounts, is John Smith eligible to receive a top-heavy minimum contribution due to his 2012 former key status? Or is he considered a key employee based on his 2011 key determination and not eligible for a top-heavy minimum contribution? Meaning if you do use the 2012 key employee designation, an employee could be the reason why a plan is top-heavy but actually get a minimum allocation.

A. John Smith would be considered a key employee for the 2012 plan year but not for the 2013 plan year. So his balance would be included in the 2012 test (i.e. as of 12/31/2011) but excluded from the 2013 test (i.e. as of 12/31/2012). He would need to receive a TH minimum contribution in the 2013 plan year.