Employee Benefits for the Closely Held Business

Lisa C. Germano
EMPLOYEE BENEFITS FOR THE
CLOSELY HELD BUSINESS

Presented by:

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I. Overview

A. Closely held businesses often have conflicting objectives: save for retirement and help employees accumulate retirement income but also provide competitive current compensation to employees. Many small businesses have done away with the qualified retirement plan in order to provide better current compensation and benefits. When pressured by employees who want a pre-tax savings vehicle, a 401(k) plan is adopted. Many closely held companies do not know how to leverage a 401(k) plan to their benefit.

B. The nondiscrimination rules have traditionally inhibited differentiation among staff. This outline is a discussion of the advantages of saving through a qualified plan, and general ideas for plan design, emphasizing sophisticated concepts available in qualified plans. The more simple designs contained in the Savings Incentive Match Plans for Employees will not be illustrated except as a comparison to a qualified plan.

II. Introduction

A. Challenging as it is, in order to successfully design a retirement program for small business owners, be sure to put first things first:

1. What are the objectives for the owners: Tax shelter, retirement accumulation, key staff benefits, benefits for long term staff, benefits for all staff, benefits to only maximize the owner?

2. Are there key staff that wish to see a certain plan design, or is there not much interest among key staff in a program?

3. Do key people understand it enough to help you explain it to staff?

4. Do the owners need discretion in contribution level, or are they ready to commit to a contribution each year?

5. Are the owners ready to educate employees as to why they need a retirement plan?

6. How much do the owners want to contribute for everyone? Is the level of contributions of the amount that can sustain the extra expense of a qualified plan or should the design start out to be a SIMPLE creation?
B. Determining the business owner’s needs is often the most overlooked area of retirement planning. Employers install plans designed as someone told them they should be, instead of being educated about the most appropriate plan for their situation.

III. General Planning Differences Between a SIMPLE and a Qualified Plan

Too often, closely held companies are not given the information they need to make a decision. The traditional advice provided by tax advisors has been diluted by product providers who may not understand anything but the product they sell for investment purposes. We call this "in the box design." Often, the sales provider does not understand the technical opportunities. However, as professionals we must explain these concepts to the business owner to ensure an educated decision is made about the plan to be adopted, and why one design is better than another.

A. Why Consider a Qualified Plan?

1. Tax Benefits
   a. tax deduction for contribution
   b. tax deferred growth
   c. some tax advantages on distributions

2. Creditor Protection
   a. protection in bankruptcy
   b. protection from general creditors

3. Protection from the Spending Habits of Plan Participants
   Anti-alienation of plan accounts is a requirement of all qualified plans.

4. Ability to Create Additional Funding Dollars
   As employees leave, either give more to those that remain or reduce the employer's contribution, thus creating more revenue for the owner to share or take home.
B. Why Consider a SIMPLE?

1. Tax benefits as above.

2. Employees do not want to participate at any great rate.

3. Promise from the owner to give employees the right to contribute for themselves, even though the business can not make any contributions.

4. Employees want to have control over distributions and employer does not have paternalistic belief for retirement income.

5. No desire for small business owner to maximize contributions.

IV. Comparison of Defined Contribution vs. Defined Benefit

A. Description of Defined Contribution Plans

Defined contribution plans are characterized by the concept of an individual account for each participant. Just like a bank statement, the account reveals the beginning balance, deposits according to source and distributions.

1. Types of Defined Contribution Plans:
   a. Profit Sharing Plans: allow discretionary employer contributions.
   b. Thrift Plans: allow after-tax employee contributions.
   c. 401(k) Plans: allow before-tax employee contributions, must be part of a profit sharing plan.
   d. Money Purchase Pension: allow greater contributions than profit sharing plans.
   e. Stock Bonus Plans (including ESOPS): allow contributions and payments in the form of employer securities.
   f. Target Benefit Plans: allow age based allocations.
2. Advantages of Defined Contribution Plans

a. Annual contributions are predictable, and easily determined.

b. Easy for participants to understand because they have their own account and can easily see what the value of the account is.

c. May be less expensive to adopt and maintain than a defined benefit plan.

d. Discretionary funding under a profit sharing plan.

e. Participants can direct their own investments.

f. Pretax employee contributions are allowed for profit sharing plans that have a 401(k) feature.

3. Disadvantages of Defined Contribution Plans

a. Employees can access their funds before retirement, and studies show that they do not rollover the distributions to another qualified plan or IRA.

b. Benefits to be received at retirement are unknown, and subject to the risk of the employee's self direction.

c. Employees do not understand the benefits of deferred income.

B. Description of Hybrid Defined Contribution Plans

1. Types of Hybrid Defined Contribution Plans

a. Simplified Employee Pension (SEP)

b. SIMPLE IRA

These two types of plans are IRA based and the employer's contribution is made to employees' IRAs rather than a spendthrift trust fund. These plans are not defined contribution plans because they are not qualified under IRC §401.

c. Defined contribution plans that look like defined benefit plans target benefit plans, age-weighted and cross-tested profit sharing plans.
d. Target benefit plans have been around since the passage of ERISA, and have been the method to weight a defined contribution plan to older participants. However, it is a pension plan, a hybrid between a money purchase pension and a defined benefit plan. It is a defined contribution pension plan in which:

(i) The plan document targets a stated benefit at normal retirement age;

(ii) Employer contributions are made annually to fund the targeted benefit for each participant; and

(iii) The actual benefits provided at retirement or termination of employment are based on the fund balance in the plan, rather than the targeted benefit under the plan.

2. Advantages of Hybrid Defined Contribution Plans

a. Annual contributions are predictable, and easily determined.

b. Easy for participants to understand because they have their own account and can easily see what the value of the account is.

c. May be less expensive to adopt and maintain than a defined benefit plan.

d. Discretionary funding.

e. Participants can direct their own investments.

f. Pretax employee contributions are allowed in SIMPLES.

3. Disadvantages of Hybrid Defined Contribution Plans

a. Employees can access their funds before retirement, and studies show that they do not rollover the distributions to another qualified plan or IRA.

b. Benefits to be received at retirement are unknown, and subject to the risk of the employee's self direction.

c. Employees do not understand the benefits of deferred income.
C. Description of Defined Benefit Pension Plans

Defined benefit pension plans are programs that promise a specific monthly benefit for a participant beginning at a specified retirement age. The plan may also include disability and incidental death benefits. The promised benefit, the benefit that is defined in the plan document based upon a formula applied to the participant’s compensation and/or length of service, is essentially a guaranteed benefit. The plan sponsor, the employer, is guaranteeing this benefit.

Funding is required each year. The amount of the contribution is required to be determined by an actuary, using assumptions mandated by statute. Defined benefit plans, with specific exceptions, including small businesses with no common law employees or professional service entities with less than 25 employees, are required to pay premiums to the PBGC, an agency within the Department of Labor.

1. Advantages of a Defined Benefit Plan

a. Benefits can assist owners who did not have a plan at an early age to make up for lost time because the $40,000 annual addition under a defined contribution plans doesn't allow older participants to accumulate comparable benefits as those available to the younger participants.

b. Funding costs for young employees can be smaller than those required under defined contribution plans.

c. Benefits are typically not available until retirement age.

2. Disadvantages of a Defined Benefit Plan

a. Funding obligations are not predictable, and the employer bears the risk of investment loss by way of increased funding to ensure benefits are available at retirement (subject to substantial owner waiver of benefits at the time of plan termination).

b. Funding is required whether the employer has cash or profits.

c. Funding calculations are complex, and require an enrolled actuary to certify the amount required each year, and this may increase administration fees.
d. Pretax employee contributions are not available.

e. PBGC insurance premiums are an added expense for plans that maintain a benefit for a common law employee.

f. Underfunded plans cannot be terminated without liability to contribute the underfunding, or waivers by substantial owners.

D. Description of Hybrid Defined Benefit Plans

1. Floor Offset Plans

A floor offset plan is a defined contribution plan paired with a defined benefit floor. The defined benefit plan is paired with a defined contribution plan. An employee who leaves employment before retirement age receives the amount in his defined contribution account. An employee who continues to work until retirement receives the greater of the defined contribution accumulation or the promised defined benefit pension.

2. Cash Balance Plan

A cash balance plan is a defined benefit plan in which a separate account is maintained for each participant. Each year, the employer credits a certain percentage of compensation to each employee's account and credits each account with interest at a rate specified in the plan. This concept makes the plan look like a defined contribution plan.

However, these accounts are hypothetical accounts. Thus, because benefits are not based solely on actual contributions and forfeitures allocated to an employee's account and the actual investment experience and expenses of the plan are not allocated to the account, the arrangement is treated as defined benefit plan.

Participants in a cash balance plan may elect to receive their benefits in a lump sum or as an annuity. The amounts to be contributed are actuarially determined to arrive at the contribution level needed to ensure sufficient funds to provide for the benefits promised. If, at retirement, the balance in a participant's hypothetical account is less than the amount promised by the employer, the participant will receive the promised amount. A cash balance plan is covered by PBGC plan termination insurance.
V. The New 401(k) Plan Design

A. Contributions by an employer to an qualified profit sharing plan can be deducted up to 25% of the compensation otherwise paid or accrued during the taxable year to eligible employees or their beneficiaries under the plan. In determining the deduction limit, no more than $200,000 of any one eligible employee’s annual compensation can be taken into account. The new 401(k) plan design incorporates the hybrid method to allocate an employer contribution.

B. If we use the hybrid type of plan to satisfy a design feature to provide minimal contributions to staff, many owners want employees to have the option to contribute for themselves. Plan design is limited by the budget of the employer, the 25% of pay limit under IRC §404 and the applicable nondiscrimination tests for the allocation of employer contribution.

VI. A Quick Review of the 401(k) Rules

A. 401(k) Plans

A 401(k) plan is a profit sharing or stock bonus plan that contains a qualified "cash or deferred arrangement". (Money purchase pension plans also may contain a CODA, if they are a pre-ERISA plan.) The participant may elect to defer income taxation on part of their compensation and have the deferred amounts contributed to their account in the qualified plan. IRC §401(k)(2). Many 401(k) plans match the employees' salary deferrals with employer contributions. Studies have shown that the employer match encourages employee salary deferrals, because only those individuals who defer receive the match.

1. Elective Deferrals Limitations

Salary deferrals from any individual are limited to $11,000 during any calendar year, adjusted annually for changes in the cost of living. This limit includes salary deferrals under SARSEPs and tax-sheltered annuity contracts. IRC §402(g); IRC §401(a)(30).

2. Nondiscrimination Requirements

Every 401(k) plan must be tested to demonstrate that the salary deferrals, matching contributions and any after-tax employer contributions do not discriminate in favor of highly compensated employees. Unless there are no exclusions for eligibility under the 401(k) plan, the group of eligible individuals covered under the 401(k) plan must also satisfy the provisions of IRC §410(b).
3. Employer Helper Contributions to Pass the ADP and ACP Tests

A plan may permit an employer to make helper contributions. These contributions increase salary deferrals for nonhighly compensated employees (QNECs), which increases the average deferral percentage for nonhighly compensated employees or increases the matching contributions (QMACs) for nonhighly compensated employees which increases the average contribution percentage for the nonhighly compensated employees. Qualified Nonelective Contributions (QNECs) and Qualified Matching Contributions (QMACs) are thus able to help the employer satisfy the ADP and ACP tests. Use of these contributions is in lieu or in combination with excess contribution distributions necessary to satisfy the ADP/ACP nondiscrimination tests.

These contributions are made by the employer and are fully vested and subject to the same pre-59½ distribution restrictions that would apply to salary deferrals. Treas. Reg. §1.401(k)-1(g)(13) and §1.401(m)-1(b)(4)(ii)(13).

4. Annual Additions Limit

The maximum "annual additions" (salary deferrals, after-tax employee contributions, employer matching or profit sharing contributions and forfeiture reallocations) for any limitation year for any particular participant cannot exceed the lesser of $40,000 or 100% of compensation. IRC §415(c).

5. Deduction Limit

401(k) arrangements generally must be part of a profit sharing or stock bonus plan, so they are subject to the overall 25% of compensation deduction limitation of IRC §404(a)(3). IRC §401 (k)(2).

6. Deferrals Are Subject to FICA and Medicare Taxes

Salary deferrals are exempt from current federal and most state income taxes but are taxable for FICA (Social Security) and Medicare purposes. IRC §3121(v)(1). QNECs and QMACs are never subject to these payroll taxes nor are profit sharing or match contributions.

7. Restrictions on Distributions

Although a 401(k) plan generally is precluded from making distributions of elective deferrals while participants are still employed or until the employee attains age 59½, certain in-service distributions are permitted.
a. The participant's separation from service, death, disability or attainment of age 59 1/2, if the plan so provides.

b. Upon termination of the plan (as long as there is no successor plan).

c. Corrective distributions.

d. Distributions of elective deferrals to correct an excess annual addition, deferrals in excess of the IRC §402(g) limit, or deferrals that violate the ADP and ACP tests are permitted.

e. Certain financial hardship withdrawals permitted

To qualify as a hardship withdrawal, the requested withdrawal must be on account of the participant's "immediate and heavy financial need" and must be limited to only the amount "necessary to satisfy" such need. Plan documents can be drafted in several ways to handle hardship withdrawals, including the use of certain safe-harbor criteria that will satisfy the foregoing requirements automatically. Treas. Reg. §1.401(k)-1(d)(2).

f. In-service distributions of non-elective contributions

A plan document may permit in-service withdrawals of non-elective profit sharing contributions upon the occurrence of certain stated events, such as after employer contributions have been in the plan for two years.

g. When the plan is terminated, if no "successor" defined contribution plan is established (except an ESOP). Treas. Reg. §1.401(k)-1(d)(3).

h. Sale of 85% of assets to another corporation

A distribution from a 401(k) plan to employees who continue working is permitted when a corporation sells at least 85% of its assets to another corporation if certain conditions are met.

8. Nondiscrimination Tests

401(k) plans must be tested each year to demonstrate that salary deferrals, after-tax employee contributions, matching contributions and profit sharing employer contributions satisfy certain tests for nondiscrimination.
9. Excess Deferrals

Elective deferrals exceeding the annual $11,000 ceiling are called "excess deferrals".

10. The ADP Test

The average deferrals for the HCEs cannot exceed the average for the NHCEs by more than a permitted disparity as set forth in the statute.

Beginning with plan years after 1996, the current year deferrals and compensation for the HCEs are tested against the prior year deferrals and compensation for the NHCEs. That is, unless a sponsor elects to test on a current year basis. After 1997, the ability to change back to prior testing will be limited, based on regulations to be released.

a. Determining the maximum ADP for the HCEs

(i) The actual deferral percentage (ADP) test requires that the average deferral ratio of the group of eligible HCEs either:

(1) is not greater than 125% of the average deferral ratio of the group of NHCEs (the general test), or

(2) does not exceed the average deferral ratio of the group of NHCEs by more than 2 percentage points and is not more than double the average deferral ratio of the group of NHCEs. [IRC §401(k)(3)] (This is called the "alternate test.")

(ii) These limits can be demonstrated in the chart below:

<table>
<thead>
<tr>
<th>Average deferred by NHCEs</th>
<th>Maximum average permitted for the HCEs</th>
</tr>
</thead>
<tbody>
<tr>
<td>0%</td>
<td>0%</td>
</tr>
<tr>
<td>1%</td>
<td>2%</td>
</tr>
<tr>
<td></td>
<td>&quot;2 times&quot; portion of the alternate test is the limiting factor until non-HCE ratio exceeds 2%</td>
</tr>
<tr>
<td>2%</td>
<td>4%</td>
</tr>
<tr>
<td></td>
<td>----</td>
</tr>
<tr>
<td>3%</td>
<td>5%</td>
</tr>
<tr>
<td>4%</td>
<td>6%</td>
</tr>
<tr>
<td>5%</td>
<td>7%</td>
</tr>
<tr>
<td></td>
<td>&quot;2 plus&quot; portion of the alternate test is the limiting factor until non-HCE ratio exceeds 8%</td>
</tr>
<tr>
<td>6%</td>
<td>8%</td>
</tr>
<tr>
<td>7%</td>
<td>9%</td>
</tr>
<tr>
<td>8%</td>
<td>10%</td>
</tr>
<tr>
<td></td>
<td>----</td>
</tr>
<tr>
<td>9%</td>
<td>11.25%</td>
</tr>
<tr>
<td>10%</td>
<td>12.5%</td>
</tr>
<tr>
<td></td>
<td>&quot;1.25 times&quot; test is the limiting factor</td>
</tr>
<tr>
<td>12%</td>
<td>15%</td>
</tr>
</tbody>
</table>
b. Determining the average deferral ratio

(i) A participant's deferral ratio is determined by dividing his or her salary deferrals by his or her compensation. Compensation is generally taxable compensation, as defined under IRC §414(s). But the plan sponsor may elect to add to taxable compensation the salary deferrals (to a 401(k) plan) and salary reduction contributions (to a cafeteria plan) for purposes of calculating the deferral ratio. That is if the document permits it. (Note: this add-back does not currently apply for purposes of the annual additions limit of IRC §415 or the maximum deduction limit of IRC §404.)

(ii) No more than $200,000 in compensation can be counted in determining a deferral ratio. Treas. Reg. §1.401(k)-1(f)(5)(iii).

The ADP test (this was the actual test prior to 1998 and now it is used to determine the amount of deferrals needed to be distributed)

The plan shown below does not pass the ADP test and must be corrected. The plan administrator has distributed the excess contribution.

<table>
<thead>
<tr>
<th>HCEs</th>
<th>Before-Deferral Pay</th>
<th>Average Deferral (i)</th>
<th>Average Percentage</th>
<th>Average For Group &quot;Distributed&quot;</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>$100,000</td>
<td>$6,000</td>
<td>6%</td>
<td>7%</td>
</tr>
<tr>
<td>B</td>
<td>$100,000</td>
<td>$8,000</td>
<td>8%</td>
<td>&lt;2,000&gt;</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>NHCEs</th>
<th>Deferral Pay</th>
<th>Deferral</th>
<th>Percentage</th>
<th>Average For Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>C</td>
<td>$10,000</td>
<td>$300</td>
<td>3%</td>
<td></td>
</tr>
<tr>
<td>D</td>
<td>$10,000</td>
<td>$400</td>
<td>4%</td>
<td>4%</td>
</tr>
<tr>
<td>E</td>
<td>$10,000</td>
<td>$500</td>
<td>5%</td>
<td></td>
</tr>
</tbody>
</table>

deferral ratio = deferral + before-deferral pay.

The ADP test for this example fails because the 7% average for the HCEs exceeds by more than 2% the average for the NHCEs and also exceeds the NHCEs average by more than 125%. A distribution of $2,000 of employee B's deferrals will reduce the average for the HCEs to 6% so the plan will pass the ADP test.
c. Correcting excess contributions

When the plan fails the ADP test, an employer has three options to bring the plan into compliance, as dictated by the plan document:

(i) distribute "excess contributions" to the HCEs,

A plan that fails the ADP test can avoid disqualification by distributing the excess contributions (i.e., part of the salary deferrals) to one or more HCEs (plus income on the excess contributions) by the end of the plan year following the year of deferral.

(1) determining excess contributions

Excess contributions are the amount of deferrals that must be distributed to one or more HCEs to decrease the HCE average deferral ratio to pass the ADP test. The excess amount is determined by applying a leveling procedure to the HCEs. The deferral ratio of the HCE with the highest deferral ratio is reduced until the average deferral ratio for the group of HCEs passes the ADP test or the HCE's deferral percentage becomes equal to the ratio of the HCE who has the second-highest ratio (whichever comes first).

If the ADP test is not passed when that ratio is lowered to the second-highest ratio, the procedure is repeated (lowering the ratio of these two HCEs until it reaches the ratio of the third-highest HCE, etc.), and so on, until the ADP test is passed. This is called leveling the ADP. Treas. Reg. §1.401(k)-1(f)(2).

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**Pre-1997: Testing and correcting the ADP. The ADP test is corrected through a distribution of excess contributions, applying a reduction procedure to two HCEs**

### Highly Compensated Participants

<table>
<thead>
<tr>
<th>Pay</th>
<th>Deferral</th>
<th>%</th>
<th>Distributed Amount</th>
<th>Final Deferred</th>
<th>%</th>
<th>Average For Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>M</td>
<td>$150,000</td>
<td>$9,000</td>
<td>6.00%</td>
<td>$9,000</td>
<td>6.00%</td>
<td></td>
</tr>
<tr>
<td>N</td>
<td>100,000</td>
<td>$8,000</td>
<td>8.00%</td>
<td>&lt;1,500&gt;</td>
<td>6.50%</td>
<td>6.33</td>
</tr>
<tr>
<td>O</td>
<td>80,000</td>
<td>$7,000</td>
<td>8.75%</td>
<td>&lt;1,800&gt;</td>
<td>6.50%</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>$3,300</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Nonhighly Compensated Participants

<table>
<thead>
<tr>
<th>Pay</th>
<th>Deferral</th>
<th>%</th>
<th>Average For Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>P</td>
<td>$20,000</td>
<td>$600</td>
<td>3.00%</td>
</tr>
<tr>
<td>Q</td>
<td>20,000</td>
<td>800</td>
<td>4.00%</td>
</tr>
<tr>
<td>R</td>
<td>20,000</td>
<td>1,200</td>
<td>6.00%</td>
</tr>
</tbody>
</table>

For the 1996 plan year, the amounts determined under the test are distributed as one means to pass the ADP testing. First employee O's deferral is reduced to 8% of pay, then deferrals of both O and N are reduced to 6.5%, when the test is passed.

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(ii) Post-1996 correction method

For plan years after 1996 the amount to be distributed is determined under the rules in effect in 1996. The amount so determined is distributed from the HCEs, starting with the HCEs who have the highest deferral amount, then reducing those deferrals until they equal the next highest deferral amount for an HCE or the amount has been distributed. This leveling process continues until the amount determined in the ADP testing has been distributed.

Post 1996 Corrections

The amount to be distributed follows the procedure in the preceding example. The amounts are actually distributed as shown below:

**Highly Compensated Participants**

<table>
<thead>
<tr>
<th>Pay</th>
<th>Deferral</th>
<th>Actual Distribution</th>
<th>Final Deferral</th>
<th>Distribution Percent</th>
<th>Average For Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>M</td>
<td>$150,000</td>
<td>$9,000</td>
<td>&lt;2,100&gt;</td>
<td>$6,900</td>
<td>4.60%</td>
</tr>
<tr>
<td>N</td>
<td>100,000</td>
<td>$8,000</td>
<td>&lt;1,100&gt;</td>
<td>6,900</td>
<td>6.90%</td>
</tr>
<tr>
<td>O</td>
<td>80,001</td>
<td>$7,000</td>
<td>&lt;100&gt;</td>
<td>6,900</td>
<td>8.62%</td>
</tr>
</tbody>
</table>

**Nonhighly Compensated Participants**

<table>
<thead>
<tr>
<th>Pay</th>
<th>Deferral</th>
<th>Distribution Percent</th>
<th>Average For Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>P</td>
<td>$20,000</td>
<td>$600</td>
<td>3.00%</td>
</tr>
<tr>
<td>Q</td>
<td>20,000</td>
<td>800</td>
<td>4.00%</td>
</tr>
<tr>
<td>R</td>
<td>20,000</td>
<td>1,200</td>
<td>6.00%</td>
</tr>
</tbody>
</table>

The distribution is made first to M to reduce the deferral amount to $8,000, then to M and N to reduce their deferrals to $7,000, then an additional $100 is distributed to M, N and O.

(2) Distribution of income

Income attributable to excess contributions during the plan year in which the excess contributions were made and after plan year-end must be distributed. For the period between year-end and the date of distribution, the document controls whether interest must be distributed. Treas. Reg. §1.401(k)-1(f)(4)(i) and (ii).
(iii) make additional fully vested contributions (QNECs) to the accounts of the NHCEs, or

An employer is permitted to make additional contributions called qualified nonelective contributions (QNECs) to NHCEs in order to increase the average deferral ratio of the group of non-HCEs. This option must be included in the plan document. These contributions must be fully vested at all times and are treated as elective deferrals for the distribution restrictions of IRC §401(k). Generally QNECs are allocated among non-HCEs in proportion to compensation, although a plan could be written in a way that allocated a certain dollar amount per capita.

Pro rata QNECs fix excess contributions

This example applies to post-1996 testing (and corrections made on a current year basis).

Highly Compensated Participants

<table>
<thead>
<tr>
<th>Pay</th>
<th>Deferral</th>
<th>Deferral Percentage</th>
<th>Average For group</th>
</tr>
</thead>
<tbody>
<tr>
<td>I</td>
<td>$100,000</td>
<td>$6,000</td>
<td>6%</td>
</tr>
<tr>
<td>J</td>
<td>$100,000</td>
<td>$8,000</td>
<td>8%</td>
</tr>
</tbody>
</table>

Nonhighly Compensated Participants

<table>
<thead>
<tr>
<th>Pay</th>
<th>Deferral</th>
<th>QNEC</th>
<th>Deferral Percentage</th>
<th>Average For group</th>
</tr>
</thead>
<tbody>
<tr>
<td>K</td>
<td>$20,000</td>
<td>$800</td>
<td>$200</td>
<td>5%</td>
</tr>
<tr>
<td>L</td>
<td>$20,000</td>
<td>$1,600</td>
<td>$200</td>
<td>9%</td>
</tr>
<tr>
<td>M</td>
<td>$1,000</td>
<td>0</td>
<td>$10</td>
<td>1%</td>
</tr>
</tbody>
</table>

Total QNEC = $410

(1) In this example the employer made a QNEC equal to 1% of each NHCE's pay (a total of $410). That contribution raised the average for the NHCEs to 5%, passing the ADP test.
IRS Announcement 93-105 confirms that a plan can provide for QNECs to only be made for a selected group of NHCEs. In the example above, a QNEC of $30 could be given to the lowest paid NHCE, which would raise the average deferral ratio for the NHCEs to 5%—so the test is passed. For employers who wish to minimize the amount of QNECs needed, this technique could be attractive but will require special wording in the plan document.

Selective QNECS to Fix Excess Contributions

This example reflects post-1996 testing and corrections if on a current year basis.

A QNEC is given to the participant with the least pay. (Note: the QNEC cannot cause the annual additions limit of IRC §415(c) to be exceeded as to that participant.)

**Highly Compensated Participants**

<table>
<thead>
<tr>
<th></th>
<th>Pay</th>
<th>Deferral</th>
<th>Deferral Percentage</th>
<th>Average For Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>I</td>
<td>$100,000</td>
<td>$6,000</td>
<td>6%</td>
<td>7%</td>
</tr>
<tr>
<td>J</td>
<td>$100,000</td>
<td>$8,000</td>
<td>8%</td>
<td></td>
</tr>
</tbody>
</table>

**Nonhighly Compensated Participants**

<table>
<thead>
<tr>
<th></th>
<th>Pay</th>
<th>Deferral</th>
<th>QNEC(^1)</th>
<th>Deferral Percentage</th>
<th>Average For Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>K</td>
<td>$20,000</td>
<td>$800</td>
<td>$30</td>
<td>4%</td>
<td></td>
</tr>
<tr>
<td>L</td>
<td>$20,000</td>
<td>$1,600</td>
<td>$30</td>
<td>8%</td>
<td>5%</td>
</tr>
<tr>
<td>M</td>
<td>$1,000</td>
<td>0</td>
<td>$30</td>
<td>3%</td>
<td></td>
</tr>
</tbody>
</table>

Total QNEC = $30

\(^1\) In this example the $30 QNEC raised the NHCEs' average to 5%. Compare the preceding example, in which the required QNEC was $410.

(3) recharacterize the excess contributions as after-tax contributions. Since this is rarely a viable option, we are not illustrating it within this presentation.
B. Top Heavy 401(k) Plans

Top heavy plans must provide a minimum contribution to non-key employees. A plan is top heavy if 60% or more of the total value of the plan is for the accounts of key employees. IRC §416. The minimum contribution is the lesser of 3% of compensation or the largest percent of compensation received by any key employee. For this purpose, any salary deferral by a key employee is treated as an employer contribution, but salary deferrals by non-key employees do not count towards the 3% minimum contribution. As a result, a top-heavy 401(k) plan requires a 3% profit sharing type of contribution by the employer in addition to any matching contributions, unless the 3% minimum is provided under another qualified plan of the employer.

1. A 401(k) plan is permitted to count qualified nonelective contributions in meeting the minimum contribution requirement, even if the QNECs have been used to satisfy the ADP test or ACP test. Treas. Reg. §1.416-1, Q&A M-18. A 401(k) plan can presumably treat QMACs for satisfying the top heavy minimums as EGTRRA specifically was enacted to override Treas. Reg. §1.416-1, Q&A M-19. (See Footnote 10 to the House Committee Report, H.R. Rep. 107-51, pt 1) IRC Section 416.

2. Family Aggregation

Effective in 1997, aggregation of certain family members was repealed. However, important in the analysis for family members is the attribution rules under IRC §318 as it relates to IRC Section 414. Some family members may be considered highly compensated, even though they do not satisfy the definition without the attribution to them.

3. Testing under an alternate definition of compensation

An employer may demonstrate that a 401(k) plan is not discriminatory by calculating the ADP and ACP tests using a definition of compensation that adds back to W-2 income any elective deferrals to the 401(k) plan and any salary reduction contributions to a cafeteria plan. This option should be provided for in the document. Treas. Reg. §1.401(k)-(1)(g)(3)(b).

4. Repeal of Minimum Participation

The minimum participation rules under IRC §401(a)(26), designed to prevent employers from maintaining multiple plans, requiring a plan to benefit the lesser of 50 employees or 40% of all employees was amended to apply only to defined benefit plans, effective for plan years beginning after December 31, 1996.
VII. Allocating Profit Sharing Contributions

A. Plain Vanilla Designs

The two most common methods of allocating employer contributions under a defined contribution plan are *pro rata* and permitted disparity. However, in recent years, there have developed other methods which have become acceptable to use to create a plan design suitable for all employees.

1. *Pro Rata*

Under a *pro rata* formula each participant receives the same percent of current year compensation. For 401(k) plans, the plan states that once an employer decides to make a contribution, it is allocated in the same proportion that an individual’s compensation bears to the total compensation for all eligible participants.

2. Permitted Disparity

The 401(k) plan may provide a formula that favors higher paid employees if it meets the "permitted disparity" rules of IRC §401(l).

Permitted disparity is a benefit or contribution formula comprising two parts: (1) the excess portion (based on compensation above a stated dollar level), and (2) the *pro rata* portion (based on total pay).

B. Cappuccino Sundae Designs

Moving away from plain vanilla, three commonly used profit sharing formulas (which do not allocate contributions merely in proportion to pay) are:

- Age-weighted
- Cross-tested, and
- Uniform point formulas

The first two maximize contributions for older and higher-paid employees. A "safe harbor" uniform point formula cannot, under regulations, produce contributions that are discriminatory in favor of HCEs, but it is useful when desiring to allocate contributions favoring long term employees.

1. Age-weighted

   a. Age-weighted plans allocate contributions on the basis of each participant’s compensation and age. Treas. Reg. §1.401(a)(4).
b. Age-weighted plans were first designed in 1991 as a result of the nondiscrimination regulations which were written to correspond to changes made by the Tax Reform Act of 1986. Those regulations allow each year's contribution for each participant to be tested for nondiscrimination based on the basis of benefits that are projected to be available at retirement age for that participant. The factors used are designed so that each participant has the same projected benefit, as a percentage of current year compensation.

c. Age-weighted plans allow significantly larger contributions for older participants without the need for costly nondiscrimination testing under the IRC §401(a)(4) regulations that apply to formulas that are not part of a safe harbor. The allocation formula in an age-weighted plan is written to produce contributions which always satisfy the IRC §401(a)(4) nondiscrimination rules.

2. Cross-tested

The IRC §401(a)(4) regulations allow other designs, and these allocations are sometimes called "cross-tested plans", "new comparability" or "maximizer" plans. These plans require annual testing using the average benefit percentage test (sometimes called the general test) to demonstrate that the plan is not discriminatory in favor of the HCEs.

The allocation formula for these plans typically divides the participants into two or more groups under the terms of the plan document, with each group allocated a different amount of contribution. Or, some plans use a permitted disparity allocation that does not satisfy IRC §401(l). Treas. Reg. §1.401(a)(4)-8(b)(2)(i)(D).

The regulations allow a discretionary profit sharing plan to be tested for nondiscrimination by comparing projected benefits at retirement age. Prior to the mathematical test, the plan administrator must show that the group of employees benefitting under the plan do not constitute a discriminatory classification of employees.

Generally, testing involves converting each participant's contribution into a projected benefit at retirement. Then the projected benefits are divided by the participant's current compensation to determine the "equivalent benefit accrual ratio" (EBAR). Employees are arranged in descending order based upon their EBARs. The NHCEs with an EBAR equal to or greater than the EBAR for a particular HCE are grouped together. These become "rate groups." Plans are not discriminatory if the percentage of NHCEs benefiting in each rate group divided by the percentage of HCEs in the rate group at least equals the midpoint between the safe and unsafe harbor percentages in Treas. Reg. §1.410(b)-4(c)4. If that test is met for each rate group, all otherwise employees are included in a test to show that the average benefit to the NHCEs is at least 70% of the average benefit provided to the HCEs.
3. Uniform Point Allocation

The nondiscrimination regulations permit a type of age and compensation-weighted formula that allocates contributions according to "points" that are awarded for age, length of service and compensation. This plan must pass a simple averaging test described below. Treas. Reg. §1.401(a)(4)-2(b)(4).

a. Allocation Formula

Contributions are allocated under a point formula in the following manner:

(1) Credited points are defined in the plan based upon a participant’s age, service or compensation. (E.g., 1 point for each year of service, 1 point for every $200 in pay.)

(2) Each year the participants' credited points are determined.

(3) The employer's contribution is allocated to each participant based on the ratio of each participant's points to the total points of all participants for the year.

(4) The average contributions as a percentage of pay for the HCE and NHCEs are compared, in order to be sure the average for the HCEs is not greater than the average percentage for the NHCEs.

Point Allocation Formula

A plan grants 200 points for each year of service and 1 point for each $200 of compensation. (No points are awarded in this plan for a participant's age.) The employer contributes $20,000, to be divided among the participants based on each employee's share of the credited points.

The table shows the total points and contribution allocation granted for each employee.

<table>
<thead>
<tr>
<th>Pay</th>
<th>Age</th>
<th>Years of Service</th>
<th>Points Credited</th>
<th>Allocation of Contribution</th>
<th>Contribution as Percentage of Pay</th>
</tr>
</thead>
<tbody>
<tr>
<td>A 100,000 HCE</td>
<td>51</td>
<td>5</td>
<td>1,500</td>
<td>2,617</td>
<td>2.8%</td>
</tr>
<tr>
<td>B 50,000</td>
<td>42</td>
<td>20</td>
<td>4,250</td>
<td>7,981</td>
<td>15.9%</td>
</tr>
<tr>
<td>C 50,000</td>
<td>35</td>
<td>2</td>
<td>650</td>
<td>1,221</td>
<td>4.1%</td>
</tr>
<tr>
<td>D 30,000</td>
<td>35</td>
<td>10</td>
<td>2,150</td>
<td>4,038</td>
<td>13.5%</td>
</tr>
<tr>
<td>E 20,000</td>
<td>35</td>
<td>10</td>
<td>2,100</td>
<td>3,943</td>
<td>19.7%</td>
</tr>
<tr>
<td>I 230,000</td>
<td>1</td>
<td></td>
<td>10,650</td>
<td>20,000</td>
<td></td>
</tr>
</tbody>
</table>

The point allocations for Employee A and Employee D are shown below:

<table>
<thead>
<tr>
<th>Employee</th>
<th>Compensation</th>
<th>Service</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>500</td>
<td>1,000</td>
<td>1,500</td>
</tr>
<tr>
<td>D</td>
<td>150</td>
<td>2,000</td>
<td>2,150</td>
</tr>
</tbody>
</table>
b. Testing for Average Contribution Percentages

The average contribution percentage for HCEs must be compared to the average contribution percentage for the NHCEs in the following way.

The percentages for the example above are:

Average percentage for HCEs = 2.8%
Average percentage for NHCEs = 13.3%

The plan is not discriminatory, because the average contribution for the HCEs (2.8%) is less than the average contribution (13.3%) for the NHCEs. (Note: this is not the average benefit percentage test; this testing method is only used with a safe harbor point allocation plan.)

VIII. Savings Incentive Match Plan For Employees

A. Beginning in 1997, small employers may establish plans permitting salary reduction contributions, called SIMPLE plans, with some restrictions:

1. contributions are limited to elective contributions and certain matching or \textit{pro rata} employer contributions,

2. only small employers may adopt these plans,

3. no other plan contributions or accrual are permitted,

4. elective contributions are limited to $7,000 during a calendar year,

5. all contributions to an employee's SIMPLE account must be fully vested, and

6. there may generally be no prohibitions imposed by the employer on withdrawals from a SEP or SIMPLE IRA.

B. \textbf{Eligible Employer}: One-hundred or fewer employees earning $5,000 or more in the preceding year. A grace period applies if, after adoption of the SIMPLE, the number of employees exceeds one-hundred. IRC §408(p)(2)(C)(i)(I) and (II).

C. \textbf{Eligible Plan}: A SIMPLE arrangement can be either an employer sponsored IRA or a qualified plan under IRC §401(a).
D. Other requirements for a SIMPLE IRA:

1. SIMPLE IRA distributions

Distributions from an IRA SIMPLE retirement account generally are taxed under the rules applicable to IRAs. Thus, they are includable in income when withdrawn, unless rolled over to another SIMPLE account and under certain circumstances to an IRA. IRC 408(d)(3)(G).

2. A special IRC §72(t) penalty applies. Withdrawals of contributions during the 2-year period beginning on the date the employee first participated in the SIMPLE plan are subject to a 25% early withdrawal tax (rather than 10%). This additional tax only applies to distributions prior to age 59½ in this period; otherwise the existing 10% early withdrawal tax applies. IRC §72(t)(6).

E. Administrative requirements

1. Each "eligible" employee must be permitted to elect, within the 60-day period before the beginning of any year (or the 60-day period before first becoming eligible to participate — the entry date), to participate in the SIMPLE plan (i.e., to make elective deferrals), and to modify any previous elections regarding the amount of contributions. IRC 408(p)(5)(C).

2. Employers are required to contribute the employees' elective deferrals to the employees' SIMPLE accounts within 30-days after the end of the month to which the contributions relate. This differs from rules that apply to 401(k) plans. IRC 408(p)(5)(A)(i).

3. Employees must be allowed to terminate participation in the SIMPLE plan at any time during the year (i.e., to stop making contributions). IRC §408(p)(5)(C).

4. The plan can provide that an employee who terminates participation cannot resume participation until the following year (in manager's report, not in statute). A plan can permit (but is not required to permit) an individual to make other changes to his or her salary reduction contribution election during the year (reduce contributions).

5. The participant must be notified that he or she may have the amounts transferred at no cost to another insurer or custodian. IRC 408(p)(7).

F. A special definition for compensation

Compensation means compensation reported on Form W-2, plus any elective deferrals to a 401(k), 457(b) and 403(b) plan. (Defined under paragraphs (3) and (8) of IRC 6051(a)). IRC 408(p)(6)(A)(i).
G. Special reporting requirements for SIMPLE IRAs

1. Summary description: this report to be given to eligible employers and must state the name and address of the employer and the trustees, the requirements for eligibility, the benefits provided under the arrangement, the time and method of making elections and the procedures for, and effects of, withdrawals (including rollovers). [IRC 408(l)(2)(B).]

2. Account statement: this annual report to be given to eligible employees shall show the amount of contributions made to the plan.

H. Penalties for failure to provide notices

1. An employer is penalized $50 for each day in which one or more employees are not notified of a right to participate in the plan as required by IRC §408(l)(2)(C). IRC 6693(c)(1).

2. Further, a trustee is penalized $50 for each day on which one or more statements as required under IRC §408(l) are not provided. These are the annual statements that notify the participants that contributions were made to the plan. These forms must be distributed by January 31. IRC §6693(c)(2).

3. Finally, a trustee is penalized $50 for each day on which one or more summary statements under IRC §408(1)(2)(B) are not distributed. IRC §6693(c)(2).

I. SIMPLE 401(k) plans

1. A 401(k) meets the safe harbor requirements for a SIMPLE 401(k) plan if:

   a. No other plan contributions: There can be no other contribution or benefit accruals to any other qualified plan for any employee covered under the 401(k) SIMPLE plan. IRC §401(k)(11).

   b. Limit on elective contributions: Employees' elective deferrals are limited to no more than $7,000. IRC §401(k)(11).

   c. Required employer contributions: The employer must either:

      (i) Match employees' elective contributions on a dollar-for-dollar deferral of 3% of compensation. Note: there is no exception as under the SIMPLE IRA's format where the employer can reduce the matching percentage below 3% of compensation.), or

      (ii) Make a 2% of compensation nonelective contribution on behalf of all "eligible employees" with at least $5,000 in compensation.
Employees must be notified of this election prior to the period during which they may elect to make elective contributions to the plan (i.e., more than 60-days prior to the start of the plan year). IRC §401(k)(ll)(B)(ii).

2. Compensation is defined as compensation under IRC §6051(a) reportable wages (i.e., W-2 compensation plus SIMPLE contribution).

J. Special nondiscrimination rules

1. A cash or deferred arrangement (i.e., 401(k) plan), is deemed to satisfy the special nondiscrimination tests applicable to employee elective deferrals and employer matching contributions if the plan satisfies the "contribution requirements" applicable to SIMPLE plans.

2. No top-heavy rules apply for any year for which this safe harbor, the "contribution requirements," is satisfied.

3. The plan is subject to the other qualified plan rules.

4. No other 401(k) contributions: No other contributions may be made to the arrangement, and

5. Full vesting: Employer contributions made under either safe harbor method must be 100% vested.

6. The 100 small employer criteria (plans are limited to employers with 100 or fewer employees $5,000 or more) applies to the prior year to determine eligible employer. IRC §401(k)(11).

K. Advantages to a Simple Plan:

1. A SIMPLE IRA is not subject to the nondiscrimination rules generally applicable to qualified plans (including the top-heavy rules) and have simplified reporting requirements. [IRC 416(g)(4)(G).]

2. SIMPLE IRAs are not limited to the IRC §415(c) annual additions limit, nor the 25% deductible limit imposed on SEPs and profit sharing contributions. IRC 415(c)(1)(A) and IRC 404(m)(2)(B).

3. A special ERISA 404(c) exception applies; the employer appears to be liable for losses in the participant's IRA account unless ERISA 404(c)(2) applies. Title I of ERISA is amended to: (a) provide that only simplified reporting requirements apply to SIMPLE plans, and (b) provide that the employer (and any other plan fiduciary) will not be subject to fiduciary liability resulting from the employee (or beneficiary) exercising control over the assets in the SIMPLE account. [ERISA 404(c)(2).]
L. Disadvantages of SIMPLE Plans:

1. Employers who sponsor SIMPLE plans must (unless certain exceptions apply) make mandatory contributions under either the 401(a) or IRA format. However, these are also the only type of employer contribution that can be made to the plan. One of two contribution requirements must be annually elected by the employer:

   a. Matching contribution formula: Under the matching contribution formula, the employer generally is required to match employee elective contributions on a dollar-for-dollar basis up to 3% of each eligible employee’s compensation. IRC 408(p)(2)(A)(iii) and IRC 408(p)(2)(C)(ii)(I).

   b. Under a special rule, in a SIMPLE IRA, the employer can elect a lower percentage of matching contribution for eligible employees making an elective contribution (but not less than 1% of each employee’s compensation) if employees are notified within a reasonable period of time prior to the 60 day period for electing to make a salary deferral. A lower percentage cannot be elected for more than 2 years out of any 5 consecutive years, even if for the first 2 years. IRC 408(p)(2)(C)(ii)(II), or

   c. Alternate pro rata contribution: For any year, in lieu of making matching contributions, an employer may elect to make 2% of pay as a nonelective contribution on behalf of each eligible employee with at least $5,000 in compensation for such year. This election must be made and communicated to employees prior to the 60 day election period at the start of the year. IRC 408(p)(2)(B)(i).

2. Employees must be included at a greater rate under a SIMPLE IRA, employees who: received at least $5,000 in compensation from the employer during any 2 prior years, and is reasonably expected to receive at least $5,000 in compensation during the plan year. [IRC 408(p)(4)(A).]

   A plan may permit a shorter period or lower dollar amount.

IX. Safe Harbor 401(k) Plans

   A. Safe Harbor ADP/ACP

   In 1999, a new safe harbor for nondiscrimination testing became available. For plan years beginning in 1999, safe harbor alternatives to the ADP test and the employer matching contributions part of the ACP test are available to employers. This means that as long as an employer satisfies the requirements for the safe harbor, the employer does not need to satisfy the ADP and ACP tests. Although the safe harbor is not required, plans that make any type of employer contribution should look at the option for their plan.
An employer can choose to use the safe harbor for one year and choose not to use it for the next year. Use is optional, but a decision whether to use the safe harbor must be made before the plan year begins.

B. Requirements for Using the Safe Harbor

A safe harbor may not be adopted unless the employer provides written notice to each employee eligible to participate in the plan of their rights and obligations under the plan. The notice must be provided within a reasonable period before the plan year, and must be comprehensive and written in a manner calculated to be understood by the average employee eligible to participate in the plan.

C. ADP Alternative Safe Harbor

1. If the employer uses the safe harbor for the ADP test, a plan must make either:

   a. A 3% (three percent) of compensation nonelective contribution for all NHCE eligible to participate in the plan. The contribution must be made even if the employee did not make a salary deferral contribution for that plan year.

      This is 3% of pay for all employees eligible to participate. This safe harbor contribution must be communicated to employees before the end of the year it is offered. However, the election is a year-by-year election. Contributions are 100% vested when made and in return for this contribution, the salary deferrals may be made by highly compensated employees without nondiscrimination testing. This contribution can also be leveraged by the employer and used in nondiscrimination testing for New Comparability and can also satisfy the 3% top heavy requirement if the plan is top heavy.

      or

   a stipulated matching contribution to each NHCE. The matching contribution safe harbor requires an employer to make a matching contribution on behalf of each NHCE who elects to defer salary, of: 100% of the employee's elective contributions, up to 3% of the employee's compensation, and 50% of the employee's elective contributions that exceed 3%, but that are not more than 5%, of the employee's compensation.

2. The safe harbor will not be satisfied if the match rate for highly compensated employees, at any rate of elective contribution, exceeds the match rate for NHCE's.
3. There is an alternative matching contribution option. In the event that the rate of a matching contribution, at any rate of elective contribution, does not meet the specified percentages discussed above, a plan will still satisfy the matching contribution requirement of the safe harbor if:

a. the rate of the employer's matching contribution does not increase as the employee's rate of elective contributions increases and,

b. the aggregate amount of matching contributions, at the rate of elective contribution, at least equals the aggregate amount of matching contributions that would be made if the matching contributions met the percentage rules discussed above.

c. All employer provided matching and nonelective contributions that are used to satisfy the contribution requirements of the safe harbor are nonforfeitable at all times and are subject to the restrictions on distributions from 401(k) plans.

4. Under the safe harbor method for meeting the employer matching contributions part of the ACP test, a plan must:

a. meet the contribution and notice requirements that apply under the ADP safe harbor, and

b. satisfy an additional limitation on matching contributions such that matching contributions on behalf of any employee may not be made with respect to employee contributions or elective deferrals in excess of 6 percent of the employee's compensation. In addition, the rate of an employer's matching contribution may not increase as the rate of an employee's contributions or elective deferrals increases. And the matching contribution for HCEs, at any rate of employee contribution or elective deferral, may not be greater than the match for NHCEs.

F. Other Considerations

After-tax employee contributions must still be tested under the ACP test. Employer matching and nonelective contributions used to satisfy the safe harbor rules for CODAs may not be considered in calculating the ACP test. However, employer matching and nonelective contributions that exceed the amount required to meet the safe harbor rules for CODAs may be considered in applying the ACP test.
Appendix I

Economic Growth and Tax Relief
Reconciliation Act of 2001

Selected Provisions Affecting 2002 Plan Design
For Closely Held Businesses

The Economic Growth and Tax Reconciliation Act of 2001, a/k/a EGTRRA or H.R. 1836, passed Congress on May 26, 2001 and was signed into law by President Bush on June 7, 2001. These statutory provisions are generally effective for years beginning in 2002, except as otherwise noted below. Of particular importance to note is that the entire tax bill, including all pension reform provisions, revert to prior law after December 31, 2010.

A. Limits on Contributions and Benefits

Current Law Limits:

- 401(a)(17): annual compensation limit $170,000.
- 402(g): annual elective deferrals limit $10,500.
- 415(b): maximum annual benefit in a defined benefit plan is the lesser of 100 percent of three-year high salary or $140,000 (or less for pre-65 retirees).
- 415(c): maximum annual defined contribution plan contribution is the lesser of $35,000 or 25 percent of compensation.
- 457(b): annual contribution limit is generally $8,500.
- SIMPLE: annual maximum elective deferral is $6,500.

EGTRRA:

Beginning in 2002, EGTRRA raises all of the significant dollar limits as follows:

- 401(a)(17) compensation limit increased to $200,000; and then indexed in $5000 increments.
- 402(g) annual elective deferral limit increased to $11,000 in 2002; then increased $1,000 each year until $15,000 in 2006; and then indexed in $500 increments.
- 415(b) annual benefit limit to $160,000; and then indexed in $5,000 increments. (this provision applies to plan years ending after December 31, 2001).
• 415(b) DB annual benefit limit will no longer have to be reduced for retirement ages 62 through 65. (this provision applies to years ending after December 31, 2001).

• 415(c) annual contribution limit to $40,000, and then indexed in $1,000 increments.

• 457 annual elective deferral limits to $11,000 in 2000 then increased $1,000 each year until $15,000 in 2006; and then indexed in $500 increments.

• SIMPLE annual elective deferral limit to $7,000 in 2002 then increased $1,000 each year until $10,000 in 2005; and then indexed in $500 increments.

B. Catch-up Contributions for Older Workers

Current Law:

The amount that can be contributed to a defined contribution plan on behalf of an employee for any year is limited. IRC Section 415. There are no separate limits for older workers.

EGTRRA:

In 2002, an employer can choose to allow a participant to make a catch up contribution. Participants who are age 50 or older will be allowed to make an additional contribution to a 401(k), 403(b), or 457 plan equal to $1,000 in 2002, then increased by $1,000 each year until $5,000 in 2006, and beginning in 2007 indexed in $500 increments. The catch-up amount for SIMPLE plans will be one-half of these amounts. However, this amount is by the participant’s compensation for the year, less any other elective deferrals made by the participant during the year.

The catch-up contribution will not be subject to nondiscrimination testing, provided all participating employees over age 50 are eligible to make a catch-up contribution. Also, the catch-up contribution will not count against the employer’s deduction limit under IRC Section 404, or against the participant’s overall $40,000 dollar limit. Act Section 631(a).

C. Definition of Compensation

Current Law:

To determine the maximum contribution limits under IRC Section 415, compensation includes elective deferrals. However, for purposes of the deduction limits under IRC Section 404, compensation does not include elective deferrals.
EGTRRA:

For purposes of the deduction limits under IRC Section 404, the definition of compensation will now include elective deferrals. Act Section 614(a).

D. Deduction Limitations

Current Law:

Contributions to a profit sharing plan in excess of 15 percent of aggregate employees' compensation is not deductible. For a money purchase plan, the deduction limit is 25% of aggregate compensation. IRC Section 404.

EGTRRA:

The deduction limit for profit sharing plans is increased to 25 percent of aggregate employees' compensation. Money purchase plans will also be subject to the 25 percent limit. Act Sections 616 (a)-(c).

E. Increase in 25 Percent of Compensation Limitation

Current Law:

Under IRC Section 415(c), the annual contribution made on behalf of an individual to a defined contribution plan may not exceed the lesser of 25 percent of compensation or $35,000.

EGTRRA:

The 25 percent of compensation limitation has been increased to 100 percent of compensation. The dollar limitation will still apply. The provision also repeals the maximum exclusion allowance applicable to 403(b) plans. Act Section 611(b).

F. Elective Deferrals are Excluded from Deduction Limit

Current Law:

Employer contributions (including employees' elective deferrals which are considered an employer contribution for all purposes of ERISA) to a qualified plan are deductible, subject to certain limits governed by IRC Section 404. If an employer wants to make a 15% of pay contribution and an employee wants to defer, the deferral would not be deductible because the maximum deductible limit is exceeded.
EGTRRA:

Elective deferrals will no longer be considered employer contributions for purposes of the IRC Section 404 limit. Act Section 614(a).

G. Allowable Participant Loans for Small Business Owners

Current Law:

If certain requirements are satisfied, plans may make loans to participants. But, the prohibited transaction rules prevent sole proprietors, partners, and S corporation shareholders from receiving participant loans. IRC 4972.

EGTRRA:

The prohibited transaction rules are modified to allow for participant loans to sole proprietors, partners, and S corporation shareholders. The new law applies prospectively to pre-existing loans. Act Section 612(a).

H. Top Heavy Rules are Modified

Current Law:

A plan is considered "top heavy" if more than 60 percent of plan assets are in the accounts of "key employees." Top-heavy rules affect small businesses. Key employees generally include officers earning over half the Section IRC Section 415 defined benefit plan dollar limit ($70,000 in 2001), 5 percent owners, 1 percent owners earning over $150,000, and the ten employees with the largest ownership interest in the business (as long as they earn more than $30,000). Most insidious, family members of five percent- or- more owners are deemed to be key employees under the separate family attribution rules. Top-heavy plans use specified vesting schedules and must make certain minimum contributions to all non-key employees. IRC Section 416.

EGTRRA:

Thank goodness, the new law helps out small business:

- The definition of "key employee" is modified to delete the "top ten owner" rule, provided that an employee will not be treated as a key employee based on his/her officer status unless the employee earns more than $130,000

- The four-year look-back rule to determine who is a "key employee" is eliminated.

- Matching contributions will now count toward satisfying the top-heavy minimums.
The matching contribution 401(k) plan safe harbor will be deemed to satisfy the top-heavy rules.

The five-year look-back rule applicable to distributions will be shortened to one year. However, the five-year look-back rule will continue to apply to in-service distributions.

A frozen top heavy defined benefit plan will no longer be required to make minimum accruals on behalf of non-key employees. Act Section 613(a)-(d).

I. Tax Credit for New Small Employer Plans

Current Law:

An employer's costs related to the establishment and maintenance of a retirement plan is deductible as business expenses under IRC Section 162. However, there is no tax credit for such expenses.

EGTRRA:

Effective for 2002, small businesses with 100 employees or less who receive at least $5,000 in compensation from the employer during the preceding year will be eligible for an annual tax credit of 50 percent of a maximum of $1,000 in administrative costs for the first three years of a new plan. The credit is available only if at least one nonhighly compensated employee is participating. Act Section 619 (a)-(d).

J. Elimination of IRS User Fee for Certain Determination Letter Applications

Current Law:

Plan sponsors pay a user fee to the IRS in order to obtain a Determination Letter confirming that the written form of their plan is qualified. Revenue Procedure 2001-8.

EGTRRA:

The IRS user fee for a determination letter is waived with respect to any retirement plan maintained by an employer with 100 or less employees. This waiver applies only for applications made by the later of the fifth year of a plan, or the end of any remedial amendment period that began during the first five years (e.g. the current remedial amendment period). Act Section 620.
K. 401(k) Plan Hardship Withdrawals

**Current Law:**

If a 401(k) plan chooses to use the Safe Harbor hardship withdrawal provisions a participant receiving a hardship distribution must be prohibited from making elective contributions to the plan for the twelve months following the date of distribution. Also, although salary deferrals that are distributed in a hardship distribution are not eligible rollover contributions, hardship distributions of matching contributions or profit sharing contributions may be eligible for rollover. Treas. Reg. 1.401(k)-1(d)(2)(iv)(B).

**EGTRRA:**

The Treasury Department is directed to revise its Safe Harbor hardship distribution rules to reduce to six months the period of time participants must be prohibited from making additional elective contributions. Further, all profit sharing plans must be amended to state that hardship withdrawals will not be considered eligible rollover distributions. Act Section 636(a)(1).

L. Roth 401(k) and 403(b) Plans

**Current Law:**

Defined contribution plans are generally allowed to receive after-tax contributions from participants, subject to the nondiscrimination rules of IRC 401(m). Any income on those contributions is subject to income tax when distributed.

**EGTRRA:**

In 2006, 401(k) and 403(b) plans can permit (note: a plan does not have to offer this option) participants to elect tax treatment for their salary deferrals that is similar to Roth IRA contributions. These after-tax contributions are tested along with pre-tax deferrals as part of the ADP test. The 402(g) limit applies to the combined amount of pre-tax and after-tax Roth 401(k) or 403(b) contributions. To track their special tax treatment (all distributions, are exempt from tax), these contributions must be accounted for separately. Further, like Roth IRAs, in order to receive this special tax treatment 5 years must elapse from when a participant first makes a Roth 401(k) or 403(b) contribution to when a distribution is made. Roth 401(k) and 403(b) contributions (and earnings) can be rolled over to a Roth IRA. Act Section 617(a).
M. Faster Vesting of Employer Matching Contributions

Current Law:

Employer matching contributions are subject to two vesting schedules: fully vested after the employee has completed five years of service (five year cliff), or vested in increments of 20 percent for each year, beginning with the third year of service, with full vesting after the employee has completed seven years of service (seven year graded schedule). IRC Section 411(a).

EGTRRA:

Employer matching contributions must be vested under a choice of two reduced schedules: 3 year cliff or 6 year graded vesting schedule, which begins at 20% in the employee's second year of service. Act Section 633(a).

N. Repeal of the Multiple Use Test

Current Law:

Some 401(k) plans must also satisfy an additional nondiscrimination test. The test may apply one year and not the other and is complicated in its application. IRC Section 401(m)(9).

EGTRRA:

The multiple use test is repealed. Act Section 666(a).
### Appendix II

**COMPARISON OF PRETAX SALARY DEFERRAL OPTIONS FOR RETIREMENT SAVINGS**

<table>
<thead>
<tr>
<th></th>
<th>Simple IRA</th>
<th>Safe Harbor 401(k)</th>
<th>Regular 401(k)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Maximum Employer Size</td>
<td>&lt;100 employees with $5,000 or more salary in preceding year</td>
<td>None</td>
<td>None</td>
</tr>
<tr>
<td>Employee Eligibility (max. waiting period)</td>
<td>2 years</td>
<td>1 year</td>
<td>1 year</td>
</tr>
<tr>
<td>Maximum employee deferrals</td>
<td>$7,000 or 100% of compensation</td>
<td>*$11,000 or 100% of compensation</td>
<td>Same as Safe Harbor</td>
</tr>
<tr>
<td>Maximum employer match (in dollars)</td>
<td>$7,000</td>
<td>***4% of Pay</td>
<td>**None</td>
</tr>
<tr>
<td>Maximum employer deduction (in percentage of eligible employee compensation)</td>
<td>No Limit</td>
<td>25%</td>
<td>25%</td>
</tr>
<tr>
<td>Mandatory employer contributions</td>
<td>Yes</td>
<td>Yes</td>
<td>**No</td>
</tr>
<tr>
<td>Discretionary employer PS contributions</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Last day rule available for employer PS contributions</td>
<td>No</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Deadline to establish</td>
<td>10/31</td>
<td>12/1 of PY for 3% of pay or 12/1 of preceding first plan year</td>
<td>Last day of first day of PY for Match SH</td>
</tr>
<tr>
<td>Alternative 1% match available</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Nontaxable loans</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Hardship distributions</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
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<tr>
<td>Penalty for early withdrawal within 2 years</td>
<td>25%</td>
<td>10%</td>
<td>10%</td>
</tr>
<tr>
<td>Penalty for withdrawal after 2 years and before age 59-½</td>
<td>10%</td>
<td>10%</td>
<td>10%</td>
</tr>
<tr>
<td>Nondiscrimination testing for Employer match</td>
<td>No</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Nondiscrimination testing for Salary Deferrals</td>
<td>No</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Top heavy rules apply</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Vesting schedule for Employer Contributions</td>
<td>100%</td>
<td>Varies</td>
<td>Varies</td>
</tr>
<tr>
<td>Subject to claims of creditors</td>
<td>Yes</td>
<td>No</td>
<td>No</td>
</tr>
</tbody>
</table>

* Subject to IRC §415 limit
** No mandatory contributions are required to a regular 401(k) plan if:
1. The 401(k) plan is not top heavy nor part of a required aggregation group that is top heavy; or
2. If the plan is top heavy, no Key Employee defers any compensation, or receives any forfeiture or other employer contribution.

*** The Safe Harbor Match is 100% of Pay up to 3% of pay plus 50% of pay for deferrals above 3% but less than 5% of pay. A plan may have an enhanced matching contributions on behalf of each NHCE who is an eligible employee under a formula that, at any rate of elective contributions, provides an aggregate amount of matching contributions at least equal to the aggregate amount of matching contributions that would have been provided under the basic matching formula. In addition, under an enhanced matching formula, the rate of matching contributions may not increase as an employee's rate of elective contributions increases.
Example One: Comparison of Pre-EGTRRA Profit Sharing Plan to Post-EGTRRA Profit Sharing Plan w/ 401(k) Employer Contribution is 15% of Eligible Compensation

**PLAN YEAR 2001**
**INTEGRATED PROFIT SHARING PLAN**

<table>
<thead>
<tr>
<th>AGE</th>
<th>COMPENSATION</th>
<th>EMPLOYER DISCRETIONARY</th>
<th>% OF TOTAL</th>
<th>ACCUMULATION AT AGE 65 (7%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner</td>
<td>50</td>
<td>$170,000</td>
<td>$27,882</td>
<td>$700,658</td>
</tr>
<tr>
<td></td>
<td>(capped)</td>
<td></td>
<td>55.49%</td>
<td></td>
</tr>
<tr>
<td>Manager</td>
<td>40</td>
<td>$85,000</td>
<td>$11,650</td>
<td></td>
</tr>
<tr>
<td>Staff A</td>
<td>45</td>
<td>$35,000</td>
<td>$4,689</td>
<td></td>
</tr>
<tr>
<td>Staff B</td>
<td>35</td>
<td>$25,000</td>
<td>$3,349</td>
<td></td>
</tr>
<tr>
<td>Staff C</td>
<td>25</td>
<td>$20,000</td>
<td>$2,680</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>$335,000</td>
<td>$50,250</td>
<td></td>
</tr>
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</table>

**PLAN YEAR 2002**
**INTEGRATED PROFIT SHARING PLAN WITH 401(K) OPTION**

<table>
<thead>
<tr>
<th>AGE</th>
<th>COMPENSATION</th>
<th>EMPLOYER DISCRETIONARY</th>
<th>SALARY DEFERRAL</th>
<th>TOTAL CONTRIBUTION</th>
<th>% OF TOTAL</th>
<th>ACCUMULATION AT AGE 65 (7%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner</td>
<td>50</td>
<td>$200,000</td>
<td>$32,938</td>
<td>7061.92*</td>
<td>$40,000</td>
<td>64.71%</td>
</tr>
<tr>
<td></td>
<td>(capped)</td>
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<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>Manager</td>
<td>40</td>
<td>$85,000</td>
<td>$11,364</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Staff A</td>
<td>45</td>
<td>$35,000</td>
<td>$4,571</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Staff B</td>
<td>35</td>
<td>$25,000</td>
<td>$3,265</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Staff C</td>
<td>25</td>
<td>$20,000</td>
<td>$2,612</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>$365,000</td>
<td>$54,750</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

* Subject to Nondiscrimination Test on Salary Deferrals
Example Two: Comparison of Pre-EGTRRA Profit Sharing Plan to Post-EGTRRA Profit Sharing Plan w/ 401(k) - Safe Harbor
Employer Contribution is 3% of Eligible Compensation

### PLAN YEAR 2001
**PROFIT SHARING PLAN**

<table>
<thead>
<tr>
<th>AGE</th>
<th>COMPENSATION</th>
<th>EMPLOYER DISCRETIONARY</th>
<th>% OF TOTAL</th>
<th>ACCUMULATION AT AGE 65 (7%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner</td>
<td>50</td>
<td>$170,000</td>
<td>$5,100</td>
<td>50.75%</td>
</tr>
<tr>
<td>Manager</td>
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<td>$85,000</td>
<td>$2,550</td>
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<tr>
<td>Staff A</td>
<td>45</td>
<td>$35,000</td>
<td>$1,050</td>
<td></td>
</tr>
<tr>
<td>Staff B</td>
<td>35</td>
<td>$25,000</td>
<td>$750</td>
<td></td>
</tr>
<tr>
<td>Staff C</td>
<td>25</td>
<td>$20,000</td>
<td>$600</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>$335,000</td>
<td>$10,050</td>
<td></td>
</tr>
</tbody>
</table>

### PLAN YEAR 2002
**PROFIT SHARING PLAN WITH 401(K) SAFE HARBOR**

<table>
<thead>
<tr>
<th>AGE</th>
<th>COMPENSATION</th>
<th>EMPLOYER SAFE HARBOR</th>
<th>SALARY DEFERRAL</th>
<th>TOTAL CONTRIBUTION</th>
<th>% OF TOTAL</th>
<th>ACCUMULATION AT AGE 65 (7%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner</td>
<td>50</td>
<td>$200,000</td>
<td>$6,000</td>
<td>$11,000</td>
<td>$17,000</td>
<td>77.45%</td>
</tr>
<tr>
<td>Manager</td>
<td>40</td>
<td>$85,000</td>
<td>$2,550</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Staff A</td>
<td>45</td>
<td>$35,000</td>
<td>$1,050</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Staff B</td>
<td>35</td>
<td>$25,000</td>
<td>$750</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Staff C</td>
<td>25</td>
<td>$20,000</td>
<td>$600</td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Total</td>
<td></td>
<td>$365,000</td>
<td>$10,950</td>
<td></td>
<td></td>
<td></td>
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</table>
Example Three: Illustration of New Comparability Allocation Under Final Regulations Effective 01/01/2002

### PLAN YEAR 2001
**NEW COMPARABILITY ALLOCATION BEFORE FINAL REGULATIONS**

<table>
<thead>
<tr>
<th>AGE</th>
<th>COMPENSATION</th>
<th>EMPLOYER DISCRETIONARY</th>
<th>% OF TOTAL</th>
<th>ACCUMULATION AT AGE 65 (7%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner</td>
<td>50</td>
<td>$170,000</td>
<td>$35,000</td>
<td>87.61%</td>
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<tr>
<td>(capped)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Manager</td>
<td>40</td>
<td>$85,000</td>
<td>$2,550</td>
<td></td>
</tr>
<tr>
<td>Staff A</td>
<td>45</td>
<td>$35,000</td>
<td>$1,050</td>
<td></td>
</tr>
<tr>
<td>Staff B</td>
<td>35</td>
<td>$25,000</td>
<td>$750</td>
<td></td>
</tr>
<tr>
<td>Staff C</td>
<td>25</td>
<td>$20,000</td>
<td>$600</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>$335,000</td>
<td>$39,950</td>
<td></td>
</tr>
</tbody>
</table>

### PLAN YEAR 2002
**NEW COMPARABILITY ALLOCATION AFTER FINAL REGULATIONS**

<table>
<thead>
<tr>
<th>AGE</th>
<th>COMPENSATION</th>
<th>EMPLOYER DISCRETIONARY</th>
<th>% OF TOTAL</th>
<th>ACCUMULATION AT AGE 65 (7%)</th>
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</thead>
<tbody>
<tr>
<td>Owner</td>
<td>50</td>
<td>$200,000</td>
<td>$40,000</td>
<td>82.90%</td>
</tr>
<tr>
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<td>Manager</td>
<td>40</td>
<td>$85,000</td>
<td>$4,250</td>
<td></td>
</tr>
<tr>
<td>Staff A</td>
<td>45</td>
<td>$35,000</td>
<td>$1,750</td>
<td></td>
</tr>
<tr>
<td>Staff B</td>
<td>35</td>
<td>$25,000</td>
<td>$1,250</td>
<td></td>
</tr>
<tr>
<td>Staff C</td>
<td>25</td>
<td>$20,000</td>
<td>$1,000</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>$365,000</td>
<td>$48,250</td>
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</table>
Example Four: Illustration of 401(k) Catch-up Provision for 50 year-old
Deferrals Begin at Age 51 for 15 years to Age 65
Interest Assumption is 7%

<table>
<thead>
<tr>
<th>Year</th>
<th>Age</th>
<th>Pre-EGTRRA Maximum</th>
<th>Pre-EGTRRA Accumulation</th>
<th>Post-EGTRRA Maximum</th>
<th>Post-EGTRRA Accumulation</th>
<th>Post-EGTRRA Maximum with Catch-Up</th>
<th>Post-EGTRRA Accumulation with Catch-Up</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>51</td>
<td>$10,500</td>
<td>$10,500</td>
<td>$10,500</td>
<td>$10,500</td>
<td>$10,500</td>
<td>$10,500</td>
</tr>
<tr>
<td>2002</td>
<td>52</td>
<td>$10,500</td>
<td>$21,735</td>
<td>$11,000</td>
<td>$22,235</td>
<td>$12,000</td>
<td>$23,235</td>
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<tr>
<td>2003</td>
<td>53</td>
<td>$10,500</td>
<td>$33,756</td>
<td>$12,000</td>
<td>$35,791</td>
<td>$14,000</td>
<td>$38,861</td>
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<tr>
<td>2004</td>
<td>54</td>
<td>$10,500</td>
<td>$46,619</td>
<td>$13,000</td>
<td>$51,297</td>
<td>$16,000</td>
<td>$57,582</td>
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<tr>
<td>2005</td>
<td>55</td>
<td>$10,500</td>
<td>$60,383</td>
<td>$14,000</td>
<td>$68,888</td>
<td>$18,000</td>
<td>$79,612</td>
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<tr>
<td>2006</td>
<td>56</td>
<td>$10,500</td>
<td>$75,110</td>
<td>$15,000</td>
<td>$88,710</td>
<td>$20,000</td>
<td>$105,185</td>
</tr>
<tr>
<td>2007</td>
<td>57</td>
<td>$10,500</td>
<td>$90,867</td>
<td>$15,000</td>
<td>$109,919</td>
<td>$20,000</td>
<td>$132,548</td>
</tr>
<tr>
<td>2008</td>
<td>58</td>
<td>$10,500</td>
<td>$107,728</td>
<td>$15,000</td>
<td>$132,614</td>
<td>$20,000</td>
<td>$161,827</td>
</tr>
<tr>
<td>2009</td>
<td>59</td>
<td>$10,500</td>
<td>$125,769</td>
<td>$15,000</td>
<td>$156,897</td>
<td>$20,000</td>
<td>$193,155</td>
</tr>
<tr>
<td>2010</td>
<td>60</td>
<td>$10,500</td>
<td>$145,073</td>
<td>$15,000</td>
<td>$182,880</td>
<td>$20,000</td>
<td>$226,675</td>
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<tr>
<td>2011</td>
<td>61</td>
<td>$10,500</td>
<td>$165,728</td>
<td>$15,000</td>
<td>$210,681</td>
<td>$20,000</td>
<td>$262,543</td>
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<tr>
<td>2012</td>
<td>62</td>
<td>$10,500</td>
<td>$187,829</td>
<td>$15,000</td>
<td>$240,429</td>
<td>$20,000</td>
<td>$300,921</td>
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<td>2013</td>
<td>63</td>
<td>$10,500</td>
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<td>$15,000</td>
<td>$272,259</td>
<td>$20,000</td>
<td>$341,985</td>
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<td>2014</td>
<td>64</td>
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<td>$236,780</td>
<td>$15,000</td>
<td>$306,317</td>
<td>$20,000</td>
<td>$385,924</td>
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<tr>
<td>2015</td>
<td>65</td>
<td>$10,500</td>
<td>$263,855</td>
<td>$15,000</td>
<td>$342,759</td>
<td>$20,000</td>
<td>$432,939</td>
</tr>
</tbody>
</table>

$263,855          $342,759          $432,939