The DATAIR News

NEWS FOR THE DATAIR PENSION AND BENEFITS PROFESSIONAL SPRING 2001

FROM THE TOP

By Aaron Venouziou, President

I hope by the time you read this the 2000 5500s will have been approved and PR would be in the mail. Whether it is or not, this will give you an idea of what we have to go through.

Last year we introduced the Pension Reporter for Windows at the same time that the Department of Labor began its EFAST system for the 5500 Forms. With understandable delays for a department of the government that is unfamiliar with these forms, DATAIR was one of the first to receive certification of our printed forms (March 29, 2000) and the first to release an EFAST system.

We knew the 1999 filing year would be a transition, but with only one minor change to the forms for 2000 we expected the new year to be quicker and easier. However, every step along the way the DOL has failed in its promises to expedite the process so that we can get you the forms for you to process simultaneously with your plans. Worse still, the DOL doesn't seem to have an understanding or appreciation for how TPAs, actuaries or consultants go about gathering the data, completing the forms, obtaining signatures, and actually filing the forms.

At first, the DOL didn't intend to provide the software vendors with the EFAST print control needed to produce each form with the encrypted bar code. Last year all vendors were forced to design their systems around this print control, so it appeared that we were going to have to re-write a large amount of the system just so we could print the new forms. After raising our concerns over their changing the rules (which we only found out about by mere coincidence), the DOL relented and indicated they would provide vendors with the source code for the 1999 print control which we would then have to update ourselves for the 2000 forms. A month later, on February 22, at the EFAST developer's conference, they surprised us all and provided us with a beta version of the complete print control for 2000. Promises were made to deliver the final version of the print control and the required test data for certification the following week.

Four weeks later, they delivered the print control and the test data but the test data was wrong.

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DATAIR PROFILE

By Laurie Brophy

This past January marked Charlotte O'Connell's third anniversary with DATAIR as Marketing and Sales Assistant. Charlotte manages the day-to-day leads, establishes an annual advertising budget, tracks and measures the effectiveness of our ads and direct mail promotions, maintains the sales literature, as well as coordinates all trade show-related activities.

Charlotte graduated Cum Laude from North Central College with a degree in Marketing while her children were in school. Shortly after graduation, Charlotte worked as a Marketing Assistant with a subsidiary of Blue Cross/Blue Shield. After gaining some experience in marketing, Charlotte joined Ameritech as a Manager of National Accounts. Having paid her dues with long hours and extensive travel, Charlotte switched gears and opted for a less-stressful position at DATAIR.

Working part-time affords Charlotte the opportunity to volunteer at not-for-profit organizations such as Habitat for Humanity and CASA (Court Appointed Special Advocates), a children's special interest group. Some of her other favorite activities include running, golf, tennis and traveling with her husband, Kevin. Longing for a little sunshine, Charlotte and Kevin recently vacationed in Florida. (And who wouldn't trade a week in Chicago for a day at the beach?!)

What's the best thing about DATAIR, Charlotte? "I enjoy working at DATAIR because it allows me to keep up with things that are happening in the business world."

THE DOPPLER EFFECT

By Gary Ward

Treasury Regulation §1.401(m)-1 (b)(5) allows Qualified Non-Elective Contributions (QNECs) and Elective Contributions (Salary Deferrals) to be included in the calculation of the Actual Contribution Percentage for the non-discrimination test under §401(m) of the Internal Revenue Code (the ACP Test).

"… All or part of the qualified non-elective contributions and elective contributions made with respect to any or all employees who are eligible employees under the plan of the employer being tested may be treated as matching contributions …"

Basically, if the Plan satisfies §401(a)(4), and the plan satisfies the ADP Test, then we can "shift" part of the ADP into the ACP. However, when we shift deferrals into the ACP Test we cannot then include those deferrals in the ADP. This is a fundamental requirement of both tests— what is used in one cannot be also used in the other.

Section 401(k)(3) requires that a cash or deferred arrangement (CODA) satisfy the participation test of §410(b) and that the actual deferral percentage of the highly compensated employees (HCEs) does not exceed the actual deferral percentage of the Non-Highly Compensated Employees (NHCEs) by more than either a multiple of 1.25 (125%) or the lesser of 2 percentage points or a multiple of 2 (2+ / 2x). This is what we refer to as "the greater or the lesser of." The ADP of the HCEs cannot exceed the ADP of the NHCEs by the *greater of* 125% *or the lesser of* 2 plus or 2 times. The 125% test is the primary test. The 2+ / 2x is the alternative test.

The ACP Test is a perfect mirror of the ADP Test. The only differences are the contributions measured, and the participants included. The actual contribution percentage is calculated again for all HCEs and all NHCEs who are eligible to receive the contribution. This is not necessarily all participants who are eligible to defer, but only those who are eligible to receive the match, whether they defer or not.

When both the ADP Test and the ACP Test have to use the alternative limit, an additional test is required that is technically called The Multiple Use of the Alternative Limit Test (MU), or something like that. The MU itself is a combination of the two limits used in each of the individual tests. We add the primary limit for the ADP to the alternative limit for the ACP to come up with one number. Then, we take the primary limit for the ACP and add it to the alternative limit for the ADP to come up with another. The MU maximum is the greater of the two. If we can shift enough of the ADP into the ACP to pass using the primary limit in either test, then we won't be required to run the MU.

It is permissible to reverse the direction of the shift, but certain other requirements must be placed on the matching contributions before they can be included in the ADP. First, they must be 100% fully vested, even for those participants whose matching contribution is zero. After all, we are not shifting dollars when we do this, we are shifting the actual contribution percentage which is a number calculated using the matching contributions for all NHCEs. Therefore, all of the matching contributions must be fully vested. Secondly, and this is more difficult, the distribution requirements that §401(k) imposes on the salary deferrals must also be placed on the matching contributions. This is primarily the hardship withdrawal restriction. It's hard enough to calculate hardship limits for salary deferrals; try tracking matching contributions at the same time.

Though the regulations do not mention any requirement of a written document or election to utilize the principles of shifting. Notice 2000-20 indicates that the requirements for a prototype plan include an election in the adoption agreement that specifies the employer's election. Therefore, before an administrator attempts to shift deferrals into the ACP test, he/she should examine the plan document for any mention of this principle. If no such detail is specified then it could be argued that the option is open to the administrator as an ordinary function of running the tests.

The DATAIR News

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The DATAIR News strives to provide our customers with valuable and enjoyable information about DATAIR software, services, and the pension industry. Reader contributions are welcome.

YOUR CLIENT AND THE NEW 5500 SERIES

By Kristina Kananen, QPA

With the new DOL instructions, now is the time to teach clients responsible signing, dating and mailing of the 5500 series. The first page of the 5500 instructions has a section called "EFAST Processing Tips" which states "To reduce the possibility of correspondence and penalties, we remind filers that:" Based on this wording, if you fail to follow the "tips", you can expect a letter from the DOL and perhaps the rejection of your filing. In other words, do not treat these tips as tips, but as rules. Here are the rules.

"Paper forms must be obtained from the IRS or printed using software from an EFAST-approved software developer."

If the forms you prepared were not obtained from the IRS or an EFAST approved software developer, you are not to file them with the DOL.

"Original forms are preferable. Photocopies may be rejected or cause correspondence requiring additional information."

Keep the original for filing with the DOL (but don't mark it the original). The rule of thumb used to be that you could get away with a first generation copy and copies of copies were not acceptable, but it is apparent that they had a problem last year.

"All information should be in the specific fields or boxes provided on the forms and schedules. Information entered outside of the fields or boxes may not be processed."

Simply said, do not write on the form anywhere other than where the information or answer is supposed to be. Put the footnotes for a given schedule on a plain white sheet referencing the Schedule, repeating A, B, C and D from the Schedule in question and referencing the item number from the schedule. This way the information you feel is important, but outside what the form is asking, will still be scanned into the DOL files.

"Do not use felt tip pens or other writing instruments that can cause signatures or data to bleed through to the other side of the paper. One-sided documents should have no markings on the blank side."

If you file one-sided forms and the signatures bleed through to the other side, expect a letter and a possible rejection of the filing as "do not use" is fairly clear.

"Paper should be clean without glue or other sticky substances."

They are talking about Post-It glue. The "Sign and Date Here" arrow tags go through a transformation when left on forms which are then piled up in Lawrence, Kansas. The glue on the "Sign and Date Here" tags has been known to migrate to the 5500 forms, so the glue remains and jams the scanners. This jamming may have been the reason that Clients received letters from the DOL about incomplete filings.

"Do not staple forms. Use binder clips or other fasteners that do not perforate the paper."

OK, stick with me here. They say "Do not". They mean "Do not". Last year the DOL believed that filers would know that staples could not be used on scanned forms. HA! Little did they know that not only did filers use those really big staples, but some filers (and you know who you are) stapled all pages of a schedule together and then stapled the schedule to the 5500 with the staples being in numerous positions on the forms. Consider the EFAST employee assigned last year to removing all of those staples. This year consider the employee assigned to return stapled forms to your client.

"Do not submit extraneous material or information, such as arrows used to indicate where to sign, notes between preparers, notations on the form, e.g., 'DOL Copy,' etc."

For the fourth time, they are telling us not to write or stamp on the form. Take heed!

"Do not submit unnecessary or blank schedules. Except for certain Schedule SSA filings specifically permitted by the instructions, ..."

If you have indicated on page 3 of the 5500 that a Schedule is attached, attach it. If you don't answer questions on a Schedule, leave the box unchecked on the 5500 and leave the schedule out of the filing.

"Manual entries on the machine print forms are not permitted."

You should gather all information required to complete the forms before you sit down to complete the forms. The days of completing most of a 5500 series and forwarding it to the client for completion are over. You should mail only completed forms to your client for filing.

If you will note, five of the above "tips" contain the word "not". Somehow you are going to have to figure out how to provide the client with the 2000 5500's that are NOT:

- Stapled;
- Festooned with Post-It notes full of instructions;
- Decorated with "Sign and Date Here" tags; or
- Stamped with "DOL Copy".

(Continued on page 4)

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ROUTE TO:

___ _____
___ _____
___ _____
___ _____
___ _____

(**5500 Series**, *continued from page 3*)

And have that client file the appropriate 5500 copy and schedules with the DOL. This is going to take training, responsibility and trust.

A suggestion from an EFAST processing person is that perhaps the easiest approach would be for you to provide the client with a set of 5500's where the schedules are in alphabetical order, with the exception of the signature pages. By putting the signature pages (5500 page 1, Schedule P and Schedule SSA page 1) on top of the set, with the balance of the schedules in alphabetical order, it should be easier to explain in the cover letter which pages require signature. Even though the Schedule P and the first page of the Schedule SSA are out of order, they are easily accessible to the client for signature and can be found without the "Sign and Date Here" tags.

PWBA OPENS THE 5500 HELPLINE

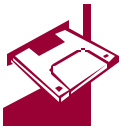
Effective March 1, 2001, 5500 questions can be directed to one toll free number (866/463-3278) which will provide easy access to technical assistance from the PWBA, IRS and the PBGC.

(**From the Top**, *continued from page 1*)

Six weeks later we received a version of the print control that actually corrected the one field that was changed for the 2000 forms. That same day (March 21) we produced and submitted our 2000 forms for certification. Last year it took four days for the DOL to approve the 1999 forms. Four weeks later we are still waiting for approval on the 2000 forms. It is our understanding that all of the people that did the certifications last year have left and they are training new people. To quote the contractor – "Things are going slower than expected."

The DOL promises improvements for next year, but offer no guarantees. We hope that they will learn from their experience. One thing is certain, however – DATAIR remains committed to getting you the forms you need to complete your business as quickly as we possibly can. To keep abreast of the current status on this process, be sure to check our website regularly at www.datair.com.

CURRENT SOFTWARE VERSIONS



PE	Pension Administration	3.13
PR/WIN	Pension Reporter	1.04
RD	Retirement Plan Doc	1.41
CA	Cafeteria Administration	4.53
CD	Cafeteria Plan Document	1.23a
CM	Client & Task Manager	1.03
PA	Plan Accountant	2.03
QP	Qualified Plan Distribution	1.52
FA	FAS 132 Reporting	2.01
PT	Participant Term. Calc	1.50
DE	Data Entry & Review	1.13a
DV	DATAIR Voice	1.02

Safe Harbor 401(k) Plan
Plan Administrator's Summary

(Do not give to Employees)

A Plan satisfies the requirements to be a Safe Harbor 401(k) Plan for any Plan Year only if:

(1) it has been amended to provide for the ADP Test Safe Harbor Contribution, and, if applicable, the ACP Test Safe Harbor Contribution; and,

(2) it meets the Notice Requirements for that particular Plan Year.

AMENDING A PLAN

For any plan year, a plan must be amended to include the Safe Harbor provisions no later than 30 days before the end of the plan year in which it is intended to be a Safe Harbor plan. However, the Notice Requirement must be met no later than 30 days prior to the beginning of the plan year.

For 1999 plan years and 2000 plan years relief was given on the Notice Requirement to allow plan sponsors to amend for Safe Harbor after the plan year had begun, but for the 2001 plan year we have not yet seen any such relief. Therefore, if the sponsor of a 401(k) plan did not give a notice to its employees that it may amend the plan prior to the end of the 2001 plan year for Safe Harbor, it is too late to do so now. You will have to wait until the 2002 plan year. But, plan ahead so that you do not miss the 30-day prerequisite notice for that year.

(*See Converting to a Safe Harbor Mid-Year, page 3*.)

ESTABLISHING A NEW PLAN

A new plan may be established without difficulty as long as the Notice Requirement is met on or before the first day of the new plan's first year. Therefore, the plan is usually established prior to the effective date so that you can prepare and distribute the notice to the employees before they become participants. This is either done by creating a Plan Year that begins on a prospective date (rather than retroactive) or by creating an initial short year. Since most plan sponsors and administrators do not like non-calendar 401(k) plans, the initial short year is more beneficial. However, Notice 98-52 prohibits a plan year shorter than 3 months, unless the plan sponsor is itself a new entity and it establishes the plan as soon as administratively possible following the establishment of itself.

THE SAFE HARBOR PROVISIONS

The ADP Test Safe Harbor is satisfied if the plan provides for the allocation of either an employer non-elective contribution or a matching contribution on behalf of all non-highly compensated employees (NHCEs) who are eligible to defer at any time for the plan year. Highly compensated employees (HCEs) may also share in the allocation. Otherwise excludable employees may be omitted from the allocation. In the case of the non-elective contribution that is not allocated to the HCEs, you may wish to specify that all non-key employees will also share in the allocation. This would allow you to use the non-elective contribution to satisfy the top-heavy minimum allocation.

The ACP Test Safe Harbor is satisfied by definition if the matching contribution option is used to satisfy the ADP Test Safe Harbor. However, if the non-elective contribution option is chosen to satisfy the ADP Test Safe Harbor, a matching contribution may also be made that satisfies the ACP Test Safe Harbor. Though the plan may be intended to satisfy the ADP Test Safe Harbor, it is certainly not prohibited from making a matching contribution that does not satisfy the ACP Test Safe Harbor. In this situation the ACP Test is still required, and, as it currently stands, so is the Multiple Use.

THE ADP TEST SAFE HARBOR

The ADP Test Safe Harbor contribution must be 100% fully vested at all times. It must be allocated to all NHCEs who are eligible to defer. An hours requirement or last day requirement cannot be imposed. The contribution must be either a non-elective contribution or a matching contribution.

The Non-Elective Contribution

The non-elective contribution must be at least 3% of eligible compensation. It is permitted to restrict this to compensation only from date of entry into the plan, but, if your plan is top-heavy, and you wish to use the non-elective contribution to satisfy the top-heavy minimum, you should allocate the non-elective based on gross compensation for the plan year. If a normal employer contribution is being allocated for the plan year, and that contribution is integrated with social security under the rules for permitted disparity, the safe harbor non-elective contribution must be ignored for purposes of that allocation. However, if the normal employer allocation requires a §401(a)(4) General Test, you may use the safe harbor non-elective to help in the calculation of that test but you cannot use any method in the General Test that imputes permitted disparity.

The Matching Contribution

A matching contribution, by definition, is only allocated to participants who defer. The matching contribution must be either a Basic Matching Formula or an Enhanced Matching Formula. The Basic Matching Formula is 100% of salary deferrals up to 3% of compensation, then 50% of the salary deferrals for the next 2% of compensation. The Enhanced Matching Formula must be at least as generous as the Basic and cannot benefit HCEs at a higher level than any NHCE who defers at the same rate. When comparing the Enhanced to the Basic, a participant under the Enhanced must receive a match of at least 3% of compensation if he defers only 3% of compensation. If he defers 4% of compensation, he must receive a match under the Enhanced formula of at least 3.5% of compensation; and if he defers 5% or more he must receive a match of at least 4% of compensation.

Be careful with the Enhanced Formula. If the formula you design recognizes any deferrals that are in excess of 6% of compensation then the ACP Test will be required. Also, if the matching contribution option is being used to satisfy the ADP Test Safe Harbor there can be no other matching contribution in the plan.

THE ACP TEST SAFE HARBOR

A plan cannot satisfy the ACP Test Safe Harbor unless it also satisfies the ADP Test Safe Harbor. A plan that satisfies the ADP Test Safe Harbor by use of the matching contribution option satisfies the ACP Test Safe Harbor by definition, unless there are other employee contributions such as mandatory or voluntary post-tax contributions. If the non-elective contribution option is being used to satisfy the ADP Test Safe Harbor, then a matching contribution may also be allocated. If this matching contribution, together with any other matching contributions in the plan, does not satisfy the ACP Test Safe Harbor requirements, or there are other employee contributions such as mandatory or voluntary post-tax contributions, then the plan must satisfy the ACP Test and Multiple Use.

THE ACP TEST MATCHING CONTRIBUTION

The requirements for the ACP Test Safe Harbor Matching Contribution are the same as for the ADP Test Safe Harbor Matching Contribution with one notable exception and one exciting addition. The exception is that the contribution does not need to be fully vested, but instead may be subjected to a vesting schedule. The addition is that an additional discretionary matching contribution may be allocated that does not exceed 4% of compensation and is allocated only on deferrals that do not exceed 6% of compensation. Therefore, if the non-elective contribution is used to satisfy the ADP Test Safe Harbor, the plan sponsor may also allocate a Basic or Enhanced matching contribution plus a discretionary contribution all of which could satisfy the ACP Test Safe Harbor.

NOTICE REQUIREMENT

The following explanation of the notice requirements for 401(k) Safe Harbor Plans has been taken from section V.C. of Internal Revenue Notice 98-52. All individuals involved in the administration of a 401(k) plan with safe harbor features should read this notice in its entirety.

General Rule

The content requirement for the Safe Harbor Employee Notice required by IRS Notice 98-52, section V.C.1. is satisfied if the notice:

(1) is sufficiently accurate and comprehensive to inform the employee of the employee's rights and obligations under the plan, and
(2) is written in a manner calculated to be understood by the average employee eligible to participate in the plan.

A notice is not considered sufficiently accurate and comprehensive unless the notice accurately describes:

(1) the safe harbor matching or non-elective contribution formula used under the plan (including a description of the levels of matching contributions, if any, available under the plan);
(2) any other contributions under the plan (including the potential for discretionary matching contributions) and the conditions under which such contributions are made;
(3) the plan to which safe harbor contributions will be made (if different than the plan containing the CODA);
(4) the type and amount of compensation that may be deferred under the plan;
(5) how to make cash or deferred elections, including any administrative requirements that apply to such elections;
(6) the periods available under the plan for making cash or deferred elections; and
(7) withdrawal and vesting provisions applicable to contributions under the plan.

Timing Requirement

The timing requirement of IRS Notice 98-52, section V.C.2. is satisfied if the notice is provided within a reasonable period before the beginning of the plan year (or, in the year an employee becomes eligible, within a reasonable period before the employee becomes eligible). The determination of whether a notice satisfies the timing requirement is based on all of the relevant facts and circumstances.

Deemed Satisfaction of Timing Requirement

The timing requirement of section V.C.2. of IRS Notice 98-52 is deemed to be satisfied if at least 30 days (and no more than 90 days) before the beginning of each year, the notice is given to each eligible employee for the plan year. In the case of an employee who does not receive the notice within the period described in the previous sentence because the employee becomes eligible after the 90th day before the beginning of the plan year, the timing requirement is deemed to be satisfied if the notice is provided no more than 90 days before the employee becomes eligible (and no later than the date the employee becomes eligible). Thus, for example, the preceding sentence would apply in the case of any employee eligible for the first plan year under a newly established section 401(k) plan, or would apply in the case of the first plan year in which an employee becomes eligible under an existing 401(k) plan.

CONVERTING TO A SAFE HARBOR MID-YEAR

Notwithstanding section XI.A. of Notice 98-52, a plan that provides that it will satisfy the current year ADP (and, if applicable, ACP) testing method for a plan year may be amended not later than 30 days before the last day of the plan year to specify that the 401(k) safe harbor non-elective contribution method will be used for the plan year (including that the safe harbor non-elective contribution will be made), provided that the plan otherwise satisfies the ADP (and, if applicable, ACP) test safe harbor for the plan year (including the notice requirement under section V.C. of Notice 98-52, as modified by this

notice). For purposes of the preceding sentence, in applying the content requirement of section V.C.1 of Notice 98-52:

(1) Instead of stating the amount of the safe harbor non-elective contribution to be made under the plan, the notice given to eligible employees before the beginning of the plan year must provide that (a) the plan may be amended during the plan year to provide that the employer will make a safe harbor non-elective contribution of at least 3 percent to the plan for the plan year, and (b) if the plan is so amended, a supplemental notice will be given to eligible employees at least 30 days before the last day of the plan year informing them of such an amendment; and,

(2) An additional supplemental notice must be provided to all eligible employees no later than 30 days before the last day of the plan year stating that a 3 percent safe harbor non-elective contribution will be made for the plan year. For administrative convenience, the supplemental notice may be provided separately or as part of the safe harbor notice for the succeeding plan year.

Similar rules apply if, pursuant to section IX.A.1. of Notice 98-52, the safe harbor non-elective contribution is made to another plan of the employer.

RETURNING TO UN-SAFE WATERS MID-YEAR

A plan that uses the 401(k) safe harbor matching contribution method will not fail to satisfy section 401(k) (or section 401(m)) for a plan year merely because the plan is amended during the plan year to reduce or eliminate matching contributions, provided:

(1) A supplemental notice is given to all eligible employees explaining the consequences of the amendment and informing them of the effective date of the reduction or elimination of matching contributions and that they have a reasonable opportunity (including a reasonable period) to change their cash or deferred elections and, if applicable, their employee contribution elections;

(2) The reduction or elimination of matching contributions is effective no earlier than the later of (i) 30 days after eligible employees are given the supplemental notice and (ii) the date the amendment is adopted;

(3) Eligible employees are given a reasonable opportunity (including a reasonable period) prior to the reduction or elimination of matching contributions to change their cash or deferred elections and, if applicable, their employee contribution elections;

(4) The plan is amended to provide that the ADP test and, if applicable, the ACP test will be performed and satisfied for the entire plan year using the current year testing method; and,

(5) All other safe harbor requirements are satisfied through the effective date of the amendment.

TIMING OF CONTRIBUTIONS

In the case of either the non-elective or matching contributions the funding obligation may be met on an on-going basis. With respect to the matching contributions, since there are limitations involved that could fluctuate as deferral elections are changed, the plan may choose to "true-up" the contribution level on either a payroll basis, a monthly basis, quarterly or for the entire year. It is recommended that this "true-up" option be included in the language of the Safe Harbor provisions.

IN CONCLUSION

Everything turns on a fine tight-rope of timing. There is no guarantee that if you miss the timing on as little as one day for as few as a single participant, that the IRS will not expect the plan to satisfy the ADP and/or ACP test for that year. So be careful. Treat the issuance of the Notice with the same diligence you use for the filing of the 5500 – get it done ahead of time if you can. The Notice can be supplied as early as 90 days before the beginning of the next plan year, so you may want to target November 1 for a calendar year plan rather than December 1, just so you can verify that no one slips through the cracks.