

Minimum Coverage Test

Among many other Internal Revenue code requirements, a tax-qualified retirement plan must cover a minimum percentage. The percentage of Non-Highly Compensated Employees (NHCEs, including leased employees) benefiting under the plan must be at least 70% of the percentage of Highly Compensated Employees (HCEs) who benefit under the plan. This is called the Ratio Percentage Test. If a plan does not pass this test, it must pass the more complex Average Benefits Test (ABT). The plan must pass one of these tests on either a daily basis, a quarterly basis, or on an annual basis as of the last day of the plan year. The 401(k) and 401(m) portions of a plan each must meet the minimum coverage requirement on an annual basis as of the last day of the plan year.

This minimum coverage test must also consider employees of the plan sponsor, as well as the employees of companies controlled by, or affiliated with, the plan sponsor.

In general, another company is controlled by the plan sponsor if it is 80 percent or more owned by the sponsor, or 80 percent or more owned by the owners of the sponsor.

Sometimes an employer wishes to exclude certain groups of employees from their qualified retirement plan. They may wish to exclude a certain class of employees, like all hourly employees or all salaried employees. In other instances, the employer may consist of a controlled group of companies and they may wish to include employees from Companies A and C but not Company B.

The minimum coverage tests that determine whether an employer can exclude certain groups of employees are many and varied. To determine if a group can be excluded requires a great deal of information including complete and accurate ownership information and census data.

As a sponsor of your plan, it is your responsibility to provide complete and accurate information, both at the inception of your plan and on an ongoing basis. If there are any changes in your company's structure such as acquisition of a new affiliate, sale of an affiliate, ownership changes, etc., you must notify Executive Benefit Plans immediately so the plan can be tested appropriately.

A plan which does not pass the required minimum coverage tests may be required to make contributions on the behalf of previously excluded employees in order to satisfy the minimum participation requirements.