RETIREMENT PLANNING & EMPLOYEE BENEFITS FOR FINANCIAL PLANNERS
4TH EDITION UPDATES

CHAPTER 3

Example 3.16, page 76

Desk Emporium has the following 10 employees.

EMPLOYEE	SALARY	OWNERSHIP%
A	$200,000	65%
B	$150,000	35%
C	$130,000	-
D-J	$30,000	-

Utilizing the general definition of highly compensated (greater than five percent owner or compensation greater than $105,000 for 2008), employee A and B would be highly compensated because both are greater than five percent owners of Desk Emporium. Employee C would also be considered a highly compensated employee because his salary is in excess of $105,000 for 2008. So, in this example, three of the 10 employees would be considered highly compensated.

If Desk Emporium elected to only count those employees as highly compensated if they were also in the top 20 percent of employees ranked by compensation, only employees A and B would be considered highly compensated. Employee C would not be considered highly compensated because he is not an owner of the company and if ranked by salary, C is not in the top 20 percent. In a company with 10 employees, only the top two ranked by salary would be considered as in the top 20 percent. In this case, employee C is ranked third by salary and is therefore not considered highly compensated. By making the election, Desk Emporium was able to reduce the number of highly compensated employees to two of the 10 employees. In a situation like this, the employer would make the 20% election and reduce the number of highly compensated employees to help pass the coverage tests.

	Desk Emporium Highly Compensated Test			
	General Rule		**20% Election**	
Employee	**> 5% Owner**	**> $105,000 Compensation**	**>5% Owner**	**Top 20% (ranked by compensation)**
A	✓	✓	✓	✓
B	✓	✓	✓	✓
C		✓		
D				
E				
F				
G				
H				
I				
J				

Example 3.44, Page 104

Trinity Audio has employed Ronald for 12 years. Trinity Audio operates a defined benefit plan that provides a benefit to its employees equal to one percent per year of service of the average of employee's three highest consecutive years compensation. Ronald has earned $275,000, $325,000, and $350,000 for the past three years, his highest consecutive years of compensation. The maximum benefit Trinity Audio can provide Ronald with at retirement considering the plan formula and the 2008 covered compensation of $230,000 is $27,600 (1% x 12 x $230,000) annually.

Example 3.46, Page 106

Pretzels, Inc. sponsors a defined contribution plan for its employees. Ashley, a long-term employee, with compensation of $135,000 for 2008, has received a $33,500 profit sharing plan contribution and $2,000 of forfeiture allocations. Ashley could still defer $10,500 ($46,000 - $33,500 - $2,000) in the 401(k) plan to maximize her annual contribution limit of $46,000 for the plan year.

Multiple Choice #10, Page 118

10. WHR, LLC sponsors a defined contribution plan. Vaughn, age 44, has compensation of $150,000 for the year. WHR has made a $15,000 profit sharing plan contribution on Vaughn's behalf and $4,000 of plan forfeitures were allocated to Vaughn's profit sharing plan during the year. How much can Vaughn defer into his CODA plan (401(k)) to maximize his annual contributions to the qualified plan for 2008?

    a. $15,500.
    b. $18,000.
    c. $19,000.
    d. $27,000.

The answer is a.

The annual additions limit permits $46,000 of contributions to be made on Vaughn's behalf to qualified plans for the year. The employee deferral limit is $15,500 for 2008 and is included in the $46,000 calculation. In this problem, Vaughn received a total contribution of $19,000 on his behalf into the plan so his deferral limit is not limited because of the other calculations and Vaughn can defer the maximum, or $15,500, to the plan for 2008. Vaughn's employer could match up to an additional $10,500 and still satisfy the annual additions limit.

Multiple Choice #11, Page 118

11. SJ, Inc. covered the following employees under a qualified plan.

    1. Joan, a 9% owner and employee with compensation of $30,000.
    2. Lind, a commissioned salesperson with compensation of $150,000 last year (the highest paid employee).
    3. Reilly, the chief operating officer, with had compensation of $107,000 last year but was not in the top 20% of paid employees.
    4. Garner, the president, who was in the top 20% of paid employees with compensation of $155,000.

    Assuming the company made the 20% election when determining who is highly compensated, which of the following statements is correct?

    a. Exactly three people are key employees.
    b. Exactly two people are highly compensated.
    c. Lind is a key employee but is not highly compensated.
    d. Reilly is neither highly compensated nor a key employee.

The correct answer is d.

For 2008, a key employee is an employee who at any time during the plan year or prior year met one of the following definitions:

- A greater than 5% owner;
- A greater than 1% owner with compensation > $150,000 (not indexed); or
- An officer with compensation in excess of $150,000.

For 2008 highly compensated employees are employees that are:

- A more than 5 percent owner at any time during the plan year or preceding plan year, or
- An employee with compensation in excess of $105,000 for the prior plan year, and if elected, is in the top 20% of paid employees ranked as to compensation.

Employee	Highly Compensated	Key Employee
Joan	Yes – greater than 5% owner.	Yes – greater than 5% owner.
Lind	Yes – greater than $105,000 and in top 20% of paid employees.	No – not an officer or owner.
Reilly	No – greater than $105,000 but not in top 20% of paid employees.	No – he is an officer but does not have compensation greater than $150,000
Garner	Yes – greater than $105,000 and in top 20% of paid employees.	Yes – officer with compensation greater than $150,000.

Multiple Choice #13, Page 119

13. Charles earns $400,000 per year at Home Cleaning Services, Inc. where he has been employed for the last ten years. Home Cleaning Services sponsors a defined benefit plan that provides its employees with a benefit equal to 1.5% per year of service of the employees final compensation. At the current time, what is Charles' retirement benefit payable from the defined benefit plan?

    a. $34,500.
    b. $60,000.
    c. $185,000.
    d. $230,000.

    The correct answer is a.
    Charles' current projected benefit from the defined benefit plan is $34,500. For the calculation of the benefit the employer cannot consider compensation in excess of $230,000 for 2008. 1.5% x 10 x $230,000 = $34,500.

Multiple Choice #14, Page 119

14. Milton, age 38, earns $170,000 per year. His employer, Dumaine Consulting, sponsors a qualified profit sharing 401(k) plan and allocates all plan forfeitures to remaining participants. If in the current year, Dumaine Consulting makes a 20% contribution to all employees and allocates $4,000 of forfeitures to Milton's profit sharing plan account, what is the maximum Milton can defer to the 401(k) plan in 2008?

    a. $0.
    b. $8,000.
    c. $15,500.
    d. $20,500.

    The correct answer is b.
    The maximum annual addition to qualified plan accounts on behalf of Milton is $46,000 for the plan year. This maximum annual additions limit is comprised of employer contributions, plan forfeiture allocations, and employee deferrals. If Dumaine contributes $34,000 ($170,000 x 20%) to the profit sharing plan account and Milton receives $4,000 of forfeitures, he may only defer $8,000 ($46,000 - $34,000 - $4,000) before reaching the $46,000 limit.