

GLOSSARY OF TERMS

2024 Limits

ADP/ACP Tests: These tests compare the contribution percentages of the highly compensated group (HCG) to the non-highly compensated group (NHCG). Generally, the HCG percentage cannot be more than 2 percentage points above the NHCG average. Refer to your year-end request package for the date we will need the required data to complete the tests and issue refunds if necessary. Refunds must be made within 2½ months after the plan year end to avoid a mandatory excise tax of 10% of the amount of the excess contribution, and before the close of the following plan year to avoid disqualification.

Affiliated Service Group: Generally, an affiliated service group consists of two or more related service or management organizations, whether incorporated. Employees of the members of an affiliated service group are treated as employed by a single employer for plan qualification purposes. (Please see the more detailed explanation below beginning on page 3).

Cafeteria Plan: A cafeteria plan is a plan specifically authorized by Section 125 of the Internal Revenue Code. Generally, employees are given a choice to "redirect" part of their salary. Each employee then uses the "redirected" part of his salary to purchase benefits from a "menu" of non-taxable benefits offered by the plan (hence the term "cafeteria"). The employer may make further contributions to the plan which employees may also use to purchase allowable benefits. Allowable benefits include dependent care programs, uninsured medical expenses not covered by the typical group medical plan, group life, medical and disability premiums otherwise paid by the employee, and contributions to 401(k) plans. Because cafeteria plans allow employees to choose the benefits they want, they are often referred to as flexible spending or flexible benefit plans.

Compensation Limit: The compensation limit is **\$345,000** for plan years beginning in **2024**. This limit is considered in calculating actual deferral and actual contribution ratios, allocation of contributions and various other required tests.

Controlled Group of Corporations: There are three types of controlled groups: 1) the parent-subsidary controlled group; 2) the brother-sister controlled group; and 3) the combined group. Two tests must be met to have a "parent-subsidary" controlled group: 1) stock equal to 80% of the combined voting power of each corporation, is owned by one or more of the corporations of the group; and 2) the common parent corporation owns at least 80% of the voting power or value of at least one of the corporations of the group.

Two tests must be met to have a "brother-sister" controlled group: 1) five or fewer persons own at least 80% of the combined voting power or value of two or more corporations; and 2) considering the ownership of each stockholder only to the extent that it is identical in each of the corporations involved, the five or fewer persons own more than 50% of the combined voting power or value of the corporations involved. (Please see the more detailed description below beginning on page 3).

Discretionary Formula Plan: A profit sharing plan that provides the amount of each year's contribution will be determined by the board of directors of the sponsoring employer, in its discretion. (Contributions must be "recurring and substantial" to keep the plan in a qualified status.)

Family Members: Family members include the employee's spouse, any lineal ascendants and descendants, and spouses of lineal ascendants or descendants.

Fiduciary: Any person who exercises discretionary authority or control over the management or disposition of plan assets or who gives investment advice to the plan for a fee or other compensation.

Highly Compensated Employee: An employee who, during the year or the preceding year is (or was) a more than 5% owner and an employee who, during the preceding year (during **2023**) received **more than \$150,000** in compensation, and was in the top paid group if so, elected by the Plan Administrator (adjusted for cost-of-living increases). An employee is also considered highly compensated if he or she is a spouse, a lineal ascendant or

descendant of a more than 5% owner. (See the "Family Members" definition.)

Individual Contribution Limit (annual additions): This is the limit on annual additions allowed by an employee. The maximum is the lesser of 100% of compensation or **\$69,000**. The annual additions include 401(k) deferrals, employer match, profit sharing contributions and forfeiture re-allocations.

Key Employee: At any time during the plan year, a key employee is: 1) an officer who earned over **\$215,000** in the **2023** year (the previous plan year) 2) a more than 5% owner; or 3) a more than 1% owner earning more than \$150,000. The family ownership attribution rules continue to apply.

Leased Employee: A leased employee is an individual who performs services for another person under an arrangement between the recipient and a third person (the leasing organization) who is otherwise treated as the individual's employer. The leased employee is treated as the recipient's employee if the leased employee has performed services for the recipient pursuant to an agreement with the leasing organization on a substantially full-time basis for a period of at least one year and the services are of a type historically performed by employees in the recipient's business field.

Minimum Funding: The minimum amount that must be contributed by an employer that has a defined benefit, money purchase, or target benefit pension plan. The minimum is made up of amounts that go to cover "normal costs" plus other plan liabilities such as "past services costs". If the employer fails to meet these minimum standards, in the absence of a waiver from the IRS, an excise tax will be imposed on the amount of the deficiency.

Officer: The determination as to whether an employee is an officer is made based on all the facts and circumstances, including, for example, the source of the employee's authority, the term for which the employee was elected or appointed, and the nature and extent of the employee's duties. As generally accepted in connection with corporations, the term "officer" means an administrative executive who is in regular and continued service and received more than **\$215,000** in compensation for the **2023** year (the previous plan year). It implies continuity of service and excludes those employed for a special and single transaction, or those with only nominal administrative duties. The number of employees that can be considered officers is equal to 10% of all employees, or three, whichever is greater. In no case, however, can the total number of officers exceed 50.

Top-Heavy: A plan is deemed "top-heavy" if the total account balances of the key employees compared to the total account balance of the plan is 60% or more. If the plan turns out to be top-heavy there could be a requirement for a mandatory employer contribution to non-key employees.

Trustees: The parties named in the trust instrument or plan that are authorized to hold the assets of the plan for the benefit of the participants.

Trust I.D. Number: When implementing a retirement trust, it is important that the trust be registered correctly. Since the assets of the plan are tax-exempt, the pension trust must be identified by a separate number (other than the employer's Tax I.D. number). A Trust Identification Number is applied for through the Social Security Administration on Form SS-4. All assets of the trust should be registered under the Trust I.D. number.

The Trust I.D. number is referenced when reporting distributions on Form 1099-R. Also, plan administrators are required to withhold taxes on distributions unless the participant elects not to have taxes withheld. It is important to note that the Trust is withholding the taxes, not the employer. Therefore, the Trust I.D. number should be used on Form 945 when reporting taxes withheld from plan distributions. Often the employer's investment advisor, accountant or attorney will apply for a Trust I.D. number on behalf of the plan administrator. We ask that you please check to see if you have a Trust I.D. number. If you currently have a separate Trust I.D. number, please provide your plan administrator with the number. If not, we have Form SS-4 available and we would be happy to assist you in applying for a number.

Controlled Group and Affiliated Service Group Definitions

THIS IS A SUMMARY OF IMPORTANT POINTS ONLY. IT IS INTENDED TO PROVIDE THE PLAN SPONSOR WITH ENOUGH INFORMATION TO DETERMINE WHETHER OR NOT THE ADVICE OF COUNSEL SHOULD BE SOUGHT. AS WE ARE NOT A LAW FIRM, WE ARE NOT PROVIDING THIS SUMMARY AS LEGAL ADVICE AND YOU SHOULD NOT RELY ON IT AS SUCH. FOR MORE DETAILED INFORMATION, PLEASE REFER TO IRS CODE SECTIONS 414(B) AND 414(M) AND RELATED REGULATIONS OR CONSULT WITH A QUALIFIED ATTORNEY.

Controlled Group

The definition of Controlled Group is found in IRS Code Section 1563(a). There are various types of controlled groups. First, there is a parent-subsidiary controlled group in which the parent company owns 80% or more of at least one of each subsidiary firm and 80% or more of each subsidiary firm is owned by other members of the group. Second, there is a brother-sister controlled group in which the same five or fewer persons own 80% or more of each firm and more than 50% of each firm when ownership is limited to ownership identical for each firm.

Finally, there is a special type of controlled group which is relevant only for purposes of determining maximum benefit limitations. We will refer to this as an IRC 415 Controlled Group. (See Internal Revenue Code Section 415). This is the same as a brother-sister controlled group but with the 80% or more rule reduced to more than 50%.

For determining controlled groups, there are some complicated rules which are stated in Internal Revenue Code Section 1563 for constructive ownership of businesses which are owned either by partnerships of which you are a partner, or estates and trusts or your spouse, your parents, grandparents, children, or grandchildren. Under these rules, you may be considered to own the portion of any business owned by these individuals or entities.

Affiliated Service Group *(There are three types of Affiliated Service Groups)*

First, an Affiliated Service Group exists between two service organizations, in which the first service organization has ownership in the second (after application of constructive ownership rules) and regularly performs services for the second organization or is regularly associated therewith in performing services for other entities.

Second, an Affiliated Service Group exists between a first service organization and any other organization (even if the business is non-service) if 10% or more is owned by Highly Compensated employees of the first service organization and a significant portion of the business is performing services for the first service organization which are historically performed by employees.

Third, an Affiliated Service Group exists between an organization whose principal business is performing management functions, on a regular and continuing basis, for one organization or related organizations and the organization or related organizations receiving management services.

Under proposed IRS Regulations, a firm will be a service organization if capital is not a material income-producing factor for the organization or if the gross income consists principally of fees, commissions or other compensation for personal services performed by an individual. However, an organization engaged in health, law, engineering, architecture, accounting, actuarial science, performing arts, consulting or insurance is automatically a service organization. A significant portion is defined as 5% or more of business receipts from services or 10% or more of total business receipts.

For purposes of determining ownership, a person may be considered to constructively own a proportional portion of a business owned either by a partnership of which he or she is a partner, an estate or trust or, his or her spouse, children, grandchildren, or parents. There is no exception for a separate business owned by a spouse.

Separate Line of Business Rules

A member of a Controlled Group may be considered a separate line of business and not required to be aggregated with the other members of the Controlled Group if it is in a separate geographic area and separately operated for a bona fide business reason and a) the business has 50 or more non-union employees who have been employed six or more months, normally work seventeen and one-half or more hours per week and six or more months per year and are at least 21 years old and b) the IRS approves the separate line or a safe-harbor rule is passed.

If you think the separate line of business rule may be available to avoid the Controlled Group rule, please contact your Pension Consultant. This cannot be used to avoid Affiliated Service Group rules.

Effect of Controlled Group or Affiliated Service Group

For retirement plan purposes, employees of different firms which are part of a Controlled Group or Affiliated Service Group will be treated as employees of one firm.

The plan may exclude employees of the other members of a Controlled Group or Affiliated Service Group only if the plan may pass certain coverage and non-discrimination tests. The plan will pass these tests if the plan covers at least 70% of the Non-Highly Compensated Employees who meet the eligibility requirements. The plan may also meet more complicated coverage tests.

If you are a member of an IRC 415 Controlled Group only due to the reduction of 80% or more, to more than 50%, the only result is that contributions may need to be reduced for any employee of the other entity who participates in another plan or has ever received benefits as an employee of the other entity in a Defined Benefit Plan.

If you are a member of a Controlled Group or Affiliated Service Group, R.J.L. Pension Services, Inc. will need information on the employees of the other members of the Controlled Group or Affiliated Service Group so that we may be sure you pass these tests. Alternatively, the plan may be adopted by the other members and their employees covered under the plan. The fee for performing these tests will be based on the time necessary to complete the test.

We do recommend if you have other companies or think you may be part of a controlled group or an affiliated service group, that you seek the advice of legal counsel and/or your tax advisor(s). This determination is complex and is subject to other variables such as gross receipts, management and how the companies interrelate which R.J.L. Pension Services, Inc. may not be privy to. If you are interested in additional more detailed articles regarding controlled groups and affiliated service groups with examples, please contact our office.