

Employee Benefit Plans

Explanation No. 1

Minimum Participation Standards

Note:

Plans submitted during the Cycle A submission period must satisfy the applicable changes in plan qualification requirements listed in Section IV of Notice 2010-90, 2010-52 I.R.B. 909 (the 2010 Cumulative List).

The purpose of the Worksheet Number 1 (Form 5622) and this explanation is to identify any major problems an employee benefit plan might have in satisfying the minimum participation standards of Internal Revenue Code section 410(a). However, there may be issues not mentioned in the worksheet that could affect the plan's qualification.

The worksheet concerns plans to which Code section 410 applies, except those mentioned in section 410(c) (such as governmental plans) and plans that cover participants who are employed in maritime or seasonal industries.

Generally, a Yes answer to a question on the worksheet indicates a favorable conclusion, while a No answer signals a problem concerning plan qualification. This rule may be altered by specific instructions for a given question. Please explain any No answer in the space provided on the worksheet. The numbers in brackets correspond to the paragraph number on the Employee Plan Deficiency Checklist and EDS generated Letters 1196, 1197, and 1955.

The sections cited at the end of each paragraph of explanation are from the Internal Revenue Code, the Income Tax Regulations, and Department of Labor (DOL) Regulations.

A plan with participation requirements that are more generous than the statutory minimum will not fail to qualify merely because the plan does not adhere to the specific language found in the statute if it can be demonstrated that the minimum statutory requirements are met. For example, a plan that provides immediate participation would satisfy the statutory minimum participation requirements even though language about a requirement for certain years of service is not found in the plan.

I. Age and Service

Line a. If you answer No to this question, **DO NOT** complete the rest of the worksheet. If the plan provides for participation only on specified entry date(s), but no other age or service requirements are provided, complete only I.c. of the worksheet.

410 (a) (1) (A)
1.410 (a) -3 (a)

Line b. Generally, an employee who is otherwise eligible (for example, a salaried employee in a salaried only plan) must be eligible to participate in the plan at age 21, or upon completion of 1 year of service, whichever is later. However, if the plan provides full and immediate vesting, an employee otherwise eligible must also be eligible to participate at age 21 or upon completion of 2 years of service, whichever is later. Schools substitute age 26 for age 21 if the school's plan provides for full and immediate vesting and requires no more than 1 year of service as a condition of participation.

If the plan uses the elapsed time method of crediting service, substitute "period of service" for "year of service" above.

410(a)(1)
1.410(a)-3T
1.410(a)-7(c)
1.410(a)-3

Line c. General Rule—Once an employee, otherwise eligible, meets the statutory age and service requirements, the plan must cover him or her on either the first day of the plan year after the employee has met the statutory requirements, or 6 months after the day on which the employee fulfills such requirements, whichever is earlier. There is an exception to this rule if an employee was separated from service and did not return before the applicable entry date referred to above. If the separated employee returns, after either date, without incurring a break in service, the employer must cover the employee upon return. When a plan's service requirements are more generous than the statute allows, the plan will qualify if the total waiting period is not longer than the statutory minimums. For example, in a plan with no age or service requirement, a new employee, otherwise eligible, may be excluded until the next annual anniversary date of the plan after employment. This provision will not disqualify the plan because no employee can be required to wait longer than a 12-month period under the terms of the plan. Rules concerning a rehired employee who has a break in service are in II.j. and k. and III.g. and h. of these explanations.

Special rules apply where the plan uses the elapsed time method of crediting service. These are: a plan using the elapsed time method must provide that an employee, once eligible, who satisfies the statutory age and service

requirement must be covered on the first day of the plan year after the employee has met the statutory requirements, or 6 months after the day on which the employee fulfills such requirements, whichever is earlier, unless the employee was separated from service before the applicable entry date. Apply different rules if the separated employee returns after the applicable entry date, whether or not the employee had a period of severance. A period of severance begins on the date of severance from service. A "severance from service" occurs either when an employee quits, retires, is discharged, or dies; or on the first anniversary of the first day of a period of absence from service for any other reason (such as vacation, holiday, disability, or layoff), whichever date comes first. Thus, if an employee separates, for any reason other than quitting, retiring, or discharge and returns within 12 months, there is no period of severance. In that case, if the employee returns after either entry date, the employer must cover the employee no later than the date the absence ended, effective the first applicable entry date that occurred during the absence from service. In the case of a period of severance, if the separated employee returns after a period of severance of less than 1 year and that period includes an entry date applicable to the employee, then the employer must cover the employee no later than the date on which the employee ended the period of severance. Rules for a rehired employee who has incurred a 1-year period of severance are in III. g. and h. of these explanations. The above rule is illustrated in the following examples.

Example 1.

A plan provides for a minimum age requirement of 21 and a minimum service requirement of 1 year with semi-annual entry dates. Employee X, after satisfying the minimum age requirement, became disabled for 9 consecutive months and then returned to service. Since X separated from service because of a disability, there is no severance from service until the first anniversary of the date the separation occurred. X therefore did not have a period of severance under the elapsed time rules. During the period of absence, X completed a 1-year period of service and passed a semi-annual entry date after satisfying the minimum service requirement. Accordingly, the plan must make X a participant no later than the return to service, effective as of the applicable entry date.

Example 2.

Employee B, after satisfying the minimum age and service requirements, quit work (date the period of severance begins) before the next semi-annual entry date, and then returned to service before incurring a 1-year period of severance but after the semi-annual entry date. Employee B is entitled to become a participant immediately upon the return to service, effective as of the date of the return.

410(a) (4)
1.410(a)-4(b)
1.410(a)-7(c) (3)

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II. Years of Service

If the plan has no service requirement, **DO NOT** complete this section.

Line a. An eligibility computation period is a 12-consecutive-month period used to determine whether an employee has completed a year of service for participation purposes. Any plan must designate an eligibility computation period, except a plan that uses an "elapsed time" method of counting service or a plan that has no service requirement for eligibility to participate. If the plan uses the "elapsed time" method of counting service, check N/A and skip to section III.

DOL Regs. 2530.200b-1(a)

Line b. Depending on the definition of "hours of service" and the method used to count these hours, a plan must credit an employee with 1 year of service for eligibility if the employee completes at least 1000, 870, or 750 hours of service in an eligibility computation period.

(i) (H = 1000) A plan that counts all hours of service, or that uses an equivalency based on a period of employment (day, week, semi-monthly payroll period, month, or shift), cannot require the completion of more than 1000 hours of service.

410(a) (3) (A)

DOL Regs. 2530.200b-1(a)

DOL Regs. 2530.200b-3(e)

(ii) (H = 870) A plan that counts "hours worked," or that uses an equivalency based on earnings for an employee who is compensated on an hourly rate, cannot require the completion of more than 870 hours of service.

DOL Regs. 2530.200b-3(d) (1)

DOL Regs. 2530.200b-3(f) (1)

(iii) (H = 750) A plan that counts "regular time hours," or that uses an equivalency based on earnings for an employee who is compensated on a basis other than an hourly rate, cannot require the completion of more than 750 hours of service.

DOL Regs. 2530.200b-3(d) (2)

DOL Regs. 2530.200b-3(f) (2)

Answer the following by using the applicable method of counting hours (i, ii, or iii above).

Line c. If a plan counts all hours of service, credit each hour for which (1) an employee is paid or entitled to payment for performance of duties, (2) an employee is paid or entitled to payment because of a period of time during which no duties are performed, and (3) back pay is either awarded or agreed to by the employer.

DOL Regs. 2530.200b-2(a)

If a plan credits hours of service by an equivalency based on a period of service, and an employee is required to be credited with at least 1 hour of service under the paragraph above, then, depending on the basis used, the plan must credit hours of service as follows:

Basis of Equivalency: Number of Hours Credited:

Day	at least 10
Week	at least 45
Bi-weekly payroll period	at least 95
Month	at least 19

If a plan counts "hours worked," credit each hour for which an employee is paid or entitled to payment for the performance of duties; also credit hours for which back pay is awarded, or agreed to, by the employer to the extent that the back pay covers a period in which the employee would have been employed in the performance of duties for the employer.

DOL Regs. 2530.200b-3(d) (3) (i)

If a plan counts "regular time hours," credit each hour for which an employee is paid or entitled to payment for the performance of duties (except hours for which a premium rate is paid).

DOL Regs. 2530.200b-3(d) (3) (ii)

If a plan credits hours of service by an equivalency based on earnings for an employee who is compensated on an hourly rate, an employee must be credited during a computation period with at least the number of hours equal to either the employee's total earnings-

(1) from time to time during the computation period, divided by the hourly rate of those times; or

(2) for performance of duties during the computation period divided either by the employee's lowest hourly rate during that time, or by the lowest hourly rate payable to an employee in the same, or a similar, job classification.

DOL Regs. 2530.200b-3(f) (1) (i)

If a plan credits hours of service by an equivalency based on earnings, and determines compensation other than on an hourly rate, an employee must be credited during a computation period with at least the number of hours equal to his or her total earnings for duties performed during that period, divided by the employee's lowest hourly rate of compensation during the same period. (See the DOL Regulations.) Note: If the same hourly rate of compensation is used for all employees, this method may result in discrimination in favor of highly compensated employees.

DOL Regs. 2530.200b-3(f) 2

Line d. If H = 1000 in b, above, answer this question; otherwise check N/A. If a plan credits hours of service of periods during which no duties are performed, the plan must designate the method of determining the number of hours to be credited and the method of crediting the hours to the computation periods.

The plan must conform to the requirements of DOL Regulations sections 2530.200b-2(b) and (c). Section 2530.200-2(f) of the DOL Regulations, however, also indicates that a plan is not required to state these rules if they are incorporated by reference.

DOL Regs. 2530.200b-2(b) and (c)

DOL Regs. 2530.200b-2(f)

Line e. In general, the plan must initially use an eligibility

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computation period of 12-consecutive-months, beginning with the employee's employment commencement date. This date is the first day for which the employee is entitled to be credited with an hour of service for the performance of duties.

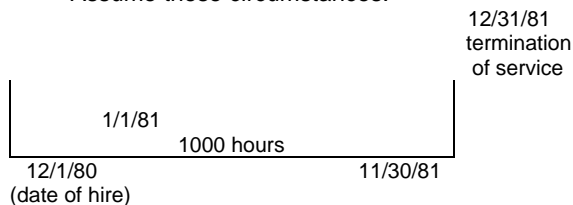
An alternative eligibility computation period, which may be used when employment commencement dates cannot be specifically determined, is specified in DOL Regulations section 2530.202- 2(e). If this alternative is properly used, check Yes to this question.
DOL Regs. 2530.202-2(a)&(e).

Line f. If eligibility computation periods under a plan are determined solely on the anniversary of employment, check N/A.

In general, an eligibility computation period is used to determine whether an employee has fulfilled service requirements for admission into the plan. It can also have a continuing use in determining whether an employee or participant with no vested interest in employer-derived accrued benefits remains eligible to be a plan participant under the rule of parity (see j. and k. of these explanations). To determine years of service for either initial eligibility or retention of eligibility to participate in the plan and consequent nonforfeiture of accrued benefits, plans may choose one of two eligibility computation periods after the initial computation period. First, the plan may continue to measure years of service, beginning on the employment commencement date and its anniversaries, or plans may shift to the plan year. However, the first plan year must include the last day of the initial eligibility computation period. This overlapping is essential to assure that the employee does not lose creditable service as a result of a gap between computation periods. A shift in the eligibility computation period must be made with respect to all employees.

The application of the above rules is given in the following example:

Assume these circumstances:



The chart shows an employee is hired on December 1, 1980, and the plan year is a calendar year. The employee terminates service on December 31, 1981, and has a 1-year break in service (December 31, 1982). The employee has no vested right in any employer contributions. The employee worked 1000 hours between January 1, 1981, and November 30, 1981, and attained 1 year of service within the 12-month period following the date of hire. Figuring the pre-break service under DOL Regulations section 2530.202-2(c), the employee would receive credit for 1 year of service from December 1, 1980 (the date of hire) to November 30, 1981, and credit for another year of service for the plan year

(calendar 1981) which includes the last day of the initial eligibility computation period. Thus, the employee receives credit for 2 years of service.

*DOL Regs. 2530.202-2(b)
410(a) (3) (A)*

If the plan uses the alternative eligibility computation period described in DOL Regulations section 2530.202-2(e), special rules apply for the eligibility periods following the initial computation period. If this alternative is properly used, check Yes to this question.

DOL Regs. 2530.202-2(e) (2)

Line g. The break in service rules allow a plan to disregard certain service before the employee has a break. If all of an employee's service with an employer is counted for participation, the plan need not provide these rules. In this case **DO NOT** complete questions g. through k. of the worksheet.

Depending on the definition of "hour of service" and the method used to count these hours, a plan may charge an employee with a break in service for eligibility computation period in which the employee fails to complete more than B hours of service. The number required for B, if a certain method of counting hours is used, equals half the hours used in question b. of this section of the worksheet.

Therefore, a plan may provide that an employee be charged with a break in service if in a computation period the employee fails to complete: more than 500 hours of service in a plan that counts all hours of service; or, more than 435 hours of the basis used is "hours worked"; or, more than 375 if the basis is "regular time hours."

DOL Regs. 2530.200b-3

DOL Regs. 2530.200b-4

Line h. To apply the break in service rules, the plan must use the same computation periods to measure breaks in service that it uses to measure prior service for eligibility to participate. When a plan defines a year of service as 1000 (870 or 750) hours and an employee has hours of service of more than 500 (435 or 375) but less than 1000 (870 or 750) hours, there is no break in service even though the plan will not credit the employee with a year of service.

DOL Regs. 2530.200b-4(a) (2)

Line i. An individual shall be credited with certain hours of service if such individual is absent from work for any period by reason of 1) pregnancy of the individual, 2) birth of a child of the individual, 3) placement of a child with the individual in connection with an adoption or 4) caring for a child described in (2) or (3) immediately following such birth or placement. This credit is credit for maternity or paternity leave. Credit for maternity or paternity leave is *only made* to avoid a break in service and *not to obtain a year of service*. The absence does not have to be approved leave.

Credit for maternity or paternity leave is required only if such leave is on account of the reasons described above.

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Thus if an individual quits employment with employer A and two years later adopts a child, no credit under this provision would be given if the individual eventually returns to work for employer A because said individual's absence from employer A's workplace is on account of quitting and not on account of the adoption of or the caring for the child immediately following the adoption.

Hours of service must be credited to the computation period in which the first hour of maternity or paternity leave occurs, if such individual would experience a break in service with respect to such computation period if such maternity or paternity leave is not credited and such individual will not experience a break in service if such maternity or paternity leave is credited. If such maternity or paternity leave is not credited to the first computation period, it is credited to the second computation period whether or not it is needed to preclude a break in service. The rules may be illustrated with the following example: Individual A separates from service on March 1, 1986, of a calendar year computation period after earning 300 hours of service. The plan defines a year of service as a computation period in which the employee earns 1000 hours. The employer provides for paid maternity leave for a period not to exceed 300 hours.

Under the normal rules of crediting service paid maternity leave must be credited for service. Therefore, individual A in 1986 would not experience a break in service even if the hours required to be credited under REA are not so credited. Accordingly, no hours of service would be credited to the first computation period in 1986. Therefore, all such hours of service are credited in the second computation period of 1987.

The number of hours credited with respect to a computation period is the number of hours such individual would normally have worked in the computation period if such individual were not on maternity or paternity leave. If the number is not ascertainable, the plan may credit 8 hours with respect to any date said individual is absent on maternity or paternity leave. The plan may limit the number of hours credited to any computation period to the number of hours needed to avoid a break in service, i.e., 501 hours, 436 hours, or 376 hours depending on how hours are counted. The plan may provide that the participant has the burden of proving that the absence was by reason of one of the covered causes.

The plan can use a simplified method for complying with the requirements relating to maternity and paternity absences. If the plan's break in service rules require a minimum of six consecutive one year breaks in service for service to be disregarded (versus the statutory minimum of five), then the plan will not have to include any special rules relating to maternity and paternity absence. This simplified method is available only if the plan computes years of service on the basis of hours of service or permitted equivalencies. It does not apply to elapsed time plans.

410(a)(5)(E)
1.401(a)-9

Lines j. and k. In general, an employee's pre-break service does not have to be credited until the employee has completed 1 year of service after the break. This should not

be confused with the following rule of parity. If a participant with no vested interest has a break in service under the rule of parity, service before the break need not be counted for participation if the number of consecutive 1-year breaks equals or is more than the greater of 5 or the aggregate years of service completed before the break. The aggregate years of service completed before the break does not include years of service that need not be counted because of earlier breaks. In the case of a plan described in section 410(a) (1) (B) (i), that is, a plan that provides for 100 percent vesting after 2 years of service, an employee who has not met the plan's service requirement and has a one year break in service need not have pre-break service taken into consideration for purposes of meeting the plan's service requirement.

When an employee's pre-break service must be taken into account after a year of service, an employee who meets the plan's eligibility requirements and has a break need to be credited with the pre-break service until completion of a year of service after returning. However, at that time the employee would be required to retroactively participate under the plan. The following examples illustrate this rule:

Example 1.

A calendar year plan provides that an employee may enter the plan on the first semi-annual entry date, January 1, or July 1, after satisfying the minimum age and service requirements. Employee C, after working 10 years, separated from service in 1976 with a vested benefit. On February 1, 1990, C returns to employment covered by the plan. C then completes a year of service. C must participate either immediately on returning or, after the year of service, retroactively on February 1, 1990. The prior service cannot be disregarded because of the vested benefit C had upon separation; therefore, the plan may not postpone participation until July 1, 1990.

Example 2.

A defined contribution plan has a 1-year service requirement for participation and no age requirement. Contributions and allocations are made for eligible employees on December 31. An employee is hired on January 1, 1985, and works 1000 hours in 1985 and 600 hours in 1986. On June 30, 1986, the employee separates from service without a vested interest. The employee then has a break in service for the years 1987, 1988, and 1989. The employee returns on July 1, 1990. In accordance with the break in service rules, the plan provides that the employee must complete 1 year of service after returning before the pre-break service is credited (year 1985). Therefore, no contribution need be made on the employee's behalf on December 31, 1990, because the employee is not eligible to participate at that time. On June 30, 1991, the employee completes 1 year of service and is credited with the pre-break service. Because the number of consecutive breaks in service is less than 5, the pre-break service may not be ignored; thus the employee must participate retroactively from July 1, 1990. If the employee is not covered on December 31, 1990, the

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waiting period is longer than the maximum allowed, taking into account the pre-break service.

410(a)(5)(C) & (D)
1.410(a)-4

III. Years of Service and Breaks in Service Based on Elapsed Time

If the plan has no service requirement or does not use an elapsed time method of crediting years of service for eligibility, **DO NOT** complete this section.

Unlike the general method of crediting service for an employee, which is based on hours and years of service, the elapsed time alternative generally credits an employee with the total time that elapses during his or her employment. This alternative lessens the administrative burdens of maintaining records of hours of service. It enables the employer to credit service from date of employment to date of severance without counting hours of service completed during that time.

Line a. The employment commencement date must be no later than the date on which the employee first performs an hour of service for the employer. The severance from service date is the earlier of the date an employee quits, retires, is discharged, or dies, or the first anniversary of the first day of a period of absence from service for any reason other than quitting, retiring, discharge, or death. The employee must be credited with a period of service equal to at least the time between the employment commencement date and the severance from service date.

1.410(a)-7(b)

Line b. Generally, a plan must aggregate all separate periods of service, except any that may be disregarded because of the rule of parity. (See III.h.) Alternatively, instead of keeping separate periods of service, the plan may aggregate by adjusting the employment commencement date. If the plan used the alternative to credit the aggregate period of service, check Yes for question b.

1.410(a)-7(b) (6) (ii)
1.410(a)-7(b) (2) (iv)

Line c. A period of severance is the time between the employee's severance from service date and the date the employee again performs an hour of service for the same employer.

If an employee severs from service by quitting, being discharged, or retiring, and then performs an hour of service within 12 months of the severance from service date, the plan must consider the period of severance as a period of service.

Also, if an employee severs from service for any reason other than quitting, being discharged, or retiring, and within the next 12 months or less quits, is discharged, or retires and then performs an hour of service within 12 months of the date on which he or she was first absent from

service, the plan must consider that period of severance as a period of service.

1.410(a)-7(c) (2) (iii)

Line d. When a plan has a service requirement and uses the elapsed time method of crediting service, an employee must be considered to have satisfied that requirement as of the date he or she has credit for a period of service equal to the requirement. All periods of service, except those disregarded due to the rule of parity, must be aggregated. Certain periods of severance must be considered as periods of service (see question c) when determining this eligibility date.

Section I deals with the date an employee must begin participation in these situations.

1.410(a)-7(c) (2)

Line e. The break in service rules allow a plan to disregard certain service before the employee has a break. If all of an employee's service with an employer is counted for participation, the break in service rules need not be provided by the plan. In this case, check N/A for questions e. through h. of the worksheet. If a plan uses elapsed time substitute "1-year period of severance" for "1-year break in service." A 1-year period of severance is a 12-consecutive-month period beginning on the severance from service date and ending on the first anniversary of that date provided that within this period the employee does not perform an hour of service for the employer maintaining the plan.

1.410(a)-7(c) (4)

Line f. An individual shall not incur the first 12-month period of severance that would otherwise be counted if severance is due to maternity or paternity leave. Such 12-month period is neither counted as a year of service nor as a period of severance. Maternity or paternity leave is a period an individual is absent from work by reason of 1) pregnancy of the individual, 2) birth of the child of the individual, 3) placement of a child with the individual for adoption or 4) caring for a child described in (2) or (3).

Credit for maternity or paternity leave is required only if such leave is on account of the reasons described above. Thus, if an individual quits employment with employer A and two years later adopts a child, no credit under this provision could be given if the individual eventually returns to work for employer A because such individual's absence from employer A's workplace is on account of quitting and not on account of the adoption of or the caring for the child immediately following the adoption.

If an individual works until July 1, 1986, is first absent from employment on July 1, 1986 on account of maternity or paternity leave, and on July 1, 1989 performs an hour of service, the period of service must include the period from the employment commencement date until June 30, 1987 (one year after the date of separation for a reason other

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than an employee quitting, retirement, discharge or death). The period from July 1, 1987 to June 30, 1988 is neither a period of service nor a period of severance. The period of severance would be from July 1, 1988 to June 30, 1989.

410(a)(5)(E)

1.410(a)-9

the period of severance is less than 5 years. If this employee is not covered on December 31, 1990, the waiting period is longer than the maximum allowed, taking into account the pre-break period of service.

Lines g. and h. In general, an employee's service before a 1-year period of severance is not required to be credited until the employee completes a 1-year period of service after the period of severance. The rule of parity applies to employees who are not vested. If a participant with no vested interest has a 5-year or more period of severance, service before the severance need not be counted for participation if the period of severance equals or is more than the aggregate periods of service before the break. The period of service completed before the period of severance does not include service that need not be counted because of earlier periods of severance.

When service before a 5-year or more period of severance must be taken into account after a 1-year period of service, an employee who meets the plan's eligibility requirements and has a 1-year period of severance need not be credited with pre-break service until he or she completes a 1-year period of service after severance. However, at that time the employee would be required to participate under the plan retroactively. The following examples illustrate this rule:

Example 1.

A calendar year plan provides that an employee may enter the plan only on the first semi-annual entry date, January 1, or July 1, after satisfying minimum age and service requirements. Employee C, after 10 years of service, separated from service in 1976 with a vested benefit. On February 1, 1990, C returns to employment covered by the plan and completes a 1-year period of service. C must participate either immediately on returning or, after a 1-year period of service, retroactively to February 1, 1990. C's prior service cannot be disregarded because of the vested benefit C had when separating from service. Therefore, the plan may not postpone participation until July 1, 1990.

Example 2.

A defined contribution plan has a 1 year service requirement for participation, and no age requirement. Contributions and allocations are made for eligible employees on December 31. An employee is hired on January 1, 1985, and separates from service without a vested interest on June 30, 1987. The employee returns on July 1, 1990, after a 3-year period of severance. Under the break in service rules, the plan provides that the employee must complete a 1-year period of service after returning before the 2½-year period of pre-break service is credited. Therefore, no contribution need be made on the employee's behalf on December 31, 1990, because the employee is not eligible to participate at that time. On June 30, 1991, the employee completes a 1-year period of service and is credited with the pre-break service and must participate retroactively from July 1, 1990 because