



Strategy & Design

IMPORTANT Message from Innovative Pension --- 401(k) test to potentially avoid refunds ---

Dear 401(k) Plan Sponsor:

As you know, after each year-end, certain non-discrimination tests must be performed and satisfied regarding your 401(k) plan. One such test, the Annual Deferral Percentage (ADP) test, may result in 401(k) refunds to Highly Compensated Employees (HCEs = generally those earning over \$110,000 in the prior year or are the business owners or family members of business owners). This test compares the deferral percentage of the HCEs to the Non-Highly Compensated Employees (NHCEs) to demonstrate that 401(k) salary deferrals do not favor HCEs.

Plans that do not satisfy the requirements of the ADP test are required to:

- 1. Refund a portion of the HCEs Salary Deferrals until the requirements are satisfied; or alternatively**
- 2. Provide a fully vested contribution to each NHCE until the requirements are satisfied**

By providing the information noted below we will prepare a preliminary test of your 401(k) plan to determine if the plan is projected to pass the final ADP and other required non-discrimination tests for employee deferrals and/or employer matching contributions for your plan year 2009. This preliminary qualification test, prior to the close of the calendar year, will allow you the ability to make the appropriate 401(k) deferral adjustments to your HCE employees to potentially avoid refunds or employer contributions as outlined above.

To prepare this preliminary ADP test for your 401(k) plan we ask that you submit your year-to-date payroll information in electronic format (Excel spreadsheet) prior to October 31, 2009. Please include:

- 1. List of all employees, with dates of birth, hire & termination**
- 2. 3rd Quarter year-to-date gross compensation & 401(k) deferrals (or annualized estimate)**
- 3. 3rd Quarter year-to-date 401(k) match (if applicable) (or annualized estimate)**

Please be sure to note if you anticipate substantially different Q4 income (bonus, commissions, new hires, etc.).

Upload your Excel file at the Secure Upload at www.ipds.com/portal/ . File Description: "Your Company Name" Preliminary Testing". Check the Technical Services Box. You may also postal mail this information to us on a disk.

We will notify you of the results of this ADP test once completed to allow you to adjust your HCE 401(k) deferrals.

This preliminary ADP test is intended to provide you the opportunity to adjust your HCE participant 401(k) deferrals prior to year-end to potentially eliminate 401(k) refunds. This preliminary test cannot guarantee elimination of all 401(k) refunds because your final ADP test, based on actual income and 401(k) deferral information, may differ from the estimated information used to perform this preliminary test.

Preparation of this preliminary ADP test is time consuming; therefore we can only complete this test for those who provide us the requested information prior to October 31, 2009. Additional information is attached for your review.

For questions, please call David or Meghann your Customer Service Representatives at 858-748-6500.

Thank you for your cooperation.

Respectfully,

Wendy Hugé
Technical Services Director



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HOW TO AVOID 401(k) REFUNDS to your HCEs

Often Plan Sponsors voice consternation over their inability of the Plan to meet the ADP non-discrimination requirement. Since typically, HCEs (Highly Compensated Employees) are better retirement planners and desire to defer more into the 401(k) plan, presented herein is a review of the options for increasing the participation of your NHCE (Non Highly Compensated Employees) in the Plan.

Increase Participation:

- a. Employee education and awareness increases participation.
- b. Consider quarterly enrollment meetings
- c. Payroll envelope stuffers are available with 401(k) information
- d. Annual benefit statements that show how 401(k) savings can grow.

Eliminate 401(k) refunds by electing Safe Harbor 401(k) for 2010. These require one of two options:

1. **Safe Harbor Match** – made only for those employees who actually defer. HCE employees can be excluded from this match. Employer match must be 100% up to 4% of pay. **This option provides automatic satisfaction of the ADP test.... no 401(k) refunds!**
2. **Safe Harbor QNEC** – 3% of pay to every eligible employee, whether they defer or not. If you are already planning a Profit Sharing contribution, consider using the first 3% contributed to satisfy this Safe Harbor requirement. **This option provides automatic satisfaction of the ADP test.... no 401(k) refunds!**

*NOTE: All Safe Harbor employer contributions described above are immediately 100% vested to the employee. Variations and restrictions to the Safe Harbor Match contribution apply. **Notice to participants must be provided 30 days prior to beginning of year for which Safe Harbor applies.***

Automatic Enrollment – 2 types; Standard and Safe Harbor:

1. **Standard:** Employees are automatically enrolled on a specified participation date at a rate of the employer's choosing from 1% to 10% of pay. The employee may opt out at any time by informing the employer in writing within 90 days that they do not wish to be enrolled. Employer is not required to provide any incentives. Employer's time to provide 401(k) refunds to HCEs without excise tax is extended to 6 months past applicable year-end. **Increased enrollment may allow Employer to pass ADP test to minimize 401(k) refunds.**
2. **Safe Harbor:** New employees are enrolled automatically at a rate of 3% to 6% of pay. Employer is generally not required to enroll current non-participants. Employee's deferral percentages are automatically increased each year until 6% of pay is reached. Employer provides a Safe Harbor Match of 100% of the first 1% and 50% of the next 5%. Match vests 0% the first year and 100% the second year. **This option provides automatic satisfaction of the ADP, ACP and Top Heavy Tests.... no 401(k) refunds!**

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