Shannon & Associates LLP
Certified Public Accountants
Management Consultants

Employee Benefit Advisor

COMMITTED TO YOUR SUCCESS

Winter 2013

CONSEQUENCES OF PLAN DISQUALIFICATION

A tax-qualified retirement plan, such as a 401(k) plan, provides you, as the employer, and the employees who participate in your plan with numerous advantages. These advantages are lost if you fail to follow tax law requirements and your retirement plan loses its qualified status.

Essentially, when the IRS disqualifies a plan, the plan's trust ceases to be tax exempt. Instead, it becomes a nonexempt (or taxable) trust. This status change affects plan participants, the employer, and the trust.

For plan participants

Generally, participants must include in gross income any amounts the employer contributed to the plan for their benefit in the years the plan is disqualified (to the extent the participant is vested in those contributions). As a result, participants are subject to current federal income tax on those contributions. Highly compensated employees may have to include their entire vested plan balance in income (any amount not previously taxed) if the plan is disqualified for certain reasons.

In addition, distributions from a plan that has been disqualified are not considered eligible rollover distributions. Consequently, employees receiving distributions cannot roll them over to an individual retirement account or another employer's retirement plan. Distributions generally are taxable to the recipients in the year they are received.

For employers

If your retirement plan is disqualified, your deductions for contributions to the plan could be restricted and delayed. Once a plan is disqualified, different rules apply to the amount an employer can deduct for plan contributions and when deductions are allowed. Unlike contributions to a qualified plan, contributions to a nonexempt employees' trust cannot be deducted until the contributions are includable in employees' gross income. Employers that sponsor a defined benefit plan (or other plan that does not maintain separate accounts for each employee) cannot deduct any contributions.

For the plan trust

When a plan is disqualified, the plan trust must pay income tax on the trust earnings. Qualified plan earnings are not taxed to the plan trust but, rather, generally, to plan participants in the year those earnings are distributed to them from the plan.

Regaining tax-exempt status

Before the IRS will reinstate a plan's qualified status, generally, the error that caused the disqualification has to be corrected. Corrections can be made through the IRS Voluntary Correction Program or, if the plan is under examination by the IRS, through the Audit Closing Agreement Program.

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Top ten plan errors

- Failure to amend the plan for tax law changes by the required date.
- Failure to follow the plan's definition of compensation for purposes of determining contributions.
- Failure to include eligible employees in the plan or to exclude ineligible employees from the plan.
- Failure to satisfy plan loan provisions.
- Impermissible in-service withdrawals.
- Failure to satisfy required minimum distribution rules.
- Employer eligibility failure.
- Failure to pass annual nondiscrimination testing.
- Failure to properly provide the minimum top-heavy benefit or contribution to non-key employees.
- Failure to observe the limits on maximum annual contributions a participant can receive (in a defined contribution plan) or the amount of benefits a participant can accrue (in a defined benefit plan).

Can We Help?

Our firm offers a broad range of employee benefit plan services. If we can be of service to you, please call!

Effective 1/1/13

Washington State minimum wage increased to $9.19 per hour

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BENEFIT NOTES

Fee disclosure reminder

With the initial annual fee disclosures to participants out of the way for many plan sponsors, you should have your eye on the due date for the first required quarterly fee disclosures. Initial annual disclosures were due to participants and beneficiaries by August 30, 2012, for calendar-year plans. The first quarterly disclosures for these plans were due by November 14. To help sponsors meet their disclosure obligations, the U.S. Department of Labor has issued guidance in the form of 38 frequently asked questions at www.dol.gov/ebsa/regs/fab2012-2.html.

New FSA cap for 2013

Under the Patient Protection and Affordable Care Act, for tax years beginning after December 31, 2012, the maximum annual amount an employee can contribute to a health flexible spending account (FSA) under a qualified cafeteria plan is $2,500 (subject to future inflation adjustment). The IRS recently provided guidance on the effective date of the limit and on when and how plans should be amended to comply. Among the points included in the guidance: The $2,500 limit does not apply for plan years that began before 2013 or to FSAs for dependent care assistance. The term "taxable year" refers to the tax year of the cafeteria plan, not the employee or employer. Plans may adopt required amendments to reflect the $2,500 limit at any time through the end of calendar year 2014, as long as the plan otherwise operates in accordance with the new requirements.

The importance of 401(k) plan participation

According to the Employee Benefit Research Institute (EBRI), being able to participate in a 401(k) plan at work is one of the single most important factors in closing the retirement savings gap for Generation X (those born between 1965 and 1974). EBRI gap modeling estimates that Gen Xers with at least 20 years of future eligibility to participate in a 401(k) or other defined contribution plan will have an average financial shortfall at retirement of approximately $23,000. For those with no future years of eligibility, the projection of the average retirement savings shortfall widens to $78,000.

OFFICIAL 2013 RETIREMENT PLAN INFLATION ADJUSTMENTS

The IRS has announced many cost-of-living adjustments (COLAs) that apply to retirement benefit plan limitations. Below are selected COLAs for 2013, compared to their 2012 levels.

- Limit on elective deferrals to 401(k), 403(b), and 457 plans — $17,500, up from $17,000.
- Traditional and Roth IRA contribution limit — $5,500, up from $5,000.
- Maximum SIMPLE contributions — $12,000, up from $11,500.
- Limit on annual additions to defined contribution plans — $51,000, up from $50,000.
- Maximum annual benefit accrued under a defined benefit plan — $205,000, up from $200,000.
- Compensation limit for qualified plan purposes — $255,000, up from $250,000.
- Traditional IRA deduction – begins to phase out at Modified Adjusted Gross Income (MAGI) of $95,000 for a married couple filing jointly, up from $92,000 (single or head of household filers: $59,000, up from $58,000).
- MAGI phase-out range for Roth IRA contributions — $178,000 to $188,000, up from $173,000 to $183,000 (married filing jointly); singles and heads of households: $112,000 to $127,000, up from $110,000 to $125,000.

- MAGI limit for the Retirement Saver's credit — $59,000 for married couples filing jointly, up from $57,500 ($29,500 for singles and heads of households, up from $28,750).

Limits on catch-up contributions remain the same for 2013: for IRAs, the limit is $1,000; for 401(k) and 403(b) plans, $5,500; and for SIMPLE plans, $2,500.

If you have any questions regarding the limitations and how they apply to you, feel free to contact us. We're here to help.

PUTTING YOUR MONEY WHERE YOUR MOUTH IS: SETTING A STRONG TONE AT THE TOP

By Jessica Kinney, CPA, CFE

It is easy for management to proclaim, "there is zero tolerance for fraud and unethical behavior," but is it just as easy to cite specific examples of management's actions displaying this strong 'tone at the top'? The term 'tone at the top' is all a buzz in recent years due to many highly public fraud cases. The 'tone at the top' refers to the ethical atmosphere that is created in the workplace by the organization's leadership.

In the newspaper every day you can find examples of how management's actions or what was portrayed by management to the employees was, to put it gently, less than ideal. How often do you hear of the positive things a company's management is doing to promote an ethical environment?

Here are three critical things management can do to help promote a culture of integrity:

1. Implement an Independent Hotline for Anonymous Reporting of Unethical Behavior

2. Provide Fraud Training for Employees
3. Implement a Formal Ethics Policy

Implementing the above suggestions sends a strong message to employees that integrity and ethical behavior is a top priority and that any deviation will not be tolerated. For information on the implementation of these items including our independent hotline, Red Flag Reporting, which includes fraud training for all employees, please contact Jessica Kinney at JKinney@Shannon-CPAs.com or 253-852-8500.

Red Flag Reporting

Protecting Organizations and Their People

For more info, email: RedFlagReporting@Shannon-CPAs.com

Julie Courtney, CPA, Partner, our Director of Accounting and Auditing for Shannon & Associates, is in charge of the firm's employee benefit plan audit practice. Julie is involved in all aspects of the audits we perform as well as plan consulting and advisory services.

Julie has over 20 years of public accounting experience. Her areas of expertise include benefit plan and financial audits and financial reporting. Her responsibilities include advising closely-held businesses, internal control review, and various tax engagements. She also assists in quality control and staff training for the firm. Julie attends the AICPA National Conference on Benefit Plans annually. She has served clients in many industries including the following: manufacturing, non-profit organizations, real estate development, wholesale distributors, restaurant, construction (home builders), and professional services. Julie holds a Bachelor of Arts degree in Accounting from Western Washington University.

Bethany Hulbert, CPC, our Employee Benefits Consultant, has over 9 years experience specializing in defined contribution plan administration and holds the Certified Pension Consultant (CPC) credential from the American Society of Pension Professionals and Actuaries (ASPPA). This experience, along with her educational background in accounting and attendance at numerous seminars and courses, has resulted in an up-to-date mastery in profit sharing, 401(k), and money purchase pension plans. We encourage you to contact Bethany regarding any questions you may have with your defined contribution plans.

Bethany provides expert and timely services in the following areas:

- Plan document design, implementation and submission to the IRS
- Employee communications
- All aspects of plan administration
- Evaluation of controlled groups and related businesses
- Discrimination/coverage testing and solutions
- Compliance with all reporting required by the IRS and DOL
- Minimum required distributions

SHANNON & ASSOCIATES, LLP
Certified Public Accountants & Management Consultants
1851 Central Place South, Suite 225, Kent, WA 98030 | 253-852-8500
info@Shannon-CPAs.com | www.Shannon-CPAs.com