
Highly Compensated Employees (HCEs) §IRC 414(q)

Qualified plans, including 412(i) plans, are subject to nondiscriminatory coverage and participation requirements, which in turn are based on the definition of Highly Compensated Employee. The term "Highly Compensated Employee" (HCE) includes, for any plan year, any employee who:

1. was at least a 5% owner (including Family Attribution rules if applicable) of the employer during the plan year or the preceding year; and/or
2. received more than \$90,000 (indexed for inflation¹) of annual compensation from the employer for the preceding year and, *as an optional election*², was in the top-paid 20% of the employer's employees.³

For this purpose, "compensation" means that received from the employer for the year determined without regard to Code Sections 125, 402(a)(8), and 402(h)(1)(B) and without regard to Code Section 403(b) in the case of employer contributions made under a salary reduction agreement.⁴ In the case of a self-employed individual, "compensation" means the person's earned income for the year.

Before implementing these rules, it is necessary first to apply the rules for Controlled Groups, Common Control, Affiliated Service Group aggregation, and leased employees. As a result, then, "employer" includes all companies or entities that are part of a Controlled Group of corporations or an Affiliated Service Group.

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1. For short plan years, indexed compensation limits are pro-rated.
 2. Once made, such election remains in force until changed. Notice 97-45
 3. Notice 2001-84 and Notice 2001-53 IRB 642
 4. Temp. Treas. Reg. 1.414(q)-IT, A-13