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# Minimum Coverage Requirements (IRC §410(b))

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Minimum Coverage rules require employers to offer their qualified benefit plan to a cross section of employees. For this purpose, each employee of each employer of a Controlled Group or Affiliated Service Group must be considered. A plan must meet either of two specified tests: the Ratio Percentage Test, or the Average Benefits Test.

As part of the family of defined benefit plans, 412(i) plans must also meet additional rules.

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## *Ratio Percentage Test*

A plan meets the Ratio Percentage Test for a plan year if the percentage of its benefiting Non-Highly Compensated Employees (NHCEs) is at least 70% of the percentage of its benefiting Highly Compensated Employees (HCEs). To "benefit" under a 412(i) plan, a participant must receive an allocation of employer contributions<sup>1</sup> funding for the year's benefit accrual.

**Example:** ABC Company 412(i) Plan benefits 70% of its Non-Highly Compensated Employees and 100% of its Highly Compensated Employees. The plan meets the Ratio Percentage Test because its percentage of NHCEs benefiting (70%) is at least 70% of its percentage of HCEs benefiting (100%).

**Example:** XYZ Company 412(i) Plan benefits 40% of its NHCEs and 60% of its HCEs. The plan does not meet the Ratio Percentage Test because its percentage of NHCEs benefiting (40%) is 67% of its percentage of HCEs benefiting (60%).

The following plans automatically satisfy the minimum coverage requirements of this test:

1. A plan with no NHCEs at any time during the plan year.
2. A plan benefiting no HCEs during the plan year.
3. A plan benefiting only collective bargaining employees.

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1. Reg. 1.410(b)-2(b)(2)(i) and Reg. 1.410(b)-9

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### *Average Benefits Test*

The Average Benefits Test is an alternative to meeting the minimum coverage requirements. All plans should initially attempt to pass the Ratio Percentage Test. If the plan does not pass the Ratio Percentage Test, employers should consult with legal counsel.

The Average Benefits Test has two components: (1) a "nondiscriminatory classification" test and (2) the "average benefit percentage" test. Both components must be met.<sup>2</sup>

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### *Excludable Employees*

Certain classifications of employees can be excluded when performing either of the above coverage tests<sup>3</sup>:

1. employees covered by a collective bargaining agreement,
2. nonresident aliens receiving no U.S. earned income, and
3. generally, employees who have not met the minimum age and services requirements<sup>4</sup> of the plan, as long as all such employees are excluded.
4. employees who have met the eligibility requirements but who terminated service during the plan year with fewer than 500 Hours of Service.

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### *Additional Rules For Defined Benefit Plans*

In addition to satisfying the above general coverage rules, defined benefit plans (including 412(i) plans) on a representative day each plan year must benefit<sup>5</sup> the lesser of:

1. 50 employees, and
2. the greater of 40% of all employees or 2 employees (or if there is only one employee, then that employee)<sup>6</sup>

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2. Reg. 1.410(b)-2(b)(3)

3. Reg. 1.410(b)-6(d) and Reg. 1.410(b)-9

4. However, when applying the Average Benefit Percentage Test, only those employees can be excluded who have not satisfied the lowest age and service requirements for *any* plan taken into account.

5. Plans out of compliance have may be amended retroactively no later than 9½ months after the end of the plan year. Treas. Reg. 1.401(a)(26)-7(c), and Treas. Reg. 1.401(a)(4)-11(g).

6. IRC 401(a)(26)