

CODE SECTION 105(h) NONDISCRIMINATION TESTING

WORKSHEET

Employer Information:

Name of Employer _____

Address of Employer _____

Employer Contact: Name _____

Phone _____ Email address: _____

Is the Employer part of a controlled group of Employers No. Yes. If the answer to the question is Yes, please list the names of all of the related employers below:

Please indicate the total number employees working for the Employer (include employees working for all members of the controlled group, if applicable) _____.

Please indicate the number of employees working for the Employer that are highly compensated (include employees working for all members of the controlled group, if applicable) _____.

Note: Code Section 105(h)(5) defines "highly compensated" as an individual who is:

- one of the five highest-paid officers;
- a shareholder who owns more than 10% of the value of stock of the employer's stock; or
- among the highest-paid 25% of all employees (other than excludable employees who aren't participants).

Please indicate the number of employees working for the employer that are nonhighly compensated (include employees working for all members of the controlled group, if applicable) _____.

Are there any employees who are not eligible for the coverage under the health plan(s)? No. Yes. Please indicate why:

Note: Code Section 105(h)(2)(B) excludes the following individuals from the highest-paid 25% of all employees, provided that they are not already participants:

- employees who have not completed three years of service;

- employees who have not attained age 25;
- part-time or seasonal employees;
- collectively bargained employees; and
- nonresident aliens who receive no U.S. source earned income.

The individuals listed above are referred to as “excludable employees.” Individuals not in that list are called “non-excludable employees.” These exclusions will apply only if these employees are not eligible to participate in the employer’s health plans.

Health Plan(s) Information:

What health plans are offered to employees? Please indicate _____

Are all health plans offered to all employees? Yes. No. If the answer to the question is No, please indicate which health plans are offered to which employees. _____

If not all health plans are offered to all employees, please indicate the number of highly compensated employees and nonhighly compensated employees eligible to participate in each health plan.

What are the eligibility requirements for each health plan? Please indicate _____

Benefits Test

The Benefits Test has two components: testing for discrimination on the face of the plan and testing for discrimination in operation.

Discrimination on the face of the Plan:

For each health plan offered by the employer, please answer the following questions:

- Does the same waiting period apply to all employees eligible under the plan Yes. No.
- Are the required employee contributions identical for each benefit level? Yes. No.
- Does the maximum benefit level not vary based on age, years of service, or compensation? Yes. No.
- Are the same type of benefits available to HCEs also available to Non-HCEs? Yes. No.

If the answer to any of the above questions is No, then the health plan does not pass the discrimination on the face of the plan test.

Discrimination in operation of the Plan:

- Has the health plan discriminated in favor of HCEs in actual operation? Yes. No. If Yes, Please describe
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Note: This is a “facts and circumstances” determination. Discrimination in operation “may occur where the duration of a particular benefit coincides with the period during which an HCE utilizes the benefit.

If the answer to the above question is Yes, then the health plan does not pass the test for discrimination in operation of the health plan.

Eligibility Test:

A health plan may pass under any one of four alternative tests:

- 70% Test. The plan covers 70% or more of all non-excludable employees.
- 70%/80% Test. The plan covers 80% or more of all non-excludable employees who are eligible to benefit, if 70% or more of all non-excludable employees are covered under the plan.
- Nondiscriminatory Classification Test. The plan benefits a nondiscriminatory classification of employees. This requires (1) a bona fide business classification for any exclusion, and (2) a sufficient ratio of benefiting non-HCEs to benefiting HCEs.
- Fair Cross Section Test. The plan benefits employees in fair cross section of employees

In running the Eligibility Test, an employer may exclude the following employees from consideration:

- employees who have not completed three years of service;
- employees who have not attained age 25;
- part-time or seasonal employees;
- collectively bargained employees; and
- nonresident aliens with no U.S. source income.

Note: The excludable categories can be excluded for testing purposes if they are not eligible to participate in the plan,

In conducting the Eligibility test, all employees are the controlled group must be considered.

70% Test: Does the each health plan cover 70 percent or more of all nonexcludable employees? Yes. No.

If the answer to the question is No, the 70% Test is failed, the employer should run the 70%/80% Test next.

70%/80% Test. Does each health plan cover 80% or more of all non-excludable employees who are eligible to benefit, if 70% or more of all non-excludable employees are covered under the plan. Yes. No.

If the answer to the question is No the 70%/80% Test is failed, the employer should run the Nondiscriminatory Classification Test.

Nondiscriminatory Classification Test:

A plan will satisfy this test for a plan year only if for the plan year both of the following requirements are met:

Reasonable Classification Test. The plan benefits employees who qualify under a reasonable classification established by the employer. A reasonable classification is established if, based on all the facts and circumstances, the classification is reasonable and uses objective business criteria that identify the category of employees who benefit under the plan. Reasonable classifications generally include specified job categories, nature of compensation (i.e., salaried or hourly), geographic location, and similar bona fide business criteria.

Nondiscriminatory Classification Test. The classification of employees is nondiscriminatory. This means that the group of employees included in the classification benefiting under the plan must satisfy either an objective Safe Harbor Percentage Test or a subjective Facts and Circumstances Test for the plan year.

Reasonable Classification Test:

Is the classification reasonable? Yes. No Please describe why the classification is reasonable:

Is the classification established under “objective business criteria that identify the category of employees who benefit under the plan”? Yes. No. Please describe what criteria is used:
reasonable: _____

If the answer to both questions is Yes, then proceed to the next section, Nondiscriminatory Classification. If the answer to either question is no, then the Plan fails the Reasonable Classification Test. Please skip testing under the Nondiscriminatory Classification Test and the health plan must be tested under the Fair Cross Section Test below.

Nondiscriminatory Classification Test

This test requires several mathematical calculations. The classification of employees benefiting under the health plan must satisfy a ratio percentage test, but under a reduced standard. The classification must satisfy either the “safe harbor test” or the “facts and circumstances test.”

Safe Harbor Test:

If a health plan’s ratio percentage is equal to or greater than the health plan’s “safe harbor percentage,” then the health plan passes the nondiscriminatory classification test. This determination requires three steps:

Step 1: The health plan’s ratio percentage is calculated. The health plan’s “Ratio percentage” means the percentage derived by dividing the percentage of non-HCEs benefiting under the health plan by the percentage of HCEs benefiting under the plan.

To calculate the percentage of non-HCEs covered under the health plan, the employer calculates a fraction: The numerator of the fraction is the number of non-HCEs who are covered under the Plan. The denominator is the total number of non-HCEs in the controlled group. Excludable non-HCEs are not counted in the denominator.

The fraction for the covered HCEs is calculated in a similar manner: The numerator of the fraction is the number of HCEs who covered under the health plan. The denominator is the total number of HCEs in the controlled group. Again, excludable HCEs are not counted in the denominator.

These fractions are converted to percentages and calculated to the nearest one-hundredth of a percentage point. The fractions for the ratio percentage test look like this:

$\frac{\text{Non-HCEs who benefit}}{\text{Total non-HCEs in controlled group}} = \text{Non-HCE benefiting percentage}$
$\frac{\text{HCEs who benefit}}{\text{Total HCEs in controlled group}} = \text{HCE benefiting percentage}$
$\frac{\text{Non-HCE benefiting percentage}}{\text{HCE benefiting percentage}} = \text{Plan's ratio percentage}^*$

* If this percentage is at least 70%, the benefit being tested passes the coverage test.

The health plan’s ratio percentage is _____.

Step 2: The “non-HCE concentration percentage” is calculated. The non-HCE concentration percentage is calculated using the following fraction: The numerator is the total number of the employer’s non-HCEs, and the denominator is the employer’s total employee population. These numbers are calculated on a controlled group basis, and excludable employees are disregarded.

The non-HCE concentration percentage is _____.

Step 3: The employer determines whether the health plan’s ratio percentage (calculated in Step 1) is equal to or greater than a safe harbor percentage, determined under the following table:

Non-Highly Compensated Employee Concentration Percentage	Safe Harbor Percentage	Unsafe Harbor Percentage
0-60	50.00	40.00
61	49.25	39.25
62	48.50	38.50
63	47.75	37.75
64	47.00	37.00

65	46.25	36.25
66	45.50	35.50
67	44.75	34.75
68	44.00	34.00
69	43.25	33.25
70	42.50	32.50
71	41.75	31.75
72	41.00	31.00
73	40.25	30.25

Non-Highly Compensated Employee Concentration Percentage	Safe Harbor Percentage	Unsafe Harbor Percentage
75	38.75	28.75
76	38.00	28.00
77	37.25	27.25
78	36.50	26.50
79	35.75	25.75
80	35.00	25.00
81	34.25	24.25
82	33.50	23.50
83	32.75	22.75
84	32.00	22.00
85	31.25	21.25
86	30.50	20.50
87	29.75	20.00
88	29.00	20.00
89	28.25	20.00
90	27.50	20.00
91	26.75	20.00
92	26.00	20.00
93	25.25	20.00
94	24.50	20.00
95	23.75	20.00
96	23.00	20.00
97	22.25	20.00
98	21.50	20.00
99	20.75	20.00

If the health plan's ratio percentage is above the Safe Harbor Percentage, then the health plan passes the Nondiscriminatory Classification Test and the health plan is not discriminatory. If the health Plan's ratio percentage is below the Unsafe Harbor Percentage, then the health plan fails the Nondiscriminatory Classification Test and health plan must be tested under the Fair Cross Section Test, described below. If the health plan's ratio percentage is between the below the Safe Harbor Percentage and not less the Unsafe Harbor Percentage, then the health can be tested under the Facts and Circumstances Test, described below.

Facts and Circumstances Test:

The classification for those employees covered under the health plan must also, based on all the relevant facts and circumstances, be found to be nondiscriminatory by the IRS. In reaching a conclusion, the IRS will not deem any single factor to compel a particular conclusion. Rather, the IRS will review the following relevant circumstances:

- the underlying business reason for the classification (the greater the business reason for the classification, the more likely the classification is to be nondiscriminatory—however, reducing the employer's cost of providing health benefits is not a relevant business reason);

The business reason for the classification is _____

- the percentage of the employer's employees covered under the health plan (the higher the percentage, the more likely the classification is to be nondiscriminatory);

The Percentage of the employees covered under the health plan is _____

- whether the number of employees covered under the health plan in each salary range is representative of the number of employees in each salary range of the employer's workforce (in general, the more representative the percentages of employees covered under the health plan in each salary range, the more likely the classification is to be nondiscriminatory); and

What salary ranges are covered under the health plan is _____

- the difference between the health plan's ratio percentage and the employer's safe harbor percentage (the smaller the difference, the more likely the classification is to be nondiscriminatory).

The difference is _____

After reviewing all of the above factors, the plan passes the facts and circumstances test or fails the facts and circumstances test.

If the plan fails the facts and circumstances test, the plan must pass the Fair Cross-Section Test.

Fair Cross-Section Test

Using this final method, the health plan may pass the Eligibility Test regardless of the percentage of eligible participants who actually participate. A health plan will satisfy the Fair Cross-Section Test, even when most plan participants are members of the prohibited group, if the following requirements are met:

- compensation of the participants is substantially the same as that of the excluded employees;

- the health plan covers employees in all compensation ranges;
- those in the middle and lower compensation range are covered in more than nominal numbers; and
- the classification on its face does not discriminate in favor of employees who are officers, shareholders, or HCEs

In addition, to assess whether the Fair Cross-Section Test is satisfied, the difference between the participation rates of the prohibited group members and the nonprohibited group members covered by the health plan must be examined, allowing for a reasonable difference between the two ratios.

After reviewing all of the above factors, the health plan passes the Fair Cross Section Test, or fails the Fair Cross Section Test.

If the plan fails the Fair Cross Section Test, the plan is deemed to be discriminatory.