From the compliance desk...

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Leased Employees – Impact on Eligibility

If leased employees are part of your workforce, there are potential impacts that must be considered with regard to eligibility and minimum coverage requirements. The provisions of your plan document define an employee as a common law employee, self-employed individual, leased employee or other person the Internal Revenue Code treats as an employee of the employer for purposes of the employer's qualified plan. Therefore, a leased employee is considered an employee with respect to your retirement plan. In addition, the IRS will treat a leased employee as an employee when determining whether your plan is in compliance with IRS rules.

> ***"...a leased employee is considered an employee with respect to your retirement plan..."***

The purpose of this newsletter is to provide guidance on who is considered a leased employee, the impacts of excluding leased employees from your retirement plan and how to credit service for any individual you employed through a leasing organization that you hire as a regular employee.

Who is considered a leased employee?

While an employer (the recipient) may utilize the services of an individual through a temporary employment agency or leasing organization, that individual is not considered a leased employee until the following criteria are satisfied:

- The individual works substantially full-time for at least one year. Substantially full-time means 1,500 hours in a 12-month period (or 75 percent of the customary hours in that job position, if less). If 75 percent is used, more than 500 hours must be credited to be substantially full-time, even if 75 percent of customary hours would be 500 or fewer hours
- Services are provided for a fee. The services must be performed under an agreement between the recipient and a leasing organization
- The recipient has primary direction or control over the individual's services
- The leasing organization, not the recipient, is the common law employer of the individual

Until an individual who works through a leasing organization satisfies the criteria of a leased employee they are considered as working for an unrelated employer for retirement plan purposes. This means they are totally disregarded when it comes to performing coverage and

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other nondiscrimination testing. If the leasing organization sponsors a money purchase plan for the leased employees with a contribution rate of at least 10 percent of compensation, immediate entry and immediate vesting, then the individual would not meet the definition of a leased employee and would not be considered an employee of the recipient.

Can a leased employee be excluded from the Plan?

An employer can exclude a class of employees from their retirement plan (e.g., leased employees, truck drivers, etc.) as long as the employer's plan can satisfy the minimum coverage requirements (a/k/a coverage test). There are several components involved in performing the coverage test, but simply stated, the minimum coverage requirements are satisfied if 70 percent of the nonhighly compensated employees benefit under the plan relative to the percentage of highly compensated employees who benefit under the plan. All employees that have satisfied eligibility are included in the calculation. Employees in an excluded class of employees (e.g., leased employees) that would have satisfied the plan's eligibility requirements are considered not benefiting under the plan for purposes of calculating the benefiting percentage.

If leased employees are excluded from the plan: Once an individual is considered a leased employee, and satisfies the plan's eligibility conditions, including meeting a plan entry date, it would be necessary to include him/her in the plan's coverage test. He/she would be considered not benefiting. A number of factors, including how many leased employees your company maintains, can cause the plan to fail the coverage test. If the plan fails the coverage test, one or more of the leased employees may have to be offered participation in the plan which would require the employer to fund a contribution(s) on behalf of the employee to make-up the employee's missed opportunity.

If leased employees are not excluded from the plan: Once an individual is considered a leased employee, and satisfies the plan's eligibility conditions, including meeting a plan entry date, he/she becomes an eligible participant and should be provided enrollment paperwork. Please note, that if your plan's eligibility conditions are less than a "year of service" the leased employee, in most cases, will have satisfied the plan's eligibility conditions and met a plan entry date, making him/her an eligible participant immediately.

What if a leased employee is hired as a regular employee?

If an individual who worked for you through a leasing organization is hired as a "regular" or common law employee, the service that individual performed for you through the leasing organization counts when determining eligibility and vesting. Therefore, you would need to count service from the date the individual started working for you through the leasing organization to determine when he/she satisfies eligibility under the plan. Failure to credit this service for retirement plan purposes could lead to operational compliance issues, such as missed contributions and incorrect vesting.

Given this information it is important to consider the impact of maintaining leased employees. For a number of employers it is a necessary part of doing business. Because of this, careful consideration should be given to:

1. How many leased employees are maintained
2. Length of time they are maintained
3. Impact on the plan if they are hired as a regular employee
4. Impact on the plan if they are not hired as a regular employee

In essence, maintaining leased employees can have a financial impact on your business as far as your qualified plan is concerned. If you have any questions, contact American Trust at 800.548.2994.