NATIONAL RETIREMENT SERVICES, INC.

LEASED EMPLOYEES CAN PRESENT RETIREMENT PLAN COMPLICATIONS

Employee leasing has been praised in many quarters as a boon to businesses. Employers may turn to an employee leasing company either due to the need for specialized employees or the desire to transfer all staffing, payroll and payroll accounting functions to an employee leasing organization.

Leased Employee Defined

Per Internal Revenue Code section 414(n), a Leased Employee is **not** a common law employee of the organization for whom he or she performs services (known as the "*recipient*") but is treated as an employee of the recipient for qualified retirement plan purposes. The following three conditions must also be met in order for an individual to be classified as a Leased Employee:

Services must be performed under an agreement between the common law employer (known as the "*leasing organization*") and the recipient of the individual's services. The agreement can be formal or informal.

Services must be performed for at least one year on a *substantially full time basis* (generally 1500 hours in a 12 month period, or 75% of the customary annual hours for that position, if less).

The individual's services are under the recipient's primary direction and control.

Any individual who satisfies the Leased Employee definition is treated as an employee of the recipient for retirement plan purposes, although Leased Employees may participate in retirement plans of the leasing organization. This includes plan coverage compliance, vesting rules, maximum Code 415 benefits, discrimination tests, and top heavy requirements.

Leased Employees for Specific Jobs

When companies choose to use leasing organizations for specific jobs, the number of Leased Employees is usually a relatively small percentage of total employees. Recipient companies who use Leased Employees' services frequently design their retirement plans to exclude Leased Employees. This simplifies matters for the recipient company and, as long as Leased Employees represent 30% or less of the work force, their exclusion from the recipient's retirement plans poses no problem. This is because coverage rules permit plans to exclude employees by classification. At least 30% of those employees not otherwise excluded due to plan minimum age or service requirements can be excluded due to employment classification. If a recipient chooses to not design the plan to exclude Leased Employees, these individuals are eligible after meeting the plan age and service eligibility requirements.

Leased Employees for the Whole Company

A company that wants to avoid most payroll and staffing headaches may contract with a leasing organization to lease virtually all of their employees. Technically, the employees cease to be common law employees of the original employer (now the recipient) and become employees of the leasing organization.

Suppose that the recipient has a tax qualified retirement plan. Does this mean that all employees other than the owners are terminated and can no longer participate in the old company's plan? The simple answer is, "No. Generally, the people who participated in the recipient's retirement plan before the leasing agreement went into effect continue to participate in the plan after it goes into effect." Similarly, no benefit distributions are required or permitted to participants as a result of their change in common law employers as long as they remain Leased Employees of the recipient. The reason that a leasing arrangement does not change retirement plan demographics is mainly because the *substantially full time basis* requirement includes examining prior employment history with the recipient employer. If someone already was a substantially full time employee of the recipient before the leasing agreement, they have already satisfied the "substantially full time basis" requirement.

Continued on the next page…

NATIONAL RETIREMENT SERVICES, INC.

New Leasing Agreement Impact on Retirement Benefits

As mentioned above, if a current employee becomes a Leased Employee because of an employee leasing agreement, retirement plan participation normally continues uninterrupted unless the plan excludes Leased Employees. Employment with the leasing organization counts as Vesting Service in the recipient's plan to the extent services are performed for the recipient. Those considered as Leased Employees may still be excluded from the plan based on their union status, age, hours, or length of service.

When Leased Employees are excluded by the plan and all or most employees are Leased Employees, the recipient should either eliminate the Leased Employee eligibility restriction or stop all future plan contributions. Otherwise, the plan will probably fail minimum coverage requirements. There is a special exception when testing for plan coverage compliance; but it has limited practical application. As long as the Leased Employees are covered in a money purchase plan providing a 10% of compensation employer contribution on a fully vested basis and as long as the employer leases no more than 20% of the workforce, the Leased Employees may be ignored for coverage compliance purposes.

If a recipient company has a Leased Employee on a substantially full time basis and subsequently hires the employee as a common law employee, the employee may become immediately eligible for the plan if he or she has met the plan age and service requirements. (Note that if the plan did not exclude Leased Employees, the individual may have already been a plan participant.) Vesting service would continue, dating back to the date the new common law employee first began work for the recipient company.

Retirement plans for employers that utilize leased employees present a myriad of relatively complex issues. Just determining whether there is a leasing agreement or whether certain individuals are Leased Employees can be difficult. Fortunately, upon request, the IRS will review presented facts and make an official determination of whether a leasing arrangement exists.

NRS can assist in the administration of Leased Employee retirement benefits and can provide coordination of any desired IRS submission.

REMINDERS FOR APRIL

April 15 - Refund excess 401(k) deferrals to participants

April 15 - File Form 5500 for PYE 6/30/11 if on extension

April 15 - Quarterly defined benefit plan contributions due

April 30 - PBGC Forms due for small calendar year DB plans

April 30 - EGTRRA document restatement required for pre-approved DB plans

FOR MORE INFORMATION OR TO REQUEST A PROPOSAL, PLEASE VISIT OUR WEBSITE AT WWW.NRSERVICES.COM, OR FOR SALES SUPPORT, PLEASE CONTACT:

CENTRAL & EASTERN TIME

Jim Houpt
Executive Vice President
T| (800) 627-1610 x 2207
E| jim.houpt@NRServices.com

PACIFIC & MOUNTAIN TIME

Kevin Spaeth
Sales Representative
T| (800) 350-2172 x 260
E| kevin.spaeth@NRServices.com

Continued on the next page…