

# *Qualified Retirement Plans*

## *Practice Alert*

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### **Workforce Reductions Can Trigger a Partial Termination**

With economic conditions causing significant layoffs it is possible that those employers that sponsor a qualified retirement plan may have inadvertently triggered a partial termination of their plan. The determination of whether or not a partial plan termination has occurred is based on the facts and circumstances in each case. Ultimately the analysis considers whether or not there has been a significant reduction in plan participants; if a plant or facility shutdown results in the exclusion of a group of employees from participation in the plan; a plan amendment that results in the exclusion of a group of employees from participation; or any other event the IRS determines to be a partial termination.

If a partial termination occurs the terminated participants must become 100% vested immediately regardless of their vesting service. General guidance is provided in Revenue Procedure 2007-43 indicating that a turnover rate of at least 20% creates a presumption that a partial termination has occurred. In any case the 20% is only a guideline, the facts and circumstances may indicate that a partial termination has not occurred. In some cases a partial termination may occur if the turnover is less than 20%. The turnover rate is calculated by dividing the terminated participants by the sum of the participants at the beginning of the plan year and employees that become participants during the plan year. Terminated participants are only those that have had an employer initiated termination during the year, i.e. not including voluntary termination, death, disability, etc. The IRS assumes all terminations are involuntary unless facts and circumstances show otherwise.

For defined benefit plans there is a special rule. If the benefits in the plan are frozen and as a result of that action there is a potential reversion of assets to the employer a partial termination has occurred. A reversion could occur if the assets in the plan are in excess of those necessary to pay the participants their accrued benefits, i.e. the benefits earned up to the date the plan was frozen. In addition a defined benefit plan must report certain events to the Pension Benefit Guarantee Corporation (PBGC) including a reduction of participants below 80% of those active at the beginning of the plan year or a facility shutdown that causes more than 20% of the participants to be terminated.

A partial termination does not by itself create a distributable event, i.e. those affected may not be able to receive a distribution of their benefits unless the participant has severed employment. An employer may apply to the IRS for a determination as to whether or not a partial termination has occurred although this process may take some time before a response is received. As an alternative the employer may take the position that a partial termination has occurred if the turnover rate is more than 20% and proceed with 100% vesting for those affected participants.

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