

# FYI<sup>®</sup> In-Depth

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## Health and Welfare Nondiscrimination Testing: A Series Summary

Certain employer-provided benefits are eligible for tax exclusions under the Internal Revenue Code. Each exclusion comes with an important condition — for executives and other highly paid individuals to take advantage of the exclusion, an employer must demonstrate that the benefit satisfies applicable nondiscrimination tests. Although the various tests include common elements, they can differ in significant respects. Over the past year, we have issued a series of six *FYI In-Depths* that discusses the general principles behind the nondiscrimination tests as well as the specific tests applicable to a particular benefit. This *FYI In-Depth*, the last of the series, is intended to serve as a consolidated easy-reference document and contains an overview of health and welfare benefit discrimination tests in a summary [table](#).

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## FYI Nondiscrimination Series

Our *FYI* series consists of the following previous issues of *FYI In-Depth*:

### Health and Welfare Nondiscrimination Testing: An Overview

After identifying the benefits that are subject to nondiscrimination testing under the Internal Revenue Code and explaining the rationale for the nondiscrimination requirements, this *FYI In-Depth* describes the elements common to all nondiscrimination testing, such as a prohibited group, an eligibility test, and a benefits/contributions/utilization test.

### Dependent Care Nondiscrimination Testing: An Overview

This *FYI In-Depth* discusses the four nondiscrimination tests applicable to employer-sponsored dependent care assistance programs — the eligibility test, the contributions and benefits test, the “5-percent owner” test, and the “55 percent average benefits” test. It also provides suggestions for how to reduce the likelihood of failing the eligibility test and the 55 percent average benefits test.

### Cafeteria Plan Nondiscrimination Testing: An Overview

This *FYI In-Depth* discusses the three nondiscrimination tests applicable to cafeteria plans — the eligibility test, the contributions and benefits test, and the "key employee" concentration test. This *FYI In-Depth* discusses the three nondiscrimination tests applicable to cafeteria plans — the eligibility test, the contributions and benefits test, and the "key employee" concentration test. It also describes how the definition of highly compensated for cafeteria plan discrimination testing differs from the definition used for other tests.

### Nondiscrimination Testing of Self-Insured Health Benefits: An Overview

This *FYI In-Depth* discusses the two nondiscrimination tests applicable to self-insured health benefits — the eligibility test and the benefits test. It describes how the determination of the prohibited group under this test differs significantly from the other tests and how retirees are taken into account.

### Nondiscrimination Testing of Life Insurance: An Overview

This *FYI In-Depth* discusses the two nondiscrimination tests applicable to group term life insurance benefits — the eligibility test and the benefits test — and describes how these apply only to "key employees."

### Nondiscrimination Testing of Educational and Adoption Assistance Programs: An Overview

This *FYI In-Depth* discusses the two nondiscrimination tests applicable to educational and adoption assistance programs — an eligibility test and a concentration test. It describes special rules for determining when an employee will be deemed eligible to benefit under a program and points out that failure to satisfy the nondiscrimination tests can adversely affect all program participants, not just those in the prohibited group.

### In closing

Running nondiscrimination tests on a regular basis enables an employer to demonstrate compliance and reduces the likelihood that they will face adverse tax consequences. In addition, testing results can create opportunities for employers to improve their benefit strategy and design.

## Overview of Health and Welfare Benefit Discrimination Tests

Regulatory Basis	Component Tests	Compensation for Determining Highly Compensated/Key Employee Status for 2019 (Calendar Year Plans)
Section 125 (Cafeteria Plan)	<ul style="list-style-type: none"> <li>• Eligibility Test</li> <li>• Contributions and Benefits Test</li> <li>• Key Employee Concentration Test</li> </ul>	<p>Highly compensated: 2018 compensation of at least \$120,000 and 2019 compensation of at least \$125,000 for those in first year of employment. Subject to top-paid group election<sup>i</sup>.</p> <p>Key employee: Officer with 2018 compensation of at least \$175,000; more than 1% owner with 2018 compensation of at least \$150,000<sup>ii</sup>. Limited to 50 officers for large employers. A governmental entity will have no key employees.</p>
Section 129 (Dependent Care)	<ul style="list-style-type: none"> <li>• Eligibility Test</li> <li>• Contributions and Benefits Test</li> <li>• More than 5% Owner Concentration Test</li> <li>• 55% Average Benefit Test</li> </ul>	Highly compensated: 2018 compensation of at least \$120,000. Subject to top-paid group election <sup>i</sup> .
Section 105(h) (Self-insured health plans including HRAs and health FSAs)	<ul style="list-style-type: none"> <li>• Eligibility Test</li> <li>• Benefits Test</li> </ul>	25% highest paid nonexcludable employees. Based on current plan year compensation.
Section 79 (Group Term Life)	<ul style="list-style-type: none"> <li>• Eligibility Test</li> <li>• Benefits Test</li> </ul>	Key employee: Officer with 2019 compensation of at least \$180,000; more than 1% owner with 2019 compensation of at least \$150,000. A governmental entity will have no key employees.
Section 127 (Educational Assistance)	<ul style="list-style-type: none"> <li>• Eligibility Test</li> <li>• More than 5% Owner Concentration Test</li> </ul>	2018 compensation of at least \$120,000. Subject to top-paid group election <sup>i</sup> .
Section 137 (Adoption Assistance)	<ul style="list-style-type: none"> <li>• Eligibility Test</li> <li>• More than 5% Owner Concentration Test</li> </ul>	2018 compensation of at least \$120,000. Subject to top-paid group election <sup>i</sup> .

<sup>i</sup> Top paid group election. Subject to certain restrictions, an employer may elect to assign highly compensated status on to those individuals/participants who meet the applicable compensation threshold and, for the applicable year, were among the group consisting of the top 20% of nonexcludable employees when ranked on the basis of compensation during such year.

<sup>ii</sup> Key employee for cafeteria plan testing purposes. The proposed cafeteria plan regulations state that for testing purposes, a key employee is a participant who was a key employee at any time during the *preceding* plan year. However, IRS Publication 15-B, *Employer's Tax Guide to Fringe Benefits*, seems to use current plan year status.

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