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IRS PROVIDES RELIEF FROM DISQUALIFICATION OF DEFINED CONTRIBUTION RETIREMENT PLANS MAINTAINED BY PROFESSIONAL EMPLOYER ORGANIZATIONS

WASHINGTON - The Internal Revenue Service today issued guidance intended to assist professional employer organizations (PEOs) with maintaining defined contribution plans.

PEOs are also commonly known as employee leasing organizations. These organizations, a growing industry in the past decade, contract with firms to undertake their human resource and personnel functions. The services PEOs provide may include health benefits, workers' compensation claims, payroll, payroll tax compliance, retirement plans and unemployment insurance claims. The industry's trade association estimates that nationally there are more than 2 million workers employed through these organizations.

Questions have arisen, however, regarding the qualified status of plans maintained by PEOs. If a plan provides benefits for individuals who are not the employees of the employer maintaining the plan, the plan could be disqualified because it would not satisfy the exclusive benefit rule of section 401(a)(2) of the Internal Revenue Code. The exclusive benefit rule provides that a trust forming part of a qualified plan must be established and maintained by an employer for the exclusive benefit of that employer's employees.

In recognition of the complexity involved in determining whether workers are common law employees of a PEO or its clients, the IRS is providing limited relief. This relief provides plan administrators and other interested parties with some certainty that defined contribution plans that are currently being maintained by PEOs will not be treated as violating, or as having violated, the exclusive benefit rule solely because the plan provides benefits to workers performing services for clients.

In this regard, the revenue procedure provides that a PEO that maintains a defined contribution plan that benefits workers of its clients can avoid disqualification for violating the exclusive benefit rule by adopting a multiple employer plan.

For PEOs that do not want to adopt a multiple employer plan, the revenue procedure provides transition rules under which the existing defined contribution plan will be treated as a qualified plan if it is terminated by a date specified in the revenue procedure. The revenue procedure also provides relief for clients with workers currently participating in a plan maintained by a PEO.

Revenue Procedure 2002-21 will be available on the IRS Web site at and *www.irs.gov* and will be published in the Internal Revenue Bulletin 2002-19 on May 13.

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