Exam Number

UNIVERSITY OF KENTUCKY

COLLEGE OF LAW

EMPLOYEE BENEFITS LAW PROFESSOR MOORE

FINAL EXAMINATION SPRING 1995

TIME LIMIT: 3 HOURS

INSTRUCTIONS

This is an open book examination. You may use a hand-held calculator and any written materials, including notes, outlines, books, articles, etc., during the exam.

The exam consists of 5 questions. The point allocation for each question is as follows:

Question I 70 points
Question II 60 points
Question III 30 points
Question IV 10 points
Question V 10 points

The number of points allocated to each question indicates how much time you should spend on it.

For purposes of this examination, assume that inflation does not exist. Thus, ignore any cost-of-living adjustments that may have been made to statutory dollar amounts.

This is not a test of your mathematical ability. A correct description of how an answer should be calculated is likely to earn more credit than simply giving the correct number.

Write your answers in pen in the blue books. Only write on the front side of each page of the blue book(s). Although you may use scratch paper, I will only consider materials written in the blue books in grading the exam. Be sure to put your exam number on this page and the cover of each blue book. At the end of the examination, please number your blue books, e.g., 1 of 2, 2 of 2, and turn in your exam, your blue book(s), and any scratch paper you have used. These materials should be collected and turned in together inside one blue book.

All academic endeavors of the students of the University of Kentucky College of Law are governed by the Honor Code. The Honor Code prohibits lying, cheating, stealing, and interference with academic pursuits. In addition, the Honor Code places an affirmative duty to report a breach of the Code on all students. A failure to report is a violation of the Honor Code.

In turning in this exam, I hereby pledge on my honor as a student that I have neither given nor received any unauthorized aid on this exam.
QUESTION ONE
(SUGGESTED TIME: 70 MINUTES)

A, B, C, and D, individuals, have negotiated two joint investments, which they will carry out in the form of Corporations P and Q. Ninety (90) percent of the stock in P and 80% of the stock in Q is held in equal shares by investors A, B, C, and D.

Corporation P has 4 employees: a President, E, who makes $40,000 per year; A who makes $38,000 per year; and two salesmen (F and G) who make $48,000 per year.

Corporation Q has 5 employees: a President (H) who makes $42,000 per year; 3 salesmen (I, J, and K) who make $45,000 per year; and a salesman (L) who makes $53,000 per year.

H, the President of Corporation Q would like to set up a profit-sharing plan for the employees of Corporation Q to which the company would contribute 6% of the compensation earned by H and I, and 5% of the compensation earned by J, K, and L.

Please explain to H why the plan would or would not satisfy IRC sections 401(a)(26), 410(b), and 401(a)(4), and why the Code requires that a plan satisfy these provisions in order to be tax-qualified.

QUESTION TWO
(SUGGESTED TIME: 60 MINUTES)

Zara, age 65, has worked for Wethington Enterprises and participated in the Wethington Enterprises Profit-Sharing Plan for the last 20 years. Recently, she announced that she plans to retire from her position as an accounting clerk at the end of the month. She has requested that her vested account balance in the Wethington Enterprises Profit-Sharing Plan be distributed to her in the form of a life annuity when she retires. As Mitchell, Zara's boss, was calculating her annuity, he discovered that for the last fifteen years Zara had been allocating all forfeitures to her account rather than allocating them among all the participants' accounts on the basis of their vested account balances as required by the terms of the Plan.

Section 6.8 of the Plan provides that "notwithstanding any other provisions of this Agreement to the contrary, the right of any Participant or former participant to receive or to have paid to any other person and the right of any such other person shall be forever forfeited if such Participant's employment with the Employer is terminated because of his fraud, embezzlement, or dishonesty." Section 15.5 provides that "Plan Fiduciaries shall be absolved from any and all liability for any breach of their fiduciary responsibilities."

Brian, President of Wethington Enterprises, has advised you that he plans to terminate Zara before the end of the month and wants to sue her and Mitchell for (1) breach of contract, (2) breach of the implied covenants of good faith and fair dealing, (3) bad faith tort, (4) breach of ERISA 404(a)(1)(A), (5) breach of ERISA 404(a)(1)(B), and (6) breach of ERISA 404(a)(1)(D).

Brian has asked you to assess the likelihood of each of these claims succeeding and the amount of damages likely to be awarded if any of the claims are successful. Brian has also asked you whether Zara is entitled to any annuity in light of her dishonesty, and if she is entitled to an annuity, whether that annuity must include amounts attributable to her dishonesty.
QUESTION THREE
(SUGGESTED TIME: 30 MINUTES)

Your cousin, Selfish, heads up a division of a department store. There are two other divisions. Your cousin makes $85,000 per year; the others in the division make between $20,000 and $50,000. The yearly compensation for all employees in the store comes to around $10 million; total compensation is roughly equal between the divisions.

The store does not have a retirement plan. The Board of Directors wants to establish a profit-sharing plan for its employees. The Board's only requirements are that all employees be covered, that the yearly contribution cost to the plan be no more than $500,000, and that the plan be tax qualified.

Selfish is assigned to work with the store's accountant to develop the plan and is given complete authority in setting contributions levels, so long as the Board's requirements are met. Selfish consults his own financial advisor, who tells him that a plan providing for employer contributions of 8% of his compensation will perfectly suit his personal retirement needs. Selfish then goes to the store's accountant and suggests an 8% employer contribution plan. The accountant says that this is not feasible since 8% of each and every employee's compensation would have to be contributed and that would make its cost too high for the board.

Selfish still wants an 8% plan for himself so he asks the accountant whether anything can be done to reduce the store's overall obligation to contribute, while at the same time giving him an 8% contribution and meeting the store's requirements. The accountant says "no" and repeats his explanation in the preceding paragraph. Is the accountant right? Discuss.

QUESTION FOUR
(SUGGESTED TIME: 10 MINUTES)

Verboten announces that, as of January 1, 1996, it is amending its defined benefit plan so as to eliminate the availability of all early retirement benefits for its factory workers. Such benefits have been available since the early 1960s. What issues does this raise? If you were the company's attorney, how would you advise it to restructure its amendment?

QUESTION FIVE
(SUGGESTED TIME: 10 MINUTES)

Maria is terminating employment with Host Corp., her employer. Host Corp. maintains a tax-qualified defined benefit pension plan under which Maria may elect to receive benefits in the form of a life annuity or a lump sum. Maria is only 45 years old and has an accrued benefit in the defined benefit plan which has an actuarial lump sum present value of $50,000. Maria would like to preserve the tax exempt status of this benefit but is unsure whether to leave the money behind in the pension plan or take it out and put it somewhere else.

Please advise Maria on the various ways in which she may avoid paying tax on her benefits and what conditions she must satisfy to do so.