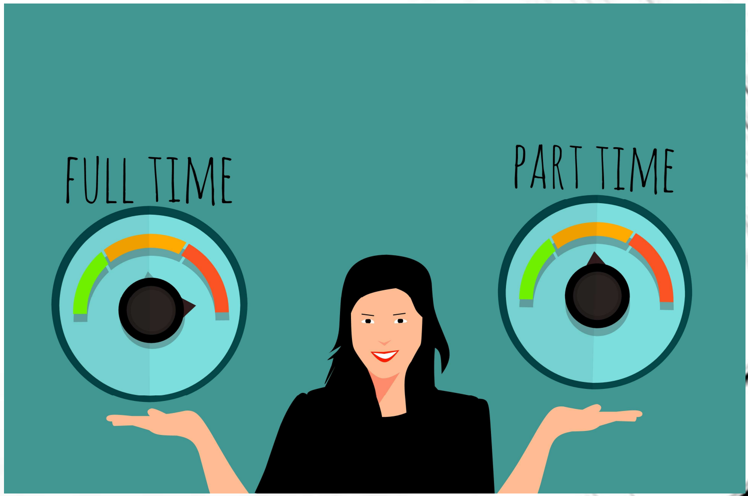
Long-Term Part-Time Employee Rules:
Will they apply to my plan?



Presenter Information

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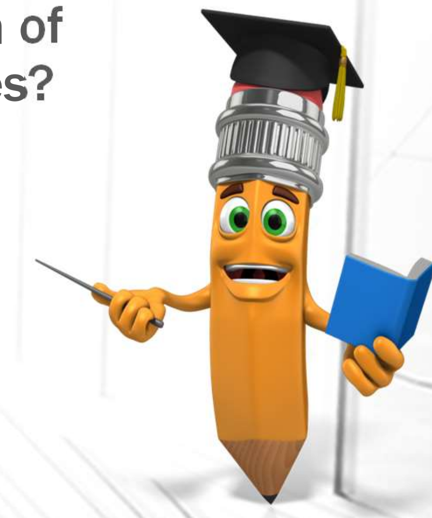
What we'll cover

- Fundamentals of the Eligibility Rules
- Rehired employees
- Part-time employee exclusion
- LTPT employee provision
- Top heavy changes
- LTPT Employee Rule – SECURE 2.0
- Can we design a 401(k) plan to avoid the application of the LTPT employee rules?
- Elapsed Time



Fundamentals of the Eligibility Rules

Age and service conditions

- Statutory Maximum Eligibility Requirements
  - A plan using a vesting schedule may not require more than **one year of service** (YOS) and **age 21** as eligibility conditions
  - A plan that provides immediate 100% vesting upon participation may require **two years of service** as an eligibility condition (**not deferrals**)
- All Service Counts
  - Plan must count all of an EE's service for eligibility purposes unless a break in service (BIS) rule applies

Early eligibility

- Plans may permit early eligibility (i.e., less than 1 YOS or less than age 21, or both)
- Review plans terms for:
  - early eligibility conditions, and
  - what are the eligibility conditions if the early eligibility conditions are not initially satisfied
- Hours requirement within short period is typically prorated based on YOS (i.e., 500 HOS in 6 months)
- Typically, if no hours of service requirement, the condition is merely the passage of time
- If early eligibility conditions not initially satisfied may not under any circumstances require more than the statutory maximum (i.e., age 21 and 1 YOS)

Early eligibility (con’t)

- Examples of early eligibility conditions:
  - 3 months with 250 hours of service
  - 6 months with 500 hours of service
  - 6 months (no HOS requirement - mere passage of time)
- What is the eligibility condition if the early eligibility condition not initially satisfied:
  - Default to a regular year of service (1 YOS), or
  - Reset eligibility period (only if condition is 6 months or less)

What is the required time of participation?

- Once an EE has satisfied plan's eligibility conditions, EE must enter the plan on the earlier of two dates:
  - Six months after completing plan's eligibility conditions
  - First day of next PY

  Beware of re-employed EEs!

Rehired Employees

Service and eligibility guiding principle

- Hours and Years of Service always count for purposes of eligibility
    - And they don't stop counting
    - Only exception is BIS (break in service rules)
        - Very, very limited
        - Many plans have eliminated BIS rules for eligibility purposes because they rarely apply and are difficult to administer

Classes of rehired employees and when they enter (re-enter)

Class	Entry
Already satisfied minimum age and service and entered plan	Immediately upon rehire
Already satisfied minimum age and service but terminated employment before entry date	Immediately upon rehire (or original entry date, if later)
Already satisfied minimum service but didn’t enter plan because of minimum age requirement	Immediately upon rehire (or entry date following attainment of minimum age, if later)
Didn’t satisfy minimum service requirement	Wait until entry date following satisfaction of eligibility requirements

- Break in service rules can affect this, depending on plan terms

Case study: When does Bob enter (re-enter?)

- ABC hired Bob May 1, 2017
- ABC calendar year 401(k) plan has:
  - 1 YOS/Age 21 entry requirements
  - January 1/July 1 entry dates
  - Shifting eligibility computation period
  - No eligibility break-in-service rules
- Bob always works 150 hours/month
- *When does Bob enter/re-enter plan after rehire?*

	Bob's Birthday	Bob Quits	Bob Rehired
a)	Feb. 1, 1982	Aug. 1, 2018	May 15, 2020
b)	Feb. 1, 1982	Feb. 1, 2018	May 15, 2020
c)	Feb. 1, 1982	Feb. 1, 2018	May 18, 2018
d)	Feb. 1, 1982	Aug. 1, **2017**	Mar. 1, 2019
e)	Feb. 1, 2000	Aug. 1, 2018	May 15, 2019
f)	Feb. 1, 2000	Aug. 1, 2018	Dec. 15, 2021

Part-Time Employee Exclusion

Can we exclude part-time EEs as a classification?

- IRS can challenge such an exclusion as a “disguised service condition”
  - Any exclusion category that defines itself by service (*e.g.*, temporary, seasonal, etc.) is potentially an issue
  - Ex.: Plan excludes part-time employees. Plan defines part-time as anyone who normally works less 30 hrs/week. Plan has effectively imposed a 1500 hr. eligibility condition. Violates eligibility rules
- Code §410(a) establishes parameters of service condition (1,000 hours)

February 14, 2006 Quality Assurance Bulletin

- Instructed agents to challenge part-time EE exclusions based on hours of service
  - No reliance on post 6/30/01 DL letters
- QAB provides guidance on how to design a part-time EE exclusion:

1. Plan can exclude part-time as long as part-time defined as EE scheduled to work less than 1,000 HOS
2. Must also include fail-safe language for part-time EE who actually works 1,000 HOS

Part-time EE exclusion

- Plan may exclude part-time employees (e.g., typically defined as "expected to work not more than 1000 hrs/year)
- Plan design:
  - Safe harbor 401(k) match
  - Immediate eligibility for deferrals
  - 1 YOS/age 21 for nonelective
  - Excludes part-time employees
  - Top-heavy plan
- Benefit: Part-time employees don't participate (saves administrative costs and employer contributions)
  - If TH plan, no TH minimum for part-timers because they are not participants

Long-Term Part-Time (LTPT) Employee Provision

SECURE Act 1.0

Long Term Part-Time Employee Provision

- Except in the case of collectively bargained plans, the SECURE Act 1.0 provision will require employers maintaining a 401(k) plan (and 403(b)) to have a dual eligibility requirement
- An employee must be treated as satisfying the plan's eligibility service requirement on the earlier of completing:

1. one year of service requirement (with the 1,000-hour rule), or
2. three consecutive years of service where the employee completes at least 500 hours of service.

Effective for plan years beginning after 2020

Eligibility Rules

- **Age requirement.** The LTPT employee also must satisfy the plan's age requirement to enter the plan
- **Entry dates.** In applying the new long-term part-time employee provision, the plan may apply plan entry date provisions – early of the first day of the plan year or 6 months following completion of the eligibility requirements (e.g., semi-annual entry dates)
- **Service periods.** In apply the service requirements, the plan determines the service periods (12-month periods) in the same manner as it determines years of service
  - Anniversaries of the employment commencement date or the plan may switch to the plan year
- **Crediting service.** A plan doesn't have to begin crediting eligibility service until 2021
  - First entry would be in 2024

Statutory Exclusions

- LTPT employee rule does not affect the statutory exclusions:
  - Union employees
  - Non-resident aliens with no US source income
  - Airline pilots subject to certain union agreements

Example

- Company X maintains a calendar year 401(k) plan
  - Eligibility: 1 YOS/age 21/semi-annual entry dates
  - Eligibility computation period: switches to plan year after first year
- Mary is a part-time employee (50hrs/month)
  - Commenced employment on December 1, 2023
  - She will complete 2 consecutive years under LTPT rule on December 31, 2024 and enter the plan on January 1, 2025
- Assume the same facts except the plan measures computation periods on anniversaries of the employment commencement date
  - Mary will complete 2 consecutive years on November 30, 2025 and enter the plan on January 1, 2026
- ***Note: 401(k) plans should consider no longer shifting eligibility computation periods***

Employer Nonelective and Matching Contributions

- The new LTPT employee rule <u>only</u> requires the plan to make elective deferrals available to such employees
- The plan does not need to provide employer nonelective or matching contributions for the LTPT employees
  - However, an employer may provide employer contributions to LTPT employees
- The plan does not need to provide top heavy minimums

Nondiscrimination Testing

- **Exclude LTPT employees.** In the case of employees who are eligible solely by reason of the new rule (500 HOS in three consecutive years), the employer may elect to exclude such employees from:
  - Coverage and nondiscrimination testing, including the ADP and ACP tests
  - If the employer elects to provide employer nonelective or matching contributions to LTPT employees, the employer may elect to excude such employees from nondiscrimination and testing
- **Cross-testing plans.** An employer may find that providing nonelective contributions to LTPT employees and including them in the nondiscrimination testing may be beneficial
  - Employers have the option to include the LTPT employees

Exclusions

- If the LTPT employee is part of a plan exclusion class (e.g., mailroom employees, division A employees, truck drivers), will the employee be excluded even if he/she satisfies the eligibility requirements?
  - *Possibly. We will need to see additional guidance from the IRS.*
- If the plan excludes part-time employees, will a long-term part-time employee be excluded from participating?
  - *No. The part-time employee exclusion is effectively a service requirement and not an exclusion. Accordingly, if an employee satisfied the conditions of the LTPT employee, the plan would need to allow them to participate in the 401(k) plan irrespective of the part-time employee exclusion.*
  - *The plan could continue to apply the part-time employee exclusion to deferrals up until the LTPT employee rule is triggered. Also, the plan could apply the part-time employee exclusion to employer contributions*

Vesting

- **Vesting YOS.** If the part-time employee receives an employer contribution, the plan will determine his/her vesting percentage, the plan will treat each 12-month period for which the employee has at least 500 hours of service as a year of service
- **BIS rules.** The plan will apply the break-in-service rules by substituting 'at least 500 hours of service' for 'more than 500 hours of service
- **Crediting vesting YOS.** Years before 2021 are disregarded for 401(k) vesting (applies immediately). *SECURE 2.0 Technical Correction to SECURE 1.0*
  - Unless an exception exists (e.g. disregarding of years of service prior to age 18), a LTPT employee will receive credit for all service from January 1, 2021 for purposes of vesting

Employees Who Become Full-Time Employees

- The new long-term part-time employee provision will cease to apply (with the exception of the vesting provision) to any employee as of the first plan year beginning after the plan year in which the employee meets the plan's normal eligibility requirements

Top Heavy Changes
Secure Act 2.0 §310

Top Heavy

- Employees who are eligible to participate in the plan solely because of the new part-time provision are excluded from the vesting and benefit provisions of the top heavy rules
  - Such employees also are not included in determining whether the plan is top heavy
- A Safe Harbor 401(k) plan that is designed to be top heavy exempt will <u>not</u> lose its top heavy exempt status because a LTPT employee doesn't receive Safe Harbor 401(k) nonelective or match

Top-Heavy and Otherwise Excludable Employee

- If plan covers otherwise excludable employees (less than 1 YOS), can treat them as a separate group for purposes of top-heavy minimum contribution in defined contribution plan
  - This means the OEEs don't need to receive the TH minimum
- However, a safe harbor 401(k) which allows OEEs to defer but not receive the SH contribution will not be a safe harbor 401(k) top heavy exempt plan

Act Section
310
Code Section
416
Qualified
DC
403(b)
No
457(b)
No
Eff. Date
Plan years after 2023

Example

- Law firm maintains a safe harbor 401k plan
  - One YOS/age 21 eligibility requirements
  - In addition to deferrals, the plan provides a basic SH match and PS contributions
  - For 2023, the law firm doesn't make a profit sharing contribution
  - The plan is top heavy exempt and the firm doesn't have to make an additional TH minimum contribution

Example: Law Firm, Inc. (2023)

Name	Position	Net Comp	Deferral	Basic SH Match	TH Minimum	Fulltime?	1 YOS?
Sam	Shareholder	$330,000	$30,000	$13,200	$0	Full	Yes
Sue	Shareholder	$330,000	$22,500	$13,200	$0	Full	Yes
Anne	Associate	$84,000	$6,000	$3,360	$0	Full	Yes
Maria	Office Manager	$58,000	$2,000	$1,870	$0	Full	Yes
Tony	Secretary	$39,000	$1,000	$1,000	$0	Full	Yes
Frank	Filing Clerk	$24,000	$0	$0	$0	Full	Yes
Tina	Secretary	$30,000	$0	$0	$0	Full	No
Carl	Law Clerk	$13,500	$0	$0	$0	800 HOS	No

- Eligibility: 1 YOS/age 21 (so Tina and Carl don't participate)
- Safe harbor 401(k) plan is top heavy exempt
- The firm doesn't need to make a TH minimum contribution for Tony and Frank

Example

- Assume the same facts as in the previous example, except the law firm amends the plan to provide immediate eligibility for deferrals (one YOS/age 21 continues to apply for the SH match) and excludes part-time employees
  - For 2023, X applies the OEE rule for coverage and nondiscrimination
  - Under the OEE rule, the upper group plan is SH and doesn't need to apply the ADP or ACP tests
  - Since the OEE doesn't apply for TH purposes, X will have to make TH minimum contributions for all eligible EEs, including those EEs with less than a year of service (Tony, Frank and Tina)

Example: Law Firm, Inc. (2023)

Name	Position	Net Comp	Deferral	Basic SH Match	TH Minimum	Fulltime?	1 YOS?
Sam	Shareholder	$330,000	$30,000	$13,200	$0	Full	Yes
Sue	Shareholder	$330,000	$22,500	$13,200	$0	Full	Yes
Anne	Associate	$84,000	$6,000	$3,360	$0	Full	Yes
Maria	Office Manager	$58,000	$2,000	$1,870	$0	Full	Yes
Tony	Secretary	$39,000	$1,000	$1,000	$200	Full	Yes
Frank	Filing Clerk	$24,000	$0	$0	$720	Full	Yes
Tina	Secretary	$29,500	$500	$0	$900	Full	No
Carl	Law Clerk	$13,500	$0	$0	$0	800 HOS	No

- Safe harbor 401(k) plan is NOT top heavy exempt
- Tony, Frank and Tina must receive the TH minimum

Example

- Assume the same facts as in the previous example, except the plan year is 2024
  - For 2024, X applies the OEE rule for coverage and nondiscrimination
  - Under the OEE rule, the upper group plan is SH and doesn't need to apply the ADP or ACP tests
  - Commencing in 2024, Section 310 provides that the firm will not need to make a TH minimum contribution to the OEEs (Tina)
  - Unfortunately, Section 310 doesn't address the top heavy exemption for the "upper" group
    - Accordingly, the firm will need to make a TH minimum contribution for the upper group employees

Example: Law Firm, Inc. (2024)

Name	Position	Net Comp	Deferral	Basic SH Match	TH Minimum	Fulltime?	1 YOS?
Sam	Shareholder	$330,000	$30,000	$13,200	$0	Full	Yes
Sue	Shareholder	$330,000	$22,500	$13,200	$0	Full	Yes
Anne	Associate	$84,000	$6,000	$3,360	$0	Full	Yes
Maria	Office Manager	$58,000	$2,000	$1,870	$0	Full	Yes
Tony	Secretary	$39,000	$1,000	$1,000	$200	Full	Yes
Frank	Filing Clerk	$24,000	$0	$0	$720	Full	Yes
Tina	Secretary	$29,500	$500	$0	$0	Full	No
Carl	Law Clerk	$13,500	$0	$0	$0	800 HOS	No

- Eligibility: Immediate eligibility for deferrals (Tina can defer) but excludes part-time EEs (Carl can't participate); 1 YOS/age 21 for SH match (so Tina and Carl don't participate)
- SECURE §310 states that the plan doesn't need to give TH minimum to OEE (Tina), however, it doesn't preserve TH exemption (Tony and Frank)

Example

- Assume instead the plan year is 2025 and the plan imposes the following eligibility conditions:
  - 6 months and 500 hours/age 21 for elective deferrals
  - One YOS/age 21 for the SH Match
- 2025
  - Tina enters the plan under the early eligibility provision and is eligible to defer but not yet eligible for the SH match. Because of Section 310, Tina doesn’t receive the TH minimum.
  - Carl is eligible to defer under the LTPT employee rules.
  - Because of Tina, the plan is not top heavy exempt

Example

- Forbes Family Dentistry (FFD) maintains a 401(k) plan
  - Eligibility requirements: 1 YOS/Age 21
  - Semi-annual entry dates: 1/1 and 7/1
  - Matching and Profit Sharing contributions
  - Top heavy
- Ann, a dental assistant, has worked part-time (600-800 HOS/year) for FFD since 2018
  - Because of the plan's eligibility requirements she has never participated in the plan

Example (cont.)

- *Will Ann be eligible under the new law? If so, when?*
  - Yes. January 1, 2024
- *Will Ann be eligible for the match? Profit sharing contribution? Top heavy minimum?*
  - No with respect to all three questions
- *Will Ann be included in the coverage test? ADP test? ACP test? Top heavy determination?*
  - No with respect to all four questions
- *If the plan excluded all dental assistants, would Ann be eligible to participate in the plan?*
  - Not certain. We will need guidance from the IRS to answer this question.
- *If the plan excluded part-time employees, would Ann be eligible to participate in the plan?*
  - Yes. We are confident that the LTPT employee rule will trump the part-time employee exclusion.

Example

- Corporation X maintains a 401(k) plan with one YOS/age 21 eligibility conditions and semi-annual entry dates (1/1 and 7/1)
  - Plan provides for deferrals, matching contributions and profit sharing contributions
  - In addition to its 30 full-time employees, X employs 4 part-time employees who have been with the company for several years
- How will the new LTPT employee rule affect their participation in the 401(k) plan?

	Ann	Ben	Cathy	Don
2021	500	500	500	0
2022	500	1000	400	500
2023	500	500	500	500
2024	500	500	500	500
2025	500	500	500	500
2026	400	500	500	500

	Ann	Ben	Cathy	Don
2021	500 V E	500	500	0
2022	500 V E	1000	400	500
2023	500 V E	500	500	500
2024	500 V P (enters plan)	500	500	500
2025	400 P	500	500	500
2026	500 V P	500	500	500

	Ann	Ben	Cathy	Don
2021	500	500 V E	500	0
2022	500	1000 V E	400	500
2023	500	500 V? P (enters pan)	500	500
2024	500	500 V? P	500	500
2025	500	500 V? P	500	500
2026	400	500 V? P	500	500

	Ann	Ben	Cathy	Don
2021	500	500	500 V E	0
2022	500	1000	400	500
2023	500	500	500 V E	500
2024	500	500	500 V E	500
2025	500	500	500 V P (enters plan)	500
2026	400	500	500 V P	500

	Ann	Ben	Cathy	Don
2021	500	500	500	0
2022	500	1000	400	500 V E
2023	500	500	500	500 V E
2024	500	500	500	500 V E
2025	500	500	500	500 V P (enters plan)
2026	400	500	500	500 V P

LTPT Questions and Issues

- Are LTPT employees part of Form 5500 participant account?
  - Yes.
  - However, starting with the 2023 plan year, DC plans will determine large-plan status using the number of participants with account balances at the beginning of the plan year
  - Employees who are eligible (including LTPT employees) but not participating don't count toward the audit threshold
- Does the new LTPT employee provision apply to 457(b) plans?
  - No.

Mandatory Automatic Enrollment

- New 401(k) and 403(b) plans required to have automatic enrollment EACA
- Default deferral percentage
  - First year 3% to 10%
  - Auto increase of 1%/year thereafter
    - Capped at 10 – 15%
- QDIA unless participant makes different choice
- Must allow permissible withdrawals (up to 90 days after first auto deferral)
- **Will apply to LTPT employees**

Act Section
101
Code Section
414A
Qualified
401(k)
403(b)
Yes
457(b)
No
Eff. Date
Plan Years after **2024**

Exemptions

- SIMPLE 401(k)
- Plans established before 12/29/2022
- Governmental and church plans
- Plans sponsored by employer that <u>normally</u> employs fewer than 11 employees
  - Exemption expires 1 year after close of first tax year after employer goes over limit
- New business: exempt during first 3 years of existence of the business or a predecessor business

LTPT Employees SECURE Act 2.0

Long-Term Part-Time Employee Rule (SECURE 2.0)

- LTPT is EE who has 2 consecutive eligibility computation periods with 500 – 999 HOS and attained age 21
  - Replaces the 3 consecutive years requirement
  - Disregard years before 2023 for eligibility
  - Disregard years before 2021 for vesting
  - Added LTPT employee provision to ERISA

Act Section
125
Code Section
401(k)(15)
Qualified
401(k)
403(b)
YES
457(b)
No
Eff. Date
Plan Years after 2024

403(b): LTPT EE Rules

- LTPT rules apply to 403(b) plans
  - Limited to 403(b) plans subject to ERISA
    - Doesn't apply to governmental or church 403(b) plans
  - Disregard years beginning before 2023 for eligibility and vesting
- LTPT is EE who has 2 consecutive eligibility computation periods with 500 – 999 HOS and attained age 21
- Why do you need LTPT EE rule when 403(b) plans apply universal availability?
  - Overrides 20-hour and student employee exemptions from universal availability

Universal Availability Rules

- 403(b)(12)(A) – Universal Availability rules
  - Permits the exclusion of student employees and employees who normally work less than 20 hours per week
- Exclusion group is still subject to LTPT employee rules
  - Appears then, that even if 403(b) Plan has these exclusions, these employees will be subject to LTPT requirements
- IRS guidance will need to clarify

403(b) Exclusions

- Below is the excerpt from Internal Revenue Code (the "Code") Section 403(b)(12)(A) regarding Universal Availability, as written before SECURE 2.0 kicks in:
- For purposes of paragraph (1)(D), a plan meets the nondiscrimination requirements of this paragraph if … (ii) all employees of the organization may elect to have the employer make contributions of more than $200 pursuant to a salary reduction agreement if any employee of the organization may elect to have the organization make contributions for such contracts pursuant to such agreement.
- … For purposes of clause (ii)…
- Subject to the conditions applicable under section 410(b)(4), there may be excluded for purposes of this subparagraph employees who are students performing services described in section 3121(b)(10) and employees who normally work less than 20 hours per week.
- The student employee and 20 hours-per-week exemptions are contained in the last sentence quoted above.

403(b) Exclusions

- Here is that last sentence, as changed by SECURE 2.0, effective for plan years beginning after 2024:
- Subject to the conditions applicable under section 410(b)(4) and section 202(c) of the Employee Retirement Income Security Act of 1974, there may be excluded for purposes of this subparagraph employees who are students performing services described in section 3121(b)(10) and employees who normally work less than 20 hours per week. [Emphasis added to reflect change by SECURE 2.0]
- ERISA section 202(c) is the new ERISA LTPT rule.

LTPT: 2024 vs. 2025

- 2024 plan years must apply SECURE 1.0 Rules
  - 3-year eligibility rule
  - BUT the new vesting and TH rules apply as though in SECURE 1.0
  - *First EEs to enter under the 3-year rule will enter on January 1, 2024*
- 2025: begins new LTPT Rules
  - 2-year eligibility
  - *First EEs to enter under the 2-year rule will enter on January 1, 2025*

Example

- Corporation X maintains a 401(k) plan with one YOS/age 21 eligibility conditions and semi-annual entry dates (1/1 and 7/1)
  - Plan provides for deferrals, matching contributions and profit sharing contributions
  - In addition to its 30 full-time employees, X employs 4 part-time employees who have been with the company for several years
- *How will the new LTPT employee rule affect their participation in the 401(k) plan?*

	Ann	Ben	Cathy	Don
2021	500	500	500	500
2022	500	400	400	500
2023	500	500	400	400
2024	500	500	500	500
2025	500	500	500	500
2026	400	500	400	400

	Ann	Ben	Cathy	Don
2021	500 V E	500	500	500
2022	500 V E	400	400	500
2023	500 V E	500	500	400
2024	500 V P (enters plan)	500	500	500
2025	400 P	500	500	500
2026	500 V P	500	500	400

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2024	500	500 V E	500	500
2025	500	500 V P (enters pan)	500	500
2026	400	500 V P	400	400

	Ann	Ben	Cathy	Don
2021	500	500	500 V E	500
2022	500	400	400	500
2023	500	500	400	400
2024	500	500	500 V E	500
2025	500	500	500 V E	500
2026	400	500	400 P (enters plan)	400

	Ann	Ben	Cathy	Don
2021	500	500	500	500 V E
2022	500	400	400	500 V E
2023	500	500	400	400
2024	500	500	500	500 V E
2025	500	500	500	500 V E
2026	400	500	400	400 P (enters plan)

Plan Fees

- LTPT participating in a 401(k) plan will be subject to per participant fees
- Participant notifications
  - if plan sponsor doesn't choose to use SECURE 2.0 §320 (Notices to "Unenrolled" Participants"),
  - then cost of preparing and distributing all notices to LTPT employees may be significant

Questions and Answers

- Will we have to amend every plan that has LTPT employees? What does that amendment look like?
  - *The employer will need to amend all 401(k) and 403(b) plans. The amendment probably include options for the plan to provide nonelective and/or matching contributions*
- Can you include employer contributions to some LTPT employees and not for others?
  - Yes. In fact, a cross-tested plan may want to provide nonelective contributions to some LTPT employees to help with testing

Questions and Answers

- Will the LTPT employees need to sign a elective deferral form?
  - *Yes. However, if the plan is subject to automatic enrollment, the elective deferral will occur unless the employee makes an election not to defer*
- Is the employer liable if a LTPT employee is not informed that he/she can defer?
  - *Yes. The employer will need to correct by making a corrective QNEC contribution under EPCRS (unless the brief exclusion rule applies)*

Questions and Answers

- What eligibility exclusions can be used under the new LTPT employee rules?
  - *We will need guidance from the IRS to answer this question definitively.*
  - *A plan probably can still exclude classes of employees (e.g., truck drives, division A employees)*
- Can a plan exclude part-time employees?
  - *A plan can exclude part-time employees for employer contributions. Also, the plan can exclude part-time employees for elective deferrals, however, once the LTPT employee rule is triggered, it will trump the part-time employee exclusion.*

Questions and Answers

- Are LTPT employees excluded from top heavy minimums?
  - *Yes. However, once the employee satisfies the plan's normal eligibility requirements (e.g., one YOS/age 21), the employee would be eligible for the top heavy minimum.*
- How will the new LTPT employee rules affect the 5500 count?
  - *If the LTPT employee makes a deferral contribution or receives an employer contribution, the employee would be included as a participant for determining large or small plan status.*

Can we design a 401(k) plan to avoid the application of the LTPT employee rules?

Avoiding the LTPT employee rule by plan design?

- In determining whether an employer can design an eligibility provision to avoid the application of the LTPT employee rules, the practitioner need to examine the provision carefully
  - If there is any possibility that an employee can complete 500 HOS in three consecutive eligibility computation periods and not be eligible to make elective deferrals, the design does NOT avoid the LTPT employee rules
  - *Note: Very few designs will be able to avoid the LTPT employee rules*

Avoiding the LTPT employee rule by plan design?

- Corporation X maintains a 401(k) plan (with discretionary match and profit sharing) with 1 YOS/age 21 eligibility provision
- X amends the eligibility provision to 6 months/500 HOS to avoid application of the LTPT employee rule
  - Does it work? No. Why not?
  - For any EE that doesn't satisfy the 6 months/500 HOS requirement, most plans will then revert to the 1 YOS rule (1,000 HOS)
  - This will trigger the application of the LTPT employee rule
  - Vesting: 500 HOS for LTPT employees

Avoiding the LTPT employee rule by plan design?

- Assume the same fact except the plan continues to apply the 6 months/500 hos for EEs who don't satisfy the eligibility requirement initially
  - Continually "rolls" the 6 months/500 HOS eligibility condition
- Will this avoid the application of the LTPT employee rules? No. Why not?
  - Let's illustrate with an example:
  - Ann works 300 HOS (or, any amount less than 500 HOS) in each of 4 consecutive six month periods, she will not enter the plan under the plan's eligibility provision. However, under LTPT rule she would be eligible to enter the plan.
  - Vesting: 500 HOS for LTPT employees

Avoiding the LTPT employee rule by plan design?

- Corporation X amends SH 401(k) match plan (top heavy exempt) with a 1 YOS eligibility provision to 6 months/500 hos for elective deferrals (SH match continues to apply 1 YOS) to avoid the application of the LTPT employee rule
  - Relies on SECURE 2.0 §310 to retain top heavy exempt status (i.e., commencing in 2024, no longer need to provide TH minimum to otherwise excludible EEs)
- Does the amendment allow the plan to avoid the application of the LTPT employee rule? Is the plan top heavy exempt? **No and No. Why not?**
  - **LTPT employee rule.** For the same reasons explained in the previous slides
  - **Top heavy exempt status** – Under Section 310, a plan will not need to provide TH minimums to the otherwise excludible employees. However, Section 310 doesn't permit a SH plan with dual eligibility to retain TH exempt status
    - EEs with more than one YOS who don't receive at least a 3% employer contribution, will need to receive an addition contribution to bring them to the TH minimum
  - **Vesting.** 500 HOS for LTPT employee

Avoiding the LTPT employee rule by plan design?

- Company X maintains a 401(k) Plan with matching and profit sharing contributions
  - Eligibility. One YOS/age 21
  - Plan excludes Union and Seasonal employees
- Would the LTPT employee rule apply <u>only</u> to the Seasonal employees?
  - No. The LTPT employee rule would apply to Seasonal employees and any other employee (nonseasonal) who satisfies the LTPT employee requirements

Avoiding the LTPT employee rule by plan design?

- Corporation X maintains a 401(k) plan (with discretionary match and profit sharing) with 1 YOS/age 21 eligibility provision
- X amends the eligibility provision to 12 months with no hours of service (i.e., mere passage of time) to avoid application of the LTPT employee rule
  - Does it work? Yes. Why?
  - A "LTPT" employee would always enter under the plan's eligibility provision before he/she would enter under the LTPT employee rule
  - This will trigger the application of the LTPT employee rule
  - Vesting. 500 HOS for LTPT employees

Avoiding the LTPT employee rule by plan design?

- Can you avoid the LTPT employee rule by amending your eligibility requirements for elective deferrals to immediate eligibility?
  - Yes. However, the plan should weigh the costs in adopting such an amendment against the LTPT employee rule
- Could the plan avoid the LTPT employee rules if it amended its elective deferral eligibility provision to immediate eligibility but excluded part-time employees
  - No. We're confident that the IRS will take the position that the LTPT employee rule trumps the part-time employee rule
  - The plan can continue to include the part-time employee exclusion. The exclusion would apply until the LTPT employee rule applies. Furthermore, the part-time employee exclusion could apply to the employer contributions

Avoiding the LTPT employee rule by plan design?

- Private University has a 403(b) plan with a matching contribution
  - Eligibility. One YOS/age 21
  - No class exclusions
- Universal Availability applies to deferrals, so LTPT employee rule will not apply
  - Vesting should remain at 1,000 HOS

Avoiding the LTPT employee rule by plan design?

- Private University has a 403(b) plan with a matching contribution
  - Eligibility. One YOS/age 21
  - Exclusions. student employees and employees who normally works less than 20 HOS/week
- Although Universal Availability applies to deferrals, the exclusion will trigger the application of the LTPT employee rule
  - Vesting will be 500 HOS for LTPT employees
- What if the plan didn't apply the exclusion to deferrals (applied to matching contributions only)?
  - LTPT employee rule would not apply

Elapsed Time

Elapsed Time

- Will a plan's use of elapsed time allow a plan to avoid the application of the LTPT employee rules?
  - *Absent IRS guidance which permits plans with elapsed time to avoid the application of the LTPT employee rules, it appears such plans will need to apply the LTPT employee rules*

Elapsed time method

- The elapsed time method may be used in lieu of the hours counting method for determining eligibility, vesting, and benefit accrual
  - The elapsed time method may be used for all three purposes, or a plan can use elapsed time method for one or two purposes and the hours counting method for the other(s)
  - Under the elapsed time method, one year equals one year
  - One year minus a week does <u>not</u> equal one year

Period of Service

- Credited service is expressed as "periods of service" rather than years of service, although periods of service are generally measured in years
  - A period of service runs from the hire date to the severance from service date
- The severance from service date is the earlier of:
  - the date the employee quits, is discharged, retires, or dies, or
  - the first anniversary of the date the employee is absent from service for any other reason (*e.g.*, disability, vacation, leave of absence, layoff, etc.)
- The difference between a "severance from service" and a mere "absence" is an important one

Elapsed Time Method

- In contrast to the actual or equivalency methods, the elapsed time method determines service taken into account by reference to a "**period of service**" rather than by reference to hours credited toward a "year of service."
  - A period of service begins on the employee's employment (or reemployment) commencement date, and ends on the employee's date of severance from service
  - If a plan uses the elapsed time method, "one year period of severance" replaces "one year break in service" for purposes of applying the break in service rules. The regulations require the plan to take into account certain periods of severance.
  - The plan may use the elapsed time method in applying the vesting and benefit accrual rules
  - **Service crediting provisions.** A plan may credit different classes of employees under different methods of crediting hours of service. The plan's service crediting provision must not discriminate in favor of highly compensated employees, based on all relevant facts and circumstances.

Service Spanning Rules

- For purposes of eligibility and vesting, an employee who has severed from service by reason of a quit, discharge, or retirement but is rehired within 12 months will get credit for the entire time between the severance date and the rehire date
- However, if the employee was absent for any other reason and then quits, the employee must be rehired within 12 months after the absence began to get credit, even though that is less than 12 months after the date of severance. This is to prevent having to give credit for more than 12 months of service after an employee is absent or severs from service.
- For purposes of benefit accrual, periods of severance need not be taken into account

Example – Rehire

- Plan X maintains a calendar year 401(k) plan
  - Eligibility. One YOS/age 21; semi-annual entry dates
  - Vesting. 6 year graded
- Ann is hired on 01/01/2023 and quits on 04/01/2023 after working 600 hours
  - She is rehired 09/01/24 (working 600 hours by 12/31/24)
  - This is more than 12 months after her termination date
  - Under the LTPT employee rule, she enters on 01/01/25
  - Vesting: 500 HOS for Ann

Example – Rehire

- Plan X maintains a 401(k) plan
  - Eligibility. One year/age 21; semi-annual
  - Vesting. 6 year graded
  - Uses elapsed time for eligibility and vesting
- Ann is hired on 01/01/2023 and quits on 04/01/2023 after working 600 hours
  - She is rehired 09/01/24 (working 600 hours by 12/31/24)
  - This is more than 12 months after her severance date
  - She would not get credit for the days from 04/01/2023 to the rehire date
  - Rather, the clock would restart on her rehire date
  - Her service beginning on the rehire date would be added to her 01/01/2023 through 04/01/2023 service

Example (cont.)

- The plan could adjust her hire date to account for the period of severance, or it could track the two discrete periods of service separately and add them together
- Under the LTPT employee rules, she would be eligible to defer on 01/01/25
- *Note: Will the IRS require the plan to apply the LTPT employee rules, or, will it create an elapsed time version of the LTPT employee rule?*

Service Provider Issues

- Coding of LTPT employees and then conversion to full-time
- Tracking vesting service
- Language in Plan documents
- Split of eligibility
- Issuance of SMM/Updated SPD – when to do this?
- System programming – ability to display new eligibility rules

THANK YOU