



ALERTS

IRS Sets Deadline For Using 401(k) Plan Forfeitures

March 1, 2023

Highlights

The Internal Revenue Service issued proposed regulations for use of forfeitures for plan expenses

New deadline is 12 months after the end of the plan year in which forfeitures occurred

New rule would become effective for plan years beginning on or after January 1, 2024

On February 27, 2023, the Internal Revenue Service (IRS) issued proposed regulations imposing a deadline for when a qualified defined contribution plan (like a 401(k) plan) must use forfeitures to pay plan administration expenses, reduce employer contributions or be reallocated to other participant accounts. The new deadline is 12 months following the close of the plan year in which forfeitures were incurred under the plan terms.

This rule is the formalization of informal positions taken by both the IRS in previous guidance and the U.S. Department of Labor in its more recent audit activities.

This new rule is proposed to become effective for plan years beginning on or after January 1, 2024. To provide transition relief, the rule provides that

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all forfeitures incurred during plan years beginning before January 1, 2024 will be treated as having been incurred in the first plan year that begins on or after January 1, 2024. For plan sponsors that have been accumulating forfeitures, this means those forfeitures will need to be used by the end of the 2025 plan year.

Key Takeaways

Under the proposal, plans have the flexibility to determine when a forfeiture is deemed to have occurred. In some instances, that could be as of the date the participant terminates employment and receives (or is deemed to receive) a distribution. In other instances, the actual forfeiture of the unvested account balance can be delayed. Sponsors should consider reviewing their plan documents and determine which of these forfeiture timing methodologies best suits their goals and objectives.

For more information, please contact the Barnes & Thornburg attorney with whom you work or Lori Shannon at 312-214-5664 or lori.shannon@btlaw.com.

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