



ALERTS

New Guidance On Rules For Long-Term, Part-Time Employees In 401(k) Plans

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Highlights

The U.S. Treasury Department and the IRS have proposed regulatory rules for long-term, part-time employees' 401(k) plan eligibility for plan years beginning on and after Jan. 1, 2024

A long-term, part-time employee is an employee who is eligible to make elective deferral contributions to an employer's 401(k) plan when meeting certain criteria

These proposed regulations note which employees would and would not be covered by this rule, as well as special vesting, eligibility, and participation rules for these employees; public comments are due Jan. 24, 2024

On Nov. 27, 2023, the U.S. Treasury Department and the Internal Revenue Service (IRS) published [proposed regulations](#) addressing the new rules for long-term, part-time (LTPT) employees' plan eligibility first established under the SECURE Act of 2019 and modified in the SECURE 2.0 Act of 2022 (SECURE 2.0). Under the SECURE Act, employers were required to expand plan eligibility to allow employees who worked at least 500 hours in three consecutive years to make deferral contributions to the 401(k) plan.

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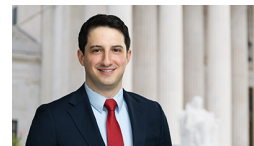
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SECURE 2.0 further expanded this new eligibility rule by reducing such requirement from three consecutive years to two consecutive years and expanded the LTPT rules to include 403(b) tax-advantaged retirement plans.

The proposed rule provides long-awaited guidance on these new rules for plan years beginning on and after Jan. 1, 2024, on topics such as:

- Whether an employee is an LTPT employee
- How to track hours of service for LTPT employees and apply alternative methods for service crediting
- The impact of the new rule on certain eligibility and participation requirements
- The vesting requirements for LTPT employees

Public comments must be received by Jan. 24, 2024, and can be submitted electronically via the Federal eRulemaking Portal at www.regulations.gov. A public hearing on the proposed rule will be held on March 15, 2024.

Background

Before the SECURE Act and SECURE 2.0, employers were allowed to require employees to work at least 1,000 hours during a 12-month period before being eligible to participate in the employers' 401(k) plan. The SECURE Act changed that and required employers to allow LTPT employees to participate in 401(k) plans by 2024. An employee would be considered an LTPT employee if they reached age 21 and worked at least 500 hours in three consecutive years. The updated SECURE 2.0 reduced the LTPT service requirement from three consecutive years to two consecutive years and expanded the LTPT rules to include 403(b) tax-advantaged retirement plans.

Overview of the Proposed LTPT Regulations

The proposed rule covers these topics:

Who is an LTPT employee?

An LTPT employee is an employee who is eligible to make elective deferral contributions to an employer's 401(k) plan, or qualified cash or deferred arrangement, solely because the employee:

- Completed two consecutive 12-month periods where the employee is credited with at least 500 hours of service
- Reached age 21 by the end of the second plan year

LTPT employees do not include:

- Employees who are eligible to participate in a 401(k) plan due to satisfying other eligibility requirements and not solely

as a result of the LTPT requirements. For example, if the 401(k) plan has immediate eligibility for all employees or a “30 days of employment” eligibility requirement, employees who become eligible for the 401(k) plan under such terms would not be considered LTPT employees.

- Collectively bargained employees
- Certain nonresident aliens
- Employees who do not meet plan eligibility for reasons other than age or any service requirements. For example, a plan may require that an employee have a specified job classification or work at a specific location to be eligible to participate in the plan.

How does the proposed rule apply to plans that use the elapsed time method to credit service?

Under the elapsed time method of crediting service, a plan determines eligibility by the period of time that passes while an employee is employed, without regard to the actual number of hours that an employee works. Plans using this method may not require an employee to complete more than one year of service for eligibility. Therefore, an employee in a plan that uses the elapsed time method could not be classified as an LTPT employee because each employee would satisfy the plan’s eligibility requirements by the end of their first 12-month period, regardless of the number of actual hours worked during such period.

This means that under the proposed rule, an employer using an elapsed time method is not required to begin tracking hours of service to identify LTPT employees.

How does the proposed rule apply to plans that use equivalency methods to credit service?

Under an equivalency method of crediting service, a plan applies an alternative method to crediting hours of service that is not based upon the actual number of hours an employee works. Because an employee is still credited with a specified number of hours under an equivalency method, the proposed rule permits employers to continue using a permissible equivalency method to determine whether an employee is credited with at least 500 hours of service during a 12-month period.

Therefore, under the proposed rule, an employer could continue using an existing equivalency method to identify LTPT employees, and an employer would not be required to separately track each hour that an employee actually worked.

What special rules apply to LTPTs for eligibility and plan participation?

Calculating hours of service for LTPT employees:

- The initial 12-month period begins the first day the employee is credited with an hour of service

- Subsequent 12-month periods are calculated by applying the first day of the plan year. If the new plan year begins within the initial 12-month period, then the two periods are treated as consecutive 12-month periods.

Determining when an eligible LTPT employee can begin participating in the plan: Once an LTPT employee meets eligibility requirements, the employee must be able to join an employer's 401(k) plan no later than any other eligible employee in the plan. Therefore, an LTPT employee must enter the plan no later than:

- The first day of the first plan year after the employee meets the eligibility requirements or
- Six months after the LTPT employee meets the eligibility requirements

Reduction in an LTPT employee's hours:

- If an LTPT employee works fewer than 500 hours during a later 12-month period, the LTPT employee's eligibility to participate in the 401(k) plan will not be affected

What are the vesting rules for LTPT employees?

While employee deferrals are always vested fully, it is important to understand the vesting rules applicable to any employer contributions made on behalf of former LTPT employees who have become eligible for employer contributions that are subject to a vesting schedule.

Vesting rules for LTPT employees:

- An LTPT employee must be credited with a year of service for purposes of vesting for each 12-month period where the employee was credited with at least 500 hours of service
- 12-month periods from before Jan. 1, 2021, are excluded for LTPT employee vesting purposes
- Vesting periods for LTPTs will be required if an employee later meets the plan's standard eligibility requirements or the plan offers employer contributions with a vesting schedule to LTPT employees

Vesting rules for former LTPT employees:

- If an employee becomes eligible to participate in a plan solely because the employee met the LTPT requirements, but is later credited with 1,000 hours of service, or completes the plan's regular eligibility standards, the employee would then become classified as a former LTPT employee. In this situation, a former LTPT employee would still be credited with a year of vesting services for any 12-month period where the employee was credited with at least 500 hours of service. Therefore, a former LTPT employee would not subsequently be required to meet 1,000 hours of service for vesting purposes.

Other Notable Items

The proposed rule also states:

- LTPT employees may be excluded from non-discrimination and top-heavy testing for all employer contributions, but to do so, this language must be included in the plan document
- Employers may still exclude LTPT employees from employer matching contributions, employer non-elective contributions, catch-up contributions, and Roth contributions.

Takeaways

When planning for these proposed regulations to be approved, employers should consider these action steps:

- Discuss the purposed rule with the plan's record-keeper
- Determine whether there is a need to develop a system for tracking employee hours and vesting periods
- Consider design changes to the plan to address compliance requirements
- Review agreements with service providers to incorporate these new compliance requirements
- Consult your legal department or benefits counsel with questions related to implementation of these new requirements and plan amendment matters

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