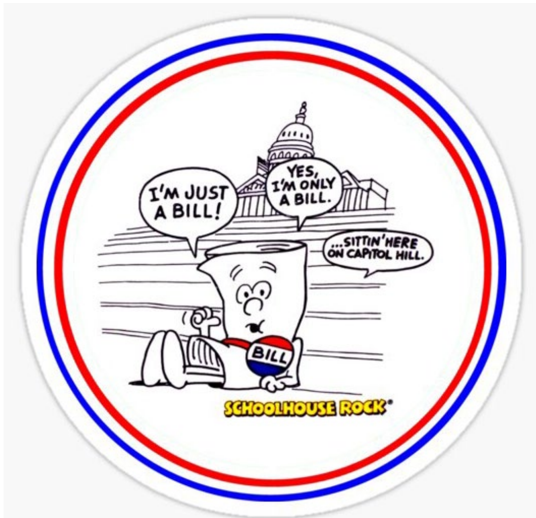
Who Is a Long-Term, Part-Time Employee and Why Does It Matter?



Keeping Your 401(k) Plan Compliant With the SECURE Act

While the SECURE 2.0 Act is working its way through the legislative process, there is a change, brought about by the original act, which took effect last year. If you're a small business owner, we want to make sure you are aware of the updated guidelines regarding which employees are eligible for inclusion in plans, and help keep you abreast of all changes that may be forthcoming.

Historically, 401(k) plans could exclude individuals who worked less than 1,000 hours in the plan year. However, the **Setting Every Community Up for Retirement Enhancement (SECURE) Act**, in its effort to expand access to employer retirement plans, introduced the concept of a "long-term, part-time employee." Starting in 2021, plans needed to consider these employees for eligibility and vesting purposes.

What Changed?
A "long-term, part-time employee" is any employee who in each of the last three consecutive years (long-term) worked at least 500 but less than 999 hours (part-time). They also need to meet any applicable age requirements of the plan. For eligibility purposes, only those years **beginning after December 31, 2020** are counted. Therefore, the first year any long-term, part-time employee will be required to be eligible for the 401(k) plan is 2024. Plans can be more generous and allow entry into the plan sooner.

For vesting purposes, the IRS has clarified that all years in which the long-term, part-time employee worked more than 500 but less than 1,000 (even prior to 2021) are counted. Even though long-term, part-time employees are eligible to defer, the plan can still impose the 1,000-hour rule to be eligible for company contributions.

Example:
ABC Corp. has a 401(k) plan providing that an employee must be 21 and work 1,000 hours per year to be eligible to participate. Employees must work at least 1,000 hours to be eligible for a matching contribution and a vesting year of service.

Suppose employee Robin turns 18 in 2020 and works 750 hours in 2020. Robin goes off to college in 2021 but during the summer and holiday breaks in 2021 to 2023 she works 550 hours each year.

Prior to passage of the SECURE Act, Robin could be completely excluded from the ABC Corp. 401(k) plan. She never worked more than 1,000 hours. She has zero years of service for eligibility, vesting, and matching contribution purposes. However, because Robin works more than 500 hours in each year in 2021, 2022 and 2023, she is eligible to start making 401(k) plan contributions starting in 2024. That's because Robin is a "long-term, part-time" employee.

Because Robin is a long-term, part-time employee for vesting purposes, any year in which she worked more than 500 hours counts. Therefore, Robin would be credited with four years of vesting service (2020, 2021, 2022, and 2023).

But is Robin eligible for company contributions? No. She would not be eligible for a matching contribution until she is working 1,000 hours or more during a plan year.

Even though the long-term part-time employees are eligible to defer, they may be excluded for non-discrimination and top-heavy testing purposes, and the employer is not required to make matching or other contributions for them unless their plan document provides for a contribution.

Please contact our office if you have questions about the changes resulting from the SECURE Act, or any other questions you may have regarding a tax-deductible retirement plan.