Who Is A "Long Term, Part Time" Employee? 401(k) Plans Will Soon Need To Know The Answer

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Historically, 401(k) plans could exclude individuals who worked less than 1,000 hours in the plan year. However, the 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 will need to consider these employees for eligibility, vesting, and company contribution 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 age requirements (generally age 21 for participation and age 18 for vesting). For eligibility purposes, ONLY those years after 2021 are counted. 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.

In September, the IRS clarified that for vesting purposes 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. Finally, the plan can still impose the 1,000-hour rule to be eligible for company contributions. Collectively bargained plans are exempt from these new rules.

Example
La Vida Loca restaurant has a 401(k) plan providing that, prior to 2024, 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. Matching contributions vest 20% each year over five years.

Suppose employee Shaun turns 18 in 2019 and works 750 hours in each of 2019 and 2020. Shaun goes off to college in 2021, but comes home and during the summer and holiday breaks in 2021-2023 he works 550 hours.

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

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Because Shaun is a long term, part time employee for vesting purposes, ANY year in which he worked more than 500 hours counts. As Shaun has more than five years (two years before 2021 and three years after) where he worked more than 500 hours, he is 100% vested in any company contributions.

But is Shaun eligible for company contributions? No. Only those who work at least 1,000 hours under the La Vida Loca plan are eligible to receive a contribution. He would NOT be eligible for a matching contribution.

Let's say Shaun decides to go to work for La Vida Loca on a full-time basis in 2024. Shaun is eligible to make his own 401(k) deductions immediately (long term, part time), he is eligible for matching contributions (works more than 1,000 hours in 2024), and is 100% vested in those contributions immediately (he has at least five years where he worked at least 500 hours).

Next Steps For Employers

Here are some next steps for you to consider:

- Plans will want to coordinate with their plan administrators and employers will want to check with their payroll providers to ensure they can track hours appropriately.
- Key plan design decisions include:
- Do we want to let ALL part-time employees make their own 401(k) contributions (so we don't have to track hours?)
- Do we want to be more generous than the law requires and let "long time, part time" employees into the 401(k) plan prior to 2024?
- Do we want to impose a 1,000-hour rule to be eligible for matching contributions?
- Do we want to impose age restrictions of 18 (for vesting) and age 21 (for participation)?
- Do we want to revise our company contribution vesting schedule?
- You will need to update olan documents, summary plan descriptions, and other plan communications (like employee handbooks) to advise employees of these new rules.

We recommend you coordinate with your attorney or any attorney in our Employee Benefits Practice Group to discuss these developments in advance of 2021.

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