

December 2023

## IRS Issues Proposed Regulations on the Long-term, Part-time Employee Requirements

The Setting Every Community Up for Retirement Enhancement Act of 2019 (SECURE 1.0 Act) added the long-term, part-time (LTPT) employee) provision for 401(k) plans. In addition, the SECURE 2.0 Act of 2022 added several new LTPT employee requirements. On November 24, 2023, the Internal Revenue Service (IRS) issued [proposed regulations](#) addressing certain issues related to the LTPT employee requirements, while leaving some important questions unanswered. This article will focus on a few key issues that were included in the proposed regulations. The proposed regulations will be referred to as “regulations” throughout this article.

### Background

The SECURE 1.0 Act changed the maximum 401(k) plan service requirement for employees effective for plan years beginning after December 31, 2020, to be the earlier of:

- (1) 1,000 hours of service in a 12-month eligibility service computation period (the “regular service requirement”) or
- (2) three consecutive years of service if the employee completes at least 500, but not more than 1,000, hours of service a year in each 12-month eligibility service computation period (for plan years beginning in 2024, the “LTPT service requirement”).

The regulations provide that employee service for a 12-month eligibility service computation period may be based on the employee’s:

- Date of hire through their employment anniversary date or
- Date of hire through their employment anniversary date for the first year, and then switching to the plan year for each 12-month eligibility service computation period for each year thereafter.

The SECURE 2.0 Act made two changes for plan years beginning after December 31, 2024:

- For 401(k) plans – the three-consecutive years’ service requirement is reduced to two consecutive years and excludes service for any computation period that began before 2023 (for plan years beginning after December 31, 2024, the “LTPT service requirement”).
- 403(b) plans subject to ERISA must comply with the LTPT employee requirements.

A plan sponsor can avoid the LTPT service requirement by using a service requirement that permits employees to participate sooner than required under the LTPT service requirements, such as immediate, one- or two-month requirements. A 401(k) plan can still require the employee to satisfy each of the following requirements:

- Be at least age 21 or older, but a plan is not required to have an age requirement,
- Wait until an entry date, which may be daily, monthly, quarterly, or semi-annual, and
- Not be part of a permissible excluded class of employees.

Collectively bargained employees, nonresident aliens with no U.S. source income, and any employees described under Internal Revenue Code section 410(b)(3) are excluded from the SECURE 1.0 Act. An employee who first meets the regular service requirement and is otherwise eligible for the plan will enter the plan under the rules as in place prior to the SECURE 1.0 Act. An employee who first meets the applicable LTPT service requirement will enter the plan as an LTPT employee. An LTPT employee is only required to be eligible to make deferral contributions (pre-tax, after-tax, or Roth), but an employer may include or exclude them from receiving any employer contributions and/or from nondiscrimination testing.

The LTPT employee requirements apply to 401(k) plans, including, as clarified by the regulations, governmental and church 401(k) plans.

## **Employee Service**

The regulations make it clear that a plan that permits a more liberal service requirement will not be subject to the LTPT employee requirements of three consecutive years of at least 500 hours of service. A plan's eligibility service requirement determines whether an employee is a LTPT employee. The regulations make clear that an employee is an LTPT employee only if they are first eligible for the plan solely because they have satisfied the applicable LTPT service requirement, attained age 21 (if the plan has an age requirement), have satisfied the applicable entry date requirements, and are not part of a permissible excluded class of employees. Conversely, an eligible employee who becomes first eligible for a plan by satisfying the plan's regular service requirements will not be an LTPT employee. Even if that employee terminates their employment and is later rehired, they nevertheless would not be treated as an LTPT employee after rehire except in rare cases because plan documents generally are required to include a provision that allows a rehired employee who was a participant to re-enter the plan again immediately as a participant after they are rehired.

A plan sponsor must review their LTPT employees each year to determine if they satisfy the plan's regular service requirement. If they do satisfy that requirement, then they will switch from being an LTPT employee to an employee who is instead eligible under the plan's regular rules, but only on the first day of the next plan year. This could have implications for how the employee is treated under the plan, such as for example, when the employee becomes eligible for employer contributions.

## **Excluded Employees**

There has long been confusion over the classifications of employees that can be permissibly excluded under the regular service requirement. The regulations did nothing to end that confusion, either with respect to the regular service requirement or the new LTPT service requirement. The regulations do not define classifications such as seasonal, temporary, casual, or per-diem employees, and they have never

been clearly defined previously. The regulations identified that the exclusion of an employee based on a job classification is acceptable only if "the class is not a proxy for imposing an impermissible age or service requirement." Note that any class exclusion must pass the minimum coverage test.

Plans that exclude one or more classifications of employees may be impacted if, under the facts and circumstances, the class is a proxy for impermissibly excluding part-time employees who are not permitted to be excluded under the LTPT employee requirements. This requirement applies to 401(k) plans that use either the hours of service or elapsed time method to determine employee eligibility service. This provides some clarity because it is the same rule as previously applied (and continues to apply) with respect to the regular service requirements, but it also creates some subjectivity based on a reasonable interpretation of a particular classification of employees. An exclusion based on location, division, job classification, or certain other types of jobs may still be acceptable to the same extent it was permissible before the SECURE 1.0 Act became effective. However, a plan sponsor cannot disguise an hours or age exclusion by using an excluded classification of employees to avoid the LTPT employee requirements.

Before the issuance of the regulations, one of the questions was, "What is the impact of the LTPT employee requirements on 401(k) plans that use the elapsed time method to determine employee eligibility service?" Under the regulations, if a 401(k) plan that uses elapsed time either does not exclude any employees to which the LTPT employee requirements could apply or previously excluded such employees but is amended to include them based on the 401(k) plan's normal service requirement (using elapsed time of 1 year or less), then all eligible employees will be treated as regular employees, and the 401(k) plan will not be subject to any of the LTPT employee requirements. However, if the 401(k) plan continues to exclude these as part of a classification of employees, then the plan may be subject to the LTPT employee requirements. Plan sponsors should review this issue and other excluded employee issues with their legal counsel to determine the impact on their 401(k) plan.

## **Plan Document Amendments**

The plan document must incorporate all the relevant applicable LTPT employee requirements in the SECURE 1.0 and 2.0 Acts and related plan sponsor elections. The current plan amendment deadline is the last day of the plan year that begins in 2025 (2027 for governmental plans)#. The regulations clarify that an election to exclude LTPT employees from nondiscrimination tests and being eligible to receive any top-heavy contributions must be included in the plan document amendment.

The regulations allow a 401(k) plan sponsor that wants to adopt a service requirement allowing employees who otherwise would be subject to the LTPT employee requirements to be eligible for the plan sooner than required under those requirements, such as immediate eligibility or elapsed time, that would result in the plan avoiding the LTPT employee requirements in the 2024 plan year may adopt such an amendment by the last day of the plan year that begins in 2025.

Important: For plan sponsors using the Fidelity Preapproved Plan Document, you must contact your Fidelity representative now to start the process to amend the Adoption Agreement, so it is aligned with the administration of the plan.

## **Comments and Public Hearing**

The Treasury/IRS will be accepting written comments by Jan. 26, 2024, and they will hold a public hearing on the regulations on March 15, 2024 on the regulations. We will be working with various industry trade

groups to provide comments on the key issues.

Fidelity is committed to keeping plan sponsors informed about this legislative change. The [Long-term, Part-time Resource Center](#) includes new and updated resources for plan sponsors including information on eligibility requirements and plan sponsor decisions.

# The IRS issued Notice 2024-2 (SECURE 2.0 Grab Bag) in late December that delayed the date that plan documents must be amended for the CARES, SECURE 1.0 and 2.0 Acts.

Dec. 31, 2026	Dec. 31, 2028	Dec. 31, 2029
<ul style="list-style-type: none"> <li>• Non-governmental qualified plans (401(a)/(k) plans)</li> <li>• Non-public school 403(b) plans</li> </ul>	<ul style="list-style-type: none"> <li>• Applicable collectively bargained 401(a)/(k) and 403(b) plans</li> </ul>	<ul style="list-style-type: none"> <li>• Governmental 401(a) plans</li> <li>• Public school 403(b) plans</li> <li>• Eligible governmental 457(b) plans<sup>1</sup></li> </ul>

<sup>1</sup>December 31, 2029, or the first day of the first plan year beginning more than 180 days after the date of notification regarding inconsistent administration with Code Section 457(b).

The long-term, part-time provision does not apply to all plans. We encourage plan sponsors to consult with legal counsel to discuss potential impact to their plan.

Fidelity does not provide legal or tax advice, and the information provided is general in nature and should not be considered legal or tax advice. Consult an attorney, tax professional, or other advisor regarding your specific legal or tax situation.

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Fidelity Investments Institutional Operations Company LLC, 245 Summer Street, Boston, MA 02210

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