

Proposed Regulations Regarding Long-Term, Part-Time Employees

By **Eric D. Altholz** on December 8, 2023

Newly issued IRS Proposed Regulations regarding the special eligibility and vesting requirements for long-term, part-time employees provide guidance that 401(k) plan sponsors have been waiting for since these requirements were established under SECURE 1.0. Though it has been three years since SECURE 1.0 was enacted, the Proposed Regulations were published less than a year after the passage of SECURE 2.0, which modified and expanded the scope of the new rule – a breathtaking pace by IRS standards. With only weeks remaining before 401(k) plans must comply with the new rule in operation, the Proposed Regulations explain how plan sponsors are to identify long-term, part-time (“LTPT”) employees. The Proposed Regulations also establish other administrative rules necessary to define the rights of LTPT employees and prescribe the related obligations of plan sponsors. Plan sponsors can rely on the Proposed Regulations in administering their plans until the regulations are finalized, probably sometime next year.

For readers whose organizations sponsor 403(b) plans, do keep reading. While these Proposed Regulations apply only to 401(k) plans, future regulations addressing the treatment of LTPT employees for 403(b) plans are likely to be similar.¹

401(k) Plan Eligibility for LTPT Employees

The LTPT eligibility rule for 401(k) plans generally requires that employees who are credited with at least 500 hours of service in each of two consecutive 12-month periods, and have attained age 21, must be allowed to make elective deferrals to the plan. The rule applies to 401(k) plans for plan years beginning on or after January 1, 2024, with service prior to January 1, 2021, disregarded for purposes of determining eligibility.² The rule takes effect for 403(b) plans for plan years beginning on or after January 1, 2025, with service prior to January 1, 2023, disregarded for eligibility purposes. (For more background information, including an explanation of how

¹ The drafters of the 403(b) plan regulations will need to address the impact of the LTPT eligibility rule on the long-standing exception from the “universal eligibility” requirement for employees who normally work less than 20 hours per week. It will be interesting to see whether the IRS will conclude that the exception has to be eliminated.

² Note that for the 2024 plan year only, the original SECURE 1.0 eligibility rule will apply to 401(k) plans. Under the original rule, an employee was required to achieve at least 500 hours of service in each of THREE consecutive 12-month periods. SECURE 2.0 reduced the number of periods to two.

SECURE 2.0 modified the original rule, you can read our earlier [summary here](#).) The LTPT provisions of SECURE 1.0 were fairly skeletal, and SECURE 2.0 added little in the way of details. The Proposed Regulations flesh out the core requirements and provide the guidance necessary to allow employers to admit LTPT employees to their 401(k) plans starting next month (for plans with a calendar year plan year).

Who is an LTPT employee?

An employee is considered an LTPT employee if he or she becomes eligible to participate in a 401(k) plan *solely* as a result of being credited with at least 500 hours of service during each of two consecutive 12-month periods (and having attained age 21 by the end of the second 12-month period). So if an employee first gains eligibility to make elective deferrals for other reasons (e.g., the plan provides for immediate entry upon hire), he or she will not be considered an LTPT employee. (This turns out to be an important distinction for vesting and other purposes.) Collectively bargained employees and nonresident aliens with no U.S. source income do not qualify for LTPT treatment. In addition, individuals who could be considered LTPT employees but fall into a permissible classification of excluded employees that is not tied to service or age – such as employees in a particular operating division or subsidiary that is not covered by the plan – can still be excluded.

Which service crediting methods can be applied to determine LTPT eligibility?

A 401(k) plan sponsor may apply its existing service crediting method in identifying LTPT employees. So if a plan sponsor credits service by counting actual hours, it can use that method to identify LTPT employees. Likewise, if the plan sponsor applies an equivalency method (e.g., 45 hours for each week for which the employee would be required to be credited with at least one hour of service), it can use that method.³ Importantly, the Proposed Regulations do not require a 401(k) plan to begin counting hours if it does not already do so. So a 401(k) plan that credits service using the elapsed time method can continue to do so. A plan that uses the elapsed time method of crediting service should never have LTPT employees in their covered workforce because hours of service would not be relevant in determining eligibility to participate in the plan.

Consistent with standard service crediting requirements, service during a period when a potential LTPT employee was a member of an excluded classification must be counted when determining eligibility if the employee no longer falls within the excluded classification. So, for example, if a part-time employee moves from a subsidiary not

³ Many plans provide for the application of the actual hours method for hourly employees and an equivalency method for salaried employees. One would expect the typical LTPT employee to be paid on an hourly basis, but the plan sponsor should apply the service crediting method it would normally use based on the classification of the potential LTPT employee.

covered by the 401(k) plan to a covered subsidiary after having been credited with 500 hours of service for a 12-month period, that employee would only need to achieve 500 hours of service during the immediately following 12-month period in order to become eligible for the plan.

How are the 12-month periods of service determined?

The initial 12-month period for service crediting purposes must begin on an employee's hire date. However, consistent with standard service crediting rules, the 401(k) plan document may provide that, after an employee's initial 12-month period of employment, subsequent 12-month periods will begin on the first day of each plan year, beginning with the plan year in which the initial 12-month period ends.

When can an LTPT employee enter the plan?

The standard entry date rules for retirement plans apply to LTPT employees. Therefore, an LTPT employee must be allowed to begin making elective deferrals as of the first day of the first plan year after the employee meets the eligibility requirement or, if earlier, six months after the employee meets the requirement.

What kinds of contributions must LTPT employees be eligible to make or receive?

A 401(k) plan must permit LTPT employees to make elective deferrals, but plans may continue to apply otherwise permissible eligibility requirements – such as 1,000 hours of service during a 12-month eligibility computation period – for employer matching and nonelective contributions. LTPT employees may be allowed to make Roth contributions and catch-up contributions as well, but that is not required by the rule. LTPT employees may also be excluded from safe harbor contributions without jeopardizing a plan sponsor's ability to satisfy the safe harbor contribution requirements for all other participants. If a plan sponsor wishes to exclude LTPT employees from receiving safe harbor contributions, it must do so explicitly in the terms of the plan document.

How is service credited for vesting purposes?

If an LTPT employee does receive employer contributions under a 401(k) plan, special vesting rules apply. Specifically, the LTPT employee must be credited with one year of service for vesting purposes if the employee is credited with 500 hours of service within the applicable 12-month vesting computation period set forth in the plan document. Service prior to January 1, 2021, is not taken into account for vesting purposes, *provided* the LTPT employee attained eligibility pursuant to the new rule. The Proposed Regulations also provide that even if an LTPT employee at some point completes a year of service under the standard rules (e.g., 1,000 hours of service in a

plan year), the employee would still have to receive vesting credit based on the 500 hours of service requirement.⁴

How are LTPT employees treated for nondiscrimination and coverage testing?

The Proposed Regulations allow plan sponsors to exclude LTPT employees from nondiscrimination and coverage testing. This includes ADP testing (for elective deferrals), ACP testing (for matching contributions), nondiscriminatory amounts testing for employer nonelective contributions, and the minimum coverage test (sometimes referred to as the “70% test”). If a plan sponsor intends to exclude LTPT employees from nondiscrimination and coverage tests, the plan document must contain language allowing this election to be made, and the LTPT employees must be excluded from all nondiscrimination and coverage testing.⁵ Finally, although LTPT employees must be taken into account in applying top heavy testing, they can be excluded from the minimum contribution and vesting requirements that are triggered when a plan becomes top heavy.

What should plan sponsors do now?

401(k) plan sponsors should review employee service records for periods beginning on and after January 1, 2021, and make sure their internal employment record systems are properly programmed to enable them to identify LTPT employees. Employees who meet the service and age requirements for eligibility must be allowed to commence elective deferrals as early as January 1, 2024. Sponsors of 403(b) plans may wish to begin reviewing employee service records (for periods beginning on and after January 1, 2023), update their service crediting process to identify LTPT employees, and be prepared to admit them to the elective deferral component of their 403(b) plan as early as January 1, 2025. Finally, as a reminder, plan sponsors have until December 31, 2025, to amend their plan documents to comply with the requirements of the CARES Act, SECURE 1.0, and SECURE 2.0.

If you have questions regarding the LTPT eligibility and vesting rules or any other aspect of SECURE 2.0, please contact a member of Verrill's Employee Benefits and Executive Compensation Group.



Eric D. Altholz

Partner

T (207) 253 4908

[email](#)

⁴ The special vesting rules also apply to “former LTPT employees.” Be aware that the definition of “former LTPT employee” is nuanced.

⁵ Note that LTPT employees who are credited with 1,000 hours of service in a plan year have to be swept back into the testing population because they are no longer considered LTPT employees.