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## Long-term, Part-time Employee Rule Impact of Employee Exclusions

*The information in this article applies to employees who are excluded from participating in a 401(k) plan and the impact of the long-term, part-time employee provision in the SECURE 1.0 Act, regardless of whether the employer adopted a preapproved plan or individually designed plan document. However, the article focuses on employers that adopted the Fidelity Preapproved Defined Contribution Profit Sharing/401(k) Plan Document.*

The long-term, part-time employee (LTPT) provision enables part-time employees (generally classified as such based on the number of hours of service they work) to become eligible to participate in a 401(k) plan and make deferral contributions. Section 1.04(d)(1) of the Fidelity Preapproved Defined Contribution Profit Sharing/401(k) Plan Adoption Agreement (2020 Version)<sup>1</sup> requires an employer to specify the class(es) of employees eligible to participate in the plan, but they may exclude certain classes of employees in Section 1.04(d)(2), which states: "Notwithstanding the selection in 1.04(d)(1), certain Employees of the Employer are excluded from participation in the Plan."

The IRS issued proposed regulations on November 24, 2023, for the LTPT rules. Those proposed regulations permit certain classifications of employees to be excluded from the LTPT employee requirements as long as such exclusions are "not a proxy for imposing an impermissible age or service requirement," which is the same rule that applies under the current age and service requirements for 401(k) plans. Exclusions that *may* be a proxy for age and service are classifications such as seasonal, temporary, or intern employees, which the IRS did not further define within the proposed regulations what or when classifications are proxies for age and service. Accordingly, plans that exclude one or more classes of employees may be impacted by the LTPT rules if under the facts and circumstances an excluded class would be viewed by the IRS as a proxy for age or service, resulting in such employees being subject to the LTPT rules.

The table below identifies several scenarios and our understanding under the proposed regulations of how the LTPT employee requirements apply depending on the classes of employees an employer elected to exclude in their plan document. Plan sponsors should consult with legal counsel to discuss their specific scenario.

Employee Eligibility Service Method	Adoption Agreement Section	Do the LTPT Employee Requirements Apply?
1. Hours of service <sup>2</sup>	1.04(d)(1)(A) – All employees are included, except the following employees in 1.04(d)(2): <ul style="list-style-type: none"> <li>○ Collectively bargained employees**,</li> <li>○ Leased employees (if this box is checked),</li> <li>○ Nonresident aliens with no US source of income**</li> </ul> <b>Note:</b> No other classes of employees are excluded	Yes*  No No No
2. Elapsed time <sup>3</sup>	1.04(d)(1)(A) – All employees are included, except the following employees in 1.04(d)(2): <ul style="list-style-type: none"> <li>○ Collectively bargained employees**,</li> <li>○ Leased employees (if this box is checked)</li> <li>○ Nonresident aliens with no US source of income**,</li> </ul> <b>Note:</b> No other classes of employees are excluded.	No  No No No
3. Hours of service <sup>2</sup>	1.04(d)(1)(A) – All employees are included, except the following employees in 1.04(d)(2): <ul style="list-style-type: none"> <li>○ Collectively bargained employees**,</li> <li>○ Leased employees (if this box is checked)</li> <li>○ Nonresident aliens with no US source of income**,</li> <li>○ Other<sup>4</sup> – part-time, seasonal, temporary, or other hours of service-based employees.</li> </ul>	Yes*  No No No  #
4. Elapsed time <sup>3</sup>	1.04(d)(1)(A) – All employees are included except the following employees in 1.04(d)(2): <ul style="list-style-type: none"> <li>○ Collectively bargained employees**,</li> <li>○ Leased employees (if this box is checked)</li> <li>○ Nonresident aliens with no US source of income**,</li> <li>○ Other<sup>4</sup>– part-time, seasonal, temporary, or other hours of service-based employees.</li> </ul>	No  No No  #

\* Depends upon the Eligibility Service Requirement elected in 1.04(b) for purposes of employee deferral contributions. The LTPT rules do not apply if employees are eligible to make elective deferrals sooner than would be required under the SECURE 1.0 and SECURE 2.0 Acts (meaning, generally, sooner than after 3 consecutive 12-month periods in which the employee worked 500 or more hours after January 1, 2021, or

sooner than after 2 consecutive 12-month periods in which the employee worked 500 or more hours after January 1, 2023, and obtained age 21?}).

\*\* This is a statutory exclusion under the SECURE 1.0 Act.

# A 401(k) plan may exclude certain employees based on a job classification if “the class is not a proxy for imposing an impermissible age or service requirement.” Plans that exclude one or more classes of employees may be impacted by the LTPT rules if under the facts and circumstances the excluded class is a proxy for impermissibly excluding part-time employees. The facts and circumstances to be considered include whether the plan provides that employees in an otherwise excluded class are no longer excluded, and therefore eligible, after attaining age 21 with 1 year of service pursuant to an election in 1.04(d)(2)(E)(i). Plan sponsors should consult with legal counsel to discuss their specific scenario.

<sup>1</sup> **The Fidelity Adoption Agreement** was submitted to the IRS before the SECURE 1.0 and SECURE 2.0 Acts were enacted, and it does not include the relevant language for the LTPT employee provision. The document will be amended for those Acts before the last day of the plan year that begins in 2025. Fidelity will prepare a good faith amendment to incorporate the LTPT employee requirements and timely distribute it to employers that adopted the Preapproved Plan Document.

<sup>2</sup> **Hours of service method: Under this method, the plan requires the** employee to complete a certain number of hours of service before they become eligible to participate in the 401(k) plan. In many cases, an employee must complete one year of service, which is usually a requirement to complete at least 1,000 hours of service in a 12-month eligibility service computation period.

<sup>3</sup> **Elapsed time method:** An employee is not required to complete a certain number of hours of service before they become eligible to participate in the 401(k) plan. All they are required to do is complete a certain number of days or months of service (generally, up to 1 year).

<sup>4</sup> **Other exclusion:** A plan must pass the minimum coverage test each year. However, it may exclude a nondiscriminatory class of employees from participating in the plan if it is based on objective and reasonable business criteria. For example, a class of employees excluded from participating in the plan based on their work location, job grade, job title, division, etc. Employees who are excluded from the plan based on a service requirement are subject to the LTPT employee requirements unless the existing service requirement allows employees to participate sooner than required under the LTPT rules.

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