

# THE BENEFIT BULLETIN

## *FAST FACTS ABOUT RETIREMENT PLANS*

The following article contains general plan facts and is intended for informational purposes only. To ensure that your plan contains specific provisions outlined in this and future articles, please contact your third party administrator or plan ERISA attorney.

### **Plan Eligibility**

Eligibility is the determination of when an employee satisfies the conditions to become a participant in a plan. Certain requirements for eligibility can be built into the plan document, in order for an employer to have some flexibility on which employees participate in the plan and when.

The Employee Retirement Income Security Act (“ERISA”) sets limitations on the requirements for eligibility relating to age and service. A plan may impose both an age and a service requirement, either an age or a service requirement, or neither requirement.

In regards to setting an age requirement, a plan cannot require an employee to reach an age older than 21 as a condition to become a participant in the plan. A more liberal requirement, such as a younger age requirement or no age requirement at all, is acceptable but may not be advisable for the employer.

In regards to setting a service requirement, generally, the plan cannot require more than one year of service as a condition to become a participant in the plan. Again, a shorter service requirement or no service requirement is allowed. A plan may impose up to two years of service as a requirement if the plan provides for immediate vesting. However, 401(k) arrangements may not exceed the one-year rule. Employers often use a one year service requirement if they have a high employee turnover rate. Requiring an employee to wait one year before entering the plan can help reduce costs by eliminating certain participant charges.

After an employee has satisfied any age and/or service requirements for eligibility purposes, the employee will actually become a plan participant on the “plan entry date” following satisfaction of the eligibility conditions. The plan entry dates are typically semi-annually, quarterly, or monthly and are set in the plan document.

It is also possible to design the plan to include different eligibility requirements for different groups of employees. For example, for the first year of the plan, the employer may wish to allow everyone employed at the time the plan is established to become immediately eligible for the plan regardless of their length of service with the company, but require a specific service requirement for those hired after the effective date of the plan. Or the employer may wish to exclude a certain group of employees from the plan (such as hourly paid or seasonal employees) which is acceptable as long as coverage and discrimination tests are still passed.

Different plan features can also have different eligibility requirements. For example, the plan may allow employees to start making 401(k) deferrals immediately upon employment, but require a one year service requirement for employees to receive an employer matching contribution.

While there are many eligibility options which can be chosen for a plan document, once the requirements are set in place, it is very important to follow the plan’s guidelines. In other words, the requirements for eligibility cannot be waived for certain employees. Allowing an employee to participate in the plan before they are actually eligible creates an operational failure that must be corrected. The improperly accrued benefit is eliminated and any 401(k) deferrals must be made “whole” by returning the compensation improperly deferred to the employee.

On the other hand, if a plan administrator fails to allow an eligible employee to participate in the plan, a make-up benefit must generally be provided. In the case of this failure under a 401(k) arrangement, the employer may also need to fund additional amounts to make up for the fact that the employee did not have the opportunity to defer. These corrections are handled through the Self-Correcting Program or the IRS Voluntary Correction Program and can become very costly to the employer.

If you have any questions regarding the operation of your plan’s eligibility requirements or you would like to discuss changes to your plan, please contact your third party administrator or plan ERISA attorney.

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