



PENSION ANALYST COMPLIANCE BULLETIN



IRS finalizes rules allowing forfeitures to fund QNECs and QMACs

On July 20, the IRS issued final rules amending the definition of qualified non-elective contributions (QNECs) and qualified matching contributions (QMACs). These rules generally are substantively similar to the proposed rules issued January 2017. These rules are effective for plan years on or after July 20, 2018, but can be relied on earlier, as permitted under the proposed rules.

Background and overview

A 401(k) plan sponsor may make Qualified Nonelective Contributions (QNECs) or Qualified Matching Contributions (QMACs) to some or all non-highly compensated employees (NHCEs) to correct failed Actual Deferral Percentage (ADP) or Actual Contribution Percentage (ACP) tests. Plans may also use QNECs and QMACs to satisfy ADP/ACP safe harbor provisions or as part of certain correction methods.

Prior to the proposed rules being issued, a QNEC or QMAC had to satisfy the nonforfeitability and distribution requirements upon contribution to the plan. The proposed rules amended the definitions of QNECs and QMACs to provide that they must be nonforfeitable *at the time they are allocated to participants' accounts* instead of when they are contributed to the plan. As a result of these changes, amounts in a plan's forfeiture account may now be used to fund QNEC and QMAC contributions.

Plan amendments

In response to comments from the proposed rule, the final rules clarify that a plan amendment consistent with the final rules and applied prospectively to future plan years would not implicate the anti-cutback rule. Additionally, the final rules address a common situation where a plan provides that forfeitures are used to pay plan expenses incurred during the plan year, and that remaining forfeitures at the end of the plan year are allocated pursuant to a specified formula among active participants who have completed a certain number of hours of service. In this situation, the anti-cutback rule would not prohibit a plan amendment adopted before the end of the plan year that permits the use of forfeitures to fund QNECs and QMACs, even if one or more participants completed the specified number of hours at the time of the amendment. This is because the condition for receiving an allocation is that expenses at the end of the plan year are less than the amount of forfeitures, and that condition would not have been satisfied mid-plan year.

If a sponsor's plan document contains language requiring that QNECs and QMACs be 100% vested when contributed to the plan, an amendment will be needed to revise the document language accordingly. Amendments to plan documents must be completed by the last day of the plan year to which the change applies.

Sponsors of individually designed plans that want to have the flexibility to use forfeitures for QNEC or QMAC contributions should review their plan document and make amendments as necessary. For sponsors of plans that use Prudential's document services, Prudential previously adopted amendments allowing the flexibility in use of forfeitures as was permitted by the proposed rules. We will contact you if any revisions to the amendments are required based on the final rules.

Compliance Bulletin by Prudential Retirement

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