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IRS Final Rules Make Plan Forfeitures More Useful

This summer, the Internal Revenue Service (IRS) published final rules allowing the use of forfeitures in a qualified plan to fund safe harbor contributions. The rules also permit qualified nonelective contributions (QNECs) and qualified matching contributions (QMACs), sometimes used to help pass nondiscrimination tests. The IRS finalized the proposed rules in mid-July. If you have not already done so, now is a good time to consider amending your plan to allow the use of forfeitures for funding safe harbor contributions, QNECs, and QMACs.

The new rules reverse a long-held position that forfeitures can't be used to fund these types of contributions because the contributions are required to be fully vested when contributed to an employer plan, and not when allocated to participant accounts. The IRS interpreted this position as prohibiting employers from using forfeitures to fund these contributions because the amounts in a forfeiture account were subject to vesting at the time they were contributed to the plan as employer matching or profit-sharing contributions. This small and seemingly unimportant distinction made by the IRS (vested when contributed vs. when allocated) prevented forfeitures from being used to fund contributions that the IRS required to be fully vested when contributed.

The IRS finally relented after years of comments and lobbying from those in the benefits field and accepted the view that the better reading of the Internal Revenue Code and Treasury Regulations is that nonforfeitability must occur upon allocation to accounts instead of upon contribution to the plan, thus opening up the use of forfeitures for funding of safe harbor contributions, QNECs, and QMACs.

The rules were proposed in 2017 and specified the new rule could be relied upon immediately; however, reliance on the proposed rules would have required a discretionary plan amendment before the end of 2017. If you did not amend your plan then, now is a good

time to consider an amendment, effective January 1, 2018, so you can use forfeitures in 2018 as allowed by the new final rules.

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