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IRS Provides Guidance on Long-Term, Part-Time Employees in 401(k) Plans, Qualified Birth and Adoption Distributions, and In-Service Distributions from Pension and 457(b) Plans

In Notice 2020-68 (Notice), the Internal Revenue Service (IRS) provided guidance on several provisions of the Setting Every Community Up for Retirement Enhancement Act of 2019 (SECURE Act) and in-service distributions under the Bipartisan American Miners Act of 2019 (Miners Act) as well as applicable plan amendment deadlines. The most important clarifications for plan sponsors are related to the participation of long-term, part-time employees in 401(k) plans, qualified birth and adoption distributions, and in-service distributions from pension and governmental 457(b) plans.

Participation and Vesting of Long-Term, Part-Time Employees in § 401(k) Plans (Section 112 of the SECURE Act)

The SECURE Act requires that for plan years beginning after December 31, 2020, long-term, part-time employees must be allowed to make elective deferrals to an employer's 401(k) plan after reaching age 21 and completing at least 500 hours of service during three consecutive 12-month periods. The Notice clarifies that employers can exclude 12-month periods beginning before January 1, 2021, for purposes of this new requirement.

Employees who become eligible under this special rule for long-term, part-time employees only need to be given the opportunity to make elective deferrals; they can still be excluded from matching and profit-sharing contributions unless and until they meet the plan's current eligibility service requirement for those contributions.

However, each 12-month period of service with at least 500 hours (including periods before 2021) must be counted as a year of service for vesting purposes for employees who become eligible to make elective deferrals under this special rule. Therefore, if they later become eligible for matching and/or profit sharing contributions, those years of service will count in determining their vested percentage.

The SECURE Act requires that 401(k) plans be amended to allow participation of long-term, part-time employees. The deadline to amend is the last day of the first plan year beginning on or after January 1, 2022, but the amendment must be effective retroactively as of the first day of the plan year beginning on or after January 1, 2021.

Qualified Birth or Adoption Distributions (Section 113 of the SECURE Act)

The Notice clarifies several aspects of the new qualified birth and adoption distribution option permitted by the SECURE Act for plan years beginning after December 31, 2019. Defined contribution plans qualified under Code Section 401(a), including 401(k) plans, 403(a) annuity plans, 403(b) plans, governmental 457(b) plans and IRAs, may (but are not required to) offer qualified birth or adoption distributions, but defined benefit plans are not. Eligible plans may allow the distributions to come from elective deferrals, QNECs, QMACs and safe harbor contributions (which otherwise generally cannot be permitted to be taken as an in-service distribution until age 59 ½ or due to a financial hardship). The distributions are not subject to the 10% early distribution penalty tax under Code Section 72(t) but are includable in the individual's gross income. However, the distributions are not treated as eligible rollover distributions under the direct rollover rules, which means the plan is not required to give the 402(f) special tax notice or apply mandatory 20% withholding (although the voluntary withholding rules do apply).

Each parent may take a distribution of up to \$5,000 for the same child or eligible adoptee. In the case of multiple births (twins, triplets, etc.) or adoptions of multiple adoptees, a distribution may be taken for each child as long as the distributions are taken during the one-year period following the date that the children are born or

the legal adoption for eligible adoptees is finalized. Plan sponsors may rely on reasonable representations from the individual as to the individual's eligibility for a qualified birth or adoption distribution unless the plan sponsor has actual knowledge to the contrary.

An eligible adoptee is any individual under age 18 or an individual who is physically or mentally incapable of self-support under Code Section 72(m)(7) (i.e., unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment that can be expected to result in death or to be of long-continued and indefinite duration). The child of a taxpayer's spouse is not an eligible adoptee for purposes of the distributions.

Individuals who take a qualified birth or adoption distribution can recontribute the full amount or any portion to the plan, and the plan is required to accept the recontribution if the individual received the distribution from the plan, and the individual is eligible to make a rollover contribution to the plan at the time of the recontribution. A recontribution is treated as a direct rollover contribution (specifically, a direct trustee-to-trustee transfer).

If a plan does not choose to offer qualified birth or adoption distributions, but an individual takes an otherwise permissible in-service distribution that qualifies, the individual may treat the distribution as a qualified birth or adoption distribution on their federal income tax return and may recontribute the amount to an IRA. The IRS notes that it intends to issue regulations addressing additional requirements for recontribution, including timing considerations.

Plans that choose to offer qualified birth and adoption distributions can begin offering them in the 2020 plan year. However, the deadline to amend the plan is the last day of the first plan year beginning on or after January 1, 2022 (or the last day of the first plan year beginning on or after January 1, 2024, for governmental plans or collectively bargained plans). If plans are amended later than the deadline, the amendment must be adopted by the end of the plan year in which it is effective.

Reduction in Minimum Age for In-service Distributions (Section 104 of the Miners Act)

Effective for plan years beginning after December 31, 2019, the Miners Act allows plan sponsors of governmental 457(b) plans to lower the minimum age to take an in-service distribution from 70 ½ to 59 ½. Sponsors of pension plans (both defined benefit and money purchase pension plans) may also lower the minimum age from 62 to 59 ½ for purposes of receiving an in-service distribution. This lowered minimum age also applies to money purchase pension plan assets that have been merged into a profit sharing plan.

The Notice clarifies that employers are not required to adopt the lowered minimum age or permit in-service distributions at all. In addition, just because an in-service distribution may be taken at age 59 ½ does not mean that the plan can also change the normal retirement age to 59 ½. A plan's normal retirement age must be an age that is not earlier than the earliest age reasonably representative of the typical retirement age for the industry in which the covered workforce is employed.

The lowered in-service distribution ages are optional changes. If a plan wants to add them retroactively, the deadline to amend a qualified plan is the last day of the first plan year beginning on or after January 1, 2022 (or the last day of the first plan year beginning on or after January 1, 2024, for governmental plans or collectively bargained plans). If plans are amended later than the deadline, the amendment must be adopted by the end of the plan year in which it is effective.

The Notice also provides guidance related to the small employer automatic enrollment credit, the repeal of the maximum age for traditional IRA contributions and permitting excluded difficulty of care payments to be taken into account as compensation for purposes of determining certain retirement contribution limitations.

If you have questions about the IRS guidance or compliance with the SECURE Act or the Miners Act, please contact [Kellie Money](#) of Frost Brown Todd's [Employee Benefits and ERISA group](#).

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