In order for a company to maintain a qualified retirement plan, the plan document must be written so it adheres to all requirements of the Internal Revenue Code. The requirements are in place to ensure a plan does not discriminate unfairly against certain populations (or groups) of employees. Several of these requirements surround the employee eligibility rules for a plan. Because a plan’s eligibility rules may impact nondiscrimination testing, it’s imperative for the plan administrator to understand plan eligibility and how it may influence test results.

**Eligibility Requirements**

An employee must meet certain eligibility requirements in order to participate in his/her company’s qualified retirement plan, as dictated by the plan’s document. Any employee who has met the eligibility requirements of the plan must be allowed to participate as long as they are not part of an excluded class of employees as defined in the plan document. The plan document will indicate the following requirements:

- **Age** – In order to participate in the plan an employee must meet the minimum age requirement, as specified in the plan document. Per IRS regulations, the minimum age requirement cannot exceed age 21.

- **Service** – In order to participate in the plan an employee must also meet the minimum service requirement. The service requirement cannot exceed one year of service or 1,000 hours of service performed during the plan year.

**TIP:** A qualified 401(k) plan may require 2 years of service to receive the employer contribution if the plan states the employee will be 100% vested in all plan account balances.
A qualified plan may implement less restrictive eligibility requirements, such as a lower minimum age or service requirement.

**Continuing Eligibility**

In addition to these two requirements, a plan may choose to include a continuing eligibility requirement in their plan document. Continuing eligibility requirements state that participants must meet an additional requirement each year to receive an employer contribution.

Example: A participant may be required to be employed on the last day of the plan year to be eligible to receive the employer’s contribution for the year. This is known as the ‘last day’ provision.

A plan may have a continuing eligibility requirement as long as the plan will pass the Minimum Coverage Test.

**REMEMBER:** If the plan fails the Minimum Coverage using the Ratio Percentage Test, it will need to pass a more lenient test known as the **Average Benefit Test**. However, if the plan cannot pass the **Average Benefit Test**, it may have to forego the continuing eligibility requirement and/or exclusion of certain groups of employees in the plan.

**Plan Entry Dates**

Once an employee meets the age and service requirements under a plan, there are also rules specifying how long a plan sponsor may then make the employee wait to actively participate in the plan. The plan entry rules state an employee who is eligible must be allowed to participate in the plan the later of 6 months after the date on which the employee satisfied the age and service requirements or the first day of the plan year following the date on which the employee has satisfied both the age and service requirement.

**Excludable Employees**

A plan may exclude a group or groups of employees from participating in the plan as long as the plan will pass the Minimum Coverage Test. Examples of groups who may be excluded include those who are covered under a collective bargaining agreement or those who are considered nonresident aliens.
The employer must have established policies and procedures identifying how the groups are defined to ensure employees are accurately placed in relevant groups and if eligible for the plan, are enrolled in a timely manner.

**Collective Bargaining Agreements**

If a plan covers employees who have negotiated their retirement benefits under a collective bargaining agreement (union employees), they must be identified and tested separately from the employees not covered under a collective bargaining agreement. If the employees covered by the collective bargaining agreement are excluded from the plan, this will not negatively impact the Minimum Coverage Test since the retirement benefits were negotiated.

**Leased Employees**

A leased employee is an individual who provides services to the employer under an agreement with a third party. A leased employee is an individual who is not a common law employee of the organization, but is treated under IRS 414(n)(1) as an employee of the recipient (or employer) for qualified plan purposes.

For an individual to be treated as a leased employee the following conditions must be met:

1. The recipient must be paying a fee for the services of the individual. Service must be performed under an agreement between the recipient and a leasing organization, even if the agreement is informal.
2. The leased employee must be employed substantially full time for at least one year. Substantially full time service means 1,500 hours in a 12-month period.
3. The recipient must have primary direction or control over the individual’s services.
4. The leasing organization, not the recipient, must be the common law employer of the individual.

These leased employees are treated as an employee of the employer as long as they have worked for the employer for at least a year on a substantially full time basis. The plan’s same minimum age and service requirements apply to any leased employee, who have met the definition above, unless the plan document specifically excludes leased employees from participating in the plan.
Part Time and Temporary Employees

A plan document may specifically exclude part time employees and/or temporary employees from participating in the plan. But if written in the plan, a plan sponsor may allow such employees to participate in the plan. Part time and temporary employees may have the same eligibility requirements as other employees participating in the plan or the plan may have different eligibility requirements for those groups. Either way, the eligibility requirements for these types of employees must be specified in the plan document.

**NOTE:** Class exclusions (leased, part-time, temporary, union) are not automatic. Such exclusions from eligibility must be supported by the plan document.

Eligibility and Nondiscrimination Testing

Eligibility is a key component of nondiscrimination testing. In order for a plan’s ADP and ACP tests to be performed, the plan administrator needs to provide a participant data file with data for all employees who have received compensation, regardless of whether they are eligible to participate in the plan. This is an important point because, often, administrators only include employees participating in the plan. If only a portion of the employees are provided, it’s likely the plan’s test results will be incorrect, resulting in retesting and a delay in providing the results to the plan sponsor.

Additionally, when 410(b) minimum coverage testing is performed for a plan, all employees of the employer’s controlled group must be included in such testing, even those employees who were not eligible for the plan (e.g., employees who did not meet the plan’s eligibility requirements or those employees who were specifically excluded from the plan) as well as those employees who were not eligible for the plan because they were part of a different plan within the employer’s controlled group. As a result, when performing a plan’s 410(b) minimum coverage testing, it is possible Fidelity may request the plan sponsor provide additional employee data to ensure all controlled group employees are included in the testing as necessary.

Sometimes plan sponsors may put eligibility requirements in place to make the administration of the plan easier without realizing such changes may impact the outcome of the plan’s nondiscrimination testing results. **It is crucial to discuss any changes to your plan with a member of your Fidelity client service team to ensure adequate consideration has been taken to the effect any changes may have on the plan’s testing.**
Reports Available

Below is a list of nondiscrimination testing reports provided by Fidelity related to a plan’s eligibility. Some of the reports listed may not appear with your test results if they are not applicable to your plan.

**Ineligible Report**

This report lists employees who were identified as ineligible for the plan year tested. In general, this report would include employees who did not meet the plan’s eligibility requirements or who were specifically excluded from participation under the provisions of the plan. It is important to note some of the employees listed on this report may have terminated prior to the plan year being tested and therefore not required to be included in the plan’s nondiscrimination testing. However, you should verify none of the employees listed on this report were eligible to participate in the plan for the plan year being tested.

**Eligible without Test Salary Report**

This report lists employees identified as eligible for plan participation but for whom test compensation data was not provided. It is important to note some of the employees listed on this report may have terminated prior to the plan year being tested and therefore not required to be included in the nondiscrimination testing. However, you should verify that none of the employees listed on this report were eligible to participate in the plan for the plan year being tested.

**401(m) Ineligible Report**

This report lists employees who were disregarded for the ACP test because they were identified as ineligible to receive employer matching contributions. Please note only plans that require employees to meet separate eligibility requirements in order to receive employer matching contributions and have no after-tax contribution feature will receive a 401(m) Ineligible Report.
Frequently Asked Questions

Is it possible to have dual eligibility rules in my plan’s design?

Yes. It is possible to design a retirement plan to include different eligibility requirements for different groups of employees or to have different eligibility requirements for parts of the plan. For example, a 401(k) plan might allow employees to participate in the plan immediately after being hired, but require one year of service before the employee is eligible for the matching contribution.

When submitting my participant data file for nondiscrimination testing, what population of employees should I include as eligible for the plan?

All employees who were eligible to participate at any point during the plan year should be coded as plan eligible on the participant data file. For example:

- Include as plan eligible even if they chose not to participate.
- Include as plan eligible even if they were only eligible for one day.
- Include as plan eligible even if they separated from employment before the plan year ended.
- Include as not plan eligible only if they did not meet the plan’s service and/or entry requirements during the plan year.

*It’s important to note that your participant file should also include all employees, even those not eligible for the plan.*

Should I include all of the employees at our company in the participant data file or only those who are eligible?

Your participant data file should include both eligible and ineligible employees. All employees who received pay or earned income (via W2, K1, K2, etc.) during the plan year should be included. Contractors paid only via 1099 are not employees, and can be excluded.
Will you provide an example of who should be on the file, and how to indicate eligibility correctly?

The following scenario shows examples of employees who should be included as eligible for the plan and employer match.

**Background:** ABC Box Company sponsors a retirement plan with a 12/31 plan year end for its employees called ABC 401(k). Employees do not have a service requirement to participate in the plan and are able to enter the plan immediately upon hire. However, the plan document states there is a 1-year waiting period to receive the employer matching contribution. The plan document also includes annual profit sharing which also requires 1-year of service and

Below is a portion of the plan’s participant data file (for the 2016 plan year) with employees eligible for both the plan and employer match (in green) and employees ineligible for the plan and/or employer match (in red).

<table>
<thead>
<tr>
<th>First Name</th>
<th>Last Name</th>
<th>Birth Date</th>
<th>Hire Date</th>
<th>Term Date</th>
<th>Plan Eligible</th>
<th>401(m) Match Eligible</th>
<th>Disaggregation Code</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sue</td>
<td>Smith</td>
<td>08-11-1974</td>
<td>02-04-2010</td>
<td></td>
<td>Y</td>
<td>Y</td>
<td></td>
</tr>
<tr>
<td>Mike</td>
<td>Jones</td>
<td>06-20-1997</td>
<td>06-30-2015</td>
<td></td>
<td>N</td>
<td>N</td>
<td></td>
</tr>
<tr>
<td>Larry</td>
<td>Walker</td>
<td>03-07-1960</td>
<td>09-21-1987</td>
<td></td>
<td>Y</td>
<td>Y</td>
<td></td>
</tr>
<tr>
<td>Jane</td>
<td>Adams</td>
<td>11-14-1965</td>
<td>09-15-2016</td>
<td></td>
<td>Y</td>
<td>N</td>
<td></td>
</tr>
<tr>
<td>Eric</td>
<td>Collins</td>
<td>07-07-1970</td>
<td>06-02-1995</td>
<td>06-01-2016</td>
<td>N</td>
<td>N</td>
<td>UNION</td>
</tr>
<tr>
<td>Mary</td>
<td>Miller</td>
<td>05-28-1985</td>
<td>05-28-2007</td>
<td>05-27-2016</td>
<td>Y</td>
<td>Y</td>
<td></td>
</tr>
</tbody>
</table>

In the sample participant data file submitted for nondiscrimination testing:

- Sue, Larry and Mary we each eligible for the plan and the employer match.
- Mary was eligible to participate in the plan until her termination date, but as a result of the termination, she was not eligible for the non-elective (profit sharing) contribution given at the end of the calendar year. (Although not shown in our example, the dollar amount listed for Mary in the Non-Elective (Profit Sharing) Contributions column is ‘0.00’.)
- Mike, Jane and Eric were not eligible for the plan, but were still included in the participant data file for the plan’s testing.
- Mike was not eligible because he was not yet 21 years of age during the plan year.
• Jane was eligible for the plan, but because she had not met the plan’s 1-year requirement for the employer match, she was not eligible for the 401(m)/employer match.

• Eric was not eligible for either the plan or the employer match because he was part of the company’s union, which has negotiated retirement benefits separate from the plan and does not allow for participation in the ABC 401(k) plan. His termination date had no effect on his eligibility for the plan.

**Is it possible to have continuing eligibility requirements in my plan’s design?**

Yes. For example, a plan may require an eligible employee to meet certain continuing eligibility requirements each plan year in order to receive the employer’s matching contribution (e.g., last day rule and/or hours worked requirement during the plan year). However, the employer is not required to have such continuing eligibility requirements within the provisions of its plan. But if it does have such continuing eligibility requirements within the provisions of its plan, the plan sponsor may elect to waive the last day and hours worked requirement within the provisions of the plan for any participants who terminated employment due to death, disability or retirement. Fidelity Volume Submitter clients should contact a member of their client service team if they wish to make changes, add or remove such provisions.

**NOTE:** Safe harbor contributions cannot be subject to continuing eligibility requirements.

**Our plan is a safe harbor. Is it possible to have two-year eligibility requirements for new participants?**

No. A safe harbor plan cannot impose two-year eligibility requirements on safe harbor contributions. This is because all non-highly compensated employees in the plan must be eligible for the safe harbor contribution. The plan could, however, impose a two-year eligibility requirement on other types of contributions.
How are terminated employees treated with regard to eligibility for nondiscrimination testing?

If a terminated employee has met the initial eligibility requirements to participate in the plan, they will be included in the nondiscrimination testing, just like an employee who has not terminated. The terminated employee does not need to be eligible under the plan at the end of the plan year.

Is it possible to require re-hired employees to meet the same eligibility requirements as new hires?

Typically the participant will not lose the eligibility service that has already been earned prior to terminating from the employer. The plan’s document will have information on how to credit service for re-hired employees.

However, for each re-hired employee, it could be a difference scenario. Based on how long they were separated, a re-hired employee could either become immediately eligible, or they may have to meet the eligibility requirements again.