

IRS Announces Transition Relief From The Once-In-Always-In Requirement For Excluding Part-Time Employees Under 403(b) Plans

Article By:

Steven D Einhorn

The IRS recently issued Notice 2018-95 to provide transition relief to 403(b) plans that erroneously excluded part-time employees from eligibility to make elective deferrals when the employees should have been eligible to participate under the “once-in-always-in” requirement (“OIAI”). Under the OIAI requirement, once an employee is eligible to make elective deferrals, the employee may not be excluded from eligibility for making elective deferrals in any later year on the basis that the employee is a part-time employee. The IRS issued Notice 2018-95 to provide transition relief because many employers that sponsored 403(b) plans did not realize that the OIAI requirement applied to the part-time exclusion.

Background

403(b) plans are subject to a “universal availability requirement,” which generally requires that if any employee has the right to make elective deferrals under an employer’s 403(b) plan, the right to make elective deferrals must be universally available to all employees. However, there are certain narrow categories of employees that may be excluded from eligibility for making elective deferrals under 403(b) plans without violating the universal availability requirement. 403(b) plans may require that employees make annual contributions greater than \$200, and may also exclude:

1. employees who are eligible to make elective pre-tax contributions to certain other employer defined contribution plans;
2. nonresident aliens with no U.S. source income;
3. certain students (*i.e.*, students providing services described in Section 3121(b)(10) of the Internal Revenue Code of 1986, as amended (the “Code”)); and
4. part-time employees who normally work fewer than 20 hours per week, which is sometimes referred to as the “part-time exclusion.” The Notice 2018-95 transition relief only applies to plans that improperly applied the part-time exclusion.

In July 2007, the IRS issued final regulations under Code Section 403(b) (the “Final Regulations”) which included guidance regarding the part-time employee exclusion. According to the Final Regulations, 403(b) plans can only exclude this category of employees if all employees in that

category are excluded (*i.e.*, if the plan allows one employee who normally works fewer than 20 hours per week to make elective deferrals under the plan, all employees who qualify as part of that group must be eligible to make elective deferrals under the plan, which is referred to as the “consistency requirement”). Additionally, for purposes of excluding part-time employees, the Final Regulations impose three distinct conditions that employers must satisfy for an employee to be excluded. These include:

1. A “first-year” exclusion condition: Employers must reasonably expect the employee to work fewer than 1,000 hours for the 12-month period beginning on the date the employee’s employment commenced;
2. A “preceding-year” exclusion condition: The employee actually worked fewer than 1,000 hours of service for the preceding measurement period (*i.e.*, each plan year following the employee’s first year of employment, or, if the plan so provides, the plan can look to the 12-month periods based on the date the employee commenced employment instead of looking to plan years) (defined in Notice 2018-95 as an “Exclusion Year”); and
3. An OIAI requirement: Once the employee fails to meet the first-year exclusion or has been credited with at least 1,000 hours of service in any applicable 12-month measurement period, the employee must be allowed to participate in making elective deferrals under his employer’s 403(b) plan. Then, once allowed to participate in making elective deferrals, the employee cannot later be excluded from eligibility to make elective deferrals on the basis that the employee’s hours significantly dropped, which is referred to as the “once-in-always-in” or OIAI requirement.

In practice, many 403(b) plan sponsors did not apply the OIAI requirement. Many employers applied the first-year exclusion condition for an employee’s first year and applied the preceding-year exclusion condition separately for each succeeding Exclusion Year, but did not apply the OIAI requirement to prevent an employee who failed to meet either the first-year exclusion condition or the preceding-year exclusion condition from being excluded in all subsequent Exclusion Years.

Transition Relief under Notice 2018-95

In response to requests from 403(b) plan sponsors, Notice 2018-95 provides for a transition relief period for plans that did not properly apply the OIAI requirement. This “Relief Period” provided under Notice 2018-95 begins with tax years beginning after December 31, 2008 (which is generally the effective date for the Code Section 403(b) Final Regulations). If a 403(b) plan provides that the preceding-year exclusion is determined on a plan year basis, the Relief Period ends on the last day of the last plan year that ends before December 31, 2019. If a 403(b) plan provides that the preceding-year exclusion is determined based upon an employee’s anniversary year, the Relief Period will end on different dates for different employees based upon the date of each employee’s anniversary of employment, but no later than December 31, 2019.

Notice 2018-95 provides the following transition relief from the OIAI requirement:

1. Relief regarding plan operations: During the Relief Period, 403(b) plans will not be treated as failing to satisfy the conditions of the part-time exclusion if the plans were not operated in compliance with the OIAI requirement. However, this relief does not apply to 403(b) plans’ failure to properly apply other conditions of the part-time exclusion (*i.e.*, the “first-year” and “preceding-year” exclusion conditions) nor to the consistency requirement.
2. Relief regarding plan language: Notice 2018-95 provides different relief for 403(b) plans that have

adopted plan documents that are covered by an IRS opinion or advisory letter (*i.e.*, prototype or volume submitter plans) versus 403(b) plans that use individually designed plan documents.

- During the Relief Period, 403(b) plans that adopted an IRS pre-approved plan document will not be treated as failing to satisfy the conditions of the part-time exclusion, and the plans will not be treated as having failed to follow plan terms, merely because the plan document does not match plan operations with regard to the OIAI requirement.
- During the Relief Period, 403(b) plan sponsors whose plan documents use individually designed plan documents must amend their plans' language to reflect the plans' operation with respect to the OIAI requirement prior to April 1, 2020. Thus, if during the Relief Period, a 403(b) plan did not properly apply the OIAI requirement, the plan must be amended to reflect how it was actually operated.

Both pre-approved 403(b) plans and individually designed 403(b) plans that provide for the part-time exclusion must include explicit language concerning the OIAI requirement prior to April 1, 2020.

3. A "fresh-start opportunity" for plans:

Notice 2018-95 provides a fresh-start opportunity under which 403(b) plans will not be treated as failing to satisfy the conditions of the part-time exclusion, if the OIAI requirement is applied as if it first became effective January 1, 2018.

Employers that sponsor 403(b) plans that exclude part-time employees for purposes of eligibility for elective deferrals should carefully consider how the OIAI requirement applies to their plans and whether any changes will be necessary to either their procedures or plan documents.

© 2025 Proskauer Rose LLP.

National Law Review, Volume VIII, Number 345

Source URL: <https://natlawreview.com/article/irs-announces-transition-relief-once-always-requirement-excluding-part-time>