TaxNewsFlash

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Notice 2018-95: Transition relief from "once-in-always-in" rule, excluding part-time employees from section 403 plans

The IRS today released an advance version of Notice 2018-95 that provides transition relief from the "once-in-always-in" (OIAI) condition for excluding part-time employees under Reg. section 1.403(b)-5(b)(4)(iii)(B).

Notice 2018-95 [PDF 56 KB] explains that under the OIAI exclusion condition—for a section 403(b) plan that excludes part-time employees from making elective deferrals—once an employee is eligible to make elective deferrals, the employee may not be excluded from making elective deferrals in any later exclusion year (as defined by today's notice) on the basis that the employee is a part-time employee.

The IRS notice also provides a "fresh-start opportunity" for section 403 plans to apply the OIAI exclusion condition for exclusion years after the transition relief ends under Notice 2018-95.

Background

There is a "universal availability" requirement that a section 403(b) plan that permits employees to make elective deferrals must apply to all employees of the employer maintaining the section 403(b) plan. However, there are certain categories of employees that may be excluded from making elective deferrals despite the universal availability requirement—these include part-time employees who normally work less than 20 hours per week.

Final regulations under section 403(b) were issued in 2007 to provide rules regarding the part-time exclusion. These final regulations also provide, under Reg. section 1.403(b)-3(b)(3)(i), that a section 403(b) plan must be a written plan that satisfies the requirements of the regulations in both form and operation, and must include all the material terms and conditions for eligibility.

Under the OIAI exclusion condition, the employee may be excluded under the part-time exclusion **if and only if** in the employee's first year of employment, the employee meets the first-year exclusion condition, **and in each** exclusion year ending after the first year of employment, the employee has met the preceding-year exclusion condition. The effect of the OIAI exclusion condition is that once an employee does not meet the part-time exclusion conditions (whether in the initial year of employment or for any exclusion year), the employee may no longer be excluded from making elective deferrals under the part-time exclusion.

Relief under Notice 2018-95

The IRS and Treasury Department received requests for relief with respect to this OIAI exclusion condition. Transition relief was also requested with respect to the OIAI exclusion condition. Apparently, many employers were not aware that the part-time exclusion included the OIAI exclusion condition.

In response to these requests for relief, Notice 2018-95 provides transition relief from the OIAI exclusion condition, including:

- Relief regarding plan operations for a transition period
- Relief regarding plan language
- A fresh-start opportunity after the relief period ends

The relief period begins with tax years beginning after December 31, 2008 (the general effective date for the section 403(b) regulations). For plans with exclusion years based on plan years, the relief period ends for all employees on the last day of the last exclusion year that ends before December 31, 2019.

For plans with exclusion years based on employee anniversary years, the relief period ends, with respect to any employee, on the last day of that employee's last exclusion year that ends before December 31, 2019.

The IRS notice provides the following example:

> *If Employee A began employment on April 1, 2015, and Employee B began employment on July 20, 2015, the relief period for Employee A would end on March 31, 2019, while the relief period for Employee B would end on July 19, 2019.*

Notice 2018-95 further provides that during the relief period, a plan will not be treated as failing to satisfy the conditions of the part-time exclusion merely because the plan was not operated in compliance with the OIAI exclusion condition. However, Notice 2018-95 does not provide relief from the other conditions of the part-time exclusion such as: (1) the first-year exclusion condition (that is, for the first year of employment, an employee may not be excluded if the employee was expected to work at least 1,000 hours in the first year); and (2) the preceding-year exclusion condition (that is, for exclusion years ending after the first year, an employee may not be excluded if the employee worked at least 1,000 hours in the preceding 12-month period). The IRS notice also does not provide relief from the consistency requirement. An example is provided by the IRS to illustrate application of the relief measures.

Lastly, Notice 2018-95 provides a fresh-start opportunity. In general, for exclusion years beginning on or after January 1, 2019, a plan that provides for the part-time exclusion must apply the OIAI exclusion condition in both form and operation. However, the fresh-start opportunity (a plan will not be treated as failing to satisfy the conditions of the part-time exclusion for periods after the relief period) provides the OIAI exclusion condition is applied as if the OIAI exclusion condition first became effective January 1, 2018.

In other words, a plan may apply the OIAI exclusion condition by disregarding the fact that the first-year exclusion condition was not met for an employee if that employee began employment before January 1, 2018, or the fact that the preceding-year exclusion condition was not met for an employee in any exclusion year before the first exclusion year beginning on or after January 1, 2018.

The IRS notice states that even if a plan applies the fresh-start opportunity with respect to the OIAI exclusion condition, the plan must have been operated during the relief period in compliance with the OIAI exclusion or pursuant to the relief provided today by Notice 2018-95. Additionally, a plan—whether a section 403(b) pre-approved plan or an individually designed plan—is not required to be amended to reflect the use of this fresh-start opportunity in applying the OIAI exclusion condition.

Examples are provided to illustrate application of the fresh-start opportunity measures.