Forfeitures of Unvested Balances

Requirements for Handling Forfeitures of Unvested Balances

This document provides general information about Forfeitures and Forfeited Balances in Qualified Retirement Plans.

What are Forfeitures?

Many qualified retirement plans apply a Vesting Schedule to employer contributions. In plans that apply a vesting schedule, employees must meet a specified number of years of employment to "own" balances attributable to employer contributions.

When a participant terminates employment before meeting the service required to be fully vested and withdraws the vested balance, the participant "forfeits" the unvested portion of the account.

Some participants who are partially vested when they terminate employment choose to leave their retirement funds in the plan. In this case, after five consecutive years during which a former employee is paid for 500 or fewer hours of work, the non-vested amounts are forfeited.

What happens to forfeited funds?

Employers may specify several options for handling forfeitures. Once the option is chosen in the plan, employers must follow the options chosen.

- **Allocate to Participants** - Forfeitures may be allocated to the accounts of other participants in the plan. This is most common for plans that make profit sharing contributions.
- **Reduce Future Contributions** – Forfeitures may be used to reduce future employer contributions to the plan.
- **Pay Plan Expenses** – Forfeitures may also be used to pay plan expenses.

Forfeitures may not be paid back to the employer.

What happens if a participant is rehired after forfeiting a portion of their account?

There are complex rules that apply to govern rehired employees. In some cases, if employees return to work before having a five year break in service, employers may be required to reinstate the forfeited amount. For this to occur, the participant is required to return any balance they withdrew back into the plan.

May forfeitures be carried over to future plan years?

Forfeitures are required to be used in the current plan year or the following plan year and are not allowed to be carried over from year to year. They should not remain unspent or unallocated beyond the end of the following plan year.

Special Rules for the ADP / ACP Test

In traditional 401(k) plans, if a plan fails the ADP nondiscrimination test and refunds contributions back to a participant, the participant may need to also forfeit the match that was related to the refund.

Please contact JULY at 888.333.5859 for more information.