The Revolving Door: Rehired Employees

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What Will Be Covered

• Counting service
• Break in service rules including the “rule of parity”
• Entry requirements for rehires
• Buy-back rights
• Returning from military leave
Robert’s Rules of Rehires

• Don’t rehire former employees
• If the person was good enough to rehire, then why go to all this effort to keep the person out of the plan
• In 95 percent of the cases, the person will be eligible on the date of rehire
Eligibility Requirements
410(a) Maximum

- Code §410(a) limits maximum age and service condition plan can impose
  - Generally one year of service
  - Age 21
- Plan can’t impose higher service requirement
  - Even if plan would pass coverage
Two Years of Service

• The law allows a plan to use a two-year eligibility condition
• But pay the price
  – Full and immediate vesting
• Exception: Can’t use two-year rule for elective deferrals
• Can be years of service without an intervening break in service (first exception to rule that all service counts)
Entry Date

• EE generally enters plan on entry date after satisfying eligibility requirements

• Maximum entry date is earlier of:
  – First day of the first plan year beginning after the date requirements are met, or
  – Date that is six months after the date requirements are met

• Roughly 182 entry dates – but January 1st and July 1st meet the maximum
Employment on Entry Date

• Plan can require employment on entry date as condition to enter
• If EE comes back after entry date, must generally enter on day of return unless break in service rules let us disregard service
Example

- Judy hired May 1, 2014
- Quits April 1, 2015 with 1,800 HOS
- One year of service April 30, 2015 (?)
- Entry dates are first day of first and seventh months following (July 1, 2015 if Judy didn’t quit)
  - If rehired before July 1, 2015 then enters on July 1, 2015
  - If rehired after July 1, 2015 then enters on date of rehire unless break in service rules apply
Year of Service

• 12-month Computation Period (CP) in which EE has at least 1,000 hours of service
• No requirement to be employed on a particular day
• Have YOS even if not employed at beginning or end of CP
  – No requirement to work 12 months
  – It is a 12-month computation period during which 1,000 hours of service are completed
YOS Example

- Craig starts work January 1, 2015
- Has 150 Hours of service/month
- Quits August 1, 2015
- Had 1,050 HOS before quit
- Credit Craig with YOS at end of 12-month eligibility computation period (2015)
What Date for Crediting YOS?

- Plan has entry dates of January 1 or July 1 “coinciding with” or next following satisfaction of one YOS
- Craig hired January 2, 2014
- Does Craig enter on January 1 or July 1 of 2015?
  - If YOS credited on January 1, 2015, that’s coincident with entry date
  - If YOS credited on January 2, 2015, then next entry is July 1, 2015
What Is an “Hour of Service?”

• An hour for which an EE is paid for performance of duties
• An hour for which an EE is paid for non-performance of duties (e.g., vacation pay, sick pay)
• An hour for which an EE receives an award for back pay
Credit for Nonperformance

• Some reasons for pay for nonperformance of duty:
  – Vacations
  – Holidays
  – Illness or incapacity, including disability
  – Layoff
  – Jury duty
  – Military duty
  – Leave of absence

• It does not matter whether the employment relationship has terminated at the time of the payment
Limits on Nonperformance Credit

• Don’t have to credit more than 501 HOS for any given computation period for paid nonperformance
• No need for credits for payments under a plan to comply with:
  – Workers’ compensation
  – Unemployment compensation
  – Disability insurance laws
• These are credited hours and differ from unpaid maternity and paternity absences (hours credited just to avoid a break in service)
Credit for Nonperformance

- Erin works 900 hours of service
- Takes a four-week paid leave of absence (160 hours)
- Erin has 1,060 hours of service
No Double Counting

- Double credit is not given for the same time
- Erin has 930 hours
- She gets paid for one week of unused vacation
- Does Erin have 970 hours or 1,010 hours?
Counting HOS

• Two options for counting HOS
  – Count actual hours
    • Easy to do for workers paid by the hour
    • Time cards work well
    • Nearly impossible for salaried professionals
  – Use equivalency
• Plan document must specify method being used
Available Equivalencies

• Working hours
  – Disregard nonperformance hours
  – 870 working hours = one YOS
• Regular hours
  – Disregard nonperformance and overtime
  – 750 regular hours = one YOS
• Earnings method
  – Divide compensation by lowest hourly pay rate
• Employment period method (next slide)
Employment Period Method

- 1 day = 10 HOS
- 1 week = 45 HOS
- ½ month = 95 HOS
- 1 month = 190 HOS
- 1 shift = entire length of shift
Eligibility Computation Period (ECP)

• 12-month period used to determine whether EE has YOS for eligibility purposes
• First ECP: always starts with Date of Hire (DOH) and ends 12 months later
• Subsequent ECPs: plan choice:
  – Base on anniversary of DOH
  – Shifting to plan year
    • Most plans shift to plan year
What’s Date of Hire?

• Technical term: employment commencement date
• Date of first hour of service
  – Generally, as employee (not as contractor)
  – Leased or worksite EE – First day perform HOS for ER
  – Controlled or affiliated service group – first day of service for any group member
Shifting ECP

- JKL plan requires one YOS
- If you don’t have one YOS in first year, subsequent ECP based on (calendar) plan year
- Jennifer hired May 2, 2013, works 800 hours/year
- First ECP May 2, 2013 to May 1, 2014
- Second ECP January 1, 2014 to December 31, 2014
  - Hours performed from January 1, 2014 to May 1, 2014 counted in two different ECPs
ECP Shift Example

• Jennifer begins employment June 1, 2013
• Works part-time (60 hours per month) through May 31, 2014
• June 1, 2014 begins full time (150 hours per month – for next couple of years)
• Plan shifts to (calendar) plan year
• When does Jennifer have one YOS for eligibility?

420 hrs
6/1/13

300 hrs
1/1/14

1,050 hrs
5/31/14

12/31/14
5/31/15
ECP Shift Example

- David begins employment November, 1, 2014
- Works full time (150 hours per month)
- Plan shifts to (calendar) plan year
- When does he have two YOS for eligibility?

<table>
<thead>
<tr>
<th>300 hrs</th>
<th>(150 hrs/mon)</th>
<th>1650 hrs</th>
</tr>
</thead>
<tbody>
<tr>
<td>11/1/14</td>
<td>1/1/15</td>
<td>10/31/15</td>
</tr>
<tr>
<td>12/31/15</td>
<td>12/31/15</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>1 YOS</th>
<th>2 YOS</th>
</tr>
</thead>
<tbody>
<tr>
<td>11/1/14</td>
<td>10/31/15</td>
</tr>
</tbody>
</table>
Odd Result

- CY plan has YOS with quarterly entry
- Shift to PY for eligibility
- Individual A (rehire):
  - May 2013 - August 2013: 430 hours
  - Rehired August 2014
    - January 1 – December 31, 2014 – 950 hours
    - January 1 – December 31, 2015: if 1000 hours enters on January 1, 2016
- Individual B (new hire):
  - Hired August 2014
  - B has one YOS in August 2015 and enters on October 1, 2015
- The result: A and B (re)hired on same date but B enters earlier than A
Vesting Computation Period

• May be any 12-month period specified in plan
• Most plans use the plan year as the computation period
Elapsed Time Method

• Based on period of time that elapses while EE is employed

• Period of service
  – Starts on date of hire
  – Ends on “severance from service” date = the earlier of date of severance (e.g., quit) or one year after a leave of absence

• Period of severance
  – Starts on the “severance from service” date
  – Ends when employee returns to service
Elapsed Time (continued)

• Service spanning rule
  – If employee returns to work within one year, then must be credited with that year
  – Period of severance can also be period of service
• One-year period of service for eligibility is anniversary of employment date
  – Fractional years count
  – 30 days equals month or can use 365 days
• Break in Service (BIS) = a period of severance that isn’t counted as a period of service
Elapsed Time Example

• Frank has following employment history:
  – Hired March 1, 2012
  – Quits October 2012
  – Rehired January 2013
  – Quits February 2013
  – Rehired December 2013

• Frank has two periods of service in March 2014
  – Did not have one-year break
Other Rules

• If ER is “maintaining” a predecessor ER’s plan, the plan must count service with the predecessor ER.

• If the ER is not “maintaining” a predecessor ER’s plan, the plan may credit predecessor service on a nondiscriminatory basis.

• If a controlled or affiliated service group exists, the plan must treat service with any group member as service with the ER.

• If a multiple employer plan (MEP) service with all adopting employers counts.
Counting Service
General Rule – All YOS Count

• Break in service rules only way to disregard service
• Example:
  – Dave works five years full-time for XYZ Contractors as union employee
  – XYZ plan excludes union employees
  – Doesn’t matter: Dave has five YOS
  – Same result if working for foreign company
• Must count service before plan established or before participant enters plan
• Break in Service (BIS) = computation period where EE does not complete more than 500 HOS
Maternity/Paternity Leave

• For purposes of determining BIS only, plan must count unpaid hours for:
  – EE’s pregnancy
  – Birth of EE’s child
  – Placement of an adopted child with EE
  – Child care by EE starting right after birth
• Limit: enough hours to prevent a BIS in current year (or next year if no actual BIS in current year)
• Remember: *paid* leave = up to 501 actual HOS
Overview of Eligibility BIS Rules

• Allow you to disregard service
  – Temporarily or permanently
• Otherwise you must count prior service
• Three rules
  – Two-YOS eligibility rule
  – One-year holdout rule
  – Rule of Parity (five BIS)
Two-YOS Eligibility Rule

• Only applies to plans using two-YOS eligibility condition
  – Requires full vesting

• Plan can require completion of two YOS without intervening BIS
One-Year Holdout Rule

• If EE has BIS, then not required to count prior service until EE completes one YOS after rehire (based on date of rehire)

• Situation:
  – EE enters plan
  – Terminates employment
  – Incurs BIS
  – Rehired

• Retroactive entry to reemployment commencement date or, if later, first day of ECP that EE completes 1,000 HOS
# One-Year Holdout Rule

<table>
<thead>
<tr>
<th>Date</th>
<th>Event</th>
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<tbody>
<tr>
<td>January 1, 2010</td>
<td>Hired</td>
</tr>
<tr>
<td>December 31, 2010</td>
<td>Credited with one YOS</td>
</tr>
<tr>
<td>January 1, 2011</td>
<td>Enters plan</td>
</tr>
<tr>
<td>May 15, 2011</td>
<td>Quits (700 HOS)</td>
</tr>
<tr>
<td>December 31, 2012</td>
<td>Credited with one year BIS</td>
</tr>
<tr>
<td>August 14, 2014</td>
<td>Rehired: reemployment commencement date</td>
</tr>
<tr>
<td>March 1, 2015</td>
<td>Completes 1,000 HOS after rehire; enters retroactively to August 14, 2014</td>
</tr>
</tbody>
</table>
One-Year Holdout Rule Usually Bad Choice

• May have to give retroactive contributions
  – Including top-heavy
• Unusable for elective deferrals
  – How can you defer retroactively?
  – IRS does not believe the rule can be used for elective deferrals
• Only people it keeps out permanently are part-time rehires or those who leave soon after rehire
Rule of Parity

• Only applies to non-vested participants
• Can treat rehired EE as new employee if consecutive BIS at least equal to greater of:
  – Five, or
  – YOS prior to BIS
• If participant has five or fewer YOS, then must have five BIS
• If participant has more than five YOS, then must have BIS equal to number of YOS (but rule rarely applies because if five YOS, then at least partially vested)
## Parity BIS Eligibility Example

<table>
<thead>
<tr>
<th>Date</th>
<th>Event</th>
</tr>
</thead>
<tbody>
<tr>
<td>January 1, 2007</td>
<td>Hired</td>
</tr>
<tr>
<td>January 1, 2008</td>
<td>Enters plan</td>
</tr>
<tr>
<td>November 1, 2008</td>
<td>Quits with two YOS; no vesting</td>
</tr>
<tr>
<td>December 31, 2009</td>
<td>First one-year BIS</td>
</tr>
<tr>
<td>December 31, 2013</td>
<td>Fifth one-year BIS</td>
</tr>
<tr>
<td>August 1, 2014</td>
<td>Rehired; reemployment commencement date; must satisfy current eligibility requirements and pass entry date to enter plan again</td>
</tr>
</tbody>
</table>
Rule of Parity – No Prior Plan

• Employee worked full time for five years but employer did not have plan
• Quits
• Rehired after ten years
• Do the five years count?
  – Not clear since rule of parity applies to vested participants and there was no plan
Other BIS Notes

- BIS rules must be in plan document to apply
- Don’t assume they are there – check the document
- Remember: other than through BIS rules, rehired participant generally enters plan on date of rehire
## Classes of Rehired Employees and When They Enter (Re-enter)

<table>
<thead>
<tr>
<th>Class</th>
<th>Entry</th>
</tr>
</thead>
<tbody>
<tr>
<td>Already satisfied minimum age and service and entered plan</td>
<td>Immediately upon rehire</td>
</tr>
<tr>
<td>Already satisfied minimum age and service but terminated employment</td>
<td>Immediately upon rehire (or original entry date, if later)</td>
</tr>
<tr>
<td>before entry date</td>
<td></td>
</tr>
<tr>
<td>Already satisfied minimum service but didn’t enter plan because of</td>
<td>Immediately upon rehire (or entry date following attainment</td>
</tr>
<tr>
<td>minimum age requirement</td>
<td>of minimum age, if later)</td>
</tr>
<tr>
<td>Didn’t satisfy minimum service requirement</td>
<td>Wait until entry date following satisfaction of eligibility</td>
</tr>
<tr>
<td></td>
<td>requirements</td>
</tr>
</tbody>
</table>

Assumes no BIS rules and that person is an eligible employee
When Does Marty Enter (Re-enter?)

- ABC hired Marty (age 30) May 1, 2012
- ABC calendar year 401(k) plan has:
  - One YOS/age 21 entry requirements
  - January 1/July 1 entry dates
  - Shifting eligibility computation period
  - No eligibility break in service rules
- Marty always works 150 hours/month
- When does Marty enter/re-enter plan after rehire?

<table>
<thead>
<tr>
<th></th>
<th>Marty Quits</th>
<th>Marty Rehired</th>
</tr>
</thead>
<tbody>
<tr>
<td>c)</td>
<td>Feb. 1, 2013</td>
<td>May 18, 2013</td>
</tr>
</tbody>
</table>
Additional Rules for Vesting

• May exclude service (subject to terms of plan):
  – Prior to age 18
  – Prior to initial effective date or predecessor plan
  – During which mandatory employee contributions were not made

• After five BIS, future service is excluded in determining vesting of prior contributions
  – This is why plans provide for a forfeiture after five BIS – vested percentage of the existing account will not be increased
  – This rule does not affect vesting of future contributions
Forfeiture

• May be earlier of distribution of vested interest in plan or five BIS
  – Requires buy-back provisions
• May be after five BIS in service regardless of whether distribution is made
  – Requires full vesting if plan is terminated before participant has five BIS
Buy-Back Provisions

• Applies if employee receives distribution due to termination of participation in plan and plan forfeits non-vested interest
  – Repayment must be made by earlier of
    • Five years after re-employment
    • five breaks in service
• Deemed cash-out of $0 = deemed repayment of $0 if rehired before repayment period ends
Buy-Back and Forfeiture Restoration

• No guidance requiring notification of buy-back rights (other than in SPD)

• Buy-back
  – May be made with:
    • After-tax amount
    • Rollover
  – No adjustment for earnings unless DB plan
  – 401(k) plan may require payment of elective contributions

• Forfeiture restoration
  – Can use current year forfeitures
  – Employer must contribute
Rehired Employees and Distributions

• Example:
  – Plan allows distributions upon termination of employment
  – Plan does not permit in-service distributions
  – Larry quits July 15, 2011
  – Larry is rehired June 1, 2015
  – Larry requests distribution on June 2, 2015 claiming he was entitled to termination distribution

• IRS has informally indicated that plan could refuse to make distribution
Automatic Enrollment – Special Rules

• EACA – refund available 90 days from first automatic deferral
  – If no automatic deferrals for entire PY then treat as new participant
  – New 90 withdrawal right based on next automatic deferral
• QACA – escalation of automatic deferral based on year of initial automatic deferral
  – If no automatic deferrals for entire PY then treat as new participant
  – QACA escalation starts all over
• Rules are not limited to re-hired employees
Military Service
USERRA

- Uniformed Services Employment and Reemployment Rights Act of 1994
- Internal Revenue Code §414(u)
- USERRA generally requires employers to re-employ former employees who entered US military service
- We won’t cover re-employment rights as these are labor law issues
Most Pension Rights Contingent on Reemployment

• If an employer reemploys a worker following military service:
  – The employee is not treated as having incurred a break in service by reason of military service
  – Military service is treated as service with the employer
  – The employee receives the contribution he or she would have received had the employee remained at the employer
Compensation

• A participant’s compensation for retirement plan purposes while the participant is in the military is:
  – The pay the participant would have received had the participant not gone into the military
  – If that cannot be determined, use average pay during the year preceding military service
Contributions Included

• All contribution types
  – Top-heavy minimum
  – Safe-harbor contributions
  – Matching contributions
  – Discretionary or fixed contributions
  – Profit-sharing or pension contributions
  – Defined-benefit accruals

• No need to adjust for earnings or reallocate forfeitures
Make-Up Contributions

- Reemployed personnel have time to make up for missed deferrals or other EE contributions which they could have contributed
- Employer must then make any match
  - EE can designate year

<table>
<thead>
<tr>
<th>Time in military</th>
<th>Employee contribution make-up deadline</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 20 months</td>
<td>Three times length of service</td>
</tr>
<tr>
<td>At least 20 months</td>
<td>Five years</td>
</tr>
</tbody>
</table>
Affect of USERRA Contributions

- Employer and employee contributions count in year to which contribution relates, not in year of contribution
  - Limits such as 401(a)(17), 402(g), 415
- You do not rerun coverage, ADP, ACP and other nondiscrimination tests to take into account USERRA contributions
HEART

• Heroes Earnings Assistance and Relief Tax Act of 2008
• Retirement issues
  – Clarifies treatment of payments to employees in military
  – Allows death benefits for employees in military
  – Extends qualified reservist distributions
Military Differential Wage Payments
What is a Differential Wage Payment?

• Employer’s payment to an individual with respect to service in the uniformed services
  – Must be for active duty
  – Minimum: 30 days
  – All or a portion of the wages the individual would have received from the employer if the individual continued to work for the employer
Tax Treatment

• Differential wage payments are wages for federal income taxes
  – Moves them to W-2
  – Had been 1099-MISC if military service “disturbed” employment relationship

• FICA/FUTA
  – No change
  – Not taxable if employment relationship “disturbed” by military service
Impact on Retirement Plan

• Made final 415 regulations obsolete on this issue
  – HEART applies for years after 2008
• Inclusion of differential pay for most plan purposes is optional
  – IRS Notice 2010-15 allows exclusion for 414(s) compensation but not 415 compensation
Employment Status

• Plan must treat employee receiving differential wage payments as still employed
• No severance except for “deemed distributions” (covered later)
• Employed on last day of year
• Post-severance compensation rules are irrelevant
  – Payment for nonperformance of duties limited to 501 hours
<table>
<thead>
<tr>
<th></th>
<th>HEART</th>
<th>USERRA</th>
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<tbody>
<tr>
<td>Applies to</td>
<td>EEs receiving differential wage payments</td>
<td>EEs reemployed after qualified military service</td>
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<tr>
<td>Compensation</td>
<td>Differential wage payments</td>
<td>What compensation would have been</td>
</tr>
<tr>
<td>Count service for vesting</td>
<td>Up to 501 hours</td>
<td>Count all military service for vesting</td>
</tr>
<tr>
<td>Eligible to defer</td>
<td>Optional</td>
<td>Mandatory</td>
</tr>
<tr>
<td>Top heavy</td>
<td>Yes for differential wage pay</td>
<td>Yes for compensation</td>
</tr>
<tr>
<td>Other contributions</td>
<td>Optional</td>
<td>Mandatory</td>
</tr>
<tr>
<td>Nondiscrimination exemption</td>
<td>Yes, subject to conditions</td>
<td>Yes</td>
</tr>
</tbody>
</table>
Deemed Severance

• A plan may provide for a “deemed severance” for distribution purposes (IRS Notice 2010-15)
• If an individual elects to receive a distribution, then plan must suspend elective deferrals or after-tax for six months beginning on the date of the distribution
Mandatory Death Benefits

- Plan must provide death benefits to participant who dies in qualified military service as though reemployed on day prior to death
- Notice 2010-15 clarified that reemployment is based on reemployment under USERRA (for vesting purposes)
Application

• Does not require additional benefit accrual or allocation (i.e., not deemed compensation that would normally apply under USERRA)

• Does apply to:
  – Accelerated vesting
  – Ancillary life insurance benefits
  – Waiver of allocation conditions
  – Other survivor benefits contingent upon a participant’s death while employed
Questions?