



Insights on Layoffs and Furloughs

May 2020

How will Layoffs or Furloughs affect my 401k Plan?

Many employers are having to face the challenging decision to institute workforce furloughs or layoffs in order to survive the economic hardship caused by COVID-19 and the subsequent shelter-in-place orders.

Layoffs and furloughs can be challenging to navigate, both the emotional impacts and impacts to the benefits landscape for impacted employees and plans.

There may be impacts to your employer sponsored retirement plan, e.g. your company 401(k) or 403(b) plan. We're here to help outline the potential impacts, considerations, and support your teams through this challenging period.

Where to start to determine the potential impacts?

Start with your plan document. The plan document governs your specific plan provisions and how your plan is administered.

Review your plan's definition of the "severance of employment" and the calculation of "vesting service" provisions. You will need to determine if, according to your plan document, a layoff or furlough constitute a severance or termination of employment under your plan. If yes, these will impact you. We have put together a table outlining some of the primary plan considerations when it comes to considering layoffs or furloughs.

	Layoff	Furlough
How is it defined?	Termination of employment with the employer	Placing of an employee in a temporary nonduty, non-pay status because of lack of work or funds, or other non-disciplinary reasons (e.g. COVID-19).
Employer Sponsored Retirement Plan Impact	Terminated employees no longer receiving a paycheck, thus they lose the ability of making contributions to the plan via payroll deductions. Terminated employees with a balance can request a distribution from the plan or they can keep their balance in the plan if it is above a certain asset threshold.	Impacts plans that require participants to work a minimum amount of hours in a 12-month period (i.e. 500 hours), to receive the employer match, or be credited with vesting service. Extended furloughs could prevent employees from meeting those minimum hours, thus impacting their annual match and vesting credit.
Partial Plan Termination Considerations	Only impacts plans that fund an employer match and have a vesting schedule that is not 100% immediate (e.g. 2-6 year graded). If 20% or more of eligible plan participants are terminated, the IRS calls this a "partial plan termination" (PPT). Under a PPT scenario, any unvested match becomes 100% vested for any impacted.	Impacts plans that measure eligibility in the plan using a service requirement (i.e. 1,000 hours of service). Extensive furloughs from 2020 well into 2021 could affect this service requirement and constitute a termination of employment under your plan. These terminations could lead to a "partial plan termination" in 2021.

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How might layoffs or furloughs impact the plan's Non-Discrimination Testing?

Non-Discrimination Testing is used to ensure highly compensated employees (HCEs) do not disproportionately benefit from the plan compared to non-highly compensated employees (NHCEs). If mid-year **layoffs** disproportionately impact NHCEs, there may be higher likelihood of your plan failing testing. If the plan document requires hours of service to share in employer contributions or vesting credits a **furlough** of a significant portion of NHCEs may affect these requirements, potentially triggering a testing failure.

Recordkeeping Fee Considerations

Review your recordkeeper fee structure. Some recordkeepers charge a per participant fee for both active *and terminated* participants with a balance. To contain costs, you may consider initiating a sweep process with your recordkeeper to force out small balances from the plan and reduce the per participant cost.

Review the impact to plan forfeitures. Some plan sponsors pay fees using the plans forfeiture balance (i.e. non-vested portion of a former employee's account balance). If a PPT occurs, the non-vested balance of former employees becomes immediately vested. Thus, the balance of forfeitures available in the future to pay plan expenses and offset employer contributions may be reduced.

Action Steps to Determining Layoff and Furlough Impacts on Employer Sponsored Retirement Plans

Step 1

Review your plan document and work with your advisor and/or legal counsel to understand the impact of any workforce actions.

Step 2

Work with your recordkeeper to ensure that participant "status codes" are updated appropriately on your payroll/HRIS system to ensure the correct treatment for vesting, loan, and distribution purposes

Step 3

Be aware of the potential implication of a partial plan termination on vesting and future costs. While immediate vesting will not have an initial impact on costs, there may be a reduction to the amount of forfeitures available in future years to pay plan expenses and offset the cost of employer contributions.