

[\(484\) 574-8782](tel:4845748782)

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IRS Proposed Regulation on Use of Forfeitures



In February of 2023, the [IRS proposed regulations relating to the use of](#)

forfeitures. This would generally require that plan administrators use forfeitures no later than 12 months after the close of the plan year in which the forfeitures are incurred. The proposed regulations also clarify that forfeitures in a defined contribution plan may be used to: (1) to pay plan administrative expenses, (2) to reduce employer contributions under the plan, or (3) to increase benefits in other participants' accounts in accordance with plan terms. The proposed regulations provide a transition rule related to the 12-month deadline. Under this rule, forfeitures incurred during any plan year that begins before January 1, 2024, are treated as having been incurred in the first plan year that begins on or after January 1, 2024. Accordingly, those forfeitures must be used no later than 12 months after the end of that first plan year (by December 31, 2025).

Below are more specific explanations of the provisions of the proposed regulations related to the use of forfeitures.

Use of Forfeitures in Defined Contribution Plans

Consistent with changes made by TRA 86 providing uniform rules for the use of forfeitures in defined contribution plans (as described in the Conference Report), the proposed regulations would clarify that forfeitures arising in any defined contribution plan (including in a money purchase pension plan) may be used for one or more of the following purposes, as specified in the plan: (1) to pay plan administrative expenses, (2) to reduce employer contributions under the plan, or (3) to increase benefits in other participants' accounts in accordance with plan terms. The use of forfeitures to reduce employer contributions includes the restoration of inadvertent benefit overpayments and the restoration of conditionally forfeited participant accounts that might otherwise require additional employer contributions, for example, the restoration of accounts conditionally forfeited under § 1.411(a)-7(d) (relating to certain distributions and cash-outs of accrued benefits).

Timing for Use of Forfeitures in a Defined Contribution Plan

The proposed regulations would generally require that plan administrators use forfeitures no later than 12 months after the close of the plan year in which the forfeitures are incurred. This deadline is intended to simplify administration by providing a single deadline for the use of forfeitures that applies for all types of defined contribution plans and to alleviate administrative burdens that may arise in using or allocating forfeitures if forfeitures are incurred late in a plan year. The deadline in the proposed regulations is similar to the deadline under § 1.401(k)-2(b)(2)(v) for a section 401(k) plan to correct excess contributions by making corrective distributions, which is 12 months after the close of the plan year in which the excess contributions arise. The proposed regulations would not affect generally applicable deadlines related to the timing of contributions and

allocations under a plan, such as the deadline for correcting excess contributions to avoid excise taxes under section 4979 as set forth in § 1.401(k)-2(b)(5)(i).

The proposed regulations provide a transition rule related to the 12-month deadline. Under this rule, forfeitures incurred during any plan year that begins before January 1, 2024, are treated as having been incurred in the first plan year that begins on or after January 1, 2024; accordingly, those forfeitures must be used no later than 12 months after the end of that first plan year. As described in the section of this preamble titled “Proposed Applicability Date,” these regulations are proposed to apply for plan years beginning on or after January 1, 2024.

Although nothing in the proposed regulations would preclude a plan document from specifying only one use for forfeitures, the plan may fail operationally if forfeitures in a given year exceed the amount that may be used for that one purpose. For example, if (1) a plan provides that forfeitures may be used solely to offset plan administrative expenses, (2) plan participants incur \$25,000 of forfeitures in a plan year, and (3) the plan incurs only \$10,000 in plan administrative expenses before the end of the 12-month period following the end of that plan year, there will be \$15,000 of forfeitures that remain unused after the deadline established in these proposed regulations. Thus, the plan would incur an operational qualification failure because forfeitures remain unused at the end of the 12-month period following the end of that plan year. The plan could avoid this failure if it were amended to permit forfeitures to be used for more than one purpose.

Use of Forfeitures in Defined Benefit Plans

The proposed regulations would update rules relating to the use of forfeitures in defined benefit plans to reflect the enactment, after the issuance of § 1.401-7, of new minimum

funding requirements applicable to defined benefit plans. In addition, the requirement in existing § 1.401-7(a) that forfeitures under pension plans be used as soon as possible to reduce employer contributions would be eliminated because it is inconsistent with those minimum funding requirements. The minimum funding requirements of sections 412, 430, 431, and 433 do not allow the use of forfeitures to reduce required employer contributions to a defined benefit plan in the manner contemplated by existing § 1.401-7. Instead, reasonable actuarial assumptions are used to determine the effect of expected forfeitures on the present value of plan liabilities under the plan's funding method. Differences between actual forfeitures and expected forfeitures will increase or decrease the plan's minimum funding requirement for future years pursuant to the plan's funding method.

Proposed Applicability Date

These regulations are proposed to apply for plan years beginning on or after January 1, 2024. Thus, for example, the deadline for the use of defined contribution plan forfeitures incurred in a plan year beginning during 2024 will be 12 months after the end of that plan year. Taxpayers, however, may rely on these proposed regulations for periods preceding the applicability date.

Comments and Requests for Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any comments that are submitted timely to the Treasury Department and the IRS. The Treasury Department and the IRS request comments on all aspects of the proposed rules. Specifically, comments are requested on the following topics:

- Whether the rules for the use of forfeitures in defined benefit and defined contribution plans can be further simplified to reduce administrative costs and burdens; and

- Whether any issues arise concerning other unallocated amounts (in addition to forfeitures) with respect to qualified retirement plans, and, if issues do arise, whether guidance should be provided addressing those issues.



Written or electronic comments must be received by May 30, 2023.



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Email:

Address:

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Who We Are

Torrillo & Associates, LLC specializes in employee benefit plan audits including 401k audits, 403b audits, pension plan audits, and other retirement plan audits. We are licensed in 10 states including Pennsylvania, New Jersey, Delaware, New

York and Florida. We are also able to practice in additional states that have passed firm mobility.

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