

## Use of Forfeitures in Defined Contribution Plans

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**PRACTICES** Employee Benefits and Executive Compensation

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As a reminder, defined contribution retirement plan sponsors may use forfeitures to pay reasonable plan administrative expenses or reduce future employer contributions, if permitted by the plan and provided that such forfeitures are applied timely. The IRS requires that defined contribution plans use forfeitures no later than 12 months following the close of the plan year in which the forfeitures were incurred under the plan, as we previously reported [here](#).

Forfeitures generally result when a participant terminates employment prior to completing the service required for full vesting under the terms of the plan for purposes of employer contributions. If the plan does not specify how such forfeitures may be used or if forfeitures are not timely applied, the IRS requires that the unused forfeitures be reallocated to the plan's participants. In addition, depending on the length of time that forfeitures remain unallocated, a plan sponsor may also need to make a voluntary correction program filing with the IRS.

If permitted under the terms of the plan, forfeitures also may be used to pay plan expenses or offset employer contributions to the plan. Before applying forfeitures to pay for reasonable expenses or offset future employer contributions, plan sponsors should review their plan documents to determine if they may use the plan's forfeitures for this purpose. The plan sponsor also should ensure that it follows any ordering rules set forth in the plan document for use of forfeitures (for example, some plans require plan expenses be paid before forfeitures are used to offset employer contributions).

The plan's counsel can assist plan sponsors in determining how forfeitures can be applied under the terms of the plan, as well as help with any corrective actions that may be necessary if forfeitures were not timely and/or appropriately used.