

MANDATORY PARTICIPANT CONTRIBUTION PROVISION

DEFINED CONTRIBUTION



Plan Overview

Your MERS Defined Contribution Plan is a qualified retirement plan under Section 401(a) of the Internal Revenue Code, offering each employee a plan account to which contributions are made and assets are invested. When an employee retires, their benefits are based on the total amount

of money in their account. As a qualified plan, employees are not taxed on employer contributions, mandatory employee contributions, or earnings until assets are withdrawn.

Types of Contributions

The MERS Defined Contribution Plan is an employer-sponsored plan, with a variety of contribution options to fit the needs of every municipality. Your municipality may make employer contributions – either **matching** and/or **non-matching to employee contributions**.

In a **401(a)** plan, there can be **mandatory** participant contributions, which are made on a pre-tax basis and/or **voluntary** after-tax contributions. This guide outlines the **Mandatory Participant Contribution** provision.

Mandatory Participant Contributions

Mandatory Participant Contributions is used broadly to describe all types of allowable pre-tax contributions to a 401(a) plan. This type of plan is prohibited by the IRS from including **elective** pre-tax employee contributions similar to what is common in private sector 401(k) plans and 457(b) deferred compensation plans. To ensure that employee contributions to 401(a) defined contribution plans are not considered taxable income to the employee, the law provides that a governmental entity can “pick-up” employee contributions. To allow for this “pick-up”, the employee is limited to making an election that is:

- Exercised one-time only
- Made when the employee is first eligible to participate in any retirement plan of the governmental employer
- Is irrevocable

The employer can require a fixed contribution amount, allow for a one-time elective choice, or offer an option for both.

Required Fixed Contributions – The employer can require employees to contribute either a specific dollar amount or a percentage of their pay.

One-Time Elective Contributions – The employer can offer employees a one-time elective contribution up to 99% or the IRS contribution limit.

Importance of the Contribution Rate

Because employees do not have the flexibility to change their contributions, the initial selection of the contribution rate—whether chosen by the employer or participant—becomes crucial. It determines the ongoing savings rate for the duration of employment under the plan.

Employers should clearly communicate to participants at enrollment that the selected rate will be locked in and **cannot be modified** later.

This underscores the importance of carefully considering the **long-term impact** of the chosen contribution rate, as it will directly affect the employee’s retirement savings success over time.

See MERS Employer Toolkit for an [enrollment template](#) that you can customize for your plan.

Default Contribution Rate

The default contribution rate is the mandatory participant contribution rate established by the employer which is used in the following cases:

- Where an **employee fails** to make an election prior to the first payroll reporting in which they qualified for the plan.
- Where the participant is **transferred or rehired** into a division where the range of one-time elected options is now available to the participant for the **first time**.

- Where the participant is **transferred or rehired** into a division where the range of one-time elected options is available and the participant's initial **one-time election is unknown** to the employer.

In the absence of an employer elected rate, the plan default rate of 10% will be used.

How the Default Contribution Rate Works

		Transferring/rehiring TO a division with:		
		DC division with a required contribution	DC division with a one-time elective contribution	DC division with both a required contribution and a one-time elective contribution
Transferring/rehiring FROM a division with:	DC division with a required contribution	Participant uses the new division's required contribution rate	If the participant <u>ever</u> made a one-time election in any previous divisions (DC or the DC portion of Hybrid), they must use that rate. If no election was ever made or if the election is unknown, the new division's default rate applies.	If the participant ever made a one-time election in any previous divisions (DC or DC portion of Hybrid), they must use that rate. If no election was ever made or if the election is unknown, the new division's default rate applies.
	DC division with a one-time elective contribution	Participant uses the new division's required contribution rate	Participant must keep their previous one-time rate elected rate. If no election was ever made or if the election is unknown, the new division's default rate applies.	If the participant ever made a one-time election in any previous divisions (DC or DC portion of Hybrid), they must use that rate. This rate would be in addition to the required contribution rate of the new division. If no election was ever made or if the election is unknown, the new division's default rate applies.
	DC division with both a required contribution and a one-time elective contribution	Participant uses the new division's required contribution rate	Participant must keep their previous one-time rate elected rate If no election was ever made or if the election is unknown, the new division's default rate applies.	If the participant ever made a one-time election in any previous divisions (DC or DC portion of Hybrid), they must use that rate. This rate would be in addition to the required contribution rate of the new division. If no election was ever made or if the election is unknown, the new division's default rate applies.

How Mandatory Employee Contributions Apply to Transfers

When an employee is transferred between divisions, their mandatory contribution rate in the new division will be dependent on their initial election AND/OR the provisions in the “new” division. To help explain this, below are some examples:

Example 1:

Division A allows for a one-time election between 0-99%

Division B allows for a one-time election between 0-99%

Sally hires into Division A and elects a contribution of 15%. After a few years, she transfers to Division B. Sally must **maintain her 15%** contribution as the new division has the range provision.

Example 2:

Division A has a required fixed contribution of 7%

Division B allows for a one-time election between 0-99% with a default rate of 10%

Sally hires into Division A and makes the required fixed contribution of 7%. After a few years, she transfers to Division B. Sally must use the **default contribution** rate of Division B (10% in this case) since any elections in DC must be made at the time of first eligibility or hire date.

Example 3:

Division A allows for a one-time election between 0-99%

Division B has a required fixed contribution of 5%

Sally hires into Division A and elects a contribution of 15%. After a few years, she transfers to Division B. Sally must use the **required fixed contribution rate** of 5% since that is the provision in effect for this division.

If in a few years, Sally transfers back to Division A she must use her initial contribution election of 15%.

Example 4:

Division A has **both** a required fixed contribution of 5% and a one-time election of 0-99%.

Divisions B has **both** a required fixed contribution of 7% and a one-time election 0-99%

Sally hires into Division A she elects to contribute 1% in addition to her required 5%. After a few years, she transfers to Division B. She must maintain her election of 1% and make the required fixed contribution of 7%, meaning her total contribution would be 8%.

Contribution Structure Best Practices

In today’s competitive labor market, offering retirement plans that truly help employees reach their financial and retirement goals isn’t just a benefit—it’s a strategic advantage.

The truth is, investments aren’t the main driver of retirement success. The real difference-makers are when employees start saving and *how much* they save. That’s where employers have extraordinary influence.

Pairing a 457 plan with a defined contribution plan is one way to help employees save more, especially since IRS rules restrict changes to pre-tax elective contributions in a 401(a) plan.

Further, Secure 2.0 requires private sector plans to automatically enroll employees at a minimum of 3% in the first year and increase by 1%

annually until they reach a maximum ranging from 10%-15%. While public-sector plans aren’t required to follow this rule—those that do are giving their workforce a proven best practice that combats inertia while allowing employees to opt out anytime.

By automatically enrolling employees in the 457 plan and gradually increasing contributions, you help them build better habits and better outcomes—without requiring them to take extra steps.

The bottom line? A well-designed retirement plan helps your employees build financial security, strengthens your ability to recruit and retain talent, and positions your organization as a leader in employee well-being.

Regional Teams to Serve You

Have questions? We are here to help. **800.767.6377**