

Guide to Safe Harbor Plan Provisions

The material contained in this document is provided for informational purposes only and is not intended to constitute legal advice. This document discusses the most popular features, benefits, and requirements for safe harbor contribution plans. However, it is not a complete statement of all requirements; there are additional benefits and requirements for safe harbor contribution plans. This document discusses the most popular features, benefits and requirements. Please consult with your tax or legal advisor regarding safe harbor contribution plans and how one may benefit your company.

Sponsoring a retirement plan for employees is a great way for companies to retain good talent and subsidize an individual's retirement fund. However, some plan sponsors feel [nondiscrimination testing \(NDT\)](#) can be a frustrating part of administering a 401(k) plan. NDT is a series of annual tests required by the Internal Revenue Code (IRC). The purpose of the testing is to ensure employers are not unfairly providing the larger benefits to their highly compensated employees (HCEs). If a plan 'fails' any of the tests, there are consequences ranging from removing employer contributions from HCEs' accounts to making additional employer contributions to non-highly compensated employees (NHCEs). Because of the complexity of testing and the administrative burden to a plan sponsor, some organizations are opting to set up new plans and/or amend their current plan document to include [safe harbor contribution provisions](#). Safe harbor contribution provisions can reduce the administration of the plan and the burden of nondiscrimination testing.



NOTE: *Contact a member of your client service team if you are interested in having a Fit Assessment performed on your plan to determine whether a safe harbor contribution plan would be cost effective for your company.*

Plan sponsors who elect a safe harbor contribution provision are agreeing to follow certain eligibility, contribution, vesting and participant notice rules in exchange for bypassing some, but not all, of their plan's nondiscrimination testing.



IMPORTANT NOTE: Full safe harbor plans are still subject to 415, 402(g) and Coverage testing.

The Benefits to Plan Sponsors

If its requirements are followed, safe harbor contribution provisions provide several advantages to plan sponsors, including automatically satisfying several of the required nondiscrimination tests.

The tests automatically satisfied are the:

- Actual Deferral Percentage Test (ADP) (IRC Section 401(k)), if proper notices are provided to participants
- Actual Contribution Percentage Test (ACP) (IRC Section 401(m)), if proper notices are provided to participants and there are no after-tax contributions
- For top heavy plans, a full safe harbor plan that only includes employee salary deferrals and required safe harbor contributions (i.e., no after-tax or profit sharing) also automatically satisfies the top heavy minimum contribution requirements. No top heavy minimum contribution is required if there are:
 - Safe harbor matching contributions, or
 - A discretionary matching contribution that is within the ACP safe harbor requirements (less than 4% of eligible compensation and not matching deferrals in excess of 6% of eligible compensation).

Partial safe harbor plans (typically means participants are eligible to make deferral contributions but are not eligible to receive any safe harbor contributions; please refer to the FAQs for additional information) generally do not automatically satisfy the [top heavy](#) minimum contribution requirements. However, once the SECURE Act's Long-term, Part-time requirement becomes effective, there will be a further exception to this rule.

Often, small employers with 401(k) plans have a difficult time passing some of the tests because having only one or two HCEs can skew the test results. In that case, a safe harbor contribution plan is a great alternative.

Another advantage of safe harbor plans is the allowance for maximum deferrals by HCEs, along with the matching contributions, without the concern of having to refund participant deferrals and refund and/or forfeit matching contributions because the plan failed a portion of the NDT.

Additionally, a safe harbor contribution plan provides the ability for plan sponsors to adequately budget for their 401(k) costs since any matching contributions can be as low as 3.5% of employee compensation (in certain QACA safe harbor plans) or 4% in a traditional safe harbor match plan. Safe harbor contribution plans using a nonelective contribution can be as little as 3% of eligible employee compensation.

These are three great advantages, but to reap their benefits, the following rules must be followed regarding eligibility, employer contributions, vesting and participant notices:

Eligibility

After initial eligibility requirements are met for a participant to enter the plan, safe harbor contribution plans cannot require employees to work a certain number of hours to be eligible for plan benefits.



IMPORTANT NOTE: *If participants become eligible to participate in the safe harbor contribution portion of the plan at a later date than being eligible to make salary deferrals to the plan, ADP/ACP testing may still apply to a portion of the population, some who have not yet met the initial eligibility for the safe harbor contribution. As mentioned above, top heavy testing may also apply. Plans in this situation are considered partial safe harbor plans.*

Traditional Safe Harbor Contributions (Pre-Tax)

Traditional safe harbor plans require plan sponsors to make pre-tax contributions to their employees' 401(k) accounts in one of the following ways:

- Nonelective - Contribute at least 3% of employee compensation for the plan year to each eligible employee, regardless of whether the employee makes a salary deferral or
- Match – Contribute a matching contribution based on participants' elective deferrals at the rate of 100% of the first 3% deferred and 50% of the next 2% deferred. Plan sponsors also

have the option of matching 100% for the first 4% of compensation deferred, but either way, the 4% contribution is the maximum required match. The plan can increase the match formula up to certain limits.

The plan document must specify which method the employer will use for contributions.

Vesting for Traditional Safe Harbor Contributions

Traditional safe harbor contribution plans are required to have full and immediate vesting with respect to all deferrals and safe harbor contributions in a participant's account.

Participant Notices

Safe harbor match plans are required to provide an initial notice to newly eligible participants and an annual one to all participants with specific requirements around the content and timing of the notices.

- The content of the notice must describe the employee contribution method in use and how eligible employees may make deferrals and elections.
- Generally, the notice must be sent at least 30 days prior to the participant's entry date and the annual one at least 30 days, but not more than 90 days prior to the start of the plan year.

The SECURE Act modified some of the rules for requiring a safe harbor notice to employees, however this is only for plans using the "fixed" safe harbor nonelective plan design. These changes were required to be able to permit the adoption of a safe harbor nonelective contribution after the plan year began up until 30 days prior to the end of the plan year at 3% or even later, up until 12 months after the end of the plan year at 4%. The safe harbor notice is optional; however, the notice may be needed if the plan is an ACP safe harbor, and, in any case, the plan sponsor may want to provide a notice anyway.

To be eligible to remove the safe harbor contribution provision mid-year, the plan sponsor should include a provision in the notice that states the plan sponsor may elect to reduce or eliminate the safe harbor contribution provision. This gives the plan sponsor flexibility to control its retirement plan costs in the event of a downturn in the economy or a business decline. Most sample safe harbor notices contain this provision. Without this notice, the ability to remove the safe harbor contribution mid-year must meet more stringent regulatory requirements. Note that this requirement for a notice

the plan sponsor may elect to remove the safe harbor contribution mid-year applies even to nonelective plans that may have no other notice requirement.

Springing Safe Harbor Contributions

Springing safe harbor nonelective plans are considered traditional safe harbor nonelective plans; however, they require multiple notices and multiple amendments.

The initial notice must be provided at least 30 days, but no more than 90 days prior to the beginning of the plan year. The notice states the plan might be safe harbor and will be amended at a later date if the plan will be safe harbor for the plan year. This flexibility allows for the plan sponsor to decide to be both ADP and ACP safe harbor during the plan year.

If the plan sponsor decides to be safe harbor, at least 30 days before the end of the plan year, both an amendment must be executed to commit to the safe harbor contribution and a supplemental notice must be provided to the participants indicating the plan was amended to be safe harbor for the plan year. The notice for the following year can also be included at the same time indicating the plan might be safe harbor for the next year. With the SECURE Act changes, springing safe harbor nonelective plans will generally only be used where the springing plan also wants to have deemed satisfaction of the ACP test for the additional match.

Qualified Automatic Contribution Agreements

Beginning in 2008, an additional type of safe harbor plan became available, known as the Qualified Automatic Contribution Agreement (QACA). A QACA plan requires employees, upon becoming eligible for the plan, to be automatically enrolled at a default salary deferral rate of at least 3% of compensation, unless the employee elects not to participate, or elects a rate of deferral different from the default. In addition, employees who are automatically enrolled must have their default deferral rates automatically increased each year until at least 6% (cannot exceed 10%) of compensation is being deferred.

While not required, a QACA plan may also include an 'unwind' provision that provides for a 90-day window in which participants who were auto-enrolled can elect to discontinue deferring and withdraw their elective deferrals from the plan.

In contrast to a traditional safe harbor contribution plan, a QACA plan allows for a 2-year vesting schedule for safe harbor contributions. The participant must be fully vested after completion of two

years of service. The maximum required matching under a QACA is 3.5% of compensation, as opposed to 4% of compensation required under the traditional safe harbor. The QACA plan also requires a larger deferral percentage (6% vs. 5%) for the participants to obtain the maximum employer match for the QACA safe harbor match.

Some employers favor a QACA over a traditional safe harbor plan because:

- The automatic enrollment feature encourages high participation rates among employees who might not choose to enroll if given the choice to opt in,
- The 2-year vesting schedule assists with employee retention, and
- The vesting schedule further assists the employer with budgeting since those who terminate prior to the 2-year tenure requirement do not receive all the employer contribution.

Actual Contribution Percentage Test (ACP) (IRC Section 401(m))

Many safe harbor contribution plans automatically satisfy the ACP test. To be deemed to satisfy the ACP test, the plan must:

- Provide the notice described above at least 30 days, but no more than 90 days, prior to the beginning of the plan year.
- If the plan sponsor chooses to make an additional matching contribution to the plan (in addition to the safe harbor contribution):
 - Deferral contributions over 6% of compensation cannot be matched.
 - If the match is discretionary, the amount of the matching contribution cannot exceed 4% of compensation.
 - There can be no continuing eligibility requirements (500 or 1,000 hours of service in the current plan year or last day of the plan year) to receive the additional match.
 - HCEs cannot receive a higher match rate than NHCEs.
 - The rate of match cannot increase as the rate of deferrals increase.
- The plan cannot have after-tax contributions in the year being tested.

Full Safe Harbor Plans

Plans that are full safe harbor are deemed to satisfy the ADP and ACP tests as well as the top heavy minimum contribution requirements. To be considered full safe harbor for a given plan year, the following requirements must be satisfied:

- All employees must be eligible for the safe harbor contribution when they become eligible to defer. SECURE Act will modify this to allow for long-term part time employees to be excluded when this provision becomes effective.
- Only contributions to the plan are those that are deemed to satisfy ADP/ACP.
- There are no additional employer contributions (including the reallocation of forfeitures).
- After-tax contributions are not permitted in a full safe harbor plan.

Removing Safe Harbor Contribution Mid-Year

Safe harbor contribution provisions may be removed mid-year if certain conditions apply:

- Proper notice was provided indicating that the plan sponsor may remove the safe harbor contribution mid-year. Without this notice, the ability to remove the safe harbor contribution mid-year must meet more stringent regulatory requirements.
- Contributions accrued under the plan up to the point of removing the provision must still be funded to participant accounts through the effective date of the supplemental notice to employees that the safe harbor contribution is being removed.
- If the plan calculates the matching contribution based on the contribution period of plan year, it may not be possible to effectively remove the safe harbor match mid-year without also amending the contribution period.

Frequently Asked Questions

My plan allows after-tax contributions. What does this mean for ACP testing?

If a plan allows after-tax contributions (and is not collectively bargained), it is required to satisfy the ACP test on the after-tax contributions.

For the ACP test, the plan sponsor may choose to:

- Exclude the safe harbor match
- Include the safe harbor match
- Include only the safe harbor match that's greater than 4% of the compensation (3.5% for QACA plans)

What is a partial safe harbor plan?

A partial safe harbor plan has a safe harbor contribution feature; however, the plan may require ADP and/or ACP testing for multiple reasons:

- The safe harbor contribution is not provided to all participants.
- Participants are eligible to deferral contributions prior to being eligible for the safe harbor contribution.
- The plan allows traditional '[after-tax contributions](#)', also known as 'employee contributions'.
- The plan has a discretionary match that exceeds 4% of compensation.
- The plan matches deferrals in excess of 6%.
- The plan has an escalating match formula.
- The non-safe harbor match has continuing eligibility requirements.
- The plan makes a non-safe harbor nonelective contribution.

What are some examples of situations where a partial safe harbor plan would still be subject to ADP testing?

If a plan does not provide safe harbor contributions to all employees eligible to make deferrals, the plan is subject to limited ADP testing (and ACP testing, if applicable). Some examples of plans in this situation include:

- Plans that have an eligibility requirement for deferrals that is less than the requirement to receive the safe harbor contribution. For example, 1 month of service for deferrals, and 12 months and 1,000 hours of service requirement for the safe harbor contribution or
- Plans that allow non-union and union employees to defer, but only allow non-union employees to receive the safe harbor contribution.

How many types of Safe Harbor plans are there?

There are multiple match and non-elective options.

Type of Safe Harbor Contribution	Deemed Satisfaction of ADP Test	Deemed Satisfaction of ACP Test	Notice Requirements	Required Amendment Date*	Auto Enrollment & Increase Requirements	Removing Safe Harbor Contribution Mid-Year	Vesting
3% of Compensation Nonelective Contribution with notice	Yes	Yes, if criteria are met	30 days prior to initial eligibility and 30 days prior to the beginning of plan year	Prior to beginning of plan year	None	Requirements depend on notice provided to participants	100% immediately
3% of Compensation Nonelective Contribution without notice (SECURE ACT)	Yes	No	N/A	30 days prior to end of plan year	NA	N/A - Do not execute amendment unless safe harbor will be utilized	100% immediately
Traditional Safe Harbor Match	Yes	Yes, if criteria are met	30 days prior to initial eligibility and 30 days prior to the beginning of plan year	Prior to beginning of plan year	None	Requirements depend on notice supplied to participants; note contribution period	100% immediately
QACA Match	Yes	Yes, if criteria are met	30 days prior to initial eligibility and 30 days prior to the beginning of plan year	Prior to beginning of plan year	Yes	Requirements depend on notice supplied to participants; note contribution period	Up to 2 year cliff (100% after 2 years of service)
QACA Nonelective Contribution	Yes	Yes, if criteria are met	30 days prior to initial eligibility and 30 days prior to the beginning of plan year	Prior to beginning of plan year	Yes	Requirements depend on notice provided to participants	Up to 2 year cliff 100% after 2 years of service)
4% of Compensation Nonelective Contribution without notice (SECURE ACT)	Yes	No	N/A	12 months after plan year end, however, consult tax advisor for funding	No	N/A - Do not execute amendment unless safe harbor will be utilized	100% immediately
Springing Nonelective Contribution	Yes	Yes, if criteria are met	30 days prior to initial eligibility and 30 days prior to the beginning of plan year	30 days prior to beginning of plan year and 30 prior to end of plan year if amending	No	Don't execute amendment	100% immediately

Does the safe harbor contribution need to be calculated on gross compensation with no exclusions?

No; however, having compensation exclusions would require a 414(s) compensation test to verify the definition of compensation elected in the adoption agreement does not discriminate in favor of HCEs. Failing the compensation test will require a retroactive amendment to the definition of compensation and funding the safe harbor contribution based on the amended definition of compensation.

Are there any withdrawal restrictions on safe harbor contributions?

Yes. For safe harbor employer contributions, there are generally no in-service withdrawals before age 59 ½.

Does the election to be a safe harbor contribution plan impact anything on the Plan Year End Summary (PYES)?

No, electing a safe harbor plan provision has no impact to the Plan Year End Summary reporting.

Am I required to fund the safe harbor contribution to my HCEs?

No, if elected in the plan document, you may exclude HCEs from receiving the safe harbor contributions. The plan may still be considered a full safe harbor plan if HCEs are excluded from the safe harbor contributions.