



## CBIZ Actuarial & Benefit Consultants

### Safe Harbor 401(k) Plans

Your business is all about people. At CBIZ Actuarial & Benefit Consultants, so is ours. Our goal is to work with you to develop a successful retirement program that meets **your** objectives and allows you to attract and retain the quality employees you need to be successful.

401(k) Plans allow employees to save for their retirement on a tax advantaged basis. Under a 401(k) Plan, employees are allowed to elect to have a portion of their salary contributed to the plan for their benefit. Under a traditional 401(k) Plan, that contribution would not be included in the employee's taxable income in the year it is deferred. Distributions and any earnings on the amount deferred would be taxed at the time the money is distributed to the employee or his/her beneficiary(ies). Under a Roth 401(k) Plan, the amount deferred is included in the employee's income in the year contributed, however, distributions of the amount contributed as well as any related earnings are not taxed when distributed from the plan (assuming the amounts have been held in the plan for the required period). In most cases, a Roth 401(k) Plan will allow the employee to choose between traditional 401(k) treatment, Roth treatment, or a combination of the two.

All 401(k) deferrals are subject to certain non-discrimination requirements which can limit the amount that "Highly Compensated Employees" ("HCEs") can defer. This limit is based upon the average rate of deferrals for "Non-Highly Compensated Employees" ("NHCEs"). (This test is commonly referred to as the Average Deferral Percentage or ADP test.) Therefore, if the participation level of NHCEs is low, it can limit the deferrals for HCEs, thus limiting the effectiveness of the 401(k) Plan for HCEs.

The ADP test can be avoided entirely if the employer is willing to make a "Safe Harbor" contribution to the 401(k) Plan and satisfy certain notice and vesting requirements. A Safe Harbor contribution can be a matching contribution equal to at least 100% of the first 3% of compensation deferred into the Plan, plus 50% of the next 2% deferred into the Plan by the employee. (Other limits apply to the structure and amount of the matching contribution).

Alternatively, the Safe Harbor contribution can be a "Non-Elective" or "Profit Sharing" contribution equal to at least 3% of each eligible employee's compensation.

All Safe Harbor contributions must be 100% vested immediately.

**CBIZ Actuarial & Benefit Consultants**  
Phoenix, AZ 602.277.2371  
San Jose, CA 408.794.3536  
Denver, CO 303.790.0825  
Houston, TX 713.871.1118



## Frequently Asked Questions about Safe Harbor 401(k) Plans

*What are the advantages of a Safe Harbor 401(k) Plan?*

Some of the advantages of a Safe Harbor 401(k) Plan include:

- A plan sponsor avoids ADP testing of elective contributions and ACP testing of matching contributions.
- HCEs are able to defer the maximum amount allowed under the regulations regardless of the amount deferred by the NHCEs.
- For plans that are considered “Top Heavy”, safe harbor contributions may satisfy the top heavy contribution requirement.

*Can an existing 401(k) Plan be converted to a Safe Harbor 401(k) Plan?*

Yes, an existing 401(k) Plan can be converted to a Safe Harbor 401(k) Plan as long as the conversion amendment is adopted before the beginning of the plan year in which the conversion takes effect.

*Is any special notice to participants required for a Safe Harbor 401(k) Plan?*

Yes, every eligible employee must be given a “Safe Harbor” notice at least 30 days, but no more than 90 days, prior to the beginning of each plan year in which a safe harbor contribution will be made. In addition, employees who become eligible during the plan year should be given the notice at least 30 days prior to their eligibility date. The Safe Harbor notice is required to include certain information including:

- A description of the safe harbor contribution to be made.
- A description of any other employer contributions and the conditions under which they can or will be made.
- The type and amount of compensation that may be deferred.
- A description of how participants make deferral elections.
- A description of the withdrawal and vesting provisions.
- Who to contact for more information about the plan.

Can a different matching contribution be considered safe harbor?

Yes, a different match contribution may be used to satisfy the safe harbor as long as it is at least equal to the basic safe harbor matching formula in the aggregate and the rate of match does not increase as the rate of elective contribution increases.



*Can additional contributions be made to a Safe Harbor 401(k) Plan?*

Yes, additional contributions, such as a profit sharing contribution, may be made in addition to a safe harbor matching contribution or a safe harbor non-elective contribution.

*Can safe harbor contributions be stopped during the plan year?*

Yes, safe harbor contributions may be stopped during the plan year, but how they are stopped is dependent upon whether they are safe harbor match contributions or safe harbor non-elective contributions.

Safe harbor match contributions may be stopped or reduced during the plan year as long as employees are given notice in advance of the amendment and given a chance to change their deferral elections. The amendment cannot be effective earlier than 30 days after the notice is given to employees and the employer must make the safe harbor match through the amendment effective date. In addition, ADP and ACP testing will apply to all contributions made during the plan year.

Safe harbor non-elective contributions may also be suspended during the plan year if the above requirements are met. However, in addition to the above requirements, the employer must have also sustained a substantial business hardship as defined in IRS regulations.

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