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Safe Harbor Plans

November 2, 2017

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Agenda

- Background
- ADP safe harbor requirements
- ACP safe harbor requirements
- Top Heavy safe harbor plans
- Reducing or suspending safe harbor contributions for the current plan year
- Common questions on Safe Harbor plans
- Designing a safe harbor plan on the ftwilliam.com documents

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BACKGROUND

Why would we want to design our 401(k) as a safe harbor plan?

- Deemed to Pass Certain Non-Discrimination Tests
  - Actual Deferral Percentage (ADP) test
  - Actual Contribution Percentage (ACP) test
    - If certain additional requirements are met
  - Top-Heavy Testing
    - If certain additional requirements are met

Types of Safe Harbor Plans

- The Internal Revenue Code (IRC) provides two alternatives to satisfying safe harbor
  - Section 401(k)(12) Option: "Traditional" Safe Harbor
  - Section 401(k)(13) Option: Qualified Automatic Contribution Arrangement ("QACA") Safe Harbor
    - Includes an automatic enrollment feature

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ADP SAFE HARBOR REQUIREMENTS

ADP Safe Harbor

- Basic requirements to satisfy the ADP safe harbor (deemed to pass ADP testing):
  - Adopted by the first day of the plan year
  - In effect for the entire 12-month plan year
  - Minimum employer contributions
  - Vesting requirements
  - Annual notice
  - Withdrawal restrictions

ADP Safe Harbor Document Requirement

- Plan document must specify safe harbor provisions before the first day of the plan year
  - New plan exception – new plan can be set up as a safe harbor plan as long as there are at least 3 months in the first plan year
  - Existing profit sharing plan adding a new 401(k) feature is treated as a new plan for the new plan exception

ADP Safe Harbor Document Requirement

- Wait and See Approach (Maybe)
  - Wait and see notice provided at the beginning of the plan year
  - Follow-up notice provided at least 30 days before the last day of the plan year
  - Plan must be amended at least 30 days before the last day of the plan year to specify safe harbor provisions

ADP Matching Contribution Formula Traditional Safe Harbor

- Basic Safe Harbor Matching Formula:
  - 100% match on first 3% of compensation deferred; plus
  - 50% match on the next 2% of compensation deferred

ADP Matching Contribution Formula Traditional Safe Harbor

- Enhanced Safe Harbor Matching Formula
  - If an employer would prefer to use a formula other than the basic safe harbor formula, they may do so as long as:
    1) At each deferral rate the participant would be getting a match at least as good as the basic matching formula
    2) The formula does not provide for a higher level of match for any HCE than is provided for any NHCE who contributes at the same deferral rate as the HCE; and
    3) The rate of match does not increase as the rate of deferral increases

ADP Matching Contribution Formula Traditional Safe Harbor

Example 1 – Enhanced Safe Harbor Match

- Proposed formula is 100% on the first 2% and 75% on the next 4% of deferrals
- Proposed formula is not a valid enhanced SH match as rate of matching at a 3% deferral rate is lower than the basic rate

Deferral Rate	Basic Rate	Proposed Rate
1	1%	1%
2	2%	2%
3	3%	2.75%
4	3.5%	3.5%
5	4%	4.25%
6	4%	5%

ADP Matching Contribution Formula Traditional Safe Harbor

Example 2 – Enhanced Safe Harbor Match

- Proposed formula is 100% on the first 4% of deferrals
- Proposed formula is a valid enhanced SH match as the rate of matching at each deferral rate is at least as high as at the basic rate

Deferral Rate	Basic Rate	Proposed Rate
1	1%	1%
2	2%	2%
3	3%	3%
4	3.5%	4%
5	4%	4%
6	4%	4%

ADP Matching Contribution Formula QACA Safe Harbor

- Basic safe harbor matching formula:
  - 100% match on first 1% of compensation deferred; plus
  - 50% match on the next 5% of compensation deferred
- Enhanced matching formula also permitted
  - Same requirements as with traditional enhanced match

ADP Matching Contribution Formula QACA Safe Harbor

Example 1 – Enhanced QACA Safe Harbor Match

- Proposed formula is 100% on the first 2% and 25% on the next 4% of deferrals
- Proposed formula is not a valid enhanced SH match as rate of matching at a 5% and 6% deferral rates is lower than the basic rate

Deferral Rate	Basic Rate	Proposed Rate
1	1%	1%
2	1.5%	2%
3	2%	2.25%
4	2.5%	2.5%
5	3%	2.75%
6	3.5%	3%

ADP Matching Contribution Formula QACA Safe Harbor

Example 2 – Enhanced QACA Safe Harbor Match

- Proposed formula is 100% on the first 3.5%
- Proposed formula is a valid enhanced SH match

Deferral Rate	Basic Rate	Proposed Rate
1	1%	1%
2	1.5%	2%
3	2%	3%
4	2.5%	3.5%
5	3%	3.5%
6	3.5%	3.5%

ADP Safe Harbor Nonelective Contribution Formula

- Same requirement for traditional and QACA safe harbor plans
- The employer must provide a nonelective contribution that equals at least 3% of the participant's compensation

ADP Contribution Vesting Requirement Traditional Safe Harbor

- Must be 100% vested immediately
  - Note that the IRS has stated that forfeitures may generally not be used to fund safe harbor contributions subject to immediate 100% vesting
- The ftwilliam.com document automatically provides for 100% immediate vesting for ADP safe harbor contributions

ADP Contribution Vesting Requirement QACA Safe Harbor

- ADP Contributions under the QACA safe harbor may be subject to a vesting schedule
  - Participants must be 100% vested in no more than two years

Additional QACA Requirements

- Automatic enrollment arrangement – initial deferral percentage can be 3 to 10%
  - Participant can elect not to defer, or defer a different percentage
- If participant does not make investment election, default needs to communicated to participants
- Notice requirements

Additional QACA Requirements

- If initial deferral percentage is less than 6% of compensation, the following applies:
  - Minimum of 3% from enrollment to the last day of the following plan year
  - Minimum of 4% for the next plan year
  - Minimum of 5% for the next plan year
  - Minimum of 6% for any subsequent plan year

Annual Notice Contents - All Safe Harbor Plans

- The annual safe harbor notice must provide the following:
  - The safe harbor formula used in the plan for matching or nonelective contributions
  - Any other contributions that may be made under the plan including the potential for discretionary contributions
  - The plan to which the safe harbor contributions will be made
  - The amount and type of compensation that may be deferred
  - Vesting provisions of the plan
  - Withdrawal provisions of the plan
  - The method by which a participant may make deferral elections
  - Guidance on how to obtain further information about the plan

Annual Notice Requirements for QACA Plans

- In addition to the preceding, the annual notice for a QACA plan must also provide an explanation of:
  - The rights not to make employee contributions, or make them at a different rate to the rate set
  - How the contributions will be invested if the employee does not select investment options him or herself

Annual Notice Timing Requirement

- The annual safe harbor notice must be provided to employees within a 'reasonable time' prior to the first day of the plan year
  - The IRS has provided that this is generally considered to be between 30 and 90 days prior to the first day of the plan year
- Employers may provide newly eligible employees with a safe harbor notice up to the employee's date of eligibility
- Such notice may not be provided earlier than 90 days prior to the employee's date of eligibility
- Notice for new plans may be provided up to the first day of the first plan year of a new safe harbor 401(k) plan
- Notice for existing 401(k) plans that convert into a safe harbor 401(k) plan must be given 30 to 90 days prior to the first day of the plan year that such conversion is effective

Withdrawal Restrictions on Safe Harbor Plans

- Withdrawal of ADP safe harbor employer contributions is restricted under IRC § 401(k)2, i.e. can only be made due to:
  - Severance of employment or retirement
  - Attainment of age 59 ½
  - Disability
  - Certain payments to qualified reservists
  - Certain plan terminations
- Hardship withdrawals are not permitted

Other ADP Safe Harbor Requirements

- Plan may apply normal eligibility conditions
  - Maximum is one year/1000 hours/age 21 with semi-annual entry dates
  - Two-year eligibility not allowed
  - Eligibility may be different for deferrals and safe harbor contributions:
    - Caveat Emptor! Disaggregated testing will apply and plan will have to test for top heavy status
- No allocation conditions allowed, i.e. last day rule or hours requirement
  - Once eligibility is met, participant must receive safe harbor contributions

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ACP SAFE HARBOR REQUIREMENTS

ACP Safe Harbor

- If the matching contributions under a safe harbor 401(k) plan meet certain requirements, they are deemed to satisfy the ACP test
  - This is known as the ACP safe harbor
- The plan must satisfy the ADP safe harbor but ACP safe harbor is optional

ACP Safe Harbor Requirements

- Mandatory matching contributions may not be made on deferrals in excess of 6% of compensation
- Discretionary matching contributions may not exceed 4% of compensation
- Matching contributions may not increase as the rate of deferral increases
- Matching contributions for HCEs at any rate of deferral may not be greater than matching contributions made to NHCEs who contribute at that same rate
- No allocation conditions may be placed on matching contributions (e.g., last day rule, hours requirement)
- Fixed and discretionary matching contributions may be subject to a vesting schedule without jeopardizing the ACP safe harbor

Triple Stack Match

- This formula can maximize HCEs and only benefits other participants who defer
- Maintains the ADP/ACP safe harbor status and can provide a top heavy free pass in most circumstances
- Three types of match
  - Safe Harbor Match – maximum 4% of compensation
  - Discretionary Match - maximum 4% of compensation
  - Fixed Match - ????% of deferrals up to 6% of comp
- The Safe Harbor and Fixed formulas are specified in document

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TOP HEAVY SAFE HARBOR PLANS

Top Heavy Rules

- A safe harbor plan that would otherwise be top heavy is considered not to be provided that:
  - No other contributions are made to the plan
    - Includes forfeiture reallocation
    - If there are matching contributions, they satisfy the ACP safe harbor
  - Eligibility is the same for deferrals and safe harbor contributions
    - Plan cannot be disaggregated for top heavy testing

Top Heavy Rules

- Determination as to whether the top heavy exemption applies is made year by year
  - E.g. make a discretionary profit sharing contribution some years
- Safe harbor contributions may be used toward top heavy minimum contributions
  - Match or NEC
  - 3% NEC will generally meet requirement depending on eligibility requirements, entry dates, and definition of compensation

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REDUCING OR SUSPENDING SAFE HARBOR CONTRIBUTIONS FOR THE CURRENT PLAN YEAR

Reducing/Suspending Safe Harbor Contributions

- Safe harbor matching or nonelective contributions may be reduced/suspended for a plan year
  - Plan must experience a substantial business hardship unless the initial safe harbor notice stated that the safe harbor contribution may be reduced or removed. Factors taken into account in determining whether a business hardship exists include whether or not:
    - The employer is operating at an economic loss;
    - There is substantial unemployment/underemployment in the trade or business and in the industry concerned;
    - Sales and profits of the industry concerned are depressed or declining; and
    - It is reasonable to expect that the plan will be continued only if the amendment is adopted.
  - This requirement is waived if the annual notice contained language stating that the plan sponsor may chose to reduce/suspend safe harbor contributions mid-year. This is called "Maybe Not" language in the notice. It is not a separate notice.

Effect of Reducing/Suspending Contributions

- If an employer chooses to reduce/suspend safe harbor contributions for a plan year, then the plan will be subject to ADP/ACP testing for the entire plan year
- Employer must fund safe harbor matching contributions up until effective date of amendment
- Employer must fund safe harbor nonelective contributions taking compensation into account, up until effective date of amendment
- If the plan is top heavy, the plan may no longer rely on the safe harbor top heavy exemption

Reducing or Suspending Safe Harbor Matching Contributions

- A supplemental notice must be given to all eligible employees explaining the effect of the amendment which reduces/suspends the safe harbor matching contributions, the amendment's effective date, and information on how a participant may change his or her deferral election
  - Notice must be provided at least 30 days prior to the effective date of the reduction/suspension
- Participants must be given a reasonable opportunity to change their deferral elections before the reduction/suspension goes into effect

Reducing or Suspending Safe Harbor Matching Contributions

- The plan must be amended to reflect the reduction/suspension of the safe harbor matching contributions, and that the plan will be subject to ADP/ACP testing for that entire plan year
  - Model amendments are available on the ftwilliam.com website under 'Other Documents' on the 'Print Plan Documents Screen'

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COMMON QUESTIONS ON SAFE HARBOR PLANS

Frequently Asked Questions

When Must Safe Harbor Contributions be Made?

- Safe harbor contributions must be made no later than 12 months after the end of the plan year
- If the employer would like the contributions to be deductible for the year to which they apply, then the contribution must be made by the due date of the employer's federal income tax filing for that year
- If safe harbor matching contributions are being made on a payroll period basis, then they must be made no later than the last day of the next plan year quarter

Frequently Asked Questions

What is the definition of compensation for safe harbor purposes?

- For safe harbor purposes, the definition of compensation must satisfy Code section 414(s)
- Entry date compensation may be used

Frequently Asked Questions

I would like to amend my 401(k) plan to be a safe harbor 401(k) plan starting next year; when must the amendment be adopted?

- In order to be exempt from ADP/ACP testing for a plan year, the plan must be amended for safe harbor purposes prior to the first day of that plan year

Frequently Asked Questions

I'd like to make a mid-year amendment to my safe harbor 401(k) plan to add (or remove) a new feature. Is this allowable?

Rules changed with IRS Notice 2016-16

- Changes never allowed mid-year
  - Changing type of safe harbor plan (e.g., from a traditional safe harbor plan to a QACA plan)
  - A change to eligibility that would result in fewer employees being eligible for the safe harbor contribution
  - An increase in the number of years required for vesting in a QACA plan
- Changes allowed mid-year if other requirements are met
  - Adding or modifying a matching contribution formula that increases the possible matching contribution a participant may receive
  - Changing the definition of compensation for matching contributions if it could result in an increase in the possible matching contribution a participant may receive

Frequently Asked Questions

Mid-year Amendment

Additional Requirements for changing matching formula or matching definition of compensation where there is the possibility of an increase in the amount of matching contributions a participant may receive

- The plan is amended at least three months before the end of the plan year
- The change is effective back to the beginning of the plan year
- The notice and change opportunity requirements are met

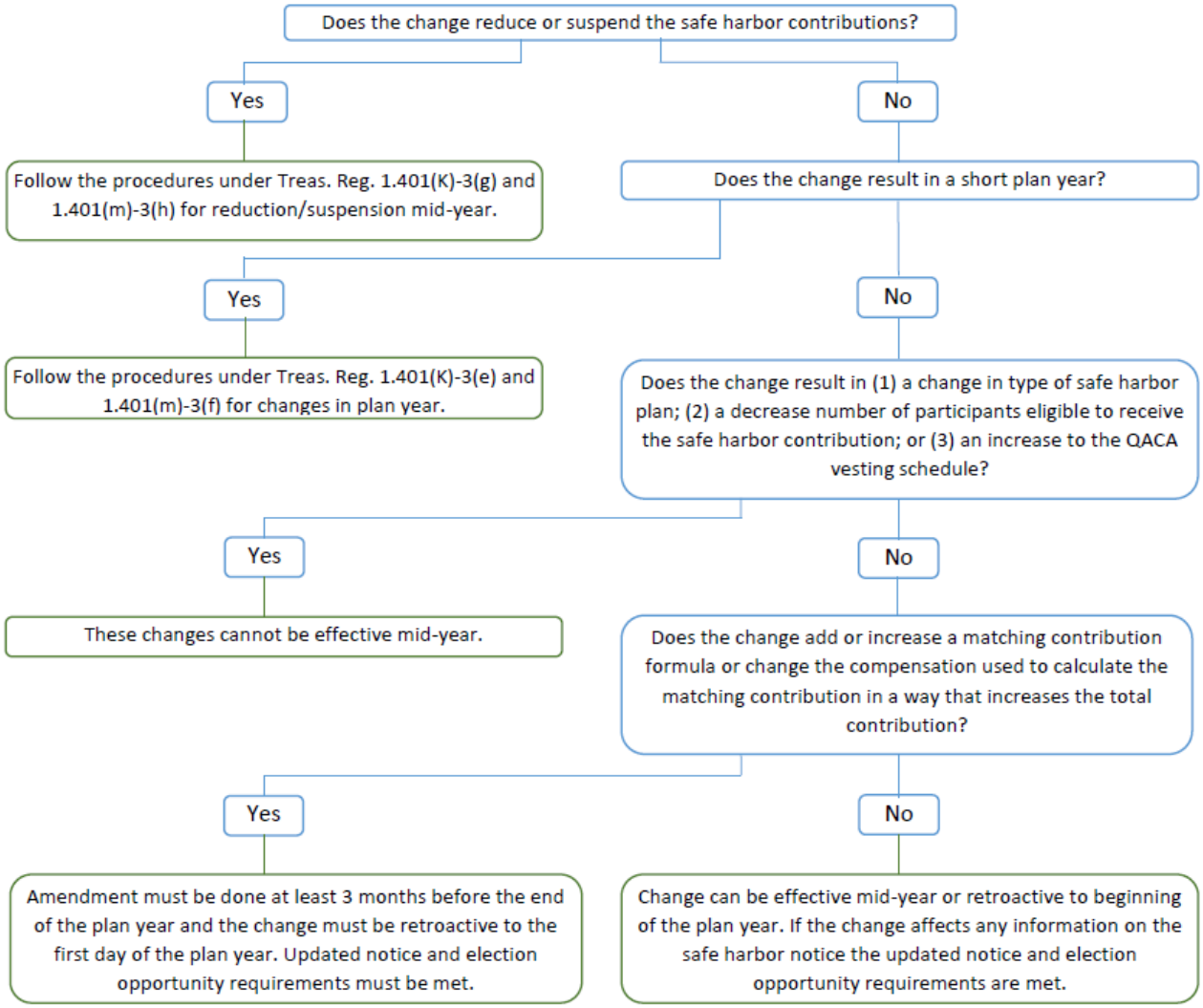
Frequently Asked Questions

Mid-year Amendment

- Notice Requirement
  - If the change affects the annual notice, participants must be given an updated notice which describes the changes and when they will be effective
  - Notice must be given within a "reasonable time frame" before the change is effective (generally at least 30 and no more than 90 days)
  - If notice cannot be given out timely (e.g., retroactive to first day of plan year), notice must be given out as soon as practicable but no later than 30 days following adoption of the change
- Election Change Opportunity
  - Participants must be given an opportunity to change their deferral elections
  - Must be at least 30 days long and, unless not practicable, must be before the effective date of the change

MID-YEAR SAFE HARBOR AMENDMENT DECISION TREE

Note: This decision tree does not take into account any amendment rules aside from safe harbor.



Frequently Asked Questions

How do short plan years of terminating plans affect safe harbor plans?

- For short plan years created by the termination of a safe harbor plan, the plan sponsor may operate the plan during its final year in one of the following ways:
  - Cease safe harbor contributions as of the date of termination and apply ADP/ACP tests to the plan for its final year using the current year testing method; or
  - The plan may continue to be a safe harbor plan for the final plan year if the safe harbor requirements are met through the date of termination, and:
    - The plan's termination is in connection with certain business transactions described in Code section 410(b)(6)(C) (e.g., change in employer's related group), OR
    - The employer incurs a substantial business hardship, as described by Code section 412(c)(2).

Frequently Asked Questions

Can forfeitures be used to fund safe harbor contributions?

- The IRS has issued new regulations that allow forfeitures to fund safe harbor contributions, QNECs, and QMACs
- PPA documents do not allow forfeitures to fund ADP safe harbor contributions but there is a snap-on amendment that can be used to allow this.

Frequently Asked Questions

Can safe harbor contributions be made to another plan?

- Yes; for example if the employer sponsors a profit sharing plan as well as a 401(k) plan, the safe harbor nonelective may be made to the profit sharing plan rather than the 401(k)
  - Plans must have same plan year
  - 401(k) plan must name the other plan in their document

Frequently Asked Questions

What is the difference between the maybe notice and the maybe not language?

- Wait and See (Maybe) Notice
  - An actual notice used by the plan administrator to indicate that the they may chose to amend the plan to be safe harbor non-elective before the end of the year. It is a full safe harbor notice with language stating that the plan administrator will let the participants know if the plan will become safe harbor
- Maybe Not
  - Additional language that can be included in the normal safe harbor notice to let the participants know that the plan may amend away from safe harbor and that they will be notified is such an amendment does take place
  - Inclusion of this language allows the plan to amend away from safe harbor status without meeting the business hardship requirement

Frequently Asked Questions

Can a plan administrator use the Wait and see option with a match?

- No, the wait and see option is only available with a non-elective form of safe harbor contribution.

Frequently Asked Questions

Can a 403(b) plan be safe harbor?

- ADP testing is not required for 403(b) plans
- ACP safe harbor is available – the plan must satisfy the following requirements:
  - Contributions must satisfy the ADP and ACP safe harbors
  - Annual notice must be furnished

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DESIGNING A SAFE HARBOR PLAN ON THE FTWILLIAM.COM DOCUMENTS

ftwilliam.com Document
Safe Harbor - Eligibility

- Eligibility is the same regardless if match or non-elective and traditional safe harbor or QACA safe harbor
- Excluded Classes
  - Follows elections for elective deferrals
  - If union are not excluded for elective deferral purposes they can be excluded separately for safe harbor contribution
  - Can also exclude HCEs or HCEs who are also key employees – cannot exclude just key employees
- Allocation Condition – Highly Compensated Employees only
  - Maximum requirement is employment on the last day and/or completion of 1,000 hours of service

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Safe Harbor – Eligibility

- Age, Service, and Entry Date
  - Follow same elections made for elective deferrals
    - If not elected disaggregated coverage testing will need to be completed
  - Complete custom age, service, and entry date
    - Must still meet the 21 and 1 year maximum eligibility requirement
  - Greatest age and service requirement using semi-annual entry dates
    - Requirement is age 21 and 1 year of service (defined as completing 1,000 hours by the end of a 12 month period)
    - Entry dates are the first day of the first and seventh month of the plan year on or immediately following the day eligibility is met
  - Greatest age and service requirement using annual entry dates
    - Requirement is age 21 and 1 year of service (defined as completing 1,000 hours by the end of a 12 month period)
    - Entry dates is the first day of the first month of the plan year closest to the day eligibility is met (may be retro-active)

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Safe Harbor – Eligibility

2. **ADP/ACP Safe Harbor Eligibility**

   a. Exclusions. For purposes of safe harbor contributions, the term "Eligible Employee" shall not include

      i. [ ] No exclusions

      ii. [ ] Participants who are Highly Compensated Employees

      iii. [ ] Participants who are Key Employees and Highly Compensated Employees

      iv. [ ] Other exclusions: _____

   b. [ ] Participants covered by a collective bargaining agreement will share in safe harbor allocations provided retirement benefits were the subject of good faith bargaining.

   c. Eligibility conditions for Safe Harbor Contributions

      i. [ ] None. Any Eligible Employee eligible to make Elective Deferrals is eligible to receive a safe harbor contribution.

      ii. [ ] The following age, service and entry date requirements: _____

      iii. [ ] Participants who have met the greatest minimum age and service conditions permitted under Code section 410(a)(1)(A) with semi-annual entry dates (first day of the first month and seventh month of the Plan Year)

      iv. [ ] Participants who have met the greatest minimum age and service conditions permitted under Code section 410(a)(1)(A) before the first day of the seventh month of the Plan Year

   d. Allocation requirements for Highly Compensated Employees

      i. [ ] Require service for Highly Compensated Employees to receive a safe harbor contribution. Hours of Service required in the applicable Plan Year for Highly Compensated Employees to receive a safe harbor contribution: _____

      ii. [ ] Require employment on the last day of Plan Year for Highly Compensated Employees to receive a safe harbor contribution

   e. [ ] Employer contributions will be offset by safe harbor contributions

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Safe Harbor – Contributions

- New for PPA – Plans can have both a safe harbor contribution and additional fixed or discretionary match that does not meet either the ADP or ACP safe harbor contribution requirements
  - Plan would be required to complete ACP and top heavy testing if match is made that does not meet the ACP safe harbor contribution requirements
- Plan can have both an ADP and an ACP safe harbor matching contribution
- Plans can have 2 ACP safe harbor matching contributions and remain ACP safe harbor as long as the ACP safe harbor contribution requirements are met (triple stack match)

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Safe Harbor – Contributions

- Completing check list for ADP safe harbor contribution
  - Match cannot be set to one of the tiered rate options (no discretionary or years of service)
  - Example shows basic matching contribution

D. Matching Contribution Formula	
6. Matching Contribution formula	Two rates
6a. First rate of Matching Contributions (without % sign - percent of elective deferrals match)	100
6a.i. Maximum amount of Employee contributions matched (without % sign - maximum percent of compensation matched at rate above)	3
6b. Second rate of Matching Contributions (without % sign - percent of elective deferrals matched at second step)	50
6b.i. Maximum amount of Employee contributions matched (without % sign - maximum percent of compensation matched at rate above)	5

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Safe Harbor – Contributions

Completing check list for ACP safe harbor contribution

- Additional match can be fixed and/or discretionary
  - Additional match would be completed the same way if either of the additional matches is non-safe harbor
- ACP Safe Harbor match limitations
  - The rate of matching Contributions cannot increase
  - Cannot be made on contributions in excess of 6% of Compensation
  - Discretionary ACP match cannot exceed 4% of Compensation.

D. Additional Matching Contributions	
7. Further discretionary Matching Contributions may be made in addition to those described as first - third steps	Yes / No
8a. Further fixed Matching Contributions will be made in addition to those described as first - third steps	Yes / No
8b. Describe any further tiered Matching Contributions	25% match on Matched Contributions up to 4% of Compensation

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Safe Harbor – Vesting

- Traditional ADP safe harbor contributions are always 100% vested
- QACA ADP safe harbor contributions are subject to the vesting schedule selected in the plan document (maximum of 2 year cliff)

E. QACA Vesting	
11a. Specify the vesting schedule for QACA contributions	Other
11b. Other QACA Schedule - less than 1 year (without % sign)	50
11c. Other QACA Schedule - 1 year but less than 2 years (without % sign)	75

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Safe Harbor – Vesting

- Discretionary ACP (traditional or QACA) safe harbor contributions are always subject to the vesting schedule selected for matching contributions
- Fixed ACP (traditional or QACA) safe harbor contributions are subject to the vesting schedule selected for matching contributions only if elected in the check list (Section E)

E. Matching Vesting

8a. Matching Contribution Account Vesting Schedule	3 Year Cliff
9. If the Plan provides for a safe harbor match, additional fixed or discretionary matching contributions beyond the safe harbor contribution will be subject to the vesting schedule above:	Discretionary only

Discretionary only
Additional fixed and discretionary

Thanks for Attending!