

Your Guide to a Safe Harbor 401(k) Plan

401(k) plans must not favor highly compensated employees (HCEs) over non-highly compensated employees (NHCEs). As such, the IRS has established required compliance tests to verify all employees have fair representation in a plan. A safe harbor plan allows you to automatically pass these tests if you meet specific contribution, vesting, and notification rules. A Safe Harbor provision can be added to traditional 401(k) plans.

What are some of the advantages of a Safe Harbor plan?

- Generally, plans that meet the Safe Harbor requirements will pass the following compliance tests:
 - The actual deferral percentage (ADP) test
 - The actual contribution percentage (ACP) test
 - The top-heavy test
- Safe Harbor plans eliminate many of the restrictions to the amount owners and HCEs can contribute to their 401(k) plans.
- Employers may be able to reduce business taxes and can help employees build a larger nest egg.
- Employers may receive additional savings from the company's discretionary matching contribution.
- Any HCE (subject to certain limitations), may contribute the full 401(k) plan annual dollar amount (\$23,000 for calendar year 2024), without regard to the amount the other employees defer.

Does a Safe Harbor plan make sense for me?

If you are an employer experiencing one of the following situations with your plan, you may benefit from a Safe Harbor provision:



HCEs' deferrals are limited because of low participation rates or low contribution rates by NHCEs



Plan is consistently top-heavy, and additional employer contributions must be made to satisfy the top-heavy requirements (with these being the only additional employer contributions made)



Generous (more than 3%) profit sharing or matching contributions are made consistently

Who is considered an HCE?

HCEs are generally defined as individual(s) with more than 5% ownership, certain family members of a more than 5% owner (spouse, parents, children, or grandparents), or employees who earned more than \$155,000 in the previous calendar year. (2024 limit; subject to IRS cost of living adjustments.)

What is required of the employer to satisfy Safe Harbor requirements?

To provide automatic compliance with the ADP and ACP tests, the employer must provide a matching or non-elective contribution. Your Safe Harbor contributions must be 100% vested and additional non-Safe Harbor contributions will have to meet non-discrimination rules. The following formulas are options to select.

Contribution Type	Formula Options		Calculation Description
Match	Basic	Enhanced 5%	Contribute a matching contribution percentage of each employee's compensation (as defined in the Adoption Agreement). An employee must contribute to receive an employer contribution. Safe Harbor match contributions are immediately 100% vested.
	Enhanced 4%	Enhanced 6%	<p>Examples:</p> <ul style="list-style-type: none"> ▪ Basic: Contribute a match of 100% on the first 3% of employee's deferrals and 50% on the next 2% of deferrals ▪ Enhanced: Contribute a match of 100% on 4%, 5%, or 6% of employees' deferrals
Non-elective	Non-elective 3%	Non-elective 5%	Contribute a percentage of each eligible employee's compensation (as defined in the Adoption Agreement). An employee does not need to contribute to receive an employer contribution. Safe Harbor non-elective contributions are immediately 100% vested.
	Non-elective 4%	Non-elective 6%	<p>Example:</p> <ul style="list-style-type: none"> ▪ Contribute a non-elective contribution of 3%, 4%, 5%, or 6% of compensation for all eligible employees

Additional administrative requirements

Aside from the typical operational compliance rules (following plan provisions, filing Form 5500 annually, etc.), you must:

- Amend the 401(k) plan document (or adopt a 401(k) for the first time) to include the Safe Harbor Basic or Enhanced match provisions prior to the start of the plan year.
- Amend the 401(k) plan document at least 30 days prior to the end of the current plan year if making 3% non-elective contributions or by the end of the following plan year if making a 4% contribution to all eligible employees.¹
- Notify participants about the Safe Harbor Basic or Enhanced match provisions 30 to 90 days before the start of each new plan year (there is no notice requirement for Safe Harbor non-elective contributions); Ascensus assists you by providing a template notice. To simplify your responsibilities, Ascensus offers a notice delivery service for certain participant notices including Safe Harbor notices (for a fee).
- Operate as a Safe Harbor plan for the entire plan year.



Safe Harbor FAQs

What is non-discrimination testing?

There are generally three main types of compliance tests required to be performed on a 401(k) plan to ensure you do not establish a plan that treats your employees unfairly:

- **Actual Deferral Percentage (ADP) test** – compares the deferral percentage of HCEs and NHCEs. (Generally, the HCE deferral amount cannot be more than two percentage points higher than the NHCEs' average.)
- **Actual Contribution Percentage (ACP) test** – compares employer matching contributions between the HCEs and NHCEs.
- **Top-heavy test** – determines if the account balances of key employees is greater than 60% of the total assets of the plan.

What will I be limited to as an owner if I don't have a Safe Harbor plan?

Generally, all HCEs will be limited to defer only about 2% more than the average of all eligible NHCEs. If the plan does not have any eligible NHCEs participating in the 401(k) plan, then none of the HCEs would be able to participate either.

NHCE Average	Calculation
Between 0%–2%	Multiply that number by two to determine the maximum average for the HCEs.
Between 2%–8%	Add two to that number to determine the maximum average for the HCEs.
Greater than 8%	Multiply that number by 1.25 to determine the maximum average for the HCEs.

What if I want to contribute more than the required match?

Many employers limit their contributions to the amounts required under their chosen Safe Harbor formula. Others choose options with greater flexibility. Because of the vast number of contribution possibilities, you should consult Ascensus' ERISA associates before making contributions beyond what the Safe Harbor rules require.

What costs are associated with implementing a Safe Harbor contribution formula?

The cost of the Safe Harbor contribution depends on the level of plan participation. If few eligible employees make deferrals, a matching formula may be more cost-effective than the non-elective contribution. If you want to increase deferral rates, even at a higher cost, you may choose an Enhanced Match formula.



When does the plan need to be established?

An employer can amend from an existing traditional 401(k) to a 3% non-elective Safe Harbor up to 31 days before the plan year end. After that date, you can still amend to a Safe Harbor up to 12 months following the plan year end, but the non-elective contribution will have to be 4%. New Safe Harbor plans are required to be set up three months prior to the plan year-end date. It typically takes two to three weeks from the purchase date to be able to install your plan.²

The amendment process may take longer than expected due to required plan paperwork. It is recommended to start the process as soon as possible before the 31 day period to allow sufficient time for this amendment.

What if employees don't receive proper notice of the Safe Harbor provisions?

Failing to provide a Safe Harbor notice constitutes an operational failure as the employer wouldn't be operating the plan in accordance with the terms of the plan document.

How do I correct an operational failure?


The appropriate correction for a late Safe Harbor notice depends upon the impact on individual participants. For example, if the missing notice results in an employee not being able to make contributions to the plan (either because he or she wasn't informed about the plan or how to make contributions to the plan), the employer may need to make a corrective contribution.

On the other hand, if an employee was made aware of the plan's features and the method for making contributions, the failure to provide notice may be treated as an administrative error. This is corrected by revising procedures to ensure that future notices are provided to employees in a timely manner.


¹The Setting Every Community Up for Retirement Enhancement (SECURE) Act of 2020 permits employers the option to amend up to 30 days before the end of a plan year if making Safe Harbor nonelective contributions of 3% or by the close of the following plan year if the plan makes Safe Harbor non-elective contributions of 4%. The SECURE Act also eliminated the participant notice requirement for Safe Harbor non-elective contributions.

²Plan installation date requirements are contingent upon the plan type being adopted and whether it is an existing or start-up plan. Specific deadlines are set for each year.

Contact your client services team for additional Safe Harbor information.

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