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IRS Temporarily Makes It Easier to Amend Safe Harbor Plans in 2020

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In order to reduce expenses during the COVID-19 pandemic, plan sponsors have expressed an interest in reducing or eliminating safe harbor contributions under their 401(k) plans. The circumstances permitting such amendments are limited, but guidance in IRS Notice 2020-52 temporarily modifies prior IRS guidance (See: IRS Notice 2016-16) to make it easier to amend a safe-harbor 401(k) plan mid-year.

A safe harbor 401(k) plan design eliminates the need to perform certain non-discrimination tests and permits highly compensated employees to contribute the maximum amount permitted by the Tax Code's annual limitations. A safe harbor contribution takes the form of either a matching contribution or a nonelective contribution.

In order to eliminate or reduce a safe harbor contribution mid-year under IRS Notice 2016-16, the annual safe harbor notice (required to be provided to eligible employees within a "reasonable" time before the beginning of each plan year⁽¹⁾) must contain the plan sponsor's reservation of the right to amend the plan during the plan year. If the safe harbor notice does not contain this language, then a mid-year amendment to safe harbor 401(k) plans is permitted only if the plan sponsor is operating at an economic loss. IRS Notice 2016-16 also requires notice to participants at least 30 days in advance of the effective date of the amendment.

IRS Notice 2020-52 permits the adoption of a mid-year amendment to a safe harbor plan in 2020 if the amendment is adopted between March 13, 2020 and August 31, 2020 and no later than the amendment's effective date. Plans with safe harbor nonelective contributions do not have to provide participants with the 30-day advance notice so long as notice of the amendment is provided no later than August 31, 2020. To give participants sufficient time to continue, change or discontinue their elective contributions, the 30-day advance notice to participants is still required for plans with safe harbor matching contributions.

Eliminating either form of safe harbor contribution requires the plan to satisfy the applicable non-discrimination rules for 2020 and those non-discrimination provisions must be contained in the plan document.

After this window of opportunity ends, the rules in IRS Notice 2016-16 will, once again, apply. We would recommend that future safe harbor notices for plans with safe harbor matching contributions contain a reservation of the right of the plan sponsor to make mid-year amendments.

1. (Safe harbor notices for plans with safe harbor nonelective contributions were eliminated by the SECURE Act).

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