

Notice 2016-16

Mid-Year Changes to Safe Harbor Plans and Safe Harbor Notices

I. PURPOSE

This notice provides guidance on mid-year changes to a safe harbor plan under §§ 401(k) and 401(m) of the Internal Revenue Code. The notice provides that a mid-year change either to a safe harbor plan or to a plan's safe harbor notice does not violate the safe harbor rules merely because it is a mid-year change, provided that applicable notice and election opportunity conditions are satisfied and the mid-year change is not a prohibited mid-year change, as described in the notice. In addition, the notice requests comments on additional guidance that may be needed, in particular with respect to mid-year changes to safe harbor plans in cases in which a plan sponsor is involved in a merger or acquisition.

II. BACKGROUND

A. Exemptions from ADP and ACP Testing for Safe Harbor Plans

Under general nondiscrimination rules, benefits under or contributions to a qualified plan must be nondiscriminatory in amount. Section 401(k) plans satisfy this requirement if elective contributions made on behalf of highly compensated employees ("HCEs") for a year satisfy the actual deferral percentage ("ADP") test. A similar actual contribution percentage ("ACP") test applies to matching contributions and employee contributions pursuant to § 401(m).

As an alternative to satisfying the annual ADP and ACP test, a plan may be structured to use a safe harbor plan design. For purposes of this notice, a "safe harbor plan" is a plan that includes a cash or deferred arrangement described in § 401(k)(12) (traditional § 401(k) safe harbor) or § 401(k)(13) (qualified automatic contribution arrangement ("QACA") 401(k) safe harbor), or a matching contribution described in § 401(m)(11) (traditional matching safe harbor) or § 401(m)(12) (QACA matching safe harbor).

For purposes of this notice, §§ 1.401(k)-3 and 1.401(m)-3 are referred to as the "safe harbor plan regulations." The safe harbor plan regulations set out requirements for a § 401(k) or 401(m) plan to be a safe harbor plan, including requirements regarding contributions, requirements that certain plan provisions remain in effect for a 12-month plan year (subject to certain exceptions), and requirements regarding the provision of safe harbor notices.

B. Safe Harbor Plan Provisions That Must Remain in Effect for Entire 12-Month Plan Year

Section 1.401(k)-3(e)(1) provides that a plan will fail to satisfy the requirements of §§ 401(k)(12) and 401(k)(13) and § 1.401(k)-3 unless plan provisions that satisfy the safe harbor plan rules of § 1.401(k)-3 are adopted before the first day of the plan year and remain in effect for an entire 12-month plan year. It also provides that a safe harbor plan that includes provisions that satisfy the safe harbor plan rules of § 1.401(k)-3 will not satisfy the nondiscrimination requirements for § 401(k) plans for a plan year if the safe harbor plan is amended to change those provisions during the plan year. Section 1.401(m)-3(f) includes similar provisions for matching safe harbor plans.

The safe harbor plan regulations set out several exceptions to the requirement that plan provisions satisfying the rules of §§ 1.401(k)-3 and 1.401(m)-3 be adopted before the first day of the plan year and continue for an entire 12-month plan year. These include exceptions for (i) a short first plan year, (ii) a change in the plan year, (iii) a short final plan year, (iv) a delayed adoption of safe harbor plan nonelective contributions (if notice of this possibility is provided before the beginning of the plan year), and (v) a mid-year reduction or suspension of safe harbor contributions (which results in loss of safe harbor plan status). See §§ 1.401(k)-3(e), (f), and (g) and 1.401(m)-3(f), (g), and (h).¹ In addition, exceptions to the prohibition against mid-year amendments may be provided in guidance of general applicability published in the Internal Revenue Bulletin. See §§ 1.401(k)-3(e) and 1.401(m)-3(f).

C. Safe Harbor Notice Requirements

The notice requirements applicable to traditional § 401(k) safe harbor plans are satisfied if each employee eligible to participate is given, within a reasonable period before any year, written notice of the employee's rights and obligations under the arrangement and the notice meets certain content and timing requirements. See § 401(k)(12)(D) and § 1.401(k)-3(d). Sections 401(k)(13)(E) and 401(m)(11)(A)(ii) impose similar notice requirements with respect to QACA and matching safe harbor plans. This notice refers to notices provided under these sections as "safe harbor notices."

To meet the content requirements, a safe harbor notice must be sufficiently accurate and comprehensive to inform an employee of the employee's rights and obligations under the plan, and written in a manner calculated to be understood by the average employee eligible to participate in the plan. Under the safe harbor plan regulations, a notice is not considered sufficiently accurate and comprehensive unless

¹ Other guidance discussing mid-year changes to safe harbor plans includes: Ann. 2007-59, 2007-25 I.R.B. 1448 (certain hardship withdrawal changes and designated Roth contribution changes); Notices 2010-84, 2010-51 I.R.B. 872, and 2013-74, 2013-52 I.R.B. 819 (certain designated Roth contribution changes); and Notice 2014-37, 2014-24 I.R.B. 1100 (certain changes related to same sex spouses).

the notice accurately describes certain information specified in those regulations, including the plan's safe harbor contributions, any other plan contributions, the type and amount of compensation that may be deferred under the plan, how to make cash or deferred elections (including any administrative requirements that apply to the elections), the plan's withdrawal and vesting provisions, and specified contact information. See §§ 1.401(k)-3(d) and 1.401(m)-3(e). In addition to satisfying the general content requirements for a safe harbor notice, a safe harbor notice for a QACA must describe certain additional items, including the level of elective contributions that will be made on the employee's behalf if the employee does not make an affirmative election and how contributions will be invested. See § 1.401(k)-3(k).

Requirements for providing safe harbor notices on a timely basis are set out in § 1.401(k)-3(d). A safe harbor notice generally must be provided within a reasonable period before the beginning of the plan year. Whether this timing requirement is met is based on all of the relevant facts and circumstances, but the timing requirement is deemed to be satisfied if a safe harbor notice is provided at least 30 days (and not more than 90 days) before the beginning of the plan year. Special timing rules apply for employees who become eligible during the plan year. These requirements for delivery of safe harbor notices also apply under § 1.401(m)-3(e). Section 1.401(k)-3(k) provides additional notice timing rules for QACAs.

D. Election Period after Receipt of Notice

The safe harbor plan regulations provide that a safe harbor plan generally may limit the frequency and duration of periods in which eligible employees may make or change cash or deferred elections under the plan, but require that an employee have a reasonable opportunity (including a reasonable period after receipt of a safe harbor notice) to make or change an election. For this purpose, a 30-day election period is deemed to be a reasonable period to make or change a cash or deferred election. See §§ 1.401(k)-3(c) and 1.401(m)-3(c).

III. GUIDANCE ON MID-YEAR CHANGES TO SAFE HARBOR PLANS AND NOTICES

A. Overview

Section III.B of this notice provides guidance on mid-year changes to a safe harbor plan or to a plan's required safe harbor notice content that do not violate the safe harbor plan rules in §§ 1.401(k)-3 and 1.401(m)-3. For purposes of this notice, a "mid-year change" is (i) a change that is first effective during a plan year, but not effective as of the beginning of the plan year, or (ii) a change that is effective as of the beginning of the plan year, but adopted after the beginning of the plan year. Also, for purposes of this notice, "required safe harbor notice content" refers to the information that is required by the safe harbor plan regulations to be provided in a plan's safe harbor notice.

Section III.C of this notice sets out special conditions that must be satisfied for a

mid-year change that alters the plan's required safe harbor notice content. Not every mid-year change to a safe harbor plan alters information required to be provided in a plan's safe harbor notice (for example, information about a plan's entry date is not required to be provided in a plan's safe harbor notice). Similarly, information required to be included in a plan's safe harbor notice can change mid-year even if no change is made to the safe harbor plan (for example, a change in contact information).

Section III.D of this notice lists prohibited mid-year changes, and section III.E of this notice provides examples illustrating certain aspects of the guidance provided under this notice.

B. Mid-Year Changes to Safe Harbor Plans and Notices

A change made to a safe harbor plan or to a plan's required safe harbor notice content does not violate the requirements of §§ 1.401(k)-3 and 1.401(m)-3 merely because the change is a mid-year change, provided that (i) if it is a mid-year change to a plan's required safe harbor notice content, the notice and election opportunity conditions in section III.C of this notice are satisfied, and (ii) the mid-year change is not described in the list of prohibited mid-year changes in section III.D of this notice.

The following mid-year changes are not subject to the provisions in the first paragraph of this section III.B, but instead would violate the requirements of §§ 1.401(k)-3 and 1.401(m)-3 unless the applicable regulatory conditions corresponding to each specified change are satisfied:

- (i) Adoption of a short plan year or any change to the plan year (permitted only as described in §§ 1.401(k)-3(e)(2), (3), and (4) and 1.401(m)-3(f)(2), (3), and (4));
- (ii) Adoption of safe harbor plan status on or after the beginning of the plan year (permitted only as described in §§ 1.401(k)-3(f) and 1.401(m)-3(g)); and
- (iii) Reduction or suspension of safe harbor contributions or changes from safe harbor plan status to non-safe harbor plan status (permitted only as described in §§ 1.401(k)-3(g) and 1.401(m)-3(h)).

Other applicable law also may affect the permissibility of mid-year changes, including, for example, § 411(d)(6) (anti-cutback restrictions), § 401(a)(4) (nondiscrimination restrictions), and § 1.401(k)-1(b)(3) (anti-abuse provisions).

C. Conditions for Mid-Year Changes to a Plan's Required Safe Harbor Notice Content

The notice and election opportunity conditions applicable to mid-year changes to a plan's required safe harbor notice content (for purposes of applying the provisions in the first paragraph of section III.B of this notice) are described in paragraphs 1 and 2 of this section III.C. This notice does not require any additional notice or election opportunities for changes to information that is not required safe harbor notice content, even if that information is provided in a plan's safe harbor notice. Also, this notice does not modify the rules governing information required to be included in a plan's safe harbor notice.

1. An updated safe harbor notice that describes the mid-year change and its effective date must be provided to each employee otherwise required to be provided a safe harbor notice under § 1.401(k)-3(d), 1.401(k)-3(k)(4), or 1.401(m)-3(e), as applicable, within a reasonable period before the effective date of the change. Whether this timing requirement is met is based on all of the relevant facts and circumstances, but this timing requirement is deemed to be satisfied if the updated safe harbor notice is provided at least 30 days (and not more than 90 days) before the effective date of the change. If it is not practicable for the updated safe harbor notice to be provided before the effective date of the change (for example, in the case of a mid-year change to increase matching contributions retroactively for the entire plan year, as described in section III.D.4 of this notice), the notice is treated as provided timely if it is provided as soon as practicable, but not later than 30 days after the date the change is adopted. For purposes of this section III.C, if the required information about the mid-year change and its effective date was provided with the pre-plan year annual safe harbor notice, an updated safe harbor notice is not required.

2. Each employee required to be provided an updated safe harbor notice under section III.C.1 of this notice must be given a reasonable opportunity (including a reasonable period after receipt of the updated notice) before the effective date of the mid-year change to change the employee's cash or deferred election (and/or any after-tax employee contribution election). For this purpose, a 30-day election period is deemed to be a reasonable period to make or change a cash or deferred election. If it is not practicable for the election opportunity to be provided before the effective date of the change (for example, in the case of a mid-year change to increase matching contributions retroactively for the entire plan year, as described in section III.D.4 of this notice), an employee is treated as having a reasonable opportunity to make or change an election if the election opportunity begins as soon as practicable after the date the updated notice is provided to the employee, but not later than 30 days after the date the change is adopted.

D. Prohibited Mid-Year Changes

The mid-year changes described in this section III.D are prohibited mid-year changes (for purposes of the provisions in the first paragraph of section III.B of this notice). However, a mid-year change described in section III.D.1-4 is not a prohibited mid-year change under this section III.D if it is required by applicable law to be made mid-year, such as a change mandated by a statutory law change or court decision.

1. A mid-year change to increase the number of completed years of service required for an employee to have a nonforfeitable right to the employee's account balance attributable to safe harbor contributions under a QACA pursuant to the safe harbor rules under § 1.401(k)-3(k)(3) or 1.401(m)-3(a)(2).

2. A mid-year change to reduce the number or otherwise narrow the group of employees eligible to receive safe harbor contributions. This prohibition does not apply to an otherwise permissible change under eligibility service crediting rules or entry date rules made with respect to employees who are not already eligible (as of the date the change is either made effective or is adopted) to receive safe harbor contributions under the plan.

3. A mid-year change to the type of safe harbor plan, for example, a change from a traditional § 401(k) safe harbor plan to a QACA § 401(k) safe harbor plan.

4. A mid-year change (i) to modify (or add) a formula used to determine matching contributions (or the definition of compensation used to determine matching contributions) if the change increases the amount of matching contributions, or (ii) to permit discretionary matching contributions. However, this prohibition does not apply if, at least 3 months prior to the end of the plan year, the change is adopted and the updated safe harbor notice and election opportunity are provided, and if the change is made retroactively effective for the entire plan year (which may require a plan that provides for periodic matching contributions as described in §§ 1.401(k)-3(c)(4) and (5)(ii) and/or 1.401(m)-3(d)(4) to be amended to provide for matching contributions based on the entire plan year).²

² As described in section III.B of this notice, adoption of safe harbor plan status on or after the beginning of the plan year is permitted only as described in §§ 1.401(k)-3(f) and 1.401(m)-3(g) and a mid-year change to reduce or suspend safe harbor contributions is permitted only as described in §§ 1.401(k)-3(g) and 1.401(m)-3(h).

E. Examples

Example 1: The employer sponsoring Plan M, a traditional § 401(k) safe harbor plan, makes a mid-year plan amendment to increase future safe harbor nonelective contributions from 3% to 4% for all eligible employees. Employees otherwise required to be provided a safe harbor notice are provided both an updated notice that describes the increased contribution percentage and an additional election opportunity in accordance with section III.C of this notice. The mid-year change does not violate the provisions of §§ 1.401(k)-3 and 1.401(m)-3.

Example 2: The employer sponsoring Plan N, a traditional § 401(k) safe harbor plan, makes a mid-year plan amendment to decrease safe harbor nonelective contributions from 4% to 3% for all eligible employees. If the reduction meets the requirements of § 1.401(k)-3(g), the plan is no longer a safe harbor plan and is required to satisfy ADP testing or other nondiscrimination standards. If the reduction does not meet the requirements of § 1.401(k)-3(g), the plan as amended does not satisfy § 401(k)(3).

Example 3: The employer sponsoring Plan O, a traditional § 401(k) and traditional matching safe harbor plan with a calendar year plan year and match calculated on a payroll-period basis, makes a mid-year amendment on August 31 to increase the safe harbor matching contribution from 4% to 5% retroactive to January 1 and to amend the plan to change from a payroll-period match calculation to an entire-plan-year match calculation. Due to the retroactive effective date of the change, it is not practicable for the plan to provide an updated safe harbor notice and additional election opportunity to employees prior to the January 1 effective date. On September 3, the first date that an updated notice and additional election opportunity can practicably be provided, employees otherwise required to be provided a safe harbor notice are provided an updated notice that describes the increased contribution percentage and an additional 30-day election period starting September 3 in accordance with section III.C of this notice. The mid-year change does not violate the provisions of §§ 1.401(k)-3 and 1.401(m)-3.

Example 4: The employer sponsoring Plan P, a safe harbor plan, makes a mid-year amendment to add an age 59 ½ in-service withdrawal feature. Employees otherwise required to be provided a safe harbor notice are provided both an updated notice that describes the withdrawal feature and an additional election opportunity in accordance with section III.C of this notice. The mid-year change does not violate the provisions of §§ 1.401(k)-3 and 1.401(m)-3.

Example 5: The employer sponsoring Plan Q, a QACA safe harbor plan with multiple investment options, makes a mid-year change in the plan's default investment fund from Fund X to Fund Y. Employees otherwise required to be provided a safe harbor notice are provided both an updated notice that describes Fund Y as the default investment fund and an additional election opportunity in accordance with section III.C

of this notice. The mid-year change does not violate the provisions of §§ 1.401(k)-3 and 1.401(m)-3.

Example 6: The employer sponsoring Plan R, a traditional § 401(k) safe harbor plan, makes a mid-year amendment to change the design to a QACA safe harbor plan. Section III.D.3 of this notice prohibits the change. The plan as amended does not satisfy § 401(k)(3). However, if the employer had made a mid-year amendment to add an automatic contribution feature (but not an amendment changing the design to a QACA safe harbor plan) and employees otherwise required to be provided a safe harbor notice had been provided both an updated notice that described the automatic contribution arrangement and an additional election opportunity in accordance with section III.C of this notice, then the mid-year change would not have violated the provisions of §§ 1.401(k)-3 and 1.401(m)-3.

Example 7: The employer sponsoring Plan S, a safe harbor plan, makes a mid-year amendment to change the entry date for commencement of participation of employees who meet the plan's minimum age and service eligibility requirements from monthly to quarterly. The amendment also changes plan rules regarding arbitration of disputes. The amendment is effective with respect to employees who are not already eligible to participate in the safe harbor plan. The safe harbor notice is not required to include the plan entry date or information on arbitration procedures; therefore, an updated notice and additional election opportunity are not required. The mid-year change does not violate the provisions of §§ 1.401(k)-3 and 1.401(m)-3.

IV. SECTION 403(b) PLANS

Section III of this notice applies on similar terms to § 403(b) plans that apply the § 401(m) safe harbor rules pursuant to § 403(b)(12).

V. COMMENTS

Comments are requested on additional guidance that may be needed with respect to mid-year changes to safe harbor plans. Specific comments are requested as to whether additional guidance is needed to address mid-year changes relating to plan sponsors involved in mergers and acquisitions or to plans that include an eligible automatic contribution arrangement under § 414(w).

Comments may be submitted in writing no later than April 28, 2016. Comments should be submitted to Internal Revenue Service, CC:PA:LPD:PR (Notice 2016-16, Room 5203, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044, or electronically to Notice.Comments@irs.counsel.treas.gov. Please include "Notice 2016-16" in the subject line of any electronic communications. Alternatively, comments may be hand delivered between the hours of 8:00 a.m. and 4:00 p.m. Monday to Friday to CC:PA:LPD:PR (Notice 2016-16), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue NW, Washington, D.C. All comments will be available for public inspection and copying.

VI. EFFECTIVE DATE

This notice is effective for mid-year changes made on and after Jan. 29, 2016.

VII. EFFECT ON OTHER DOCUMENTS

Announcement 2007-59 is revoked.

VIII. PAPERWORK REDUCTION ACT

The collection of information contained in this notice has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. § 3507) under control number 1545-2191.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid OMB control number.

The collection of information in this notice is in section III of this notice. The collection of information relates to the updated notice requirements in the case of a mid-year change. The collection of information is mandatory for those plan sponsors making these elections.

The likely recordkeepers are businesses and other for-profit institutions and nonprofit institutions. Currently, it is estimated that any effect on burden, as previously reported to OMB, will not be significant. Any potential changes on burden will be reported through the renewal of the current OMB approval number. Estimates of the annualized cost to respondents are not relevant, because each collection of information in this notice is a one-time collection.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by § 6103.

IX. DRAFTING INFORMATION

The principal author of this notice is Cynthia A. Van Bogaert of the Office of Associate Chief Counsel (Tax Exempt and Government Entities). For further information regarding this notice, contact Cynthia A. Van Bogaert at (202) 317-4102 (not a toll-free call).