

Executive Compensation, Employee Benefits and ERISA Alert

February 2, 2016

IRS Provides New Guidance on Midyear Changes to Safe Harbor 401(k) Plans

If you read one thing...

- The IRS has issued new guidance on midyear changes to a safe harbor plan under Code Sections 401(k) and 401(m) that addresses the requirement that plan provisions generally must remain in effect for an entire 12-month plan year.
- The guidance permits certain mid-year changes which, prior to this clarification, were widely assumed to be impermissible.
- The IRS notice makes clear that a midyear change either to a safe harbor plan or to a plan's safe harbor notice won't violate the safe harbor rules merely because it is a midyear change, as long as notice and election opportunity conditions are met and the change is not a prohibited midyear change that increases vesting requirements, restricts eligibility to receive safe harbor contributions, changes the type of safe harbor plan, or changes or adds matching contribution provisions.



On January 29, 2016, the Internal Revenue Service (IRS) issued [Notice 2016-16](#), which provides guidance on midyear changes to a safe harbor plan under Sections 401(k) and 401(m) of the Internal Revenue Code. The notice provides that a midyear 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 midyear change, as long as applicable notice and election opportunity conditions are satisfied and the midyear change is not a prohibited midyear change, as described in the notice. Notice 2016-16 is effective for midyear changes made on or after January 29, 2016.

Safe Harbor Plans

Contributions to a Section 401(k) plan must be nondiscriminatory in amount. A 401(k) plan meets this requirement either by satisfying annual tests for elective and matching contributions made on behalf of highly compensated employees or by being structured as a "safe harbor" plan. Safe harbor plans must satisfy the requirements set forth in IRS regulations regarding contributions and providing safe harbor notices, and the requirement that certain plan provisions generally must remain in effect for an entire 12-month plan year.

Midyear Changes to Safe Harbor Plans and Safe Harbor Notices

Due to the IRS's previously limited guidance, it has been widely assumed that no midyear amendments are permitted for safe harbor plans, unless expressly permitted by the safe harbor plan regulations or in generally applicable guidance published by the IRS, even if they do not change any plan provisions required for safe harbor plan status. However, Notice 2016-16 now makes clear that a midyear change to a safe harbor plan, or to the required safe harbor notice content, does not violate the safe harbor plan regulations merely because it is a midyear change, as long as it is not described in the notice's list of specifically prohibited midyear changes. The notice defines a "midyear change" as either (1) a change that is first effective during a plan year, but not as of the beginning of the plan year, or (2) a change that is effective as of the beginning of the plan year, but adopted after the beginning of the plan year.

The notice also sets out special notice and election opportunity conditions that must be satisfied for any midyear change to the safe harbor notice content. Specifically, an updated safe harbor notice describing the midyear change and its effective date must be provided to each employee otherwise required to receive a safe harbor notice within a reasonable period—generally at least 30 days, and not more than 90 days—before the change's effective date. If providing the updated safe harbor notice before a change's effective date is not practicable, then it must be provided no later than 30 days after the date the change is adopted. Each affected employee must then be given a reasonable opportunity and a 30-day election period to make or change the employee's elective deferral election.

Prohibited Midyear Changes

Notice 2016-16 identifies the following midyear changes as prohibited for a safe harbor plan, unless specifically required by applicable law to be made midyear:

- a midyear increase in the number of completed years of service required for an employee to have a nonforfeitable right to his or her account balance attributable to QACA safe harbor contributions
- a midyear reduction in number, or otherwise narrowing, of the group of employees eligible to receive safe harbor contributions
- a midyear change to the type of safe harbor plan, such as changing from a traditional 401(k) safe harbor plan to a QACA 401(k) safe harbor plan
- a midyear change to modify or add a matching contribution formula (including the definition of compensation used to determine matching contributions), if the change increased the amount of matching contributions, or to permit discretionary matching contributions.

However, the last type of change will not be prohibited if the change is adopted and the updated safe harbor notice and election opportunity are provided, at least three months before the end of the plan year, and the change is retroactively effective for the entire plan year.

In addition, certain midyear changes are not subject to the notice, but instead must satisfy applicable conditions under the safe harbor plan regulations. These include the adoption of a short plan year or any change to the plan year, adoption of safe harbor plan status on or after the beginning of the plan year,

and reduction or suspension of safe harbor contributions or changing from safe harbor to non-safe-harbor plan status.

Notice 2016-16 also requests comments on additional guidance that may be needed, in particular with respect to midyear changes to safe harbor plans where a plan sponsor is involved in a merger or acquisition. Comments must be submitted in writing no later than April 28, 2016.

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