

**IMPORTANT NOTICE TO SPONSORS OF 401(k) SAFE HARBOR PLANS
with a 3% Nonelective Provision**
From RPS Consulting Services

*My thanks to the **Employee Benefits Group at Sherman & Howard** for the following information.*

The CARES Act was signed into law by President Trump on Friday, March 27, 2020. The Act allows plan participants to withdraw up to \$100,000 from their retirement plan or IRA without incurring the usual 10% penalty. Please note that this withdrawal is still subject to ordinary income tax, but this tax can be spread out over three tax years. This withdrawal option is available to any participant (or for the participant's spouse or dependent) who has been diagnosed with COVID-19, or someone who experiences adverse financial consequences of being quarantined, furloughed, laid off, work hours reduced, or unable to work due to a lack of childcare, or the closing or reducing of hours of a business owned or operated by the individual due to COVID-19. This withdrawal amount can also be paid back, tax-free, into the plan or IRA over the next three years.

The CARES Act doubles the maximum participant loan amount from the lesser of \$100,000 (up from \$50,000) or 100% of the participant's vested account balance.

The Act waives the required minimum distributions for defined contribution plans such as 401(k) and 403(b) plans, (but not defined benefit or cash balance plans) and IRAs for 2020 and for any 2019 RMDs that have not yet been made.

Any ERISA-required minimum contributions to a single-employer defined benefit or cash balance plans due during 2020, including quarterly contributions, are delayed to January 1, 2021, but those amounts that are delayed will be increased for interest.

*Nathan Carlson
President*

The COVID-19 virus has suddenly placed our nation into uncharted territory and the wild financial market reflects this. A few of our clients have requested an explanation of the options available to 401(k) Safe Harbor plans.

I have a 401(k) Plan with a 3% Safe Harbor Nonelective contribution. Can I discontinue my Safe Harbor provisions mid-year? Yes, assuming that you claim that the reason for ceasing your Safe Harbor provisions is due to an



economic loss, you can discontinue your Safe Harbor provisions at any time during the plan year. However, you must provide at least a 30-day notice prior to the discontinuance of the Safe Harbor contributions and you must fund all Safe Harbor contributions that have accrued through the date of discontinuance. Also, your 401(k) Adoption Agreement must be amended by RPS to remove the Safe Harbor language. The process would be as follows:

- Notify your RPS Plan Analyst that you intend to discontinue the Safe Harbor Nonelective provision for your 2020 plan year effective _____.
- RPS will provide to you
 - The necessary plan amendment
 - A corporate resolution authorizing the change
 - The 30-day advanced employee notice

If I discontinue my Safe Harbor Nonelective provisions mid-year in 2020, can I reactivate these Safe Harbor provisions in 2020? Yes, you can reactivate these Safe Harbor provisions in 2020 or even later. If you make the decision to reactivate your 2020 Safe Harbor provisions no later than 11/30/2020, you will be required to make a 3% Safe Harbor contribution for the 2020 plan. Once again, RPS must amend your plan document to add back the Safe Harbor language.

The recently-passed SECURE-Act added new Safe Harbor flexibility. You now have until the due date of your 2020 corporate tax return, including extensions, to be a Safe Harbor plan for 2020 and make a Safe Harbor nonelective contribution. However, if you make this decision after 11/30/2020, the mandatory Safe Harbor contribution will be 4% of 2020 compensation rather than 3%. In other words, the “price” of delaying the decision until the due date of your corporate return is 1% of pay. If a decision is made in 2021 to add back the 2020 Safe Harbor provisions, RPS must amend your plan document.

Note: if you also maintain a Cash Balance plan in conjunction with your 401(k) Safe Harbor Nonelective plan, your employer Profit Sharing contribution will be at least 5% of compensation anyway, which includes any Safe Harbor Nonelective contribution.

If I discontinue my Safe Harbor Nonelective provisions in 2020, what happens to my 401(k) Plan? Your 401(k) plan will become subject to the normal ADP/ACP nondiscrimination tests for the 2020 plan year. This means that the amount that the Highly Compensated Employees (HCEs) can defer will



be limited by the average 401(k) deferral rate for the non-Highly Compensated Employees (NHCEs). An HCE is one who is either a more-than 5% owners or one who earned more than \$125,000 in 2019. (Most family members of more-than 5% owners are also HCEs).

For example, if in 2020 the average 401(k) deferral rate for all your eligible NHCEs is 3% of pay, the average 401(k) deferral rate for all your eligible HCEs must not exceed 5% of pay. If the HCE rate exceeds 5%, RPS will process taxable refunds to your HCEs after year-end.

Please note that the purpose of a 401(k) Safe Harbor provision is to prevent taxable refunds to HCEs.

A Word of Caution for Top-Heavy 401(k) Plans. A retirement plan is "Top Heavy" if as of the beginning of the plan year (or the last day of a plan's first year) more than 60% of the plan's assets reside in the accounts of Key Employees--generally, owners or officers of the business. Usually, a Top Heavy 401(k) plan (that has not elected 401(k) Safe Harbor status) must make an employer contribution equal to 3% of pay anyway to the non-key employees. Therefore, it makes sense for a 401(k) plan that is Top Heavy to make a Safe Harbor election (or remain a Safe Harbor plan) since, one way or another, an employer contribution will be required and the Safe Harbor election will also eliminate the pesky ADP/ACP nondiscrimination tests.

How do I know if my plan is Top Heavy? When RPS completed your 2018 administration work, we provided a testing report in which we told you if your retirement plan would be Top Heavy in 2019. Although we have not yet completed most of those calculations for 2020, if a plan was Top Heavy in 2019 it most likely is also Top Heavy in 2020. If in doubt, please ask your Plan Analyst.

(Please note that our fee for processing a plan amendment, employee notice, and corporate resolution is \$300.)

