

**MEMO# 11530**

January 7, 2000

## **IRS RELEASES 401(K) SAFE HARBOR GUIDANCE**

[11530] January 7, 2000 TO: PENSION MEMBERS No. 3-00 PENSION OPERATIONS ADVISORY COMMITTEE No. 2-00 RE: IRS RELEASES 401(K) SAFE HARBOR GUIDANCE

The Internal Revenue Service has released additional guidance on safe harbors for satisfying the nondiscrimination rules under Code sections 401(k) and 401(m) in Notice 2000-3. The guidance is provided in Q&A form. Notice 2000-3 modifies Notice 98-52. Notice 2000-3 modifies the current 401(k) safe harbor guidance as follows: (1) allows sponsors of existing 401(k) plans to wait as late as December 1 of a calendar year to decide to adopt the 401(k) safe harbor 3% employer nonelective contribution method for that calendar year; (2) permits 401(k) safe harbor plans to match elective or employee contributions on the basis of compensation for a payroll period, month or quarter; (3) provides an extended time (until May 1, 2000) for 401(k) plan sponsors adopting the safe harbor methods for the first time in 2000 to provide the required safe harbor notice to employees; (4) allows 401(k) safe harbor plans to require salary reduction elections to be made using whole percentages of pay or whole dollar amounts; (5) permits plans sponsors to provide the 401(k) safe harbor notice electronically and simplifies the notice requirement; (6) permits safe harbor plans to provide matching contributions on an employee's aggregate employee and elective contributions; (7) clarifies that 401(k) safe harbor plans are permitted to apply a suspension, similar to a 12-month suspension that may be applied to employee elective contributions after an in-service withdrawal, to employee after-tax contributions; (8) permits plan sponsors using the 401(k) safe harbor matching contribution method to exit the safe harbor prospectively during a plan year (and switch to ADP and ACP nondiscrimination testing) if employees are notified beforehand; (9) clarifies the interaction between the 401(k) safe harbors and the election to separately test otherwise excludable employees for purposes of the section 410(b) minimum coverage requirements; and (10) clarifies how 401(k) safe harbor rules apply in the case of a profit sharing plan to which a 401(k) feature is added for the first time during a plan year. In Notice 2000-3, the Service notes that because of the amendments made to sections 401(k), 401(m) and 414(q) by the Small Business Job Protection Act of 1996 and other legislation, certain portions of sections 1.401(k)-1, 1.401(m)-1, 1.401(m)-2, and 1.414(q)-1T of the regulations no longer reflect current law. However, these regulations will continue to apply to the extent that they are not inconsistent with the Code, Notices 97-2, 97-45, 98-1, 98-52, this notice and any subsequent guidance. In addition to requesting comments on the safe harbor provisions, the Service requests comments on the following issues: (1) potential approaches for simplifying the limitation on the multiple use test; and (2) potential approaches for applying section 414(q)'s highly compensated employee definition and the section 401(k) and section 401(m) nondiscrimination requirements in mergers and acquisitions. According to

Notice 2000-3, further guidance in these areas will take the form of proposed regulations. Comments are due by March 24, 2000. A copy of Notice 2000-3 is attached. Kathryn A. Ricard Associate Counsel Attachment Note: Not all recipients receive the attachment. To obtain a copy of the attachment referred to in this Memo, please call the ICI Library at (202) 326-8304, and ask for attachment number 11530. ICI Members may retrieve this Memo and its attachment from ICINet (<http://members.ici.org>).

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