Are We Required to Make Safe Harbor Contributions for HCEs?

Facts

My company sponsors a safe harbor 401(k) plan so that all of the highly compensated employees can maximize their deferrals without worrying about failing the ADP test each year. Although we fully intend to make the same level of contribution for the HCEs that we do for the non-HCEs, we would prefer to not to be required to do so in order to maintain flexibility with our cash flow.

Question

Is there a way to structure the plan so that the company contribution for the HCEs is optional while still maintaining the safe harbor status?

Answer

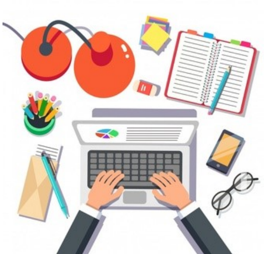
There are several caveats to keep in mind, however:

- Your plan document must contain language that specifically excludes HCEs from the safe harbor contribution. If that exclusion does not exist, then you must amend the plan in order to implement the change.
- There are special limits on how and when you can amend a safe harbor plan. This particular change is one that can only be implemented on the first day of a subsequent plan year.
- You must fund the safe harbor contribution for HCEs until you do amend your plan to implement the change.
- In order to preserve the company's ability to make a contribution on behalf of the HCEs, confirm the plan document provides for a discretionary contribution (match or nonelective, depending on which safe harbor the plan uses). In addition, it is important to confirm that any such discretionary contribution can be made for some employees without requiring it for all employees. Otherwise, you could find yourself having to make both the safe harbor contribution and the discretionary contribution for the non-HCEs.
- Any discretionary contributions made on behalf of HCEs should use the same or a lesser formula than what is used to calculate the contributions for the non-HCEs. If not, the plan could lose its safe harbor status and be subject to nondiscrimination testing.
- Another advantage of a safe harbor 401(k) plan is that as long as the only contributions made are deferrals and safe harbor contributions, the plan also gets a free pass on the top-heavy determination. If the company makes a discretionary contribution for the HCEs (as described above), it is possible it could cause the plan to lose its top-heavy exemption. As such, we highly recommend that you work with someone who understands the details of compliance testing (someone like your friends here at DWC) before making any of those contributions.

Safe harbor 401(k) plans can be a great way to allow HCEs to max out their deferrals without worrying about failed tests and refunds; however, there are other designs that can offer similar benefits. If it has been a while since you reviewed other design options, now might be a good time to revisit it. Regular plan design reviews can either help ensure that your plan adapts as your company evolves or confirm that your current design continues to be the ideal option for you.

Related Resources

- DWC Knowledge Center: Retirement Plan Design Resources



Want to get articles just like this one delivered to your inbox weekly?

Subscribe to receive regular updates from the DWC 401(k) Q&A blog.

Helpful insights without the junk, delivered on your schedule.