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Limitations On Mid-Plan Year Amendments To Safe Harbor 401(k) Plans

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Limitations On Mid-Year Amendments To Safe Harbor 401(k) Plans

Like it or not, the IRS takes a very restrictive position on the acceptability of mid-plan year amendments to “safe harbor” 401(k) plans. This restrictive position is likely intended to prevent plan sponsors of safe harbor 401(k) plans from implementing otherwise permissible mid-plan year changes to the plan provisions communicated to a participant within the mandatory annual notice required of a safe harbor 401(k) plan. Presumably, the IRS is concerned that such a change could allow plan sponsors to unfavorably revise plan provisions which may have been the basis for the deferral elections made by its participants. Originally, the legal basis for the IRS position on this issue was based exclusively on its interpretation of the application of the annual participant notice and 12 month plan year requirements set forth under the Treasury regulations with respect to safe harbor 401(k) plans. However, as time has gone on, the IRS has supplemented its arguably overzealous interpretation of those original regulations with additional guidance to further define and establish its position.

As a result of this IRS position, there are currently very few amendments that can confidently be made to a safe harbor 401(k) without potentially running afoul of this restrictive IRS position. The remainder of this article briefly discusses the limited, formally documented exceptions to the general “do not amend” rule otherwise espoused by the IRS. In the past, many practitioners took a more liberal view of what was permitted under this rule. However, with the issuance of more and more guidance on this issue by the IRS, such a liberal view becomes much more difficult, if not impossible, to justify and rely upon.

Reduce or Eliminate Safe Harbor Feature

If certain timing, notification and/or economic conditions are satisfied, the Treasury regulations clearly indicate that it is permissible to amend a safe harbor 401(k) plan mid-plan year in order to reduce, suspend or terminate the plan sponsor’s obligation to continue to offer a safe harbor 401(k) feature within its plan. However, it is important to note here that such a mid-plan year change to a safe harbor 401(k) plan carries what can be significant economic consequences. In addition to having to fund the safe harbor 401(k) contribution obligation through the prospective date of its suspension or



elimination, the non-discrimination testing that a safe harbor 401(k) plan is designed to avoid must be applied and satisfied for the entire plan year.

Hardship Withdrawals

In 2007, the IRS issued an announcement confirming that a safe harbor 401(k) plan with a hardship withdrawal feature could be amended mid-plan year in order to allow hardship distributions on account of medical expenses, college expenses and the funeral expenses for a plan beneficiary.

Roth Features

The IRS has clearly indicated that it is permissible to amend a safe harbor 401(k) plan mid-plan year in order to implement a Roth 401(k) deferral feature. In addition, in 2010, the IRS issued a notice that allowed adding “in-plan Roth rollovers” mid-plan year. However, any such amendment needed to be adopted no later than December 31, 2011. Thus, this exception is of limited utility. Finally, in 2013, the IRS issued a notice that allowed adding “in-plan Roth transfers” mid-plan year. However, this amendment would need to be adopted no later than December 31, 2014. Thus, this exception also is of extremely limited utility.

DOMA Conforming Amendments

In 2014, the IRS confirmed as permissible a mid-plan year amendment to a safe harbor 401(k) plan that was intended to revise the definition of spouse in conformance with the recent DOMA “same sex” ruling.

The aforementioned guidance was all published in Treasury regulations, IRS Notices and IRS Announcements. Therefore, all are very reliable and should be able to be followed without risk. However, the IRS has also issued additional verbal guidance on this issue at speaking engagements. If you have ever attended such a presentation then you may remember the disclaimer provided by IRS employees before engaging in such a discussion which essentially states that the comments made by the speaker are his or her own, are not attributable to the IRS and cannot be relied upon. With that caveat, please read on.



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Additional Verbal Guidance

At the 2012 ASPPA national conference, the IRS indicated that the following mid-plan year amendments to a safe harbor 401(k) plan would be permissible:

1. a change to the plan year as long as the plan remained safe harbor for both the current and subsequent plan years;
2. a change which expands the coverage of the plan in order to include previously excluded employees;
3. a change in an investment provider;
4. a change to a trustee; and
5. a retroactive change performed under the auspices of “Employee Plans Compliance Resolution System” (“EPCRS”) in order to resolve certain limited operational defects.

As the above discussion illustrates, there are very few circumstances in relation to which the IRS has provided reliable guidance that it is acceptable to perform a mid-year amendment to a safe harbor 401(k) plan. To be clear, the restrictions discussed above do not preclude a plan sponsor from implementing a plan design change prospectively in relation to a plan year that has not yet begun. Therefore, in order to avoid violating the restrictions considered herein, it becomes incumbent upon a plan sponsor of a plan with a safe harbor 401(k) feature to plan ahead, sometimes by almost a full plan year, when considering the implementation of plan design changes.

As much as we hope this article helped you to better understand this topic, it is not to be construed as financial, tax or legal advice. Therefore, if you believe that it may apply to your (or your client’s) company, be sure to further discuss it with a qualified accountant or tax professional. For more information about this topic, please contact our marketing department at 484-483-1044 or your administrator at Legacy.



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