What is a Safe Harbor 401(k) Plan?

Under the Safe Harbor Plan Design, plan sponsors can escape the 401(k) and 401(m) discrimination tests. This allows the Highly Compensated employees to defer the maximum amount allowed by law ($23,500 for calendar year 2025, $31,000 for individuals age 50 or older) without receiving a refund of their 401(k) deferrals due to a 401(k) or 401(m) discrimination test failure. Employer contributions must follow the same distribution restrictions that are applied to salary deferral contributions. New plans may be established at any time before October 1st, for a calendar year plan. An existing traditional 401(k) plan may be converted to a Safe Harbor 401(k) Plan as of the first day of the plan year, or later if specific requirements are met.

The Design Based Safe Harbor Contribution can be made by one of three methods:

> **Safe Harbor Matching Approach:** The employer matches employee contributions based on either the Basic Formula - 100% up to 3% of compensation deferred, plus 50% of the next 2% of compensation deferred, with no match on amounts deferred over 5% of compensation, or an Enhanced Formula – 100% match on at least 4% of salary deferred, not more than 6% of salary deferred. This contribution must be immediately vested. Employees must be given a Safe Harbor Notice for this type of plan design at least 30 days prior to the beginning of the Plan Year. The notice must inform each eligible employee of their rights under the plan and must state the specific matching formula used. Because of this notice requirement, the Safe Harbor Matching approach can only be added to an existing plan at the beginning of the year.

> **Qualified Automatic Contribution Arrangement (QACA) Approach:** As an alternative to the Safe Harbor Matching Approach described above, a plan may also satisfy the 401(k) & 401(m) discrimination tests if it automatically enrolls participants at a specific level, automatically increases them annually and provides a specific matching formula. Unlike the Basic Safe Harbor Match, the QACA match is 100% up to 1% of compensation, plus 50% of the next 5% of compensation deferred, with no match on amounts deferred over 6% of compensation. Although the maximum contribution percentage is lower, the overall employer contribution may be higher due to the automatic enrollment feature. It is also imperative that the plan follow the rules of the automatic escalation requirement with an annual notice. Additionally, unlike the contributions described above, the QACA match contribution may be vested after two years of service with the sponsor. Leaving prior to completing two years of service would forfeit any match received. Like the Safe Harbor Matching Approach, the employees must receive a notice at least 30 days prior to the beginning of the Plan Year, and this can only be added to an existing plan at the beginning of the year.

> **Non-elective Contribution Approach:** The employer makes a fully vested employer contribution equal to 3% of compensation for all employees who are eligible to participate in the plan or (at least all non-highly compensated employees eligible to participate in the plan). This contribution must be made without regard to whether the employee makes salary deferral contributions or is still employed at the end of the year. This approach may be added to the plan at any time. If added after the 11th month of the Plan Year, and up until the due date of the return, the amount of contribution increases from 3% to 4% of pay for all eligible employees. So, a plan may decide after the discrimination testing is complete to make a 4% contribution for all employees and satisfy the non-discrimination testing requirements and forego any corrective distributions to the Highly Compensated Employees.

Under any contribution approach, the design eliminates 401(k) & 401(m) discrimination testing, and may satisfy the top-heavy minimum contribution requirement. The plan cannot require that employees be employed on the last day of the plan year or that they complete a specific number of hours of service during the plan year to receive the Safe Harbor contribution.