

IRS Guidance on Mid-Year Changes to Safe Harbor Plans

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The IRS recently clarified what mid-year changes administrators can make to safe harbor plans (including Code Section 403[b] plans) in Notice 2016-16. Prior to the notice, employers could only make prescribed mid-year changes to safe harbor plans without risking the plan's safe harbor status. The notice provides that a mid-year change either to a safe harbor plan or to a plan's safe harbor notice does not violate the safe harbor rules merely because it is a mid-year change, provided the applicable notice and election opportunity conditions are satisfied and the mid-year change is not a prohibited mid-year change (as described below). This notice is effective for mid-year changes made on and after Jan. 29, 2016.

Prohibited Mid-Year Changes

- A mid-year change to increase the number of completed years of service required for an employee to have a nonforfeitable right to the employee's account balance attributable to safe harbor contributions under a QACA;
- A mid-year change to reduce the number or otherwise narrow the group of employees eligible to receive safe harbor contributions. However, changes to eligibility service crediting rules or entry date rules, made with respect to employees who are not already eligible, are permissible;
- A mid-year change to the type of safe harbor plan, e.g., adopting a QACA; or
- A mid-year change (i) to the matching contributions formula or definition or (ii) to permit discretionary matching contributions. However, this change can be made if, at least three months prior to the end of the plan year, the plan adopts such change, the plan provides updated safe harbor notice and election opportunity, and the change is retroactively effective for the entire plan year.

Additionally, other applicable law also may affect the permissibility of mid-year changes, including, for example, anti-cutback restrictions, nondiscrimination restrictions, changes to plan years, adopting a safe harbor plan after the beginning of the year, reduction and suspension of safe harbor contributions, and anti-abuse provisions.

In order to make a mid-year change, the plan must follow these notice and elections periods:

- **Notice** – The plan must provide an updated safe harbor notice that describes the mid-year change and its effective date to each employee otherwise required to be provided a safe harbor notice. Note that the safe harbor notice period is between 30 and 90 days prior to the effective date of the change, except for retroactive changes, with respect to which there is a 30-day safe harbor notice period that begins when the change is adopted.
- **Election** – Each employee required to be provided an updated safe harbor notice must be given a reasonable opportunity before the effective date of the mid-year change to change the employee’s cash or deferred election (and/or any after-tax employee contribution election). For this purpose, a 30-day election period is deemed to be a reasonable period to make an election change, unless it is not practicable for the election opportunity to occur before the effective date of the change (e.g., retroactive mid-year changes). In this case, the election period must last for at least 30 days after the date the change is adopted.

Our View: Notice 2016-16 provides much-needed flexibility to employers that maintain or are contemplating maintaining safe harbor plans because the notice significantly increases a safe harbor plan’s ability to make mid-year changes.

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