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Internal Revenue Service
CC:PA:LPD:PR (REG-11569-09)
Room 5203
P.O. Box 7604
Ben Franklin Station
Washington DC 20044

Re: Suspension or Reduction of Safe Harbor Nonelective Contributions
(REG-115699-09)

The American Society of Pension Professionals & Actuaries (ASPPA) is writing to comment on amendments proposed to the IRC §§ 401(k) and 401(m) regulations. The proposed changes relate to plans that utilize the safe harbor provisions of IRC §§ 401(k)(12) and 401(m)(13) and elect to suspend or reduce safe harbor nonelective contributions in the middle of a plan year.

ASPPA is a national organization of more than 6500 retirement plan professionals who provide consulting and administrative services for qualified retirement plans covering millions of American workers. ASPPA members are retirement professionals of all disciplines, including consultants, investment professionals, administrators, actuaries, accountants and attorneys. Our large and broad-based membership gives ASPPA unique insight into current practical applications of ERISA and qualified retirement plans, with a particular focus on the issues faced by small- to medium-sized employers. ASPPA's membership is diverse but united by a common dedication to the employer-sponsored retirement plan system.

ASPPA appreciates the response to our February 20, 2009 letter in which we outlined the potential problem faced by employers sponsoring safe harbor 401(k) plans. The relief provided in the proposed amendments will allow many plans to be maintained that would have otherwise been terminated. As a result, employees will continue to have access to the preferred savings vehicle of a qualified plan.

Summary of Recommendations

The following is a summary of ASPPA's recommendations. They are described in greater detail in the Discussion of Issues section which follows.

- 1) The proposed amendments permit the suspension or reduction of safe harbor nonelective contributions only if the employer has incurred a substantial business hardship. ASPPA recommends that the proposal be modified to eliminate the business hardship requirement and by doing so, provide a standard that is consistent with the regulations applicable to the suspension or reduction of matching safe harbor contributions.
- 2) ASPPA recommends that additional content not be mandated for the annual safe harbor notice. The potential for suspension or reduction in safe harbor contributions is beyond the scope of the notice and the informational needs of participants.
- 3) The preamble to the proposed regulations provides, without qualification, that in the year that safe harbor contributions are reduced or suspended, the IRC §401(a)(17) compensation limit must be prorated. ASPPA recommends that formal guidance be issued to clarify application of the IRC §401(a)(17) limit in this context. In addition, the guidance should indicate that proration will not be required in all circumstances where safe harbor contributions are suspended or reduced.

Discussion of Issues

1. Substantial Business Hardship Requirement

The proposed amendments provide, in Reg. §§ 1.401(k)-3(g)(1)(ii)(A) and 1.401(m)-3(h)(1)(ii)(A), that the suspension or reduction of nonelective safe harbor contributions is permitted only if “[T]he employer incurs a substantial business hardship (comparable to a substantial business hardship described in section §412(c)).” This provision is inconsistent with, and more restrictive than, the current regulatory requirements that apply to the suspension or reduction of safe harbor matching contributions. ASPPA believes a better approach would be to have the same standards apply, without regard to the type of safe harbor contribution provided under the plan.

In our letter of February 20, 2009, we commented that many employers were facing difficult times and economic uncertainty. The primary benefit of the proposed amendments is to allow an employer, that would otherwise be forced to terminate its nonelective safe harbor contribution plan, to continue the plan, at least for the purpose of allowing employee elective deferrals. An employer may well be experiencing declining revenues or other business challenges that do not meet the definition of substantial business hardship under IRC §412(c). If the plan provided for matching safe harbor contributions, the employer could take whatever actions are appropriate and necessary to protect the business (and save jobs) without having to terminate the plan. We believe there is no policy justification for imposing a stricter standard on plans that utilize nonelective safe harbor contributions.

Additionally it should be noted that under current regulations, an employer that terminates a safe harbor plan mid-year due to a substantial business hardship is permitted to retain safe harbor status through the date of termination. An employer who is willing to simply suspend nonelective safe harbor contributions while still maintaining the plan,

perform ADP and ACP testing for the plan year and potentially fund top-heavy minimums should not be held to the same strict standard. Otherwise, employers will be incentivized to establish that a substantial business hardship exists and then terminate the plan.

It has been suggested that the “contingent notice” approach described in Reg. § 1.401(k)-3(f), which only applies to nonelective safe harbor plans, provides a basis for imposing additional requirements when nonelective safe harbor contributions are suspended or reduced. ASPPA strongly supports the contingent notice option for nonelective safe harbor contribution plans. However, the decision to follow that approach needs to be made, for a calendar year plan, in the fall before the plan year begins. Many times employers do not anticipate the challenges they will face, up to a year after the deadline for giving the contingent notice. An employer sponsoring a nonelective safe harbor contribution plan should not be subjected to a stricter standard than the sponsor of a matching safe harbor contribution plan simply because the contingent notice approach was available.

It is understandable why the contingent notice approach is not available to matching safe harbor contribution plans. Employees might not defer if there is just a possibility that their deferrals would be matched. An employer could then decide late in the year to make the matching contribution safe harbor, and it would be too late for employees to defer sufficient amounts to receive the full matching contribution. To stem this potential for abuse, the contingent notice approach is not available to plans that use safe harbor matching contributions. However, there is no similar policy justification that would require different standards when it comes to suspension or reduction of safe harbor contributions, regardless of whether they are matching or nonelective. The prospective elimination or reduction of a safe harbor contribution would not affect a participant's earlier decision to defer.

ASPPA strongly believes that sound retirement policy should encourage the sponsorship of qualified retirement plans. Studies have shown that employees are much more likely to save for their retirement if there is an employer sponsored plan where they work. The proposed amendments should support that policy rather than force employers to terminate their plans when in doubt as to whether they have incurred a substantial business hardship.

ASPPA recommends that the final Regulations eliminate the condition that a safe harbor nonelective contribution can only be eliminated due to a substantial business hardship. This will provide consistency in the suspension and reduction provisions and will prevent the unnecessary termination of safe harbor plans and insure that employees have available a workplace retirement savings vehicle to which elective contributions can be made.

2. Additional Content in Safe Harbor Notices

The preamble to the proposal indicates that the IRS and Treasury are considering adding to the minimum content requirements for the required safe harbor notice (other than the contingent notice described in Reg. §1.401(k)-3(f)). Specifically, comments were requested on whether safe harbor notices should describe the possibility of reduced or suspended safe harbor contributions in light of the proposed amendments to the regulations.

ASPPA believes that it is unnecessary and beyond the scope of the safe harbor notice to include content describing the potential for reduced or suspended contributions. The inclusion of such a provision will not affect participants' decisions to defer. Safe harbor contributions may only be eliminated prospectively, 30 days advance notice is required, and participants must be afforded the opportunity to change existing deferral elections. ASPPA commented, as part of the IRC §401(k) and 401(m) regulatory process, that safe harbor notices are already too lengthy. Adding a description of this contingency to every safe harbor notice will only further lengthen and unnecessarily complicate what is already provided to participants. This information, coupled with notices about automatic enrollment and qualified default investment alternatives, further increases the potential for employees to simply “tune out” the notice entirely and miss important information.

Although ASPPA believes that any changes to the content requirements for safe harbor notices are unnecessary, if such a change is made, sufficient time must be provided before it will become effective. The preamble to the proposal indicates that such a change would not be effective before plan years beginning on or after January 1, 2010.

The timing requirement for the annual safe harbor notice is deemed satisfied if it is given at least 30 days and no more than 90 days before the beginning of the plan year. For calendar year plans, this means the notice can be given as early as October 3, 2009 for the 2010 year. Even if the guidance in this area was finalized before that date, many plan sponsors will not have sufficient time to update their procedures and forms to accommodate this change in time for the 2010 plan year. For this reason, any change should be made effective no earlier than the 2011 plan year (or if later, plan years beginning on or after the January 1st which is at least six months after the regulations are published in final form).

ASPPA recommends that no additional content requirements be added to safe harbor notices. *ASPPA also recommends* that if any changes are made to the content requirements for safe harbor notices, that the change be made effective no earlier than the 2011 plan year (or if later, plan years beginning on or after the January 1st which is at least six months after the regulations are published in final form).

3. Proration of Compensation Limit

The preamble to the proposal states “[A] plan that is amended during the plan year, to reduce or suspend safe harbor contributions (whether nonelective contributions or matching contributions) must prorate the otherwise applicable compensation limit under section 401(a)(17) in accordance with the requirements of Reg. §1.401(a)(17)-

1(b)(3)(iii)(A).” The cited regulation generally provides that “[I]f compensation for a period of less than 12 months is used for a plan year, then the otherwise applicable limit is reduced in the same proportion as the reduction in the 12-month period.” ASPPA believes that under some circumstances, the cited regulation would be applicable. However, ASPPA also believes that this provision does not apply in every case, for the reasons discussed below.

Safe Harbor Matching Contribution Amendments: ASPPA believes that the proration rules do not apply to amendments suspending or reducing safe harbor matching contributions that are determined on a payroll basis. Reg. §1.401(k)-3(c)(5)(ii) permits a safe harbor matching contribution to be made on a payroll basis and Reg. §1.401(a)(17)-1(b)(3)(iii)(B) provides:

“[N]otwithstanding paragraph (b)(3)(iii)(A) of this section, no proration is required merely because the amount of...matching contributions...that [are] contributed for each pay period during a plan year is determined separately using compensation for the pay period.”

This exception to the proration requirement appears applicable to safe harbor matching contributions that are made on a payroll basis, yet the preamble to the proposed regulation makes no mention of it. Plan sponsors and administrators have been routinely following this interpretation for many years and are now confused by the unqualified statement quoted from the preamble. If it is the intention of the IRS and Treasury to make a change in this regard (or if their interpretation is different than what appears to be widely practiced), ASPPA believes that more formal guidance and clarification is needed. Clarification is also needed regarding application of these rules to non-payroll based matching formulas.

Safe Harbor Nonelective Contribution Amendments: ASPPA believes that it is not clear in all cases how the proration rules would apply to the suspension or reduction of safe harbor nonelective contributions and that additional guidance is needed. Some areas needing clarification include:

Top-Heavy Plans: As pointed out in the preamble, plans which are amended to suspend or reduce safe harbor contributions will not be described in IRC §416(g)(4)(H) and will therefore be subject to the top-heavy rules for the plan year. If these plans are top-heavy, then non-key employees are entitled to top-heavy minimum contributions that are based on their compensation for the entire year. In this circumstance, ASPPA believes the proration rules do not apply because compensation for the entire year is considered as part of the allocation formula.

Non Top-Heavy Plans: ASPPA believes application of the proration rules is less clear in plans not subject to the top-heavy requirements. Reg. §1.401(a)(17)-1(b)(3)(iii)(B) provides that proration is not required merely because allocations

are based on compensation for the portion of the plan year during which the employee is a participant in the plan. It is not clear from the face of the regulation whether this exception to proration would apply when safe harbor nonelective contributions are suspended for the remainder of the year. ASPPA believes that guidance in this area is needed and that it should be prospective in application. Plan sponsors and administrators should be accorded a good faith compliance standard for actions taken before guidance is issued.

ASPPA recommends that the preamble to the final regulation clarify that whether the proration rules apply will depend on the plan’s design and the type of safe harbor contribution affected. **ASPPA also recommends** that the IRS and Treasury issue more formal guidance on application of the IRC §401(a)(17) in this context.

ASPPA appreciates the opportunity to comment on the proposal. We respectfully request that a public hearing be held at which we can present oral comments. A request to speak at the hearing and an outline of the topics we would like to discuss is included with these comments as a separate attachment. Thank you for your time and attention to this matter.



These comments were prepared by ASPPA’s §401(k) plans Subcommittee of the Government Affairs Committee, and primarily authored by Robert M. Kaplan, CFP, CPC, QPA, APA, and Chair. Please contact us if you have any comments or questions regarding the matters discussed above. Thank you for your consideration of these comments.

Sincerely,

/s/
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