SAFE HARBOR BASICS

Your Guide to a Safe Harbor 401(k) Plan

What is a safe harbor plan?

The IRS has established required compliance ("nondiscrimination") tests to verify all employees have fair representation in a plan—that highly compensated employees (HCEs) aren't favored over non-highly compensated employees (NHCEs). As such, a safe harbor plan allows you to automatically pass these tests if you meet specific contribution, vesting, and notification rules.

What are these nondiscrimination tests?

There are generally three main types of nondiscrimination tests:

- Actual deferral percentage (ADP) test – compares the deferral percentage of HCEs and NHCEs. (Generally, the HCE deferral amount cannot be more than two percentage points higher than the NHCEs' average.)
- Actual contribution percentage (ACP) test – compares employer matching contributions between the HCEs and NHCEs.
- Top-heavy test – determines if the account balances of key employees is greater than 60% of the total assets of the plan.

How does a safe harbor plan benefit me?

In addition to passing all three of the nondiscrimination tests listed above, safe harbor plans:

- Eliminate many of the restrictions to the amount owners and HCEs can contribute to their 401(k) plans.
- Potentially reduce business taxes and increase employer savings.
- Any HCE (subject to certain limitations), may contribute the full 401(k) plan annual dollar amount ($23,500 for calendar year 2025, without regard to the amount the other employees defer.

Who is considered an HCE?

HCEs are generally defined as individual(s) with more than 5% ownership, family members of a more than 5% owner (spouse, parents, children, or grandparents), or employees who earned more than $160,000* in the previous calendar year.

*2025 limit; subject to IRS cost-of-living adjustments

What do I need to do to satisfy safe harbor requirements?

To provide automatic compliance with ADP and ACP tests, the employer must provide a matching or nonelective contribution. Your safe harbor contributions must be 100% vested, and additional non-safe harbor contributions will have to meet nondiscrimination rules.

The following formulas are options to help meet these requirements:

Contribution Type	Formula Options		Calculation Description
Match	Basic	Enhanced 5%	Contribute a matching contribution percentage of each employee's compensation (as defined in the Adoption Agreement). An employee must contribute to receive an employer contribution. Safe harbor match contributions are immediately 100% vested.
	Enhanced 4%	Enhanced 6%	Examples: ▪ **Basic:** Contribute a match of 100% on the first 3% of employee's deferrals and 50% on the next 2% of deferrals. ▪ **Enhanced:** Contribute a match of 100% on 4%, 5%, or 6% of employees' deferrals.
Nonelective	Nonelective 3%	Nonelective 5%	Contribute a percentage of each eligible employee's compensation (as defined in the Adoption Agreement). An employee does not need to contribute to receive an employer contribution. Safe harbor nonelective contributions are immediately 100% vested.
	Nonelective 4%	Nonelective 6%	Example: ▪ Contribute a nonelective contribution of 3%, 4%, 5%, or 6% of compensation for all eligible employees.

What costs are associated with implementing a safe harbor contribution formula?

The cost of the safe harbor contribution depends on the level of plan participation. If few eligible employees make deferrals, a matching formula may be more cost-effective than the nonelective contribution. If you want to increase deferral rates, even at a higher cost, you may choose an enhanced match formula.

What will I be limited to as an owner if I don't have a safe harbor plan?

Generally, all HCEs will be limited to defer only about 2% more than the average of all eligible NHCEs. If the plan does not have any eligible NHCEs participating in the 401(k) plan, then none of the HCEs would be able to participate either.

NHCE Average	Calculation
Between 0%–2%	Multiply that number by two to determine the maximum average for the HCEs.
Between 2%–8%	Add two to that number to determine the maximum average for the HCEs.
Greater than 8%	Multiply that number by 1.25 to determine the maximum average for the HCEs.

Interested in adding a safe harbor provision to your plan? Contact your regional vice president or our team for additional safe harbor information, details on pricing, or a plan proposal.

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