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Guidelines for 401(k) Contribution Deposit Timing

Introduction

The timing for deposit of employee 401(k) payroll deductions continues to be on the Department of Labor's (DOL) agenda for tightening up the acceptable time frame for deposit into participants' accounts. On January 14, 2010, the DOL published final regulations on the safe harbor deadline for depositing 401(k) contributions.

Background

Previous guidance from the DOL stated that plan sponsors were required to deposit 401(k) payroll deductions into the plan as of the earliest date on which such contributions could reasonably be segregated from the employer's general assets, but no later than the 15th business day of the month following the month of the payroll deduction. Many plan sponsors ignored the "earliest date" aspect of the regulations and interpreted this guidance to mean that the employer had until the 15th day of the following month to make their 401(k) deposits. In contrast, DOL's enforcement efforts have been focused on the requirement that funds be deposited within a reasonable time period following **each pay date**. When 401(k) deposits are made late, they are deemed to be "interest-free loans to the employer," which are prohibited transactions and subject to excise tax liability. Additionally, the employer is required to make up for lost investment earnings to each of the affected participants. Pollard is recommending that lost earnings be calculated and deposited on all late deposits as a matter of standard procedure.

Safe Harbor Guidance

The safe harbor regulations are intended to provide small employers (defined as plans with fewer than 100 participants at the beginning of the plan year) with a clear time-frame to ensure compliance with the deposit standards. **Such plans will be considered to be compliant if 401(k) payroll deductions are deposited by the 7th business day following the date of withholding.** The DOL is considering similar safe harbor regulations for large plans and we are therefore advising all of our large plan clients to establish procedures to be in compliance with the "earliest date" guidelines, but in no case later than the small employer safe harbor regulations. A plan that fails to comply with the 7th business day rule will not automatically violate the regulations. However, the employer will have the burden of proof to demonstrate that deposits were made as soon as reasonably possible.

In summary, we are recommending that the best way to comply with the current regulation is to routinely submit all 401(k) employee withholdings to the plan's investment provider(s) within a fixed number of days of each pay date without exceeding the 7th business day deadline. In addition, if you are still remitting contributions to the plan by mail, the mailing time must be considered in meeting the 7-day deadline. You may want to consider changing your procedures to online submission with automatic debit to avoid this type of delay.