

TIMING OF 401(k) DEPOSITS

Client Advisories

04.20.2010

A new Safe Harbor rule provides that, if a Plan has under 100 participants at the beginning of the Plan Year, deposits of employee salary deferral contributions and loan repayments must be in the Plan no more than seven business days after those amounts have been withheld from an employee-participant's pay. The deposit period for Plans with 100 or more participants is shorter, unless the Plan Sponsor can prove that a longer period is reasonable.

The general standard is that amounts withheld from employee wages or amounts that a participant or beneficiary pays to an employer become "Plan Assets" on the earliest date on which the contributions can reasonably be segregated from the employer's general assets (the "Earliest Reasonable Date Standard" or simply the "Standard"). This Standard applies to contributions resulting from (i) payments delivered by a participant or beneficiary to an employer for deposit to a plan (such as payments on plan loans), or (ii) amounts withheld by an employer from a participant's wages pursuant to a 401(k) election.

The Department of Labor has finalized regulations creating a Safe Harbor for employer deposits to 401(k) Plans that have fewer than 100 participants as of the beginning of the applicable Plan Year. The new rule is in response to DOL findings that many employers were utilizing a provision specifying the maximum time period for depositing contributions ("not later than the 15th business day of the month following the month in which amounts were withheld or received from employees") in place of the Standard. The Standard is satisfied if the contributions are deposited with the plan no later than the seventh business day following the date on which the employee contribution is either received by the employer from the employee or is withheld by the employer from the participant's wages. The Safe Harbor is also applicable to SIMPLE IRAs, Salary Reduction SEPs, and welfare benefit plan contributions.

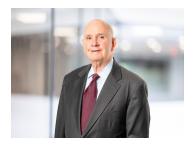
In an era of electronic banking, it may be that the earliest date on which such withheld contributions and payments can reasonably be segregated from an employer's general assets is the same day that payroll checks are direct deposited into employees' accounts. So, this regulation is a major benefit for small employers. They now have a Safe Harbor if the deposits are completed within 7 business days after the withholding date. The regulations also contain an example of an employer with a 600-participant plan that has several payroll centers and uses an outside payroll processing service. The example holds that deposits to the plan made no later than three business days after the issuance of paychecks would satisfy the general rule, assuming that the deposits are credited to a plan account on that third day. The example suggests that the earliest reasonable date for large plans will usually be less than seven business days, but not necessarily the same day.

It is clear from the final regulation that all employers must be making deposits to their 401(k) Plan at least as frequently as they withhold from payroll, unless they can document why that remittance frequency is not reasonable. If you have weekly payroll withholding, this means weekly transfers to the 401(k) Plan. If you withhold twice a month, then you should have deposits to the 401(k) Plan at least twice a month. Employers with weekly payrolls who qualify for the Safe Harbor may be able to limit their contributions to two or three a month, as long as all deposits satisfy the seven-business day Safe Harbor.

Why worry? The penalty for violating the deposit rule is that the employer must make up any investment losses experienced by the plan participants, with interest. In a steadily rising stock market, which we have had since March 2009, the amount of the penalty could be substantial. In addition to making the plan whole, a plan sponsor or fiduciary that makes late deposits could be subject to special reporting requirements and prohibited transaction penalties of 15% - 100% of the amount involved.

If you need further information on the latest updates to the contribution timing rules, please call Gerry Rigby (215-279-9684) or Nancy Wasch (215) 246-3106 in the Philadelphia Office.

Related People



L. Gerald Rigby Of Counsel ▼ grigby@archerlaw.com € 215.279.9684

© 2025 Archer & Greiner, P.C. All rights reserved.

