

## **The New Proposed 7-Day Safe Harbor Regulation and What It Means For Small Plan Sponsors**

The Department of Labor has issued new guidance proposing a safe harbor for the deposit of contributions to small plans. The general rule for the timing of deposits continues to apply to large plans.

### *The General Rule for Segregating Plan Assets*

Under Department of Labor regulations, sponsors of employee pension plans, and of welfare plans subject to trust requirements, must deposit plan funds into accounts separate from company assets. This so-called “general rule” provides that contributed funds, including elective deferrals under a 401(k) plan, must be deposited into a plan account “as of the earliest date on which such contributions can reasonably be segregated from the employer’s general assets.” Holding contributed funds longer than reasonable violates ERISA and the prohibited transaction provisions of the Internal Revenue Code.

What is considered “reasonable” timing under the general rule? The DOL sees as reasonable any timing actually demonstrated. For example, if an employer has been able to deposit deferrals within 3 days after payroll, *that* is what is reasonable for that employer. For such an employer, three days would be the general rule. For an employer who has demonstrated the ability to make deposits within 10 days of payroll, 10 days would be the general rule.

The regulations provide an outside date for deposits—for subject welfare plans, it’s 90 days; for pension plans, it’s the 15th day of the month following the effective date of contribution/deferral. The provision of the outside date for pension plans *may seem* to permit deposits just once a month even if paychecks are issued once a week. However, that is a misconception. *In fact, the regulations make no allowance for deposits to trust accounts to be made only once a month if paychecks are issued weekly.* Designated funds must be deposited to the trust as soon as possible in the normal course of business, which may be just a few days or even immediately, depending on the particular circumstances of the employer’s payroll system. The erroneous idea that the above outside dates are routinely acceptable has been a thorn in the DOL’s side for years, as it has been spending a lot of its enforcement resources policing lax deposit practices.

### *The Proposed Safe Harbor for Small Plans*

In order to reduce these costs and provide some much needed clarity, the DOL has issued a proposed final regulation, [Prop. Amendments to DOL Reg. Sec. 2510.3-102, 73 Fed. Reg. 11072 (Feb.29, 2008)] that adds a 7-day safe harbor rule to the existing general rule for small plans (plans with fewer than 100 participants at the beginning of the plan year). Under the safe harbor rule, contributions and designated deferrals to small plans will not be deemed to be plan assets for 7 business days from the date of contribution/deferral. That is, small-plan

employers who deposit designated funds within 7 business days of the effective contribution date will be deemed to have segregated the funds promptly under ERISA. Note that although the regulations are not yet final, the DOL has announced that it is already applying the safe harbor, so in practice it is in effect already.

*Department of Labor Requests for Comments from Small and Large Plans*

The period for comments on the proposed final provision expired on April 29, 2008 and the final regulation is pending. The DOL is also contemplating making the safe harbor provision applicable to larger plans (with one hundred participants or more).

*Application and Effects of the 7-Day Safe Harbor*

While the outside dates for deposits are different for welfare plans subject to trust requirements (90 days) and pension plans (15<sup>th</sup> day of month following), *the new safe harbor for small plans applies equally to pension and subject welfare plans*. Furthermore, the new proposed regulation will extend the safe harbor to loan repayments made to a plan *of any size* through employer withholding.

The safe harbor is expected to be advantageous to all concerned. In addition to saving the government money, employers and plan administrators using the safe harbor will gain a welcome certainty of compliance. There will also be a financial gain for pension plan participants whose employers shorten the period between deferral and deposit because their money will begin earning interest a few days earlier.

Officially, the safe harbor is voluntary; as proposed, it requires no action on the part of any plan sponsor, employer or participant. Nevertheless, plan sponsors should be aware that the existence of the safe harbor means that sponsors who continue to take longer than 7 business days to transfer subject funds may now have a greater presumption to overcome in justifying the longer time. It is therefore advisable for plan sponsors to review deposit practices to come within the 7-business-day safe harbor where possible. Where it is not possible, consistency in the timing of deposits and documentation of the process continue to be important for compliance with the general rule described above.

**For a copy of the proposed regulation, go to:**  
<http://edocket.access.gpo.gov/2008/pdf/E8-3596.pdf>.

For more information regarding the safe harbor, or any other DOL regulations, please contact us.

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