DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG–133300–07]

RIN–1545-BG80

Automatic Contribution Arrangements

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations under sections 401(k), 401(m), 402(c), 411(a), 414(w), and 4979(f) of the Internal Revenue Code relating to automatic contribution arrangements. These proposed regulations will affect administrators of, employers maintaining, participants in, and beneficiaries of eligible plans that include an automatic contribution arrangement under section 401(k)(13), 401(m)(12), or 414(w).

DATES: Written or electronic comments and requests for a public hearing must be received by February 6, 2008.

ADDRESSES: Send submissions to CC:PA:LPD:PR (REG–133300–07), room 5203, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (REG–133300–07), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC 20224 or sent electronically via the Federal erulemaking Portal at www.regulations.gov (IRS REG–133300–07).

FOR FURTHER INFORMATION CONTACT: Concerning the regulations, R. Lisa Mojiri-Azad, Dana Barry or William D. Gibbs at (202) 622–6060; concerning the submission of comments or to request a public hearing, *Richard.A.Hurst@irscounsel.treas.gov,* (202) 622–7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collection of information contained in this notice of proposed rulemaking has been submitted to the Office of Management and Budget for review in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)). Comments on the collection of information should be sent to the Office of Management and Budget, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503, with copies to the Internal Revenue Service, Attn: IRS Reports Clearance Officer, SE:W:CAR:MP:T:T:SP; Washington, DC 20224. Comments on the collection of information should be received by January 7, 2008. Comments are specifically requested concerning:

Whether the proposed collection of information is necessary for the proper performance of the functions of the Internal Revenue Service, including whether the information will have practical utility;

The accuracy of the estimated burden associated with the proposed collection of information;

How the quality, utility, and clarity of the information to be collected may be enhanced;

How the burden of complying with the proposed collections of information may be minimized, including through the application of automated collection techniques or other forms of information technology; and

Estimates of capital or start-up costs and costs of operation, maintenance, and purchase of service to provide information.

The collection of information in these proposed regulations is in §§ 1.401(k)–3 and 1.414(w)–1. The collection of information in § 1.401(k)–3 is required to comply with the statutory notice requirements of sections 401(k)(13) and 401(m)(12), and is expected to be included in the notices currently provided to employees that inform them of their rights and benefits under the plan. The collection of information under § 1.414(w)–1 is required to comply with the statutory notice requirements of section 414(w), and is expected to be included in the notices currently provided to employees that inform them of their rights and benefits under the plan. The likely recordkeepers are businesses or other for-profit institutions, nonprofit institutions, organizations, and state or local governments.

Estimated total average annual recordkeeping burden: 30,000 hours.

Estimated average annual burden hours per recordkeeper: 1 hour.

Estimated number of recordkeepers: 30,000.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid control number assigned by the Office of Management and Budget.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

Background

This document contains proposed amendments to regulations under sections 401(k), 401(m), 402(c), 411(a), and 4979 of the Internal Revenue Code (Code) and new proposed regulations under section 414(w) in order to reflect the provisions of section 902 of the Pension Protection Act of 2006, Public Law 109–280 (PPA '06). Section 902 of PPA '06 added sections 401(k)(13), 401(m)(12), and 414(w) to the Code to facilitate automatic contribution arrangements (sometimes referred to as automatic enrollment) in qualified cash or deferred arrangements under section 401(k), as well as in similar arrangements under sections 403(b) and 457(b). An automatic contribution arrangement is a cash or deferred arrangement that provides that, in the absence of an affirmative election by an eligible employee, a default election applies under which the employee is treated as having made an election to have a specified contribution made on his or her behalf under the plan. These regulations would also amend the comprehensive regulations under sections 401(k) and 401(m) (published in 2004) and regulations under section 4979 to reflect other changes made by section 902 of PPA '06.

Section 401(k)(1) provides that a profit-sharing, stock bonus, pre-ERISA money purchase or rural cooperative plan will not fail to qualify under section 401(a) merely because it contains a qualified cash or deferred arrangement. Section 1.401(k)–1(a)(2) defines a cash or deferred arrangement (CODA) as an arrangement under which an eligible employee may make a cash or deferred election with respect to contributions to, or accruals or other benefits under, a plan that is intended to satisfy the requirements of section 401(a). Section 1.401(k)–1(a)(3) defines a cash or deferred election as any direct or indirect election (or modification of an earlier election) by an employee to have the employer either: (1) Provide an amount to the employee in the form of cash (or some other taxable benefit) that is not currently available; or (2) contribute an amount to a trust, or provide an accrual or other benefit, under a plan deferring the receipt of compensation. For purposes of determining whether an election is a cash or deferred election, § 1.401(k)–1(a)(3) provides that it is irrelevant whether the default that applies in the absence of an affirmative election is cash (or some other taxable benefit) or a contribution, an accrual, or other

benefit under a plan deferring the receipt of compensation. Contributions that are made pursuant to a cash or deferred election under a qualified CODA are commonly referred to as elective contributions.

In order for a CODA to be a qualified CODA, it must satisfy a number of other requirements. First, pursuant to section 401(k)(2)(A), the amount that each eligible employee under the arrangement may defer as an elective contribution must be available to the employee in cash. Section 1.401(k)–1(e)(2) provides that, in order for a CODA to satisfy this requirement, the arrangement must provide each eligible employee with an effective opportunity to make (or change) a cash or deferred election at least once during each plan year.

Section 401(k)(2)(B) provides that a qualified CODA must provide that elective contributions may only be distributed after certain events, including hardship and severance from employment. Similar distribution restrictions apply under sections 403(b)(7) and 403(b)(11). Section 457(d)(1)(A) includes distribution restrictions for eligible governmental deferred compensation plans.

Section 401(k)(3)(A)(ii) applies a special nondiscrimination test to the elective contributions of highly compensated employees, within the meaning of section 414(q) (HCEs). Under this test, called the actual deferral percentage (ADP) test, the average percentage of compensation deferred for HCEs is compared annually to the average percentage of compensation deferred for nonhighly compensated employees (NHCEs) eligible under the plan, and if certain limits are exceeded by the HCEs, corrective action must be taken. Pursuant to section 401(k)(8), one method of correction is distribution to HCEs of excess contributions made on their behalf.

Section 401(m) provides a parallel test for matching contributions and employee after-tax contributions under a defined contribution plan, called the actual contribution percentage (ACP) test. Similarly, pursuant to section 401(m)(6), one method of correction of the ACP test is distribution to HCEs of excess aggregate contributions made on their behalf.

Sections 401(k)(12) and 401(m)(11) provide a design-based safe harbor under which a CODA and any associated matching contributions are treated as satisfying the ADP and ACP tests if the arrangement meets certain contribution and notice requirements. Sections 1.401(k)–3 and 1.401(m)–3 provide guidance on the requirements for this design-based safe harbor.

Sections 401(k)(13) and 401(m)(12), added by PPA '06 and effective for plan years beginning on or after January 1, 2008, provide an alternative design-based safe harbor for a CODA that provides for automatic contributions at a specified level of contributions and meets certain contribution, notice, and other requirements. A CODA that satisfies these requirements, referred to as a qualified automatic contribution arrangement (QACA), is treated as satisfying the ADP and ACP tests.

Section 414(w), added to the Code by section 902(d)(1) of PPA '06 and effective for plan years beginning on or after January 1, 2008, further facilitates automatic enrollment by providing limited relief from the distribution restrictions under sections 401(k)(2)(B), 403(b)(7), 403(b)(11), or 457(d)(1)(A) for an eligible automatic contribution arrangement (EACA).

Sections 414(w)(1) and 414(w)(2) provide that an applicable employer plan that contains an EACA is permitted to allow employees to elect to receive a distribution equal to the amount of elective contributions (and attributable earnings) made with respect to the employee beginning with the first payroll period to which the eligible automatic contribution arrangement applies to the employee and ending with the effective date of the election. The election must be made within 90 days after the date of the first elective contribution with respect to the employee under the arrangement. Sections 414(w)(1)(A) and 414(w)(1)(B) provide that the amount of the distribution is includible in gross income for the taxable year in which the distribution is made, but is not subject to the additional income tax under section 72(t).

Section 414(w)(3) defines an EACA as an arrangement under which: (1) A participant may elect to have the employer make payments as contributions under the plan on behalf of the participant, or to the participant directly in cash, (2) the participant is treated as having elected to have the employer make such contributions in an amount equal to a uniform percentage of compensation provided under the plan until the participant specifically elects not to have such contributions made (or specifically elects to have such contributions made at a different percentage), (3) in the absence of an investment election by the participant, such contributions are invested in accordance with regulations prescribed by the Secretary of Labor under section 404(c)(5) of the Employee Retirement Income Security Act of 1974 (ERISA), and (4) participants are provided a notice that satisfies the requirements of section 414(w)(4).

Section 414(w)(4) requires that, within a reasonable period before each plan year, each employee to whom the arrangement applies for such year receive written notice of the employee's rights and obligations under the arrangement which is sufficiently accurate and comprehensive to apprise the employee of such rights and obligations. Section 414(w)(4)(A)(ii) requires that the notice be written in a manner calculated to be understood by the average employee to whom the arrangement applies. Section 414(w)(4)(B) provides that the notice must explain: (1) The employee's rights under the arrangement to elect not to have elective contributions made on the employee's behalf or to elect to have contributions made at a different percentage; and (2) how contributions made under the automatic contribution arrangement will be invested in the absence of any investment decision by the employee. In addition, the employee must be given a reasonable period of time after receipt of the notice and before the first elective contribution is made to make an election with respect to contributions. In many respects, the notice under section 414(w)(4) is the same as the notice required under section 401(k)(13) for a qualified automatic contribution arrangement.

Section 414(w)(5) defines an applicable employer plan as an employee's trust described in section 401(a) that is exempt from tax under section 501(a), a plan described in section 403(b), or a section 457(b) eligible governmental plan.

Section 414(w)(6) provides that a withdrawal described in section 414(w)(1) is not to be taken into account for purposes of the ADP test.

Section 411(a)(3)(G), as amended by section 902(d)(2) of PPA '06, provides that a matching contribution shall not be treated as forfeitable merely because the matching contribution is forfeitable if it relates to a contribution that is withdrawn under an automatic contribution arrangement that satisfies the requirements of section 414(w).

Section 4979 provides an excise tax on excess contributions (within the meaning of section 401(k)(8)(B)) and excess aggregate contributions (within the meaning of section 401(m)(6)(B)) not distributed within 2½ months after the close of the plan year for which the contributions are made. Section 902 of PPA '06 amended section 4979 to lengthen this 2½ month correction period for excess contributions and

excess aggregate contributions under an EACA to 6 months. Thus, in the case of an EACA, the section 4979 excise tax does not apply to any excess contributions or excess aggregate contributions which, together with income allocable to the contributions, are distributed or forfeited (if forfeitable) within six months after the close of the plan year.

Section 902 of PPA '06 amended section 4979(f)(2) to provide that any distributions of excess contributions and excess aggregate contributions are includible in the employee's gross income for the taxable year in which distributed. However, pursuant to sections 401(k)(8)(D) and 401(m)(7)(A), the distributions are not subject to the additional income tax under section 72(t). Section 902 of PPA '06 also amended sections 401(k)(8), 401(m)(6), and 4979(f)(1) to eliminate the requirement that excess contributions or excess aggregate contributions (whether or not under an EACA) include income allocable to the period after the end of the plan year (gap period income).

Section 624 of PPA '06 amended section 404(c) of ERISA to provide that a participant in an individual account plan meeting the notice requirements of section 404(c)(5)(B) of ERISA is treated as exercising control over the assets in the account which, in the absence of an investment election by the participant, are invested in accordance with regulations prescribed by the Secretary of Labor. The specific timing and content requirements for the notice required under section 404(c)(5)(B) of ERISA are generally the same as under section 414(w)(4), but the Department of Labor (DOL) has interpretative jurisdiction for that notice.

Section 902 of PPA '06 also amended section 514 of ERISA to preempt any State law which would directly or indirectly prohibit or restrict the inclusion in any plan of an automatic contribution arrangement. The Secretary of Labor is authorized to prescribe regulations which would establish minimum standards that such an arrangement would be required to satisfy in order for this preemption to apply to such an arrangement. The definition of an automatic contribution arrangement under section 514 of ERISA is generally the same as the definition of an EACA under section 414(w)(3), (including the requirement that automatic contributions under the arrangement must be invested in accordance with regulations prescribed by the Secretary of Labor under section 404(c)(5) of ERISA), but the definition does not include a notice requirement. However, section 514(e)(3) of ERISA requires a notice to be provided to each participant to whom the arrangement applies. As in the case for the notice under section 404(c)(5)(B) of ERISA, the specific timing and content requirements under section 514(e)(3) of ERISA are generally the same as the notice requirements under section 414(w)(4), but the interpretative jurisdiction for that notice is also with the DOL.

Explanation of Provisions

1. Qualified Automatic Contribution Arrangement Under Section 401(k)(13)

The proposed regulations would amend §§ 1.401(k)–3 and 1.401(m)–3 to reflect the provisions of sections 401(k)(13) and 401(m)(12) for a QACA, the new design-based safe harbor for satisfying the ADP and ACP tests. To the extent that the requirements to be a QACA are the same as those for the safe harbor described in sections 401(k)(12) and 401(m)(11), these proposed regulations would apply the existing rules currently in §§ 1.401(k)–3 and 1.401(m)–3 to a QACA. Thus, for example, because § 1.401(k)–3(e) applies to a QACA, except to the extent otherwise provided in section 1107 of PPA '06 or § 1.401(k)–3(f) or § 1.401(k)–3(g), the plan provision implementing the QACA for an existing qualified CODA would be required to be adopted before the first day of the plan year and remain in effect for an entire 12-month plan year. Similarly under § 1.401(k)–3(c)(6), a plan would be permitted to limit the amount of elective contributions that may be made by an eligible employee under the QACA, provided that each NHCE who is an eligible employee generally is permitted to make elective contributions in an amount that is at least sufficient to receive the maximum amount of matching contributions available under the plan for the plan year, and the employee is permitted to elect any lesser amount of elective contributions.

In order to be a QACA, the plan must provide a specified schedule of automatic contributions (called qualified percentages) for each eligible employee beginning with an initial minimum qualified percentage of 3 percent of compensation. This minimum qualified percentage begins when the employee first participates in the automatic contribution arrangement that is intended to be a QACA and ends on the last day of the following plan year. Thus, this initial period for a participant could last as long as two full plan years. After this initial period, the minimum qualified percentage increases by 1 percent for each of the next three plan years. Thus, the minimum qualified percentage for the plan year after the initial period is 4 percent. This minimum qualified percentage increases to 5 percent for the next plan year, and then is 6 percent for all plan years thereafter. These are merely minimum qualified percentages. Thus, a QACA can provide for higher percentages. For example, a QACA could provide for a qualified percentage in the initial period of 4 percent of compensation. If a plan did so, it could also provide a 4 percent qualified percentage for the plan year after the initial period (the statutory minimum percentage for that plan year), 5 percent in the next plan year and 6 percent thereafter. However, the qualified percentage can at no time exceed 10 percent of compensation.

Under section 401(k)(13)(C)(iii), the qualified percentage must be applied uniformly to all eligible employees. The proposed regulations would provide that a plan does not fail this requirement merely because the percentage varies for the following reasons: (1) The percentage varies based on the number of years an eligible employee has participated in the automatic contribution arrangement intended to be a QACA; (2) the rate of elective contributions under a cash or deferred election that is in effect on the effective date of the default percentage under the QACA is not reduced; or (3) the amount of elective contributions is limited so as not to exceed the limits of sections 401(a)(17), 402(g) (determined with or without catch-up contributions described in section 402(g)(1)(C) or section 402(g)(7)) or 415. Further, the proposed regulations would provide that a cash or deferred arrangement does not fail to satisfy the uniformity requirement merely because an employee is not automatically enrolled during a period that the employee is not permitted to make elective contributions because of the requirement to suspend elective contributions for a 6-month period following a hardship distribution. In the case of an employee whose elective contributions have been suspended (for example, because of a hardship distribution), the plan must provide that the employee will, at the end of the suspension period, resume elective contributions at the level (percentage) that would apply if the suspension had not occurred.

Reflecting section 401(k)(13)(C)(ii), the proposed regulations provide that the default election ceases to apply to any eligible employee if the employee makes an affirmative election that remains in effect to not have any elective contributions made on his or her behalf or to have elective

contributions made in a specified amount or percentage of compensation on his or her behalf. Thus, an employee can make an affirmative election to contribute at a certain level and have that election apply for all subsequent plan years. Similarly, an employee can make an affirmative election to have no elective contributions made on his or her behalf. This latter election is not the same as the election to withdraw prior elective contributions under section 414(w).

The proposed regulations also reflect section 401(k)(13)(C)(iv), which provides an exception from the default election for eligible employees who were eligible to participate in the CODA (or a predecessor CODA) immediately before the effective date of the QACA and who have an election in effect on that effective date. The proposed regulations would provide that an election in effect means an affirmative election that remains in effect to have the employer make elective contributions on his or her behalf (in a specified amount or percentage of compensation) or to not have the employer make elective contributions on his or her behalf. Generally, this would require that the employee have completed an election form and chosen an amount or percentage (including zero) of his compensation to be deferred.

The proposed regulations reflect the matching or nonelective contribution requirement of section 401(k)(13)(D). As with the safe harbor in section 401(k)(12), section 401(k)(13) provides a choice for an employer between satisfying a matching contribution requirement or a nonelective contribution requirement. However, while the QACA requires the same level of employer nonelective contributions as under section 401(k)(12), the matching contribution requirement for a QACA allows for a lower level of matching contributions. Specifically, a QACA using the matching contribution alternative need only provide for matching contributions on behalf of each eligible NHCE equal to 100 percent of the employee's elective contributions that do not exceed one percent of compensation and 50 percent of the employee's elective contributions that exceed one percent but do not exceed six percent of compensation. In addition, a QACA allows a slower schedule of vesting for both matching and nonelective safe harbor contributions than the safe harbor in section 401(k)(12). All QACA safe harbor contributions must be fully vested after 2 years of vesting service (within the meaning of section 411(a)), rather than immediately as required by section 401(k)(12). In addition, the proposed regulations would apply the same distribution restrictions that apply to safe harbor contributions and nonelective contributions under section 401(k)(12) to QACA safe harbor contributions.

Each eligible employee under a QACA must receive a safe harbor notice within a reasonable period before each plan year. The proposed regulations reflect the requirement that this notice must provide the information required under section 401(k)(12). The regulations also reflect the additional timing and content requirements described in section 401(k)(13)(E)(i). Thus, the notice must also explain: (1) The employee's right under the arrangement to elect not to have elective contributions made on the employee's behalf or to elect to have contributions made in a different amount or percentage of compensation; and (2) how contributions made under the automatic contribution arrangement will be invested in the absence of any investment decision by the employee (including, in the case of an arrangement under which the employee may elect among two or more investment options, how contributions made under the automatic contribution arrangement will be invested in the absence of an investment election by the employee). These additional requirements cannot be satisfied by reference to the plan's summary plan description. Further, the proposed regulations would provide that in order to satisfy section 401(k)(13)(E)(ii)(III), under the QACA, the employee must be given a reasonable period of time after receipt of the notice and before the first elective contribution is to be made to make an election with respect to contributions and investments.

The proposed regulations interpret the requirement under section 401(k)(13)(E)(i) to provide a notice within a reasonable period before each plan year by applying the rules of § 1.401(k)-3(d)(3). Thus, the proposed regulations would provide that the general determination of whether the timing requirement is satisfied is based on all of the relevant facts and circumstances, and the deemed timing rule of § 1.401(k)-3(d)(3)(ii) applies. Under this deemed timing rule, the timing requirement is satisfied if at least 30 days (and no more than 90 days) before the beginning of each plan year, the notice is given to each eligible employee for the plan year. The proposed regulations would also provide that in the case of an employee who does not receive the notice within the period described in the previous sentence because the employee becomes eligible after the 90th day before the beginning of the plan year, the timing requirement is deemed to be satisfied if the notice is provided no more than 90 days before the employee becomes eligible (and no later than the date the employee becomes eligible). Thus, for example, the preceding sentence would apply to all eligible employees for the first plan year under a newly established plan that provides for elective contributions, and to the first plan year in which an employee becomes eligible under an existing plan that provides for elective contributions. In the case of a plan with immediate eligibility when an employee is hired, this deemed timing rule would be satisfied if the employee is provided the notice on the first day of employment.

2. Eligible Automatic Contribution Arrangement Under Section 414(w)

In order to further facilitate automatic enrollment, section 414(w) provides limited relief from the distribution restrictions under sections 401(k)(2), 403(b)(7), 403(b)(11), and 457(d) (as well as certain other relief provisions) for an applicable plan (that is, a section 401(k) plan, a section 403(b) plan, or a section 457(b) eligible governmental plan) with an EACA. Specifically, section 414(w)(2) provides that, under an applicable employer plan with an EACA, an employee can be permitted to elect to receive a distribution equal to the amount of default elective contributions (and attributable earnings) made with respect to the first payroll period to which the EACA applies to the employee and any succeeding payroll periods beginning before the effective date of the election.

An employer is permitted, but not required, to include the section 414(w)(2) permissible withdrawal provision in an applicable employer plan, and an employer who does offer this option is not required to make it available to all employees eligible under the EACA. Thus, for example, an employer might choose to make the withdrawal option available only to employees for whom no elective contributions have been made under the CODA (or a predecessor CODA) before the EACA is effective. However, under a section 401(k) plan or a section 403(b) plan, the employer may not condition the right to take the withdrawal on the employee making an election to have no future elective contributions made on the employee's behalf because such a condition would violate the contingent benefit rule under section 401(k)(4)(A) or the universal availability requirement under section 403(b)(12)(A)(ii).

Nonetheless, the employer could provide in the withdrawal election form a default election under which elective contributions would cease unless the employee makes an affirmative election.

Under section 414(w)(2)(B), the election to withdraw the contributions that were made under an EACA must be made within 90 days of the ''first elective contribution with respect to the employee under the arrangement.'' The proposed regulations would define the arrangement for this purpose as the EACA so that the withdrawal option could apply to employees previously eligible under the CODA (including a CODA that is an automatic contribution arrangement but was not an EACA). Because section 414(w) only applies to plan years beginning on or after January 1, 2008, an automatic contribution arrangement can only become an EACA on or after that date. Accordingly, a withdrawal election under section 414(w) can only apply to elective contributions made after that date. The proposed regulations would provide that the 90-day window for making the withdrawal election begins on the date on which the compensation that is subject to the cash or deferred election would otherwise have been included in gross income. In addition, the proposed regulations would provide that the effective date of the election must be no later than the last day of the payroll period that begins after the date of the election.

The proposed regulations would provide that the distribution is generally the account balance attributable to the default elective contributions, adjusted for gains and losses. The distribution may be reduced by any generally applicable fees. However, the proposed regulations provide that the plan may not charge a different fee for this distribution than would apply to other distributions. Also, if the default elective contributions are not maintained in a separate account, the amount of the allocable gains and losses will be determined under rules similar to those provided under § 1.401(k)–2(b)(2)(iv) for the distribution of excess contributions.

The amount withdrawn under section 414(w) is includible in gross income in the year in which it is distributed, except amounts that are distributions of designated Roth contributions are not included in an employee's gross income a second time. The proposed regulations would require that this amount be reported on Form 1099–R, Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc. However, the amount is not subject to the additional income tax under section 72(t). Finally, the proposed regulations would amend § 1.402(c)–2 to include these withdrawals in the list of distributions that are not eligible for rollover.

Any employer matching contribution with respect to the default elective contribution distributed pursuant to section 414(w) must be forfeited. The forfeited matching contribution is not a mistaken contribution or other erroneous contribution, and, thus, it cannot be returned to the employer (or be distributed to the employee as is permitted for an excess aggregate contribution). The proposed regulations would provide that the forfeited contribution must remain in the plan and be treated in the same manner under the plan terms as any other forfeiture under the plan.

Under section 414(w)(3)(B), an EACA must provide that the default elective contribution is a uniform percentage of compensation. The proposed regulations would provide that the permitted differences in contribution rates provided in these proposed regulations under section 401(k)(13) for a QACA also apply to an EACA.

Another requirement to be an EACA under section 414(w)(3)(C) is that automatic contributions are invested in accordance with regulations prescribed by the Secretary of Labor under section 404(c)(5) of ERISA. These proposed regulations would provide that this requirement only applies if the plan is otherwise subject to Title I of ERISA. Thus, for example, this provision would not apply to a governmental plan (within the meaning of section 414(d)).

The proposed regulations reflect the section 414(w) notice requirement under which notice must be provided to each employee to whom the EACA applies within a ''reasonable period'' before each plan year, but provide that, if an employee becomes eligible in a given year, notice must be given within a ''reasonable period'' before the employee becomes eligible. The proposed regulations provide a deemed timing requirement that is generally the same as the deemed timing rule in § 1.401(k)–3(d)(3)(ii).

3. Coordinated Notices

As noted in this preamble, PPA '06 provides for several notices relating to automatic contribution arrangements that have similar content and timing requirements, including the notices required by sections 404(c)(5)(B) and 514(e)(3) of ERISA. The IRS, in coordination with DOL, anticipates that a single document can satisfy all of these notice requirements, so long as it has all of the requisite information for plan participants and satisfies the timing requirements for each of those notices.

4. Other Provisions of Section 902 of PPA '06

The proposed regulations also reflect the amendments to section 4979 made by section 902 of PPA '06. First, the proposed regulations reflect the substitution of 6 months for 2½ months as the time period under section 4979(f) by which excess contributions or excess aggregate contributions with respect to an EACA must be distributed to avoid the excise tax under section 4979(a). Further, the proposed regulations reflect the elimination of the requirement that distributions of excess contributions or excess aggregate contributions (whether or not under an EACA) include attributable earnings for the period after the end of the plan year (gap period income). The proposed regulations also reflect the change in the tax treatment of a distribution of excess contributions or excess aggregate contributions (whether or not under an EACA) under which the distribution of excess contributions or excess aggregate contributions (including earnings) is includible in the participant's gross income for the year of the distribution (without regard to the amount of the distribution). The proposed regulations would also amend §§ 1.401(k)–2 and 1.401(m)–2 to reflect these provisions in the correction rules for the ADP and ACP tests. All of these changes are proposed to be effective January 1, 2008 and will impact corrective distributions made in 2009.

In addition, the proposed regulations would amend §§ 1.401(k)–2 and 1.401(m)–2 to reflect the provisions of section 414(w)(6) that default elective contributions distributed under section 414(w) are not taken into account in the ADP test. They are also not permitted to be taken into account in the ACP test. The proposed regulations under section 401(m) have added a conforming change for other elective contributions that are not taken into account in the ADP test. The proposed regulations would also amend § 1.411(a)–4(b)(7) to reflect the amendment to section 411(a)(3)(G) made by PPA '06 section 902(d)(2).

Effective Date

Sections 401(k)(13), 401(m)(12), and 414(w), and the amended provisions of sections 411(a)(3)(G) and 4979(f), are effective for plan years beginning on or after January 1, 2008. These regulations are proposed to be effective for plan years beginning on or after January 1, 2008. Taxpayers may rely on these proposed regulations for guidance

pending the issuance of final regulations. If, and to the extent, the final regulations are more restrictive than the guidance in these proposed regulations, those provisions of the final regulations will be applied without retroactive effect.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It has been determined that 5 U.S.C. 533(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations. It is hereby certified that the collection of information in these proposed regulations will not have a significant economic impact on a substantial number of small entities. This certification is based on the fact that most small entities that maintain plans that will be eligible for the safe harbor provisions of sections 401(k) and 401(m) or the distribution relief provisions of section 414(w) currently provide a similar notice with which this notice can be combined. Therefore, an analysis under the Regulatory Flexibility Act (5 U.S.C. chapter 6) is not required. Pursuant to section 7805(f) of the Internal Revenue Code, these regulations have been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comments on its impact on small business.

Comments and Requests for Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written (one signed and eight (8) copies) or electronic comments that are submitted timely to the IRS. The IRS and Treasury Department specifically request comments on the clarity of the proposed rules and how they can be made easier to understand. All comments will be available for public inspection and copying. A public hearing will be scheduled if requested in writing by any person who timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place of the public hearing will be published in the **Federal Register**.

Drafting Information

The principal authors of these regulations are Dana Barry, William Gibbs, and Lisa Mojiri-Azad, Office of Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities). However, other personnel from the IRS and Treasury Department participated in the development of these regulations.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended to read as follows:

Authority: 26 U.S.C. 7805 * * *

Section 1.401(k)–3 is also issued under 26 U.S.C. 401(k)(13)

Par. 2. Section 1.401(k)–0 is amended by:

1. Amending the entry for § 1.401(k)–2 by adding entries for §§ 1.401(k)–2(a)(5)(vi) and 1.401(k)–2(b)(2)(iv)(D).
2. Revising the entries for §§ 1.401(k)–2(b)(2)(vi)(A) and 1.401(k)–2(b)(2)(vi)(B).
3. Adding an entry for § 1.401(k)–2(b)(5)(iii).
4. Revising the entries for §§ 1.401(k)–3(a)(1), 1.401(k)–3(a)(2) and 1.401(k)–3(a)(3).
5. Adding entries for §§ 1.401(k)–3(i), 1.401(k)–3(j) through (j)(2)(iii).
6. Adding entries for § 1.401(k)–3(k) through (k)(4)(iii).

The additions and revisions to read as follows:

§ 1.401(k)–0 Table of Contents.

* * * * *

§ 1.401(k)–2 ADP test.

(a) * * *
(5) * * *
(vi) Default elective contributions pursuant to section 414(w).

* * * * *

(b) * * *
(2) * * *
(iv) * * *
(A) * * *
(D) Plan years before 2008.

* * * * *

(vi) * * *
(A) Corrective distributions for plan years beginning on or after January 1, 2008.
(B) Corrective distributions for plan years beginning before January 1, 2008.

* * * * *

(5) * * *
(iii) Special rule for eligible automatic contribution arrangements.

* * * * *

§ 1.401(k)–3 Safe harbor requirements.

(a) * * *
(1) Section 401(k)(12) safe harbor.
(2) Section 401(k)(13) safe harbor.
(3) Requirements applicable to safe harbor contributions.

* * * * *

(i) Reserved.
(j) Qualified automatic contribution arrangement.
(1) Automatic contribution requirement.
(i) In general.
(ii) Automatic contribution arrangement.
(iii) Exception for certain current employees.
(2) Qualified percentage.
(i) In general.
(ii) Minimum percentage requirements.
(A) Initial-year requirement.
(B) Second-year requirement.
(C) Third-year requirement.
(D) Later years requirement.
(iii) Exception to uniform percentage requirement.
(k) Modifications to contribution requirements and notice requirements for automatic contribution safe harbor.
(1) In general.
(2) Lower matching requirement.
(3) Modified nonforfeiture requirement.
(4) Additional notice requirements.
(i) In general.
(ii) Additional information.
(iii) Timing requirements.

Par. 3. Section 1.401(k)–1 is amended by:

1. Revising paragraph (b)(1)(ii)(C) and adding new paragraph (b)(1)(ii)(D).
2. Revising paragraph (e)(7) by adding a new sentence after the fifth sentence.

The additions and revisions read as follows:

§ 1.401(k)–1 Certain cash or deferred arrangements.

* * * * *

(b) * * * (1) * * * (ii) * * *

(C) The ADP safe harbor provisions of section 401(k)(13) described in § 1.401(k)–3; or

(D) The SIMPLE 401(k) provisions of section 401(k)(11) described in § 1.401(k)–4.

* * * * *

(e) * * *

(7) *Plan provision requirement.* * * * In addition, a plan that uses the safe harbor method of section 401(k)(13), as described in paragraph (b)(1)(ii)(C) of this section, must specify the default percentages that apply for the plan year, and whether the safe harbor contribution will be the nonelective safe harbor contribution or the matching safe harbor contribution and is not permitted to provide that ADP testing will be used

if the requirements for the safe harbor are not satisfied. * * *

* * * * *

Par. 4. Section 1.401(k)–2 is amended by:

1. Adding paragraph (a)(5)(vi).
2. Revising paragraphs (b)(2)(iv)(A) and (b)(2)(iv)(D).
3. Removing paragraph (b)(2)(iv)(E).
4. Revising paragraph (b)(2)(vi)(A).
5. Adding a new first sentence to paragraph (b)(2)(vi)(B).
6. Removing and reserving Example (3), Example (4), and Example (5) from § 1.401(k)–2 (b)(2)(viii).
7. Revising paragraph (b)(4)(iii) and adding paragraph (b)(5)(iii).

The additions and revisions read as follows:

§ 1.401(k)–2 ADP test.

(a) * * *

(5) * * *

(vi) *Default elective contributions pursuant to section 414(w).* Default elective contributions made under an eligible automatic contribution arrangement (within the meaning of § 1.414(w)–1(b) that are distributed pursuant to § 1.414(w)–1(c) for plan years beginning on or after January 1, 2008, are not taken into account under paragraph (a)(4) of this section for the plan year for which the contributions are made, or for any other plan year.

(b) * * *

(2) * * *

(iv) *Income allocable to excess contributions*—(A) *General rule.* For plan years beginning on or after January 1, 2008, the income allocable to excess contributions is equal to the allocable gain or loss through the end of the plan year. See paragraph (b)(2)(iv)(D) of this section for rules that apply to plan years beginning before January 1, 2008.

* * * * *

(D) *Plan years before 2008.* For plan years beginning before January 1, 2008, the income allocable to excess contributions is determined under § 1.401(k)–2(b)(2)(iv) (as it appeared in the April 1, 2007, edition of 26 CFR part 1).

* * * * *

(vi) *Tax treatment of corrective distributions*—(A) *Corrective distributions for plan years beginning on or after January 1, 2008.* Except as provided in this paragraph (b)(2)(vi), for plan years beginning on or after January 1, 2008, a corrective distribution of excess contributions (and allocable income) is includible in the employee's gross income for the employee's taxable year in which distributed. In addition, the corrective distribution is not subject to the early distribution tax of section 72(t). See also paragraph (b)(5) of this section for additional rules relating to the employer excise tax on amounts distributed more than 2½ months (6 months in the case of a plan that includes an eligible automatic contribution arrangement within the meaning of section 414(w)) after the end of the plan year. See also § 1.402(c)–2, A–4 for restrictions on rolling over distributions that are excess contributions.

(B) *Corrective distributions for plan years beginning before January 1, 2008.* The tax treatment of corrective distributions for plan years beginning before January 1, 2008, is determined under § 1.401(k)–2(b)(2)(vi) (as it appeared in the April 1, 2007, edition of 26 CFR Part 1). * * *

* * * * *

(4) * * *

(iii) *Permitted forfeiture of QMAC.* Pursuant to section 401(k)(8)(E), a qualified matching contribution is not treated as forfeitable under § 1.401(k)–1(c) merely because under the plan it is forfeited in accordance with paragraph (b)(4)(ii) of this section or § 1.414(w)–1(d)(2).

* * * * *

(5) * * *

(iii) *Special rule for eligible automatic contribution arrangements.* In the case of a plan that includes an eligible automatic contribution arrangement within the meaning of section 414(w), 6 months is substituted for 2½ months in paragraph (b)(5)(i) of this section.

* * * * *

Par. 5. Section 1.401(k)–3 is amended by:

1. Revising paragraph (a).
2. Revising the first sentence of paragraph (e)(1).
3. Revising the last sentence of paragraph (h)(2).
4. Revising the first sentence of paragraph (h)(3).
5. Reserving paragraph (i) and adding paragraphs (j), and (k).

The additions and revisions to read as follows:

§ 1.401(k)–3 Safe harbor requirements.

(a) *ADP test safe harbor*—(1) *Section 401(k)(12) safe harbor.* A cash or deferred arrangement satisfies the ADP safe harbor provision of section 401(k)(12) for a plan year if the arrangement satisfies the safe harbor contribution requirement of paragraph (b) or (c) of this section for the plan year, the notice requirement of paragraph (d) of this section, the plan year requirements of paragraph (e) of this section, and the additional rules of paragraphs (f), (g), and (h) of this section, as applicable.

(2) *Section 401(k)(13) safe harbor.* For plan years beginning on or after January 1, 2008, a cash or deferred arrangement satisfies the ADP safe harbor provision of section 401(k)(13) for a plan year if the arrangement is described in paragraph (j) of this section and satisfies the safe harbor contribution requirement of paragraph (k) of this section for the plan year, the notice requirement of paragraph (d) of this section (modified to include the information set forth in paragraph (k)(4) of this section), the plan year requirements of paragraph (e) of this section, and the additional rules of paragraphs (f), (g), and (h) of this section, as applicable. A cash or deferred arrangement that satisfies the requirements of this paragraph is referred to as a qualified automatic contribution arrangement.

(3) *Requirements applicable to safe harbor contributions.* Pursuant to section 401(k)(12)(E)(ii) and section 401(k)(13)(D)(iv), the safe harbor contribution requirement of paragraph (b), (c), or (k) of this section must be satisfied without regard to section 401(l). The contributions made under paragraph (b) or (c) of this section (and the corresponding contributions under paragraph (k) of this section) are referred to as safe harbor nonelective contributions and safe harbor matching contributions, respectively.

* * * * *

(e) * * * (1) *General rule.* Except as provided in this paragraph (e) or in paragraph (f) of this section, a plan will fail to satisfy the requirements of sections 401(k)(12), 401(k)(13), and this section unless plan provisions that satisfy the rules of this section are adopted before the first day of the plan year and remain in effect for an entire 12-month plan year. * * *

* * * * *

(h) * * *

(2) *Use of safe harbor nonelective contributions to satisfy other discrimination tests.* * * * However, pursuant to section 401(k)(12)(E)(ii) and section 401(k)(13)(D)(iv), to the extent they are needed to satisfy the safe harbor contribution requirement of paragraph (b) of this section, safe harbor nonelective contributions may not be taken into account under any plan for purposes of section 401(l) (including the imputation of permitted disparity under § 1.401(a)(4)–7).

(3) *Early participation rules.* Section 401(k)(3)(F) and § 1.401(k)–2(a)(1)(iii)(A), which provide an alternative nondiscrimination rule for certain plans that provide for early participation, do not apply for purposes

of section 401(k)(12), section 401(k)(13), and this section. * * *

* * * * *

(i) [RESERVED].

(j) *Qualified automatic contribution arrangement*—(1) *Automatic contribution requirement*—(i) *In general.* A cash or deferred arrangement is described in this paragraph (j) if it is an automatic contribution arrangement described in paragraph (j)(1)(ii) of this section where the default election under that arrangement is a contribution equal to the qualified percentage described in paragraph (j)(2) of this section multiplied by the eligible employee's compensation from which elective contributions are permitted to be made under the cash or deferred arrangement.

(ii) *Automatic contribution arrangement.* An automatic contribution arrangement is a cash or deferred arrangement within the meaning of § 1.401(k)–1(a)(2) that provides that in the absence of an eligible employee's affirmative election, a default applies under which the employee is treated as having made an election to have a specified contribution made on his or her behalf under the plan. The default election ceases to apply with respect to an eligible employee if the employee makes an affirmative election (that remains in effect) to—

(A) Have elective contributions made in a different amount on his or her behalf (in a specified amount or percentage of compensation); or

(B) Not have any elective contributions made on his or her behalf.

(iii) *Exception for certain current employees.* An automatic contribution arrangement will not fail to be a qualified automatic contribution arrangement merely because the default election provided under paragraph (j)(1)(i) of this section is not applied to an employee who was an eligible employee under the cash or deferred arrangement (or a predecessor arrangement) immediately prior to the effective date of the qualified automatic contribution arrangement and on that effective date had an affirmative election in effect (that remains in effect) to—

(A) Have elective contributions made on his or her behalf (in a specified amount or percentage of compensation); or

(B) Not have elective contributions made on his or her behalf.

(2) *Qualified percentage*—(i) *In general.* A percentage is a qualified percentage only if it—

(A) Is uniform for all employees (except to the extent provided in paragraph (j)(2)(iii) of this section);

(B) Does not exceed 10 percent; and

(C) Satisfies the minimum percentage requirements of paragraph (j)(2)(ii) of this section.

(ii) *Minimum percentage requirements*—(A) *Initial-period requirement.* The minimum percentage requirement of this paragraph (j)(2)(ii)(A) is satisfied only if the percentage that applies for the period that begins when the employee first participates in the automatic contribution arrangement that is a qualified automatic contribution arrangement and ends on the last day of the following plan year is at least 3 percent.

(B) *Second-year requirement.* The minimum percentage requirement of this paragraph (j)(2)(ii)(B) is satisfied only if the percentage that applies for the plan year immediately following the last day described in paragraph (j)(2)(ii)(A) of this section is at least 4 percent.

(C) *Third-year requirement.* The minimum percentage requirement of this paragraph (j)(2)(ii)(C) is satisfied only if the percentage that applies for the plan year immediately following the plan year described in paragraph (j)(2)(ii)(B) of this section is at least 5 percent.

(D) *Later years requirement.* A percentage satisfies the minimum percentage requirement of this paragraph (j)(2)(ii)(D) only if the percentage that applies for all plan years following the plan year described in paragraph (j)(2)(ii)(C) of this section is at least 6 percent.

(iii) *Exception to uniform percentage requirement.* A plan does not fail to satisfy the uniform percentage requirement of paragraph (j)(2)(i)(A) of this section merely because—

(A) The percentage varies based on the number of years an eligible employee has participated in the automatic contribution arrangement intended to be a qualified automatic contribution arrangement;

(B) The rate of elective contributions under a cash or deferred election that is in effect immediately prior to the effective date of the default percentage under the qualified automatic contribution arrangement is not reduced;

(C) The rate of elective contributions is limited so as not to exceed the limits of sections 401(a)(17), 402(g) (determined with or without catch-up contributions described in section 402(g)(1)(C) or 402(g)(7)), and 415; or

(D) The default election provided under paragraph (j)(1)(i) of this section is not applied during the period an employee is not permitted to make elective contributions in order for the plan to satisfy the requirements of § 1.401(k)–1(d)(3)(iv)(E)(*2*).

(k) *Modifications to contribution requirements and notice requirements for automatic contribution safe harbor*—(1) *In general.* A cash or deferred arrangement satisfies the contribution requirements of this paragraph (k) only if it satisfies the contribution requirements of either paragraph (b) or (c) of this section, as modified by the rules of paragraphs (k)(2) and (k)(3) of this section. In addition, a cash or deferred arrangement described in paragraph (j) of this section satisfies the notice requirement of section 401(k)(13)(E) only if the notice satisfies the additional requirements of paragraph (k)(4) of this section.

(2) *Lower matching requirement.* In applying the requirement of paragraph (c) of this section, in the case of a cash or deferred arrangement described in paragraph (j) of this section, the basic matching formula is modified so that each eligible NHCE must receive the sum of—

(i) 100 percent of the employee's elective contributions that do not exceed 1 percent of the employee's safe harbor compensation; and

(ii) 50 percent of the employee's elective contributions that exceed 1 percent of the employee's safe harbor compensation but that do not exceed 6 percent of the employee's safe harbor compensation.

(3) *Modified nonforfeiture requirement.* A cash or deferred arrangement described in paragraph (j) of this section will not fail to satisfy the requirements of paragraph (b) or (c) of this section, as applicable, merely because the safe harbor contributions are not qualified nonelective contributions or qualified matching contributions provided that—

(i) The contributions are subject to the withdrawal restrictions set forth in § 1.401(k)–1(d); and

(ii) Any employee who has completed 2 years of service (within the meaning of section 411(a)) has a nonforfeitable right to the account balance attributable to the safe harbor contributions.

(4) *Additional notice requirements*—(i) *In general.* A notice satisfies the requirements of this paragraph (k)(4) only if it includes the additional information described in paragraph (k)(4)(ii) of this section and satisfies the timing requirements of paragraph (k)(4)(iii) of this section.

(ii) *Additional information.* A notice satisfies the additional information requirement of this paragraph (k)(4)(ii) only if it explains—

(A) The level of elective contributions, which will be made on the employee's behalf if the employee does not make an affirmative election;

(B) The employee's right under the automatic contribution arrangement to elect not to have elective contributions made on the employee's behalf (or to elect to have such contributions made in a different amount or percentage of compensation); and

(C) How contributions under the automatic contribution arrangement will be invested (including, in the case of an arrangement under which the employee may elect among 2 or more investment options, how contributions made under the automatic contribution arrangement will be invested in the absence of an investment election by the employee).

(iii) *Timing requirements.* A notice satisfies the timing requirements of this paragraph (k)(4)(iii) only if it is provided sufficiently early so that the employee has a reasonable period of time after receipt of the notice and before the first elective contribution is made under the arrangement to make the elections described under paragraph (k)(4)(ii)(B) and (C) of this section.

* * * * *

Par. 6. Section 1.401(k)–6 is amended by revising the last sentence in the definition of ''Qualified matching contributions (QMACs)'' to read as follows:

§ 1.401(k)–6 Definitions.

* * * * *

Qualified matching contributions (QMACs). * * * See also § 1.401(k)–2(b)(4)(iii) for a rule providing that a matching contribution does not fail to qualify as a QMAC solely because it is forfeitable under section 411(a)(3)(G) as a result of being a matching contribution with respect to an excess deferral, excess contribution, excess aggregate contribution, or it is forfeitable under § 1.414(w)–1(d)(2).

* * * * *

Par. 7. Section 1.401(m)–0 is amended to read as follows:

Adding an entry for § 1.401(m)–2(b)(4)(iii).

§ 1.401(m)–0 Table of Contents.

* * * * *

§ 1.401(m)–2 ACP Test.

* * * * *

(b) * * *

(2) * * *

(iv) * * *

(A) * * *

(D) Plan years before 2008.

* * * * *

(4) * * *

(iii) *Special rule for eligible automatic contribution arrangements.*

* * * * *

Par. 8. Section 1.401(m)–1 is amended by:

1. Revising paragraph (b)(1)(iii) and adding paragraph (b)(1)(iv).

2. Revising the last sentence of paragraph (b)(4)(iii)(B).

3. Revising the fifth sentence of paragraph (c)(2).

The additions and revisions read as follows:

§ 1.401(m)–1 Employee contributions and matching contributions.

* * * * *

(b) * * *

(1) * * *

(iii) The ACP safe harbor provisions of section 401(m)(12) described in § 1.401(m)–3; or

(iv) The SIMPLE 401(k) provisions of sections 401(k)(11) and 401(m)(10) described in § 1.401(k)–4.

* * * * *

(b) * * *

(4) * * *

(iii) * * *

(B) *Arrangements with inconsistent ACP testing methods.* * * * Similarly, an employer may not aggregate a plan (within the meaning of § 1.410(b)–7) that is using the ACP safe harbor provisions of section 401(m)(11) or 401(m)(12) and another plan that is using the ACP test of section 401(m)(2).

* * * * *

(c) * * *

(2) *Plan provision requirement.* * * * Similarly, a plan that uses the safe harbor method of section 401(m)(11) or 401(m)(12), as described in paragraphs (b)(1)(ii) and (b)(1)(iii) of this section, must specify the default percentages that apply for the plan year and whether the safe harbor contribution will be the nonelective safe harbor contribution or the matching safe harbor contribution and is not permitted to provide that ACP testing will be used if the requirements for the safe harbor are not satisfied. * * *

* * * * *

Par. 9. Section 1.401(m)–2 is amended by:

1. Revising the first and second sentences of paragraph (a)(5)(iv).

2. Revising paragraph (a)(5)(v).

3. Adding a new sentence to the end of paragraph (a)(6)(ii).

4. Revising paragraphs (b)(2)(iv)(A) and (b)(2)(iv)(D).

5. Removing paragraph (b)(2)(iv)(E).

6. Revising paragraph (b)(2)(vi)(A).

7. Adding a new sentence to the beginning of paragraph (b)(2)(vi)(B).

8. Adding paragraph (b)(4)(iii).

The additions and revisions to read as follows:

§ 1.401(m)–2 ACP test.

(a) * * *

(5) * * *

(iv) *Matching contributions taken into account.* A plan that satisfies the ACP safe harbor requirements of section 401(m)(11) or 401(m)(12) for a plan year but nonetheless must satisfy the requirements of this section because it provides for employee contributions for such plan year is permitted to apply this section disregarding all matching contributions with respect to all eligible employees. In addition, a plan that satisfies the ADP safe harbor requirements of § 1.401(k)–3 for a plan year using qualified matching contributions but does not satisfy the ACP safe harbor requirements of section 401(m)(11) or 401(m)(12) for such plan year is permitted to apply this section by excluding matching contributions with respect to all eligible employees that do not exceed 4 percent (3.5 percent in the case of a plan that satisfies the ADP safe harbor under section 401(k)(13)) of each employee's compensation. * * *

(v) *Treatment of forfeited matching contributions.* A matching contribution that is forfeited because the contribution to which it relates is treated as an excess contribution, excess deferral, excess aggregate contribution, or a default elective contribution that is distributed under section 414(w), is not taken into account for purposes of this section.

* * * * *

(6) * * *

(ii) *Elective contributions taken into account under the ACP test.* * * * In addition, for plan years ending on or after November 8, 2007, elective contributions which are not permitted to be taken into account for the ADP test for the plan year under § 1.401(k)–2(a)(5)(ii), (iii), (v), or (vi) are not permitted to be taken into account for the ACP test.

* * * * *

(b) * * *

(2) * * *

(iv) *Income allocable to excess aggregate contributions*—(A) *General rule.* For plan years beginning on or after January 1, 2008, the income allocable to excess aggregate contributions is equal to the allocable gain or loss through the end of the plan year. See paragraph (b)(2)(iv)(D) of this section for rules that apply to plan years beginning before January 1, 2008.

* * * * *

(D) *Plan years before 2008.* For plan years beginning before January 1, 2008,

the income allocable to excess aggregate contributions is determined under § 1.401(m)–2(b)(2)(iv) (as it appeared in the April 1, 2007, edition of 26 CFR part 1).

* * * * *

(vi) *Tax treatment of corrective distributions—(A) Corrective distributions for plan years beginning on or after January 1, 2008.* Except as otherwise provided in this paragraph (b)(2)(vi), for plan years beginning on or after January 1, 2008, a corrective distribution of excess aggregate contributions (and allocable income) is includible in the employee's gross income in the taxable year of the employee in which distributed. The portion of the distribution that is treated as an investment in the contract and is therefore not subject to tax under section 72 is determined without regard to any plan contributions other than those distributed as excess aggregate contributions. Regardless of when the corrective distribution is made, it is not subject to the early distribution tax of section 72(t). See paragraph (b)(4) of this section for additional rules relating to the employer excise tax on amounts distributed more than 2½ months (6 months in the case of a plan that includes an eligible automatic contribution arrangement within the meaning of section 414(w)) after the end of the plan year. See also § 1.402(c)–2, A–4 prohibiting rollover of distributions that are excess aggregate contributions.

(B) *Corrective distributions for plan years beginning before January 1, 2008.* The tax treatment of corrective distributions for plan years beginning before January 1, 2008, is determined under § 1.401(m)–2(b)(2)(vi) (as it appeared in the April 1, 2007, edition of 26 CFR Part 1). * * *

(4) * * *

(iii) *Special rule for eligible automatic contribution arrangements.* In the case of a plan that includes an eligible automatic contribution arrangement (within the meaning of section 414(w)), 6 months is substituted for 2½ months in paragraph (b)(4)(i) of this section.

* * * * *

Par. 10. Section 1.401(m)–3 is amended by:

1. Revising paragraph (a).

2. Revising the first sentences of paragraphs (f)(1) and (j)(3).

The additions and revisions to read as follows:

§ 1.401(m)–3 Safe harbor requirements.

(a) *ACP test safe harbor*—(1) *Section 401(m)(11) safe harbor.* Matching contributions under a plan satisfy the ACP safe harbor provisions of section 401(m)(11) for a plan year if the plan satisfies the safe harbor contribution requirement of paragraph (b) or (c) of this section for the plan year, the limitations on matching contributions of paragraph (d) of this section, the notice requirement of paragraph (e) of this section, the plan year requirements of paragraph (f) of this section, and the additional rules of paragraphs (g), (h) and (j) of this section, as applicable.

(2) *Section 401(m)(12) safe harbor.* For a plan year beginning on or after January 1, 2008, matching contributions under a plan satisfy the ACP safe harbor provisions of section 401(m)(12) for a plan year if the matching contributions are made with respect to a qualified automatic contribution arrangement described in paragraph § 1.401(k)–3(j) that satisfies the safe harbor requirements of § 1.401(k)–3, the limitations on matching contributions of paragraph (d) of this section, the notice requirement of paragraph (e) of this section, the plan year requirements of paragraph (f) of this section, and the additional rules of paragraphs (g), (h) and (j) of this section, as applicable.

(3) *Requirements applicable to safe harbor contributions.* Pursuant to sections 401(k)(12)(E)(ii) and 401(k)(13)(D)(iv), the safe harbor contribution requirement of paragraph (b) or (c) of this section, and § 1.401(k)–3(k) must be satisfied without regard to section 401(l). The contributions made under paragraphs (b) and (c) of this section, and § 1.401(k)–3(k) are referred to as safe harbor nonelective contributions and safe harbor matching contributions.

* * * * *

(f) *Plan year requirement*—(1) *General rule.* Except as provided in this paragraph (f) or in paragraph (g) of this section, a plan will fail to satisfy the requirements of section 401(m)(11), section 401(m)(12), and this section unless plan provisions that satisfy the rules of this section are adopted before the first day of that plan year and remain in effect for an entire 12-month plan year. * * *

* * * * *

(j) * * *

(3) *Early participation rules.* Section 401(m)(5)(C) and § 1.401(m)–2(a)(1)(iii)(A), which provide an alternative nondiscrimination rule for certain plans that provide for early participation, do not apply for purposes of section 401(m)(11), section 401(m)(12), and this section. * * *

* * * * *

Par. 11. Section 1.402(c)–2, A–4 is amended by redesignating paragraph (i) as (j) and adding a new paragraph (i) to read as follows:

§ 1.402(c)–2 Eligible rollover distributions, questions and answers.

* * * * *

A–4 * * *

(i) A distribution that is a permissible withdrawal from an eligible automatic contribution arrangement within the meaning of section 414(w).

* * * * *

Par. 12. Section 1.411(a)–4 is amended by revising paragraph (b)(7) to read as follows:

§ 1.411(a)–4 Forfeitures, suspensions, etc.

* * * * *

(b) * * *

(7) *Certain matching contributions.* A matching contribution (within the meaning of section 401(m)(4)(A) and § 1.401(m)–1(a)(2)) is not treated as forfeitable even if under the plan it may be forfeited under § 1.401(m)–2(b)(1) because the contribution to which it relates is treated as an excess contribution (within the meaning of § 1.401(k)–2(b)(2)(ii) and 1.401(k)–6), excess deferral (within the meaning of § 1.402(g)–1(e)(1)(iii)), excess aggregate contribution (within the meaning of § 1.401(m)–5), or default elective contributions (within the meaning of § 1.414(w)–1(e)) that are withdrawn in accordance with the requirements of § 1.414(w)–1(c).

Par. 13. Section 1.414(w)–1 is added to read as follows:

§ 1.414(w)–1 Permissible Withdrawals from Eligible Automatic Contribution Arrangements.

(a) *Overview.* Section 414(w) provides rules under which certain employees are permitted to elect to make a withdrawal from an eligible automatic contribution arrangement. This section sets forth the rules applicable to permissible withdrawals from an eligible automatic contribution arrangement within the meaning of section 414(w). Paragraph (b) of this section defines an eligible automatic contribution arrangement. Paragraph (c) of this section describes a permissible withdrawal and addresses which employees are eligible to elect a withdrawal, the timing of the withdrawal election, and the amount of the withdrawal. Paragraph (d) of this section describes the tax and other consequences of the withdrawal. Paragraph (e) of this section includes the definitions applicable to this section.

(b) *Eligible automatic contribution arrangement*—(1) *In general.* An eligible automatic contribution arrangement is

an automatic contribution arrangement under an applicable employer plan that, for the plan year, satisfies the uniformity requirement under paragraph (b)(2) of this section, the notice requirement under paragraph (b)(3) of this section, and the default investment requirement under (b)(4) of this section.

(2) *Uniformity requirement.* An eligible automatic contribution arrangement must provide that the default elective contribution is a uniform percentage of compensation. An arrangement does not violate the uniformity requirement of this paragraph (b)(2) merely because the percentage varies in a manner that is permitted under § 1.401(k)–3(j)(2)(iii), except that the rules of §§ 1.401(k)–3(j)(2)(iii)(A) and 1.401(k)–3(j)(2)(iii)(B) are applied without regard to whether the arrangement is intended to be a qualified automatic contribution arrangement.

(3) *Notice requirement*—(i) *General rule.* The notice requirement of this paragraph (b)(3) is satisfied for a plan year if each eligible employee is given notice of the employee's rights and obligations under the arrangement. The notice must be sufficiently accurate and comprehensive to apprise the employee of such rights and obligations, and be written in a manner calculated to be understood by the average employee to whom the arrangement applies. The notice must be in writing, however, see § 1.401(a)–21 for rules permitting the use of electronic media to provide applicable notices.

(ii) *Content requirement.* The notice must include the provisions found in § 1.401(k)–3(d)(2)(ii) to the extent those provisions apply to the arrangement. A notice is not considered sufficiently accurate and comprehensive unless the notice accurately describes—

(A) The level of elective contributions which will be made on the employee's behalf if the employee does not make an affirmative election;

(B) The employee's rights to elect not to have default elective contributions made to the plan on his or her behalf or to have a different percentage of compensation or amount of elective contributions made to the plan on his or her behalf;

(C) How contributions made under the arrangement will be invested in the absence of any investment election by the employee; and

(D) The employee's rights to make a permissible withdrawal, if applicable, and the procedures to elect such a withdrawal.

(iii) *Timing*—(A) *General rule.* The timing requirement of this paragraph (b)(3)(iii) is satisfied if the notice is provided within a reasonable period before the beginning of each plan year (or, in the year an employee becomes an eligible employee, within a reasonable period before the employee becomes an eligible employee). In addition, a notice satisfies the timing requirements of paragraph (b)(3) of this section only if it is provided sufficiently early so that the employee has a reasonable period of time after receipt of the notice and before the first elective contribution is made under the arrangement to make the election described under paragraph (b)(ii)(A) of this section.

(B) *Deemed satisfaction of timing requirement.* The timing requirement of this paragraph (b)(3)(iii) is satisfied if at least 30 days (and no more than 90 days) before the beginning of each plan year, the notice is given to each eligible employee for the plan year. In the case of an employee who does not receive the notice within the period described in the previous sentence because the employee becomes an eligible employee after the 90th day before the beginning of the plan year, the timing requirement is deemed to be satisfied if the notice is provided no more than 90 days before the employee becomes an eligible employee (and no later than the date the employee becomes an eligible employee).

(4) *Default investment requirement.* To the extent the plan is subject to Title I of ERISA, default elective contributions under an eligible automatic contribution arrangement must be invested in accordance with regulations prescribed by the Secretary of Labor under section 404(c)(5) of ERISA.

(c) *Permissible withdrawal*—(1) *In general.* If the plan provides, any employee who has default elective contributions made under the eligible automatic contribution arrangement may elect to make a withdrawal of such contributions (and earnings attributable thereto) in accordance with the requirements of this paragraph (c). An applicable employer plan that includes an eligible automatic contribution arrangement will not fail to satisfy the prohibition on in-service withdrawals under sections 401(k)(2)(B), 403(b)(7), 403(b)(11), or 457(d)(1) merely because it permits withdrawals that satisfy the timing requirement of paragraph (c)(2) of this section and the amount requirement of paragraph (c)(3) of this section.

(2) *Timing.* The election to withdraw default elective contributions must be made no later than 90 days after the date of the first default elective contribution under the eligible automatic contribution arrangement. The date of the first default elective contribution is the date that the compensation that is subject to the cash or deferred election would otherwise have been included in gross income. The effective date of an election described in this paragraph (c)(2) cannot be later than the last day of the payroll period that begins after the date the election is made.

(3) *Amount of distributions*—(i) *In general.* A distribution satisfies the requirement of this paragraph (c)(3) if the distribution is equal to the amount of default elective contributions made under the eligible automatic contribution arrangement through the effective date of the election described in paragraph (c)(2) of this section (adjusted for allocable gains and losses to the date of distribution). If default elective contributions are separately accounted for in the participant's account, the amount of the distribution will be the total amount in that account. However, if default elective contributions are not separately accounted for under the plan, the amount of the allocable gains and losses will be determined under rules similar to those provided under § 1.401(k)–2(b)(2)(iv) for the distribution of excess contributions.

(ii) *Fees.* The distribution amount as determined under this paragraph (c)(3) may be reduced by any generally applicable fees. However, the plan may not charge a different fee for a distribution under section 414(w) than applies to other distributions.

(d) *Consequences of the withdrawal*—(1) *Income tax consequences*—(i) *Year of inclusion.* The amount of the withdrawal is includible in the eligible employee's gross income for the taxable year in which the distribution is made. However, the portion of the distribution consisting of designated Roth contributions is not included in an employee's gross income a second time. The portion of the withdrawal that is treated as an investment in the contract is determined without regard to any plan contributions other than those distributed as withdrawal default elective contributions.

(ii) *No additional tax on early distributions from qualified retirement plans.* The withdrawal is not subject to the additional tax under section 72(t).

(iii) *Reporting.* The amount of the withdrawal is reported on Form 1099–R, Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc., as described in the applicable instructions.

(2) *Forfeiture of matching contributions.* In the case of any withdrawal made under paragraph (c) of

this section, employer matching contributions with respect to the amount withdrawn must be forfeited.

(3) *Consent rules.* A withdrawal made under paragraph (c) of this section may be made without regard to any notice or consent otherwise required under section 401(a)(11) or 417.

(e) *Definitions.* Unless indicated otherwise, the following definitions apply for purposes of section 414(w) and this section.

(1) *Applicable employer plan.* An applicable employer plan means a plan that—

(i) Is qualified under section 401(a);

(ii) Satisfies the requirements of section 403(b); or

(iii) Is a section 457(b) eligible governmental plan described in § 1.457–2(f).

(2) *Automatic contribution arrangement.* An automatic contribution arrangement means an arrangement that provides for a cash or deferred election that provides that in the absence of an eligible employee's affirmative election, a default election applies under which the employee is treated as having elected to have default elective contributions made on his or her behalf under the plan. This default election ceases to apply with respect to an employee if the employee makes an affirmative election (that remains in effect) to—

(i) Not have any default elective contributions made on his or her behalf; or

(ii) Have default elective contributions made in a different amount or percentage of compensation.

(3) *Default elective contributions.* Default elective contributions means contributions made at a specified level or amount under an automatic contribution arrangement that are—

(i) Contributions described in section 402(g)(3)(A) or 402(g)(3)(C); or

(ii) Contributions made pursuant to a cash or deferred election within the meaning of section 457(b)(4) where the contributions are under a section 457(b) eligible governmental plan.

(4) *Eligible employee.* An eligible employee means an employee who is eligible to make a cash or deferred election under the plan.

(f) *Effective date.* Section 414(w) and this section apply to plan years beginning on or after January 1, 2008.

* * * * *

PART 54—EXCISE TAXES. PENSIONS, REPORTING AND RECORDKEEPING REQUIREMENTS

Par. 14. The authority citation for part 54 continues to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Par. 15. Section 54.4979–1(c)(1) is amended by:

Revising the first and second sentences of paragraph (c)(1) to read as follows:

§ 54.4979–1 Excise tax on certain excess contributions and excess aggregate contributions.

* * * * *

(c) *No tax when excess distributed within 2½ months of close of year or additional employer contributions made*—(1) *General rule.* No tax is imposed under this section on any excess contribution or excess aggregate contribution, as the case may be, to the extent the contribution (together with any income allocable thereto) is corrected before the close of the first 2½ months of the following plan year (6 months in the case of a plan that includes an eligible automatic contribution arrangement within the meaning of section 414(w)). Qualified nonelective contributions and qualified matching contributions taken into account under § 1.401(k)–2(a)(6) of this Chapter or qualified nonelective contributions or elective contributions taken into account under § 1.401(m)–2(a)(6) of this Chapter for a plan year may permit a plan to avoid excess contributions or excess aggregate contributions, respectively, even if made after the close of the 2½ month period (6 months in the case of a plan that includes an eligible automatic contribution arrangement within the meaning of section 414(w)). * * *

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Linda E. Stiff,

Deputy Commissioner for Services and Enforcement.

[FR Doc. E7–21821 Filed 11–7–07; 8:45 am]

BILLING CODE 4830–01–P

DEPARTMENT OF THE INTERIOR

Minerals Management Service

30 CFR Part 250

Notice of Public Workshop To Discuss the Possible Need for Suspension of Operations Specifically Related to High Pressure or High Temperature Equipment

AGENCY: Minerals Management Service (MMS), Interior.

ACTION: Notice of Public Workshop.

SUMMARY: The MMS will hold a workshop to discuss the possible need to develop a new regulation allowing for a Suspension of Operations, specifically related to high pressure or high temperature equipment needed for safe drilling, completion, or production operations. This Suspension of Operations would allow for an extension of a lease when the modification of existing technology is considered necessary in order to operate in frontier areas due to unexpected high temperatures or high pressures encountered on your lease. This type of Suspension of Operations would not apply to the initial design, development, or manufacturing of new technology.

Workshop Date: January 23, 2008, beginning at 9 a.m.

*Workshop Location:*The workshop will be held at the Gulf of Mexico Regional Office, Minerals Management Service, Room 111, 1201 Elmwood Park Boulevard, New Orleans, Louisiana 70123–2394. All interested parties are invited to attend.

FOR FURTHER INFORMATION CONTACT: Carole Danos, MMS, Gulf of Mexico Outer Continental Shelf Region, Office of Production and Development, 1201 Elmwood Park Blvd., MS 5300, New Orleans, Louisiana 70123–2394, e-mail: *carole.danos@mms.gov,* telephone (504) 736–2675.

SUPPLEMENTARY INFORMATION: The MMS received requests from industry to consider a procedure to grant lease extensions in order to develop new technology which may lead to the production of hydrocarbons. The MMS will hold a workshop to gain additional insight from industry to help determine whether such suspensions would be warranted. Also to be discussed are the accompanying data and information that would be submitted to validate a request for a lease extension.

Background: Regulations governing the granting of Suspensions of Production (SOP) and Suspensions of Operations (SOO) are found at 30 CFR 250.168–177. Our current regulations allow MMS to issue SOOs for the following reasons:

- When necessary to comply with judicial decrees (see § 250.172(a)).
- When activities pose a threat or harm to life, environment, or mineral deposits (see § 250.172(b)).
- For installation of safety or environmental equipment (see § 250.172(c)).
- When necessary to carry out NEPA requirements (see § 250.172(d)).
- When inordinate delays are encountered in obtaining required permits or consents (see § 250.172(e)).
- You fail to comply with a law, regulation, order, or lease provision (see § 250.173(a)).