

month requirement by following the rule in Notice 98–52 that allowed a short plan year in the first plan year and would allow a short plan year in certain other circumstances. Specifically, a section 401(k) safe harbor plan could have a short plan year in the year the plan terminates, if the plan termination is in connection with a merger or acquisition involving the employer, or the employer incurs a substantial business hardship comparable to a substantial business hardship described in section 412(d). In addition, a section 401(k) safe harbor plan could have a short plan year if the plan terminates, the employer makes the safe harbor contributions for the short year, employees are provided notice of the change, and the plan passes the ADP test. Finally, a safe harbor plan could have a short plan year if it is preceded and followed by 12-month plan years as a section 401(k) safe harbor plan.

Under section 401(k)(12)(F), safe harbor contributions are permitted to be made to a plan other than the plan that contains the CODA. These proposed regulations reflect that rule and provide that the plan to which the safe harbor contributions are made need not be a plan that can be aggregated with the plan that contains the cash or deferred arrangement.

Whether a contribution is taken into account for purposes of the safe harbor is determined in accordance with the rules regarding inclusion in ADP testing under proposed § 1.401(k)–2(a). Thus, for example, a plan that provides for safe harbor matching contributions in 2006 need not provide for a matching contribution with respect to an elective contribution made during the first 2½ months of 2007 and attributable to service during 2006, unless that elective contribution is taken into account for 2006.

6. SIMPLE 401(k) Plans

Pursuant to section 401(k)(11), a SIMPLE 401(k) plan is treated as satisfying the requirements of section 401(k)(3)(A)(ii) if the contribution, vesting, notice and exclusive plan requirements of section 401(k)(11) are satisfied. Section 1.401(k)–4 of these proposed regulations reflects the provisions of section 401(k)(11) in a manner that follows the positions reflected in the model amendments set forth in Rev. Proc. 97–9.

7. Matching Contributions and Employee Contributions

Section 401(m)(2) sets forth a nondiscrimination test, the ACP test, with respect to matching contributions and employee contributions that is

parallel to the nondiscrimination test for elective contributions set forth in section 401(k). Section 1.401(m)–1 of the proposed regulations would set forth this test in a manner that is consistent with the nondiscrimination test set forth in proposed § 1.401(k)–1(b). Thus, satisfaction of the ACP test, the ACP safe harbor or the SIMPLE 401(k) provisions of the proposed regulations under section 401(k) are the exclusive means that matching contributions and employee contributions can use to satisfy the nondiscrimination in amount of contribution requirements of section 401(a)(4). An anti-abuse provision comparable to that provided in connection with the proposed regulations under section 401(k) limits the ability of an employer to make repeated changes in plan provisions or testing procedures that have the effect of distorting the ACP so as to increase significantly the permitted ACP for HCEs, or otherwise manipulate the nondiscrimination rules of section 401(m), if a principal purpose of the changes was to achieve such a result.

These proposed regulations also include provisions regarding plan aggregation and disaggregation that are similar to those proposed for CODAs under section 401(k). For example, matching contributions made under the portion of a plan that is an ESOP and the portion of the same plan that is not an ESOP would not be disaggregated under these proposed regulations.

The definitions of matching contribution and employee contribution under § 1.401(m)–1 of the proposed regulations would generally follow the definitions in the existing regulations. Thus, whether an employer contribution is on account of an elective deferral or employee contribution—and thus is a matching contribution—is determined based on all the relevant facts and circumstances. However, the proposed regulations would provide that a contribution would not be treated as a matching contribution on account of an elective deferral if it is contributed before the employee's performance of services with respect to which the elective deferral is made (or when the cash that is subject to the cash or deferred election would be currently available, if earlier) and an employer contribution is not a matching contribution made on account of an employee contribution if it is contributed before the employee contribution. Thus, under these regulations, an employer would not be able to prefund matching contributions to accelerate the deduction for those contributions and, as noted above with respect to the timing of elective

contributions, employer contributions made under the facts in Notice 2002–48 would not be taken into account under the ACP test and would not satisfy any plan requirement to provide matching contributions.

8. ACP Test for Matching Contributions and Employee Contributions

Section 1.401(m)–2 of the proposed regulations would provide rules for the ACP test that generally parallel the rules applicable to the ADP test in proposed § 1.401(k)–2. Thus, for example, the ACP test may be run by comparing the ACP for eligible HCEs for the current year with the ACP for eligible NHCEs for either the current plan year or the prior plan year. Similarly, the proposed regulations reflect the special ACP testing rule in section 401(m)(5)(C) for a plan that provides for early participation, comparable to the special ADP testing rule in section 401(k)(3)(F), as set forth in proposed § 1.401(k)–2(a)(1)(iii).

The determination of the actual contribution ratio (ACR) for an eligible employee, and the contributions that are taken into account in determining that ACR, under these proposed regulations are comparable to the rules under the proposed section 401(k) regulations. Thus, for example, the ACR for an HCE who has matching contributions or employee contributions under two or more plans is determined by adding together matching contributions and employee contributions under all plans of the employer during the plan year of the plan being tested, in a manner comparable to that for determining the ADR of an HCE who participates in two or more CODAs.

The proposed regulations would retain the rule from the existing regulations under which a QMAC that is taken into account in the ADP test is excluded from the ACP test. In addition, the proposed regulations would continue to allow QNECs to be taken into account for ACP testing, but would provide essentially the same restrictions on targeting QNECs to a small number of NHCEs as is provided in proposed § 1.401(k)–2. The only difference in the rules would be that the contribution percentages used to determine the lowest contribution percentage would be based on the sum of the QNECs and those matching contributions taken into account in the ACP test, rather than the sum of the QNECs and the QMACs taken into account under the ADP test. Because QNECs that do not exceed 5% are not subject to the limits on targeted QNECs under either the ADP test or the ACP test, an employer is permitted to take into account up to 10% in QNECs