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Qualified Automatic Contribution Arrangements

A qualified automatic contribution arrangement (QACA) is an automatic enrollment and contribution program with safe harbor provisions that exempt 401(k) plans from certain testing. Such programs allow eligible employees to be treated as having enrolled in the plan and elected the amount specified by the plan, unless the employee makes an affirmative election to opt out or change the contribution amount.

Benefits

QACAs were created as part of the Pension Protection Act of 2006 with the goal of encouraging increased participation in retirement plans. The Act provides several incentives for this type of program. As an alternative safe harbor plan, QACAs automatically satisfy the top-heavy and nondiscrimination testing requirements. In addition, required employer contributions may be less expensive than those of a traditional 401(k) safe harbor plan. This is a key advantage because it allows employers to reduce contribution costs while still qualifying for safe harbor relief.

Requirements

To qualify as a QACA, the plan must satisfy certain requirements, which include:

- **Employee minimum contributions**. The minimum deferral rate is 3% of compensation. Rates must increase 1% each year, such that by the fourth year, the contribution is 6% of compensation. Contributions must not exceed 10%.
- **Employer minimum contributions**. Employers have two matching options. The first requires a matching contribution of 100% of an employee's contribution up to 1% of compensation, and a 50% matching contribution for the employee's contributions above 1% and up to 6% of compensation. The second requires a nonelective contribution of 3% of compensation to all participants, including those who choose not to contribute to the plan.
- **Vesting**. The employer minimum contribution must be 100% vested by the time an employee completes two years of service.
- **Eligibility**. The automatic enrollment features must apply to all employees eligible to defer, except those who are currently deferring or those with a previously completed election, including an election of 0%.
- **Notice**. Within a reasonable period of time prior to eligibility, plan sponsors must provide an initial notice to all eligible employees explaining the employee's right to opt out or change their deferral percentage, as well as the type and amount of the employer's contribution. With immediate eligibility, notice must be provided prior to the pay date for the payroll period that includes the date the employee becomes eligible. Annual notices of employees' rights are required between 30 and 90 days prior to the beginning of each plan year.
- **Timing**. The arrangement must generally start at the beginning of the plan year and must remain in effect for the entire 12-month plan year.

Next Steps

Evaluate the costs and benefits of a QACA against the current plan to determine whether a QACA would be beneficial. Because a QACA must be implemented at the beginning of the plan year, plan sponsors interested in this plan design must allow for enough time to amend plan documents and to satisfy the notice requirements.

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