

Safe Harbor 401(k) Guide for Your Small Business

Getting ready to offer a 401(k) retirement plan to your employees? Way to go!

Offering a 401(k) plan comes with added responsibilities. One of these tasks is making sure your plan is run fairly, and that everyone has the opportunity to fully participate.

Contributing to a 401(k) comes with significant tax advantages, so the government wants to make sure your plan doesn't unfairly benefit the company owners and the highest earners. This means that means every 401(k) comes with mandatory compliance testing.

There are three annual tests given by the IRS to make sure your plan is run fairly and benefits everyone—not just the people at the top. (These groups of high earners are referred to in the IRS world as “highly compensated employees” or “HCE”s.)

The Actual Deferral Percentage (ADP) Test:

This limits the percentage of compensation that HCEs can defer into their 401(k) based on the average contribution rates of the non-highly paid employees. This is the test that is most likely to impact small business plans.

The Actual Contribution Percentage (ACP) Test:

This ensures that the employer matching contributions and any after-tax employee contributions contributed for HCEs are not disproportionately higher as compared to non-highly paid employees.

The Top-Heavy Test:

This ensures that “Key employees” cumulatively hold less than 60% of the total plan balance. Key employees are identified through a number of factors including ownership status, officer status, and compensation.

In essence, ADP and ACP testing both make sure your plan doesn't unfairly benefit HCEs, while the top-heavy test ensures they aren't the main people contributors to your plan.

Skip the hassle with Safe Harbor 401(k)

With a Safe Harbor plan, you generally don't have to worry about the most common compliance tests. How does this happen? In exchange for getting an automatic pass on the ADP and ACP tests and the extra administrative duties that go with the testing process, business owners must make a minimum contribution to the plan each year—which must be immediately 100% vested.

By contributing on behalf of your employees, you ensure everyone benefits fairly from the plan.

Even better, those employer contributions are tax-deductible.

What happens if you fail a test:

If you fail a compliance test, you will be given instructions to correct it; however, failures can be expensive in terms of IRS penalty fees and the time spent trying to correct any problems.

In short, don't fail your compliance test if you can help it.

With a Safe Harbor plan, the employer can contribute in one of three ways:



You provide a mandatory match of 100% (dollar for dollar) on the first 3% of compensation contributed by employees, plus a 50% match on the next 2% of compensation contributed by employees.



You provide a mandatory match of 100% (dollar for dollar) on contributions of up to 4% (you can match up to 6%) of compensation contributed by employees.



You commit to a mandatory contribution of at least 3% of total compensation for all employees that meet the plan's eligibility rules, regardless of whether or not they contribute to the plan.

Are there Safe Harbor deadlines?

If you are starting a brand new 401(k) plan and want to have Safe Harbor take effect in the current calendar year, your plan must be fully set up and active by October 1, 2019.

Keep in mind, designing a plan to suit your needs (along with all associated admin tasks) takes time. This means that the very latest you should be finalizing your plan is September 20, 2019.



Is Safe Harbor right for my business?

A Safe Harbor 401(k) can seem like an obvious choice—especially if you're a small business with a significant compensation gap among employees. But, it may not be the best option for every option.

Luckily, our retirement experts at Ubiquity can walk you through the plan design options and the setup process to make sure your retirement plan is designed to fit perfectly to your needs.

Call us at **855.787.8202** or go to myubiquity.com/safe-harbor-free-consultation to schedule your consultation.