

# SAFE HARBOR 401(K) PLANS

## A Powerful Retirement Solution

The IRS added the safe harbor option in an effort to reduce the burden of compliance with the nondiscrimination tests on contributions which are made to 401(k) plans. Plans that elect to use one of the safe harbor rules are “deemed” to satisfy the nondiscrimination tests for Salary Deferral and Employer Matching Contributions (ADP & ACP tests).

In order to be a safe harbor plan the employer must elect one of the safe harbor options at least 30 days before the beginning of the plan year for which it applies. Each plan participant is provided a notice that explains the selection of the safe harbor option. All safe harbor contributions are fully vested when made.

The Employer **must elect one** of the following safe harbor options:

1. The **first contribution option** is a nonelective contribution. The employer is required to make a contribution of 3% of pay on behalf of **each eligible participant**. This contribution is made without regard to whether the employee defers from their pay. (If the Employer wishes they can elect to make the contribution to only the non-highly paid participants.) Compensation means the total compensation earned and may not exclude bonuses, commissions, etc.
2. The **second contribution option** is a matching contribution. The employer makes a matching contribution on behalf of each participant that is equal to:
  - \$1 for each \$1 deferred up to 3 percent of the employee’s compensation;
  - \$.50 on each \$1 on deferrals between 3-5% of pay.

Therefore the matching contribution is:

### Deferral Rate

- 1-3%
- 3-5%
- 5% or more

### Match

- Match equals the deferral
- 3% of pay plus ½ of rate between 3-5%
- 4% of pay

*(Example - if 4% Deferral then match = 3% +(1/2\*1%) or 3.5% of pay)*

Most Employers use a simplified match of \$1 for \$1 up to 4% of pay.

If the Employer wishes they can elect to make the match only to the non-highly paid participants. Compensation means the total compensation earned and may not exclude bonuses, commissions, etc.

Please note that each year the compensation that is used to calculate benefits is capped. For 2018, the maximum compensation limit is \$270,000.

- Therefore, you will never have a match greater than 4% of pay, and you should not match pay that exceeds \$275,000 (2018 limit)- so if someone’s pay =\$300,000 you would cap the pay at \$275,000 and the max match would be (275,000 X .04=11,000)
- Therefore, you will never have a non-elective contribution greater than 3% of pay so if someone’s pay =\$300,000 you would cap the pay at \$275,000 and the max non-elective would be (275,000 X .03=\$8,250)

If the plan is top heavy (see top heavy explanation piece) and no profit sharing contribution is made for a year the top heavy minimum contribution requirements will be met.