

401K Safe Harbors Work for Small Business

This chapter will examine the history, the present and the future of 401(k) safe harbors.

The technical rules governing 401(k) safe harbors will be explained in detail and some flexible, yet simple, small business 401(k) safe harbor plan designs will be analyzed.

THE GENESIS OF THE 401(k) SAFE HARBORS

Stay clear of 401(k) plans! This was the advice given to small businesses not so long ago. They were considered too complicated and costly for a small company. Clearly, a small business could not properly administer a 401(k) plan by itself. The amount of 401(k) contributions that could be made by the highly compensated employees ("HCEs") was dependent upon the amount contributed by the non-highly compensated employees ("NHCEs") calculated under a formula set forth in Section 401(k) of the Internal Revenue Code ("IRC"). Because of the complexities inherent in performing the anti-discrimination tests imposed by Section 401(k) and the regulations thereunder, (referred to as the "ADP tests"), a competent third party administrator was virtually required if the plan was to be kept in operational conformity with the law.

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