# 401(k) Plan Basics

Navigating the basics of 401(k) plans, and the roles and responsibilities of plan providers



FISHER INVESTMENTS®
401(k) SOLUTIONS

# What we'll cover in this course

1. Advantages of a 401(k) Plan
2. 401(k) Plan Providers
3. Features of a 401(k) Plan

# 401(k) Plans

Lots of retirement plan types out there, but 401(k) plans are the most common and most flexible, that is what we will focus on today

**Flexibility**

| | 401(k) | Solo 401(k) | SIMPLE IRA | SEP IRA |
|---|---|---|---|---|
| Contribution Limit | $73,500[1] | $73,500[1] | $19,000[1] | $66,000 |
| Can Favor Key Employees | Yes | NA | No | No |
| Employee Exclusions | Yes | NA | No[2] | No[2] |
| Roth Allowed | Yes | Yes | No | No |
| Loans Allowed | Yes | Yes | No | No |
| Vesting Allowed | Yes | NA | No | No |

[1]Assumes age 50 or older.
[2]For example, a 401(k) enables employers to exclude part-time and seasonal employees; a SIMPLE IRA allows exclusion of employees who make less than $5,000/yr.

# Part I:

## Advantages of a 401(k) Plan

# Advantages of a 401(k) Plan

### Retirement Savings

Some plans allow contributions of up to $73,500/year. These assets grow tax-deferred until retirement age.

### Tax Advantages

Contributions lower taxable income today, and grow tax-deferred. Some plans also allow Roth contributions. Plan expenses, including employer contributions, are tax-deductible business expenses.

### Attract & Retain Employees

81% of workers agree that, all else being equal, the retirement benefits offered by an employer would be a major factor in deciding to take a job.*

### Tax Credit

Up to 100% of annual plan costs can be offset by a tax credit for businesses that start a retirement plan. The credit amount is up to $5,000 per year + up to $1,000 per eligible employee for the first five years.

*2019 TransAmerica Retirement Survey

# Part II:

## Plan Providers

# 401(k) Plan Providers

**Recordkeeper**

- Website
- Contribution Types
- Statements

**Third-Party Administrator**

- Form 5500
- Plan Document
- Compliance Testing

**Plan Advisor**

- Investments
- Employee Education
- Sponsor Support
- Vendor Management Support

**Plan Sponsor**

- Administer the plan consistent with the Plan Document
- Monitor Service Providers
- Make prudent decisions on behalf of the plan participants

# Plan Fiduciaries

A **401(k) Plan Fiduciary** is somebody who makes decisions on behalf of the 401(k) plan (the plan sponsor, for example). A fiduciary is legally obligated to act solely in the best interest of the plan and its participants.

**Why it matters:**
If the sponsor fails to uphold their fiduciary responsibility, they may be personally liable for losses.

**Some fiduciary roles can be delegated:**

<table>
<tr><th colspan="2">Investment Fiduciaries</th><th>Administrative Fiduciary</th></tr>
<tr><td colspan="2">Can be delegated to the Plan Advisor</td><td>Can be delegated to the TPA or bundled Recordkeeper</td></tr>
<tr><td>3(38) Investment Manager</td><td>3(21) Investment Plan Advisor</td><td>3(16) Administrator</td></tr>
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# Investment Fiduciaries

**3(21) Investment Plan Advisor:** A co-fiduciary who doesn't have full legal responsibility for investment-related plan decisions.

**3(38) Investment Manager:** A full fiduciary who takes full legal responsibility for all investment-related plan decisions.

| Task | Who is Responsible | | |
|---|---|---|---|
| | No Outsourcing | 3(21) | 3(38) |
| **Create Investment Lineup** | Plan Sponsor | Plan Sponsor and Plan Advisor | Plan Advisor |
| **Monitor & Update Investments** | Plan Sponsor | Plan Sponsor and Plan Advisor | Plan Advisor |
| **Legally Responsible for plan Investment-Related Decisions** | Plan Sponsor | Plan Sponsor and Plan Advisor | Plan Advisor |

# Administrative Fiduciaries

**3(16) Plan Administrator:** A co-fiduciary who takes legal responsibility for some of the administrative tasks within a 401(k) plan.

**Different levels of 3(16) providers, based on the tasks they take on:**

| 3(16) Lite |
|---|
| Participant Notice Delivery |
| $ |

| 3(16) Medium |
|---|
| Participant Notice Delivery |
| Sign & File Form 5500 |
| Loan/Distribution Approval |
| $$ |

| 3(16) Full |
|---|
| Participant Notice Delivery |
| Sign & File Form 5500 |
| Loan/Distribution Approval |
| Named Fiduciary in Plan Docs |
| Oversight of Timely Remittance of Employee Contributions |
| $$$ |

# Part III:

## Plan Features

# Plan Features

- Outlined in the Plan Document, Adoption Agreement, and Summary Plan Description
- Plan Sponsor must administer the plan consistent with the features outlined in the Plan Document
- The Third-Party Administrator (TPA) or bundled recordkeeper typically writes and maintains the Plan Document
- To change plan features the Plan Document typically must be amended (by the TPA or bundled recordkeeper)

# Eligibility

| | |
|---|---|
| **What it is** | Eligibility determines who is allowed to participate in the 401(k) plan |
| **How it Works** | Eligibility can be limited by:<br>• Age (up to age 21)<br>• Service (up to 12 months of service)<br>• Annual Hours (up to 1000 hours)<br>• Employee type (leased employees, union employees, etc) |
| **Why it Matters** | Limiting eligibility can reduce cost and administrative burden. For example, a company with high turnover may consider maximum eligibility parameters to minimize temporary employees with a small balance in the plan |

# Employer Contributions

| Employer Match | Safe Harbor | Profit Sharing |
|---|---|---|
| • Company contributes, based on employee contribution<br>• Encourages participation<br>• Supports compliance testing | • Company agrees to provide a generous contribution/match to employees<br>• Immediate vesting<br>• Automatically pass most compliance testing<br>• Allows owners and HCEs to defer more | • Flexible and optional contribution<br>• Owners can increase deferrals<br>• Greater tax deduction |

# Employer Match

### % Match

**1**

**Employer matches employee contributions up to a certain percentage. For example, 100% match up to 3%.**

### $ Match

**2**

**Employer matches employee contributions up to a certain dollar amount. For example, 100% match up to $1000.**

### Stretched Match

**3**

**Employer matches a smaller percentage in order to incentive higher employee contributions. For example, 25% match up to $1000.**

## Why It Matters:

- Encourages employee contributions
- Many flexible options
- Tax-reducing business expense

# Safe Harbor

### Non-Elective Safe Harbor

**1**

- 3% AUTOMATIC employer contribution (no required employee contribution)

### Basic Safe Harbor Match

**2**

- 100% match for 3% of income
- 50% match on next 2%
- Employee must defer money to get the match!

### Enhanced Safe Harbor Match

**3**

- 100% match for 4% of income
- Employee must defer money to get the match!

## Why It Matters:

- Exempts the plan from most compliance testing
- Allows owners and HCEs to put away more money
- Non-Elective contributions count toward profit-sharing compliance testing



FI 401(k)

# Profit Sharing

**Pro-Rata**

**1**

The simplest and most common type. All employees must receive the same proportional amount, including the owner.

**New Comparability**

**2**

Allows for multiple benefit groups each with their own contribution rates, so owners can often receive a higher portion than non-owners.

**Age-Weighted**

**3**

Allows a business to allocate a higher percentage to older employees because they are closer to retirement; younger employees receive a smaller portion.

## Why It Matters:

- Substantial tax benefits
- Can allow the owner to maximize their retirement savings
- The most flexible type of employer contribution
- A way to attract and retain top talent

# Vesting Schedule

| | Immediate Vesting | Cliff Vesting | Graded Vesting |
|---|---|---|---|
| **What It Is** | Employee automatically gets 100% employer contribution | Employee goes from 0% → 100% vested after 3 years of employment | Employee earns gradual ownership of employer contribution (over a maximum 6 years) |
| **Why It Matters** | Expensive if high turnover! | Reward loyal employees, decrease turnover costs, encourage employee retention | Reward loyal employees, decrease turnover costs, encourage employee retention |

**Unvested assets, forfeited by terminated employees, can be used to off-set plan costs (including future employer contributions)**

# Roth Contributions

401(k) plans can allow for Roth contributions, regardless of income level. Some 401(k) plans even allow for **Backdoor Roth** and **Mega Backdoor Roth** options.

| | Traditional Contributions | Roth Contributions |
|---|---|---|
| **Contributions** | Made before tax | Made after tax |
| **Earnings** | Grow tax-deferred | Never taxed |
| **Withdrawals** | Taxed on current tax rate at retirement | Not taxed when used as retirement |

# Loans

| | |
|---|---|
| **What it is** | Loans are an optional feature in a 401(k) plan that can allow the plan participant to borrow against their balance in the plan. |
| **How it Works** | • No credit required<br>• Interest is typically prime rate (set by the Plan Document)<br>• Participant makes payments back to themselves in the plan every pay period |
| **Why it Matters** | Many employees enjoy this benefit because it gives them access to their funds in case of an emergency. However, borrowing against your retirement assets can reduce performance and hinder retirement savings goals. |

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# Questions?

Contact us with your questions at

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