**New Opportunities**

Tax law changes have greatly expanded and simplified the retirement plan world. Now, despite some administrative cost, a 401(k) plan may compare quite favorably to a SEP-IRA for a similar employer contribution. That’s because the owners may primarily rely on salary deferrals and secondarily add employer matching or profit sharing contributions until a participant reaches 100% of pay, not to exceed $57,000 (indexed limit for 2020). Those who are age 50 or above may also add “catch-up” contributions, if any legal or plan limitation is reached.

Salary deferrals may be either traditional pre-tax or after-tax using a “Qualified Roth Election” or both. The plans provided by Security Administrators, Inc. (SAI)—a wholly owned subsidiary of Security Mutual—can, upon request, include a Roth option so that you may achieve “tax-diversification” at retirement.

However, although you may desire to optimize the 401(k) plan by using profit-sharing and “safe harbor” contributions, consideration must be given to the employee benefit cost as well as some basic nondiscrimination issues.

**Some Issues**

Top Heavy. An issue that is very common in the small-business world is the “top heavy” concern. Once more than 60% of the plan assets attribute to the owners, or certain officers, the plan becomes “top heavy.” Although having more than 60% or more of the plan assets is often desired by the owners and other key employees, it may necessitate that the employer contribute at least 3% of salary to all the eligible employees, or the smallest percentage contributed for a key employee, if less.

**ADP Test**. Another issue for most 401(k) plans is that the amount of pre-tax salary deferrals that “highly compensated” employees (i.e., the owners, their family members and other high income participants) may save is dictated by the savings rate of the other employees. Although the rules are complex, these rules, as a percentage of pay, may be summarized as follows:

<table>
<thead>
<tr>
<th>Average Deferral Percentage (ADP)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-Highly Compensated</td>
</tr>
<tr>
<td>0%</td>
</tr>
<tr>
<td>1%</td>
</tr>
<tr>
<td>2%</td>
</tr>
<tr>
<td>3%</td>
</tr>
<tr>
<td>4%</td>
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<tr>
<td>6%</td>
</tr>
</tbody>
</table>

When designing a “Next Level” 401(k) plan, we offer three cutting-edge tools that can be used to craft the plan that best meets your goals and budget. These include:

1. Safe Harbor Nonelective
2. The Super 401(k)
3. The DASH 401(k)

The first tool is fully described in our “Safe Harbor” 401(k) companion brochure. This employer contribution must be granted each year, removes the need for the ADP test, and solves the “top heavy” concern.

The next two tools are based on the premise that a retirement plan can’t discriminate in favor of “highly compensated employees” in either contributions or benefits. As displayed in the exhibit below, this does not mean that everybody has to receive the same contribution...far from it.
### Cross-Tested Profit Sharing

Perhaps the most exciting development in pension plans, this “Next Level” design offers a method to allocate significantly different contributions to specific classes of employees. A contribution can’t discriminate in either contributions or benefits. Giving everybody 20% of pay is clearly nondiscriminatory. However, giving each the same theoretical retirement benefit is also nondiscriminatory. The reasoning is simple: with fewer years until retirement, older participants require larger contributions than younger participants to get to the same benefit level.

A Cross-tested Profit Sharing uses this age-weighted rule, but uses the weighted average age for members of specific classes to test the employer contribution for nondiscrimination. This technique works best whenever the highly compensated employees are at least 10 years older than the average rank-and-file employee. However, it might not benefit the owner if he or she is the same age or younger than the average employee.

This technique is highly customizable and can be matched to your business quite easily. For example, groups can be created for different profit centers, subsidiaries, sister companies or, most commonly, by job class—in short, any clearly identifiable group.

### Investment Options

Employer and employee contributions should be placed into an investment platform that is designed for 401(k) plans. Allowable investment options are selected by the Plan Trustees. Each eligible participant is typically given the ability to direct the investment of his or her own account by selecting from among the allowable options.

SAI’s 401(k) plan document allows substantial freedom. Suitable investments include mutual funds, group annuity contracts, life insurance, guaranteed interest contracts or combinations of all of the above.

Unlike most 401(k) plan documents offered through a mutual fund company, our 401(k) program can include an optional benefit that allows you to purchase cash value life insurance to protect your family should you not live to retirement. It may be a wise part of your asset allocation strategy.

When life insurance is purchased inside your Plan, the death benefit in excess of the cash surrender value will be paid to your beneficiaries free of ordinary income tax. Each year while the policy is in the Plan, you will pay income tax on the cost of the life insurance protection. Upon separation from service or retirement, the life insurance must be removed from the Plan. There are several options available to you at that time, each with its own advantages and tax consequences. These options are described in the brochure entitled “Beyond Retirement or Separation from Service.” Ask your financial professional for a copy.

### Common Class Definitions

<table>
<thead>
<tr>
<th>1. Owners</th>
<th>1. Executives</th>
</tr>
</thead>
<tbody>
<tr>
<td>2. Non-owners</td>
<td>2. Managers</td>
</tr>
<tr>
<td>3. All Others</td>
<td>3. All Others</td>
</tr>
</tbody>
</table>

Generally, the allocation to the top group can’t exceed three times the allocation to the bottom group. However, once you award at least 5% of pay to the bottom group, this ratio limit disappears.

### DASH 401(k) Plans

Perhaps our ultimate “Next Level” tool, as illustrated previously, is the Double Advantage Safe Harbor or “DASH 401(k)” design. This technique grants all eligible employees 3% of pay with immediate vesting and uses this non-elective safe harbor to eliminate the ADP test.

This nonelective contribution helps our super comparability testing algorithm by satisfying minimum gateway requirements and, along with other profit sharing contributions, may be used to efficiently reach the desired goal and budget whenever the members of the top groups are, on average, ten years older than the members of the bottom one.

It is important to note that the employer is making a 3% of pay commitment with immediate vesting to all eligible employees. Any profit sharing contributions beyond this minimum can be made at the sole discretion of the employer.

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