



# OVERCOMING COMMON ERRORS IN YOUR RETIREMENT PLAN

## Issue #1 - Bonus Compensation Deferral Elections

At MVP Plan Administrators, we want to bring pertinent information to our clients that they find useful and not be a waste of their time. Let's face it, we all have way too much going on today to add anything further to our plates. We get that. We also want to be as helpful as possible to everyone we work with.

With that being said, we have developed a series of informational emails and videos of the **BIGGEST ERRORS**, we see in the administration of retirement plans, that can be costly to the Plan Sponsor. In our opinion, withholding salary deferral elections on bonuses is one error we see most often for both 401k and 403b plans. If you are interested in knowing why, keep reading!

Bonus elections on deferrals in a 401(k) plan are an important consideration for plan sponsors, as they can have a significant impact on both employee contributions and the plan's compliance with regulatory requirements. Here's a breakdown of what plan sponsors need to understand about bonus elections on deferrals:

### 1. What Are Bonus Elections on Deferrals?

Bonus elections refer to the option where employees can choose to defer a portion or all their bonus payments into their salary deferral accounts. Typically, employers offer employees the opportunity to direct a percentage of their bonus to their 401(k) deferral, just as they would with their regular salary.

### 2. Plan Design Considerations

Employers have flexibility in designing the rules for how bonus deferrals are handled. Here are key elements that plan sponsors need to consider:

- **Plan Provisions:** If the plan DOES NOT exclude bonuses as a form of compensation in the plan, then participant salary deferral elections must be withheld from their bonus(es). Most commonly, the definition of compensation is W-2 wages or total gross wages. Your plan is most likely utilizing the MVP Sponsored Adoption Agreement, in which case the definition of compensation for your plan is found under Section 5 and will outline any exclusions from compensation.
- **Deferral Limits:** Employee contributions are subject to IRS annual limits for deferrals. For 2025, the deferral limit for an employee is \$23,500 (or \$31,000 if age 50 or older, and \$34,750 for those ages 60-63 due to the catch-up provision).
- **Timing of Contributions:** Bonus deferrals are generally considered in the year the bonus is paid, not when earned. However, the specific timing rules may depend on the plan's provisions. The deferrals withheld need to be paid in a timely manner to the plan as all regular contributions are, typically within a few days from when they were withheld.

### **3. Non-Discrimination Rules**

The IRS imposes non-discrimination rules to ensure that employer sponsored plans are equitable. These rules prevent highly compensated employees (HCEs) from benefiting disproportionately from deferral opportunities, including bonus deferrals. Plan sponsors need to ensure that bonus elections comply with these requirements to avoid potential penalties or plan disqualification.

### **4. Communication and Education**

Clear communication with employees is critical to ensure they understand how they can make bonus deferral elections and how those contributions will impact their overall retirement savings. This includes understanding the deferral limits, the impact on taxable income, and the potential for employer matching contributions. A separate deferral election on bonus is required to be completed **IF** the participant wants any other election other than their normal salary deferral election (including \$0 withheld), from each bonus.

### **5. Administrative Considerations**

The plan sponsor or plan administrator needs to have systems in place to manage bonus deferrals efficiently. This includes tracking the deferrals, ensuring the plan is not exceeding contribution limits, and adhering to deadlines for employee elections. Accurate recordkeeping is essential to prevent errors in contribution reporting and ensure compliance with IRS regulations.

### **Conclusion**

Bonus elections on deferrals offer employees an opportunity to enhance their retirement savings, especially if the employer matches the contributions. However, it's crucial for plan sponsors to grasp the regulations governing these elections. From contribution limits to non-discrimination testing, it's important to ensure compliance to enable employees to fully benefit from these options. Proper education, planning, and administration are key to a successful bonus deferral program.

ATTACHED IS THE BONUS ELECTION FORM, to be used for participants who wish to elect a salary deferral election other than their regular election. For Employers utilizing MVP's recordkeeping platform, this form is also available from the Plan Sponsor website under Documents & Forms. Employers may download the Form to provide to plan participants.

### **Summary Checklist for Success - Keys to Maintaining Successful Bonus Elections:**

- ✓ Ensure proper understanding of the plan definition of compensation
- ✓ Ensure a bonus election form is on file for each participant, each bonus paid if the Employer allows special election on bonus
- ✓ Ensure proper adherence to the IRS deferral limits are coded in payroll
- ✓ Ensure all contributions are made to the plan timely



If you have questions or wish to discuss in more detail, please give your Relationship Manager a call or call us directly at (919) 465-2220