News You Can Use For Advisors

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Compliance Minute: Focus on Solo 401(k)s

You've heard the term—but do you know what it means? Solo 401(k)s are popular among entrepreneurs and small business owners, though many are often misled by its name.

- **What is a Solo 401(k)?** More a marketing term than an actual plan type, the term "Solo 401(k)" simply denotes a one-person retirement plan. It is a traditional 401(k) plan that covers only a business owner (and potentially his or her spouse) and no employees. Despite its limited eligibility, it is generally subject to all rules and regulations applicable to traditional 401(k)s.

- **What kinds of contributions can owners put in?** Just as with other 401(k) plans, Solo 401(k) plans may provide for both elective deferrals and employer nonelective contributions. Elective deferrals are capped by the general deferral limit ($23,500 in 2025). Employer contributions are generally capped at 25% of compensation as defined by the plan document. Self-employed individuals must generally use their earned income as compensation. (*Pro tip*: If your client's business entity becomes an S-Corp, remember that earned income means compensation only—and does not include shareholder distributions.)

- **What about testing and reporting?** Solo 401(k) plans are generally exempt from nondiscrimination testing. This exemption no longer applies, however, if the business owner hires a common law employee. Solo 401(k) plans with more than $250,000 in assets are generally required to file annual Form 5500-EZ.

- **What happens if the business sponsoring a Solo 401(k) hires an employee?** Here's where the naming convention for these plans can often cause trouble. No matter the name of the plan, if the business hires employees who meet the plan's eligibility requirements, such employees must be permitted to participate in the plan. This often also means that the plan will need to begin nondiscrimination testing (generally unless it is a safe harbor plan).

- **Is there a problem with just using a financial institution's stock Solo 401(k) document?** Often, yes! These documents usually indicate that employers may only use them if the employer doesn't have employees. As discussed above, this can sometimes lead to plan operational errors if or when the employer grows. Perhaps most importantly, though, financial institutions often view these documents as "one and done." Unlike TPAs, financial institutions do not generally have processes in place to track plans and remind plan sponsors of required updates and changes, including restatement deadlines.

Solo 401(k)s may seem simple at first, but they come with a host of compliance-related issues. Perhaps because of the name, clients often forget that the plan is subject to qualification requirements set by the IRS and must comply with all attendant rules. Because of this, Solo 401(k) sponsors often run into operational mistakes that must be corrected. TPAs can help Solo 401(k) clients navigate and plan for unintended complexity. Now is a great time to reach out to your Solo 401(k) clients and connect them with a TPA as a value-add for your clients. Remember: an ounce of prevention is worth a pound of cure.

by Hannah Munn, Partner, Poyner Spruill

Reminders:

- July 29, 2025: Summaries of material modifications (SMMs) due to participants in calendar year plans, unless such changes have been included in an updated SPD.
- July 31, 2025: Form 5330 (used to report excise taxes) due to the IRS.
- July 31, 2025: Form 5500 due to the DOL for calendar-year plans that have not filed an extension.