



## Retirement Planning

# Retroactive First-Year Solo-401(k) Plan Deferrals Allowed for Sole Proprietors

***Eligible employers can now establish and fund a Solo-401(k) plan with salary deferrals for the prior tax year. Here are the details.***



**Brian Dobbis, QKA, QPA, QPFC, TGPC**  
*Retirement Solutions Lead*

From a timing perspective, both [SECURE Act 1.0 and 2.0](#) have made it easier for small business owners to both establish and fund a qualified retirement plan.

Prior to the SECURE Act of 2019, a small business that sought to establish a qualified retirement plan (i.e., 401(k)) for a specific tax year generally had to establish it by the last day of the business's prior tax year. Notably, a small business owner could establish and fund a Simplified Employee Pension Plan (SEP) IRA after the end of the year (up until the individual tax filing deadline plus extension) for the previous year. For example, a SEP-IRA established in June 2024 could receive contributions for the 2023 tax year.

Under the Secure Act of 2019, effective in 2020, an employer was given additional time to establish a qualified retirement plan to which deductible contributions could be made. But this extended deadline (tax filing, including extension) only applies to qualified retirement plans that are entirely funded with *employer* contributions such as Profit Sharing and Pension Plans. In other words, an employer now has the flexibility to establish a new, employer-funded qualified plan after the end of the taxable year, but *before* the employer's tax filing date (including extensions) and treat the plan as having been established on the last day of the prior taxable year. The change allowed an employer, for example, to establish a new, employer-funded qualified retirement plan for 2022 as late as September 15 or October 15, 2023, depending on the business type. The issue, however, is that the timing did not extend to employee salary-deferral contributions (i.e., pre-tax, Roth or after-tax). This limitation prevented a sole proprietor from opening a Solo-401(k) for the prior taxable year. Enter Secure Act 2.0.

Secure 2.0 corrects this oversight by allowing sole proprietors to establish a Solo-401(k) plan retroactively with both employer contributions and employee salary deferrals for the initial year.

Secure Act 2.0, Section 317, builds upon qualified plan establishment timing by allowing a [Solo-401\(k\)](#) plan set up by a [sole proprietor](#) or single-member Limited Liability Company (LLC) to make *employee salary-deferral* contributions retroactively up to the date of employer's tax return filing date for the *initial plan* year. In other words, an eligible employer can now establish and fund a Solo-401(k) plan—for the *first year only*—including employee salary deferrals (i.e., pre-tax, Roth, or after-tax contributions) for the *previous tax year*, up to the due date of the individual's tax return (*without* extension).

Section 317 is generally effective for plan years beginning in 2023. The specific plan establishment deadline is based on the type of business entity and its associated tax filing.



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**Example (Secure Act 2.0; Section 317):** Tony, a sole proprietor, owns a landscaping company. In March 2024, Tony's advisor makes him aware of the extended deadline to open a new Solo-401(k) plan for the prior tax year. Tony can retroactively open a new Solo-401(k) for 2023 funded with both employer contributions and employee salary deferrals—so long as the plan is opened by his business's 2023 tax filing deadline, not including extensions (generally April 15, 2024).

A sole proprietor is considered both an employee and employer with regard to a Solo-401(k)—thus allowing the sole proprietor to make employee salary deferrals and employer contributions. For 2024, the employee salary deferral limit is \$23,000 (pre-tax and/or Roth) and \$30,500 for those individuals age 50+, while employer contributions are 20% of adjusted net earnings (25% of compensation if business is incorporated). Overall, the 2024 limit for both employee deferrals and employer contributions is \$69,000 (\$76,500 when including the \$7,500 age-50 catch-up contribution).

The extended deadline to adopt a Solo 401(k) plan (for the prior tax year) allows the employer to retroactively adopt a new plan while also allowing for tax-deductible contributions.

Questions? Please contact your Lord Abbett representative at 888-522-2388.

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A Solo 401(k) plan is a traditional 401(k) plan covering a business owner with no employees, or that person and his or her spouse. These plans have the same rules and requirements as any other 401(k) plan.

A 401(k) plan is a qualified plan that includes a feature allowing an employee to elect to have the employer contribute a portion of the employee's wages to an individual account under the plan. The underlying plan can be a profit-sharing, stock bonus, pre-ERISA money purchase pension, or a rural cooperative plan. Generally, deferred wages (elective deferrals) are not subject to federal income tax withholding at the time of deferral, and they are not reported as taxable income on the employee's individual income tax return. A Solo **401(k)** is a traditional 401(k) plan covering a business owner with no employees, or that person and his or her spouse.

Simplified Employee Pension (SEP) plans can provide a significant source of income at retirement by allowing employers to set aside money in retirement accounts for themselves and their employees. A SEP does not have the start-up and operating costs of a conventional retirement plan and allows for a contribution of up to 25 percent of each employee's pay.

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