SIMPLE IRAs vs 401(k) SAFE HARBOR PLANS: WHAT ARE THE DIFFERENCES?

Savings Incentive Match Plans for Employees (SIMPLEs) are frequently mentioned as a low cost alternative to 401(k) Safe Harbor Plans for providing employees the opportunity to save for retirement. In particular, SIMPLE IRAs carry a lower administrative burden than 401(k) Safe Harbor Plans, due to simplified plan documents, and no annual compliance testing or 5500 government reporting requirements. Given these factors, we are frequently asked whether a small business should even bother with a qualified plan, such as a 401(k) plan. The purpose of this outline is to compare a SIMPLE IRA with a safe harbor 401(k) plan --- especially for employers who must cover participants other than just the owners.

In order for an employer to be eligible to start a SIMPLE IRA plan, it must have no more than 100 employees who earned $5,000 or more during the preceding calendar year, and it must not make contributions to the SIMPLE plan if any of its employees are also receiving allocations in another qualified plan maintained by the employer, unless that plan is for collectively bargained employees.

		SIMPLE IRAs	**401(k) Safe Harbor Plans**
A	Plan Year	May only be maintained on a calendar year.	May be calendar year or fiscal year.
B	Eligibility	Employees who earned at least $5,000 in any two calendar years preceding, and who are expected to earn $5,000 during the year for which the contribution is being made, must be included.	Can exclude employees who never worked at least 1,000 hours in a 12-month period and employees who are not at least age 21. (Long-Term Part-Time employees must be allowed to make deferrals.) Mandatory Auto Enrollment applies for new plans.
C	Maximum Employee Contribution	Employees may contribute up to the lesser of $16,500 or 100% of pay for 2025.	Employees may contribute up to the lesser of $23,500 or 100% of pay for 2025.
D	Catch-up Contributions	Participants who are 50 or above by the last day of the year may make additional contributions not exceeding $3,500 for 2025. Super Catch-up Limit of $5,250 for ages 60-63 in 2025.	Participants who are 50 or above by the last day of the year may make additional contributions not exceeding $7,500 for 2025. Super Catch-up Limit of $11,250 for ages 60-63 in 2025.
E	Employee Roth Contributions	Permitted.	May be permitted by the plan.

F	Required Minimum Employer Contribution	The employer must provide an annual election notice to employees that describes the decision to contribute either: 1) A dollar-for-dollar match on up to 3% of pay contributed by the employee* (with no cap on compensation); or 2) A nonelective contribution of 2% of pay to all eligible participants regardless of any employee contributions, and based on pay of up to $350,000 for 2025.	The employer must provide an annual Safe Harbor Notice, which describes the commitment to contribute, as stated in the plan: 1) A match at least as generous as 100% of the first 3% of pay contributed by the employee, plus 50% of the next 2% of pay contributed; or 2) A non-matching contribution of 3% of pay for all participants. Pay considered for contributions is limited to $350,000 for 2025.
G	Compensation Considered for Required Employer Contributions	When applicable, the nonelective contribution must be based on employee pay for the entire calendar year.	Plan may permit Safe Harbor Employer contributions to be based on employee pay for the entire plan year or, for new plan participants, only on pay earned after becoming eligible.
H	Other Employer Contributions	Also, there is no requirement to fund a Top Heavy Contribution.	Other employer contributions are permitted, including discretionary profit sharing and matching contributions; discretionary match is allowed and will not require ACP testing as long as allocation does not exceed 4% of pay and it is calculated using deferrals of no more than 6% of pay. The plan may be designed in such a way as to avoid requirement to fund a Top Heavy Contribution.
I	Vesting	All contributions are fully vested.	Must fully vest the safe harbor minimum contribution. But all additional contributions can be subject to the plan's vesting schedule.
J	Loans	Not permitted.	Permitted.
K	Distributions	Allowed at any time, subject to 10% early withdrawal penalty prior to age 59 ½ or 25% penalty if funds are withdrawn within 2 years of participation.	Plan may impose limitations on timing of withdrawals up to normal retirement age. Limitations apply to in-service withdrawals of Safe Harbor amounts. 10% early withdrawal penalty applies.

L	Maximum total annual contribution per person	Determined as in (C), (D) and (F) above.	Lesser of *100%* of pay or $70,000 in 2025.
M	Maximum Employer Deduction Allowed (i.e. excluding the participant's elective deferral)	Determined as in (F) above.	The total deduction of employer contributions (match plus profit sharing) for all participants combined must not exceed 25% of all combined participant salaries.

*The match must be 3% in at least 3 out of every 5 years, and may not be lower than 1%.

Starting in 2025, a SIMPLE IRA can be replaced with a safe harbor 401(k) plan mid-year. The replacement plan can be either a traditional safe harbor plan or a Qualified Automatic Contribution Arrangement (QACA) safe harbor 401(k) plan. The replacement safe harbor/QACA 401(k) plans must be effective as of the termination date of the SIMPLE IRA.

Contributions will be restricted to an aggregate elective deferral limit (including catch-up contributions) during the replacement year. The limit is based on the number of days covered in each plan. For example, if the replacement is done on June 1, 2025, the 2025 elective deferral limit – contributed to either the SIMPLE IRA or 401(k) plan – would be determined by taking the number of days covered in the SIMPLE IRA multiplied by its contribution limit (152/365) x 16,500 ($20,000 including regular catch-up) = $6,871.23 ($8,328.77) and adding the number of days covered in the 401(k)-plan multiplied by its contribution limit (213/365) x 23,500 (31,000 including catch-up) = $13,713.70 ($18,090.41) for a total deferral contribution of $20,588.93 ($26,719.18). This is using 2025 limits for illustrative purposes.