

A New Tax Credit for Contributions to 401(k) Plans

SECURE Act 2.0 added a new credit for contributing to a new pension plan



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SECURE Act 2.0 was passed at the end of 2022, and it added a new tax credit for employers or farmers who have set up a new pension plan (usually a Section 401(k) plan). In order for it to be a new plan, you must have had no type of pension plan for the last three years including a SIMPLE and SEP plans.

The new credit allows the employer to get a tax credit equal to 100% of the amount the employer puts in for each up employee up to \$1,000 per employee. This only applies for employees making less than \$100,000 which is most farm employees.

The credit is the lesser of the amount put in for each employee or \$1,000 per employee and for the first two years you get 100%, the third year 75%, the fourth year 50%, and the fifth year 25%, and nothing thereafter.

Just like most credits, you then have to reduce your expense deduction by the amount of the credit.

This new credit is effective beginning in 2023; however, you still qualify for the credit if you started a new plan before 2023, but you only get the credit for 2023 and thereafter.

As example, assume you start a new plan in 2023 and had four full-time employees and you paid into the plan at least \$1,000 for each of them. You would get a \$4,000 credit on your 2023 and 2024 return, \$3,000 on 2025 return, \$2,000 on 2026 return and \$1,000 on the 2027 return (assuming you continue to have 4 employees and pay into the plan at least \$1,000 per employee).

Now let's assume you started the plan in 2021. In this case, you do not get the 100% credit, but rather in 2023 you get \$3,000, \$2,000 in 2024 and finally \$1,000 in 2025.

If you missed the credit in 2023, you would likely need to file an amended tax return to get the credit.

The full credit is allowed for employers with less than 51 employees. There is a phase-out for employers with between 51 and 100 employees. For most farm operations, they will qualify for the full credit.

Also, your cost of setting up and administering the plan will qualify for a 100% credit for these costs in years 1-3. There is a separate \$5,000 limit on this credit.