

# Bonuses & Withholding

## *A Segment in Our Retirement Rescue Series*

*The holiday season is a time for giving. This time of year, many employers will pay their employees a holiday bonus. Are employee bonuses subject to the same 401(k) withholding as regular wages? It depends on your Plan's Definition of Compensation & special treatment of bonus compensation.*

Compensation commonly refers to any payment made to an employee by the employer for services rendered including wages and salary, fees for professional service, commissions, and bonuses. However, your Plan's Definition of Compensation, found in the Plan Document, may exclude certain payments.

• ***If your Definition of Compensation includes bonuses...***

If your Plan's Definition of Compensation includes all forms of compensation or does not specifically exclude bonuses, an employee's bonus is subject to their normal elected deferral rate.

*Adam is an employee of Company A which includes all forms of employee compensation in its Definition of Compensation. Adam's elected deferral rate is 10%. He received a \$1,000 bonus. \$100, 10% of his bonus, will be deferred into his 401(k) account.*

• ***If your Definition of Compensation excludes bonuses...***

If bonuses are excluded in your Plan's Definition of Compensation, 401(k) deferral elections will not be applied to employee bonuses.

*Bridget is an employee of Company B which specifically excludes bonuses in the Definition of Compensation contained in its Plan Document. Bridget's elected deferral rate is 12%. She received a \$1,000 bonus. No 401(k) withholding will occur because bonuses are excluded by the Plan's Definition of Compensation.*

• ***If your Plan allows for different deferral rates on bonuses...***

Your Plan's Definition of Compensation includes bonuses and allows for employees to elect a deferral rate specifically for bonuses, different than what is used for their normal wages.

*Chris is an employee of Company C. The Definition of Compensation for Company C's 401(k) Plan includes bonuses. Also, Chris is permitted to elect a separate deferral rate for bonus income. Chris' elected deferral rate for wages/salary is 15% but he has elected for 50% for bonuses. Chris received a \$1,000 bonus. \$500, or 50%, will be deferred into his 401(k) account.*

In conclusion, 401(k) withholding for bonuses depends on your Plan Provisions, including the Definition of Compensation. For more information on correcting a failure to properly use your Plan's Definition of Compensation, check out the [IRS 401\(k\) Plan Fix-It Guide](https://www.irs.gov/pub/irs-tege/epchd304.pdf).