Retirement Plan Essentials
Presented By:
Jim Vanden Branden, MAS, CPA, CFP
and
Tom O’Saben, EA, CFP
Retirement Plans – Why?

- Invest for retirement
- Employee retention
- Employee motivation
- Reduce income taxes
Retirement Plans – Why Not?

- Administrative costs
- Administrative burden – headaches
- Cash flow – employer contributions
- Lack of employee appreciation
- Owner fiduciary responsibility
- Market loss scapegoating – employee morale
Retirement Plan Types

A maze of decisions:

- IRA-based options: SEP, SARSEP, SIMPLE

- True qualified plans: profit sharing, SIMPLE 401(K), 401(k), safe harbor 401(k), single 401(k), money purchase, target benefit, defined benefit, cash balance, ESOP, §457, §403(b)
Other Retirement Plan Features

- Cash or deferred arrangement (CODA)
- Designated Roth accounts
- Age-weighted
- Automatic contribution arrangement (ACA)
- Qualified automatic contribution arrangement (QACA)
- Permitted disparity plans (integration)
Today’s Focus:

• IRA-Based Options:
  – SEP
  – SIMPLE

• Qualified Plan Options:
  – Profit sharing
  – SIMPLE 401(K), safe harbor 401(k), 401(k)
  – Single 401(k)
  – Designated Roth accounts
IRA-Based Options: SEP, SIMPLE

- SEP - simplified employee pension plan
- SIMPLE – savings incentive match plan for employees
- Retirement plans – yes
- Qualified plans – no
  - Lower adoption and on-going costs
  - Less design flexibility
- Employee establishes and owns IRA
Establishing a SEP - IRA

• Set up and fund by extended due date
• Written agreement:
  – IRS model SEP document - Form 5305-SEP
  – Prototype SEP document - through a qualified financial institution such as a mutual fund, insurance company or bank
  – Individually designed plan
• Employer contributions only
Operating a SEP - IRA

- No required contribution
- No vesting schedule
- No limit on number of employees
- No Form 5500 (in most cases)
- No plan withdrawal restrictions
  - Subject to possible 10% penalty
- Employees responsible for investments
- Minimal eligibility restrictions
SEP – Contributions

• Discretionary employer contributions
• Contributions for employees limited to lesser of:
  – $49,000 in 2009 and 2010
  – 25% of the employee's compensation
    • Compensation limited to $245,000 in 2009 and 2010
SEP – Contributions

• Reduced contribution rate for self-employed:
  – Compensation is earnings from self-employment, net of ½ SE tax and owner’s SEP contribution.
  – Circular calculation - Maximum = 20%
    • \([\text{Employee rate} / (1+ \text{employee rate})]\]
  – IRS Pub. 560, Chapter 5: rate table, rate worksheet, deduction worksheet
SEP – Deduction

- Lesser of:
  - Contributions (including any excess contributions carryover).
  - 25% of compensation paid to participants from the business that has the plan, not to exceed $49,000 per participant in 2009 and 2010
  - Compensation limited to $245,000 per participant, for 2009 and 2010
- Self-employed reduced rate (20% max.)
SIMPLE IRA Features

- Inexpensive to set up and operate
- Mandatory employer contributions
- Employees have option to help fund their retirement
- No discrimination testing required
- Lower contribution limits than some other retirement plans
- Loans not available
Establishing a SIMPLE

• New SIMPLE IRA: effective on any date between January 1 and October 1
  – If previously maintained SIMPLE IRA, new SIMPLE IRA effective only on January 1

• New businesses that comes into existence after October 1:
  – Set up SIMPLE IRA plan as soon as administratively feasible.

• Calendar-year only
Establishing a SIMPLE

- No other retirement plan:
  - No contributions can be made or benefits accrued in another plan for service in any year beginning with the year the SIMPLE IRA plan becomes effective
  - Exception: plan for collectively bargained employees
Establishing a SIMPLE

• 100 or fewer employees
  – Count if received $5,000 or more in prior year compensation
  • Count all employees, regardless of whether eligible
  – Include self-employed and leased employees
Establishing a SIMPLE

• Written agreement:
  – Form 5304-SIMPLE if each participant to select the financial institution for his or her SIMPLE IRA contributions
  – Form 5305-SIMPLE if all SIMPLE IRA contributions are required to be deposited initially at a designated financial institution
  – Prototype document from bank, etc.
  – Individually-designed plan
Operating a SIMPLE

- Required contribution
- No vesting schedule
- 100 participant employee limit
- No Form 5500
- No plan withdrawal restrictions
  - subject to possible 25% or 10% penalty
- Employees responsible for investments
- Minimal eligibility restrictions
Operating a SIMPLE

• Notify employees of the following before the beginning of the election period:
  1) The employee’s opportunity to make or change a salary reduction choice
  2) The plan’s matching contributions or nonelective contributions
  3) A summary description including the plan eligibility and basic features
Operating a SIMPLE

• Notification - continued:
  4) If using a designated financial institution, written notice that the employee’s SIMPLE IRA balance can be transferred without cost or penalty.

• Election period: Generally, the 60-day period immediately preceding January 1 of a calendar year (November 2 to December 31 of the prior calendar year)
SIMPLE Contributions

- Two Normal Employer Contribution Options:
  - Matching employees’ contributions dollar-for-dollar up to 3% of pay, or
  - A 2% nonelective contribution for each eligible employee, regardless of employee contribution
SIMPLE Contributions

• Special lower matching percentage:
  – Employer can match less than 3%, but at least 1%
  – Employee notification required within a reasonable period of time before the 60-day election period
  – Match less than 3% is not allowed for more than 2 years during the last 5-year period
SIMPLE Contributions

Contribution Limits:

• **Employee**
  – $11,500 in 2009 and 2010
  – Employees age 50 or over; “catch-up” contribution for 2009 and 2010 of $2,500

• **Employer**
  – Dollar-for-dollar match up to 3% of pay, or
  – 2% nonelective contribution per eligible employee
SIMPLE Contributions

• Employee deferrals:
  – Must be forwarded to the financial institution no later than the close of the 30-day period following the last day of the month in which they were withheld from the employees’ paychecks.

• Employer matching or nonelective contributions:
  – No later than extended due date
True Qualified Plans

– Profit Sharing
– SIMPLE 401(K), safe harbor 401(k), 401(k)
– Single 401(k)
– Designated Roth accounts
Establishing a Qualified Plan

- Defined contribution plan
- Adopt written plan
  - Master or prototype plans pre-approved by the IRS
  - Made available by plan providers for adoption by employers (including self-employed individuals)
- Banks, insurance companies, mutual funds, and others can provide
Establishing a Qualified Plan

• Individually designed plan is also acceptable if customization is required

• Determine plan's investment vehicle:
  – Establish trust (legal instrument) or custodial account to invest the funds
  – The owner, the trust, or the custodial account can purchase an annuity contract from an insurance company
Establishing a Qualified Plan

- Custodial account can be set up with a bank, savings and loan association, credit union, or other person who can act as the plan trustee
- Trust or custodial account not required to invest the plan's funds in annuity contracts or face-amount certificates
- For non-trustee holders the contracts must state they are not transferable
Qualified Plan Common Features

- Can have other retirement plans
- Can be a business of any size
- Need to annually file a Form 5500
- Testing to avoid discrimination in favor of highly compensated employees
Profit-Sharing Plan Features

- Employer contributions only
- Contributions are strictly discretionary
- Good plan if cash flow is an issue
- Employees not allowed to contribute, but W-2 pension box checked
Operating a Profit-Sharing Plan

- Pre-approved profit-sharing plans are available to cut down on administrative headaches
- Custom plan document
- Test that benefits do not discriminate in favor of the highly compensated employees
Profit-Sharing Plan Contributions

• Contributions for employees limited to lesser of:
  – $49,000 in 2009 and 2010
  – 25% of the employee's compensation
    • Compensation limited to $245,000 in 2009 and 2010
Profit-Sharing Plan
Contributions

• Reduced contribution rate for self-employed:
  – Compensation is earnings from self-employment, net of $\frac{1}{2}$ SE tax and owner’s SEP contribution
  – Circular calculation - Maximum = 20%
    • $[\text{Employee rate} / (1+ \text{employee rate})]$
401(k) Plan Features

- Employee deferrals
- Employer match
- Employer discretionary
- Loans
Operating a 401(k) Plan

- Higher administrative costs
- Ongoing discrimination testing
401(k) Plan Contributions

- **Employee** - $16,500 in 2009 and 2010

- Aged 50 and over “catch-up” contribution is allowed. $5,500 for 2009 and 2010

- **Employer/Employee** – The lesser of 25% of compensation or $49,000 in 2009 and 2010
401(k) Plan Contributions

• **Self Employed** - $16,500 in 2009 and 2010

• **Self Employed - Aged 50 and over** “catch-up” $5,500 for 2009 and 2010

• **Discretionary**: Reduced contribution rate for self-employed: Compensation is earnings from self-employment, net of $1/2 SE tax and owner’s SEP contribution
SIMPLE 401(k)

- Employer mandatory contributions
- Discrimination testing not required
- Less flexibility, less expensive to operate
- Must have 100 or fewer employers
- Cannot have any other retirement plans
- Eligible employees: $5,000 or more in compensation from the employer for the preceding calendar year
SIMPLE 401(k) Plan Features

- Employee deferrals
- Mandatory employer match
- Employer discretionary NOT allowed
- Employees are totally vested in *any and all contributions*
- Loans allowed
- No contributions or benefit accruals under any other plans of the employer
SIMPLE 401(k) Plan Contributions

- ER matching contribution of 3%, or
- ER non-elective contribution of 2%
- Employee contributions $11,500 in 2009 and 2010
- Age 50 and over, an additional “catch-up” of $2,500 in 2009 and 2010
Safe Harbor 401(k)

- Similar to a traditional 401(k) plan
- Employer contributions fully vested when made
- Not subject to annual nondiscrimination testing
- Less flexibility
- Less expensive to administer
- Written notice requirements
Safe Harbor 401(k)

- Contributions: employer matching or employer contribution regardless of employee elective deferrals allowed
- If no additional contributions are made in a year, exempted from the top-heavy rules of §416
Automatic Enrollment 401(k)

• Employer automatically reduces employee’s wages by a fixed percentage or amount and contributes to plan
• Unless the employee has affirmatively chosen not to or has a different percentage
• These contributions qualify as elective deferrals, increase participation in plan
Automatic Enrollment 401(k)

- Eligible automatic contribution arrangement (EACA)
- May allow employees to withdraw automatic enrollment contributions (and earnings) by election
Automatic Enrollment 401(k)

- Qualified automatic contribution arrangement (QACA)
- Additional “safe harbor” provisions
- Exempt from annual discrimination testing requirements
- Matching or nonelective employer contributions required
- 100% vesting within 2 years
Single Owner / Employee 401(k)

- Not a special type of 401(k)
- Written plan document, within the provisions of qualified plan rules
- Less administrative costs, no testing
- 401(k) rules and definitions allow for a maximum addition of $49,000 with the lowest amount of compensation (2010)
  
  \[ 130,000 \times 25\% = 32,500 + 16,500 = 49,000 \]
Designated Roth Accounts

- Designated Roth contributions
- Currently includible in gross income
- 401(k) or 403(b) plans only
- All elective contributions limited to $16,500 in 2009 and 2010
- Age 50 and over catch-up $5,500 in 2009 and 2010
Designated Roth Accounts

- Roth automatic enrollment OK
- No allocation of forfeitures and matching contributions
- Loans OK
- Contributions not limited by income
- Pre-tax elective contributions may not be converted to a designated Roth account
Summary of Limits

- Maximum total annual contributions - the lesser of $49,000 or 100% of compensation in 2009 and 2010
- All elective contributions limited to $16,500 in 2009 and 2010
- Age 50 and over catch-up $5,500 in 2009 and 2010
- Compensation considered $245,000 in 2009 and 2010
- Employer contribution limited to lesser of 25% of compensation or $49,000 in 2009 and 2010
  - 20% for self-employed
### Summary of Limits – $50,000 (Self-employed)

<table>
<thead>
<tr>
<th>Age 55, 2009</th>
<th>Contributions:</th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Employee</td>
<td>Catch-up</td>
<td>Employer</td>
<td>Total</td>
</tr>
<tr>
<td>SEP-IRA</td>
<td>Not Allowed</td>
<td>Not Allowed</td>
<td>9,294</td>
<td>9,294</td>
</tr>
<tr>
<td>SIMPLE-IRA</td>
<td>11,500</td>
<td>2,500</td>
<td>1,385</td>
<td>15,385</td>
</tr>
<tr>
<td>Profit Sharing</td>
<td>Not Allowed</td>
<td>Not Allowed</td>
<td>9,294</td>
<td>9,294</td>
</tr>
<tr>
<td>SIMPLE 401(k)</td>
<td>11,500</td>
<td>2,500</td>
<td>1,385</td>
<td>15,385</td>
</tr>
<tr>
<td>401(k)</td>
<td>16,500</td>
<td>5,500</td>
<td>9,294</td>
<td>31,294</td>
</tr>
</tbody>
</table>
Summary of Limits – $150,000 (Self-employed)

<table>
<thead>
<tr>
<th>Age 55, 2009</th>
<th>Contributions:</th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Employee</td>
<td>Catch-up</td>
<td>Employer</td>
<td>Total</td>
</tr>
<tr>
<td>SEP-IRA</td>
<td>Not Allowed</td>
<td>Not</td>
<td>28,274</td>
<td>28,274</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Allowed</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SIMPLE-IRA</td>
<td>11,500</td>
<td>2,500</td>
<td>4,236</td>
<td>18,236</td>
</tr>
<tr>
<td>Profit Sharing</td>
<td>Not Allowed</td>
<td>Not</td>
<td>28,274</td>
<td>28,274</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Allowed</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SIMPLE 401(k)</td>
<td>11,500</td>
<td>2,500</td>
<td>4,236</td>
<td>18,236</td>
</tr>
<tr>
<td>401(k)</td>
<td>16,500</td>
<td>5,500</td>
<td>28,274</td>
<td>50,274</td>
</tr>
</tbody>
</table>
### Summary of Limits – $300,000 (Self-employed)

<table>
<thead>
<tr>
<th>Age 55, 2009</th>
<th>Contributions:</th>
<th>Employee</th>
<th>Catch-up</th>
<th>Employer</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>SEP-IRA</td>
<td>Not Allowed</td>
<td>Not Allowed</td>
<td>49,000</td>
<td>49,000</td>
<td></td>
</tr>
<tr>
<td>SIMPLE-IRA</td>
<td>11,500</td>
<td>2,500</td>
<td>8,671</td>
<td>22,671</td>
<td></td>
</tr>
<tr>
<td>Profit Sharing</td>
<td>Not Allowed</td>
<td>Not Allowed</td>
<td>49,000</td>
<td>49,000</td>
<td></td>
</tr>
<tr>
<td>SIMPLE 401(k)</td>
<td>11,500</td>
<td>2,500</td>
<td>8,671</td>
<td>22,671</td>
<td></td>
</tr>
<tr>
<td>401(k)</td>
<td>16,500</td>
<td>5,500</td>
<td>32,500</td>
<td>54,500</td>
<td></td>
</tr>
</tbody>
</table>
## Summary of Limits – $50,000 (Employee)

<table>
<thead>
<tr>
<th>Age 55, 2009</th>
<th>Contributions:</th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Employee</td>
<td>Catch-up</td>
<td>Employer</td>
<td>Total</td>
</tr>
<tr>
<td>SEP-IRA</td>
<td>12,500</td>
<td>12,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SIMPLE-IRA</td>
<td>11,500</td>
<td>2,500</td>
<td>1,500</td>
<td>15,500</td>
</tr>
<tr>
<td>Profit Sharing</td>
<td>12,500</td>
<td>12,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SIMPLE</td>
<td>11,500</td>
<td>2,500</td>
<td>1,500</td>
<td>15,500</td>
</tr>
<tr>
<td>401(k)</td>
<td>16,500</td>
<td>5,500</td>
<td>12,500</td>
<td>34,500</td>
</tr>
</tbody>
</table>
### Summary of Limits — $150,000 (Employee)

<table>
<thead>
<tr>
<th>Age 55, 2009</th>
<th>Contributions:</th>
<th>Employee</th>
<th>Catch-up</th>
<th>Employer</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>SEP-IRA</td>
<td>37,500</td>
<td></td>
<td>37,500</td>
</tr>
<tr>
<td>SIMPLE-IRA</td>
<td>11,500</td>
<td>2,500</td>
<td>4,500</td>
<td>18,500</td>
<td></td>
</tr>
<tr>
<td>Profit Sharing</td>
<td></td>
<td></td>
<td>37,500</td>
<td></td>
<td>37,500</td>
</tr>
<tr>
<td>SIMPLE 401(k)</td>
<td>11,500</td>
<td>2,500</td>
<td>4,500</td>
<td>18,500</td>
<td></td>
</tr>
<tr>
<td>401(k)</td>
<td>16,500</td>
<td>5,500</td>
<td>32,500</td>
<td>54,500</td>
<td></td>
</tr>
</tbody>
</table>
## Summary of Limits – $300,000 (Employee)

<table>
<thead>
<tr>
<th>Age 55, 2009</th>
<th>Contributions:</th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Employee</td>
<td>Catch-up</td>
<td>Employer</td>
<td>Total</td>
</tr>
<tr>
<td>SEP-IRA</td>
<td></td>
<td></td>
<td>49,000</td>
<td>49,000</td>
</tr>
<tr>
<td>SIMPLE-IRA</td>
<td>11,500</td>
<td>2,500</td>
<td>9,000</td>
<td>23,000</td>
</tr>
<tr>
<td>Profit Sharing Plan</td>
<td></td>
<td></td>
<td>49,000</td>
<td>49,000</td>
</tr>
<tr>
<td>SIMPLE 401(k)</td>
<td>11,500</td>
<td>2,500</td>
<td>9,000</td>
<td>23,000</td>
</tr>
<tr>
<td>401(k)</td>
<td>16,500</td>
<td>5,500</td>
<td>32,500</td>
<td>54,500</td>
</tr>
</tbody>
</table>
Other Issues:

- Hiring a Spouse
- When To Adopt?
- Updating or Changing Plans
Other Issues:

• More Than One Plan
  – Per Employee
  – Per Employer

• Rollovers as Business Start-Ups (ROBS)
Thank You!!