Employer Retirement Plans

Tax and Business Update

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Qualified Retirement Plans

Retirement Plan Advantages

- Contributions to the plan are deductible by the employer when made, but not taxed to the employee until distributed.
- Accumulate funds for retirement.
- Attracts qualified employees and retains existing employees.
- Encourages loyalty among existing employees by requiring a specified number of years of service before an employee is entitled to employer contributions (known as vesting).
- Offers a benefit competitive with other companies that offer plans.
- Usually very favorable for self-employed individuals.
- Funds accumulated in a plan are generally not subject to creditors' claims.
- Certain plans allow pre-tax employee contributions.

Retirement Plan Disadvantages

- Some plans must meet complex requirements to keep the plan's tax favored status.
- Some plans are expensive and time-consuming to operate.
- Plans that cover highly compensated or key employees as well as lower paid employees may be subject to special top-heavy rules that require a minimum contribution.
- Some plans must file Form 5500 series returns.
- Plan fiduciaries, including the plan administrator, must act in the best interest of participants and beneficiaries. Fiduciaries are not only subject to significant penalties if they breach this responsibility; they may also be personally liable for any losses to the plan resulting from the breach.
- For some plan types, an annual contribution may be required.

Qualified Plan Special Rules	
Eligibility	Employees who are age 21 or older and who have completed a year of service must generally be allowed to participate in the plan.
Coverage	The plan must cover a broad range of employees and cannot discriminate in favor of owners or key employees.
Vesting	Participants generally must be entitled to 100% of their plan benefits after three (defined contribution) or five (defined benefit) years of service [six (defined contribution) or seven (defined benefit) years of service if graded vesting is used].
Nondiscrimination	Plan contributions and benefits cannot discriminate in favor of highly compensated employees.

Qualified Retirement Plan Types

Defined benefit plans promise specific benefits at retirement. For example, the plan might promise to pay an employee at retirement 80% of his average salary for the last five years of employment. The employer is required to make annual contributions to fund this benefit. This amount must be determined by an actuary.

Defined contribution plans provide benefits based on the amount contributed to an employee's individual account plus any earnings or forfeitures of other employees that are allocated to the account. The amount available at retirement equals whatever is in the employee's account at that time.

Defined contribution plans include:

- Profit-sharing plans.
- Money purchase plans.
- 401(k) plans.
- Stock bonus plans (such as ESOPs).

Contributions plus plan forfeitures allocated to a participant's account cannot exceed $53,000 for 2016 and $54,000 for 2017 or, if less, 100% of the participant's compensation.

Employer Deduction Limits	
Defined Benefit Pension Plan	Amount necessary to satisfy annual minimum funding standard. Must be actuarially determined.
Profit-Sharing Plans and SEPs	Up to 25% of total compensation paid to all plan participants.
SIMPLE IRA Plans	The employer matching or nonelective contribution, whichever is required.

Payroll Deduction IRAs

- Payroll deduction IRAs are an economical way to encourage employees to save for retirement. In effect, the employer collects employee IRA contributions and transmits them to the custodian or trustee.
- Contributions cannot exceed the lesser of the employee's compensation or $5,500 for 2016 and 2017 ($6,500 if age 50 or older).

Simplified Employee Pensions (SEPs)

- A SEP allows an employer to make contributions to employees' IRAs. Although designed for small businesses, any employer, regardless of its size or number of employees, may establish a SEP. Subject to limitations, contributions paid to a SEP are deductible by the employer and excluded from the employees' income until withdrawn.
- Employees who are age 21 or over, performed services for the employer for at least three of the immediately preceding five years and received at least $600 for 2016 and 2017 from the employer must be allowed to participate.
- Contributions are generally limited to $53,000 for 2016 and $54,000 for 2017 or, if less, 25% of the participant's compensation. Contributions must be made under a nondiscriminatory written allocation formula.

SIMPLE IRA Plans

- A SIMPLE IRA plan is a salary reduction arrangement under which employees can elect to have part of their paychecks contributed to an IRA.
- SIMPLE IRAs must cover all employees who received at least $5,000 in compensation from the employer during any two prior years, and who are reasonably expected to receive that much or more in the current year.
- A SIMPLE IRA can only be established by an employer that had 100 or fewer employees earning at least $5,000 during the preceding calendar year.
- Employee elective deferrals are limited to $12,500 for 2016 and 2017. For individuals age 50 or older, the limit is increased to $15,500 for 2016 and 2017. Employers must generally make either 3% matching or 2% nonelective contributions.

The handout is designed to provide accurate information regarding the subject matter covered. However, before completing any significant transactions based on the information contained herein, please contact us for advice on how the information applies in your specific situation.

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