

## BENEFITS CORNER



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### Retirement Plan Basics

For most folks, somewhere out on the horizon lies the magical thought and dream of a happy and comfortable retirement. To reach that dream will take some planning, and there is no time like the present to start, or has that New Year's resolution already been broken?

There are several different types of retirement plans that a small business can implement to assist the owner and many of its employees in reaching that comfortable retire-

ment dream. I would like to review many of the different types of plans and go through a few of the pros, cons, and rules for each.

As a starting point, I will be discussing only the basics of employer-sponsored qualified plans. A qualified plan means that the retirement plan has been set up in accordance with various tax and labor laws. Most retirement plans allow for the contributions made into the plan to be done on a pre-tax basis. Further, the growth of the account balances is not taxable. Taxes in a qualified plan are usually paid at retirement as money comes out of the plan to fund your retirement. (For 2006, there will be new Roth Plans that will allow post-tax contributions and no taxes at the normal withdrawal date).

Any time the government does not get its tax dollars, there are usually very specific rules and guidelines that will need to be followed. That is certainly the case with qualified retirement plans. There are rules regarding employee eligibility, maximum contribution amounts, and vesting for employer contributions into the plan. Many plans also have very specific rules to minimize any potential discrimination within the plan between the well-paid key employees and the more rank-and-file employees.

Most folks have become familiar with 401(k) plans since their introduction to the marketplace in the early 1980s. These plans are very popular with both employees and

employers because of this familiarity. 401(k) plans will work great for most employers because of the flexibility and desirability associated with them. There are times when this type of plan will not work well: employers with only a few employees or when there is very low participation in the plan by lower-paid employees. If this is the case, there are better alternatives.

For plans with very low participation from the lower-paid employees, a Safe Harbor plan or a Simple IRA would be a better alternative. These plans require the employer to match a certain percentage of the participating employee's salary deferral or to make a contribution for all eligible employees. Additionally, there can be no vesting requirements on any contributions the employer makes.

If you have only a handful of employees, a Simple IRA might be the option for you. This program has very low administrative requirements and costs but still allows for employees to make salary deferral contributions.

Some of the other programs work quite well for the self-employed business owner with no other employees. An individual 401(k) is a very attractive offer in this environment because of the contribution source flexibility and the loan provision. A very inexpensive option to set up and administer for this type of employer is the SEP-IRA, which is funded completely by the employing entity.

A SEP-IRA can still be set up for the 2005 tax year; to take advantage of this planning tool, you will need to set up the plan by your tax-filing deadline (including extensions).

All of the above retirement plan options would be considered defined contribution plans. These have grown into the most popular plan offerings because of their flexibility, low cost, and relatively easy administration. There are some other options available in the qualified plan world. These other options are for more traditional pension plans, also known as defined benefit plans. For the most part, defined benefit plans have fallen out of favor because of the large funding requirement placed upon the employer. However, this type of plan can be a great fit for tightly held businesses generating large and stable income streams.

I have included a handy chart (see below) to illustrate some of the more popular retirement plan options. This chart reviews some of the key provisions for each of the plan types. Starting a retirement plan for your business has never been easier than it is today. I would enjoy the opportunity to assist you in selecting the appropriate plan for you and your company. I look forward to hearing from you! ☎

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Plan/Info	401(k) Plan	Safe Harbor 401(k)	Individual 401(k)	Simple-IRA	Profit Sharing Plan	SEP-IRA
<b>Typical Plan Sponsor</b>	All businesses, except governmental agencies	All businesses, except governmental agencies	All businesses with no common law employees	All businesses with fewer than 100 employees, including the self-employed	All Businesses	All Businesses. Most appealing to those with 10 employees or less.
<b>Best features</b>	Provides pre-tax retirement investing and flexibility.	Provides pre-tax retirement investing and flexibility.	Provides pre-tax retirement investing and flexibility.	Provides pre-tax retirement investing and easy administration.	Allows flexible contributions.	Easy administration and flexibility.
<b>Funded By</b>	Employee and Employer	Employee and Employer	Employee and Employer	Employee and Employer	Employer Only	Employer Only
<b>Eligibility Requirements</b>	Usually employees age 21 with one year of service and 1000 hours.	Usually employees age 21 with one year of service and 1000 hours.	Usually employees age 21 with one year of service and 1000 hours.	Employees earning \$5,000 in two prior years.	Usually employees age 21 with one year of service and 1000 hrs.	Usually employees age 21 with any service in three out of five years.
<b>Maximum Annual Individual Contribution</b>	100% of compensation up to \$15,000.	100% of compensation up to \$15,000.	100% of compensation up to \$15,000.	100% of compensation up to \$15,000.	Not Applicable.	Not Applicable.
<b>Maximum Annual Employer Contribution</b>	25% of eligible compensation up to \$44,000	Required contributions: 1. ~4% Match of Salary Deferrals, or 2. Contribute 3% of Salary for all eligible employees	25% of eligible compensation up to \$44,000	Required contributions: 1.3% Match of Salary Deferrals, or 2. Contribute 2% of Salary for all eligible employees. The match can be reduced in 2 out of 5 years.	25% of eligible compensation up to \$44,000	25% of eligible compensation up to \$44,000
<b>Vesting Schedule</b>	Available	100% Immediate	100% Immediate	100% Immediate	Available	100% Immediate
<b>Compliance Testing and Government Reporting</b>	ADP-Yes Top Heavy-Yes 415 Testing-Yes Govt. Reporting-Yes	ADP-No Top Heavy-No 415 Testing-Yes Govt. Reporting-Yes	ADP-No Top Heavy-No 415 Testing-Yes Govt. Reporting-Possible	ADP-No Top Heavy-No 415 Testing-No Govt. Reporting-No	ADP-No Top Heavy-Yes 415 Testing-Yes Govt. Reporting-Yes	ADP-No Top Heavy-Yes 415 Testing-No Govt. Reporting-No
<b>Loans Available</b>	Yes	Yes	Yes	No	Yes	No
<b>When to Establish</b>	Anytime	At least 3 months prior to plan year-end	Anytime	January 1 thru October 1	Prior to fiscal year end	Anytime prior to tax filing, including extensions