

Money Matters

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Skloff Financial Group Question of the Month:

SIMPLE IRA - The Powerful Small and Middle Sized Business Retirement Plan

By Aaron Skloff, AIF, CFA, MBA

Q: We own a middle sized business and want to retain our employees by offering a valuable retirement benefit. We read your article on SEP IRAs. Is there another low cost, low maintenance retirement plan with generous contribution limits?

A: The Problem — Finding a Low Cost and Low Maintenance Retirement Plan with Generous Contributions Limits for Small and Middle Sized Businesses

Many employer sponsored retirement plans require annual testing and annual tax filings. The testing, preparation and filings can be time consuming and costly. Furthermore, many employer sponsored retirement plans have modest contribution limits.

The Solution —SIMPLE IRA

Savings Investment Match Plan for Employees (SIMPLE IRAs) provide self-employed individuals and small and middle sized businesses a low cost, low maintenance employer sponsored retirement plan with generous contributions limits and no employer tax filings.

Who Can Establish a SIMPLE IRA and Who Can Contribute. It can be established by sole proprietors, partnerships, C corporations and S corporations. SIMPLE IRAs are limited to businesses with 100 or fewer employees who earned at least \$5,000 in the preceding year. Even if employees are also employees of another company or university where they participate in their retirement plan (e.g.: 401(k) or 403(b) and/or 457(b)), they can also participate in a SIMPLE IRA. Contributions can be made by employees and employers.

Contribution Limits. Employees can contribute up to 100% of their salary, up to a \$13,500 per year (\$16,500 if age 50 or over). Employers are required to either match employee contributions 100% of the first 3% of compensation (can be reduced to as low as 1% in any 2 out of 5 years) or contribute 2% of each eligible employee's compensation (with a \$250,000 maximum compensation limit). Translation: even if an employee earns \$1 million the employer cannot contribute more than \$5,700 for 2020.

Vesting. With many employer sponsored retirement plans employer contributions can be taken back by the employer if employees do not remain employed by the employer for a certain number of years. After remaining with the employer for a number of years (five years as an example) employees can keep the employer's contributions whether or not they stay with the employer. The process of being able to keep employer contributions over time is called vesting. With a SIMPLE IRA, employer contributions are immediately vested.

Establishment Deadline. The deadline to establish a SIMPLE IRA for 2020 was October 1, 2020.

Withdrawals. Withdrawals can be taken at any time, but are subject to 10% early withdrawal penalties (25% for first two years of plan participation) if taken before the age of 59 ½. Like many retirement plans, SIMPLE IRAs are subject to required minimum distributions (RMDs) starting at age 72 (70 ½ if you reached 70 ½ before January 1, 2020).

Tax Domino Effect. Contributions to a SIMPLE IRA reduce your taxable income. This can have a positive domino effect, avoiding or reducing: capital gains and dividend taxes, net investment income taxes and itemized deductions.

Action Step — Establish a SIMPLE IRA

Offering a SIMPLE IRA retirement plan allows employees and business owners to boost their retirement savings and gain tax benefits as you close your retirement savings gap. Don't put off until tomorrow what you can do today.

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