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Deadline looms for small-business 401(k) plans

Basic retirement plans don't cost a lot to set up, can be useful recruitment and retention benefit

By Darla Mercado | *September 25, 2014 - 1:10 pm EST*

The deadline for advisers to nudge their small business clients into opening a basic retirement plan is right around the corner.

Small employers hoping to set up a new SIMPLE IRA, SIMPLE 401(k) or a safe harbor 401(k) have until Oct. 1 to do so. SEP IRAs must be set up by Oct. 15 — if that's when the taxpayer is filing his return. Solo 401(k) plans need to be set up by Dec. 31.

The plans make sense for small to medium-sized businesses that are overseen by individuals who want to help either their employees or themselves save more money for retirement and do so without the added cost of setting up a traditional 401(k).

"Why pay $2,000 to $4,000 to set up a 401(k) plan?" asked Scott A. Bishop, director of financial planning at STA Wealth Advisors. "Better to use that money to buy inventory and pay salaries."

They're also good for business. Want to attract and retain employees? Set up a retirement plan.

Another advantage is that for some of these plans, namely the SIMPLE IRA and SIMPLE 401(k), as well as the safe harbor 401(k), employers don't have to worry about non-discrimination testing, provided they follow the rules of the safe harbor 401(k). Traditional 401(k)s are subject to nondiscrimination testing each year, where the plan must show that it's providing benefits for rank-and-file workers and not just managers.

First, a breakdown of the different plans:

The Savings Incentive Match Plan for Employees, or **SIMPLE IRA**, makes sense for businesses with 100 or fewer workers with at least $5,000 in compensation during the preceding calendar year. Eligible workers can make a contribution that's pulled from their salaries, and the employer must make either a matching contribution or a non-elective contribution, according to the IRS.

The employer contribution can be done in one of two ways. He or she can match the worker's contribution on a dollar for dollar basis up to 3% of the worker's pay. Alternatively, the employer can make non-elective contributions of 2% of the worker's pay up to the annual limit of $260,000 for 2014.

Workers can defer up to $12,000 in 2014 into a SIMPLE IRA, and those who are over 50 can make an additional catch-up contribution of $2,500.

There's also the **SIMPLE 401(k)**, which has requirements similar to the SIMPLE IRA, but can have a Roth 401(k) component. The employees must be totally vested in all of the contributions.

With a **safe harbor 401(k)**, employers can make matching contributions dollar for dollar up to 3% of the worker's pay and 50 cents on the dollar for each employee contribution that exceeds 3% but not beyond 5% of that worker's salary. Plan sponsors can also choose to make non-elective contributions of 3% of salary to the worker's account.

But there are plenty of benefits to the employer who sets it up. He or she is eligible for a $500 tax credit each year for the first three years the safe harbor plan is in existence and the match is tax-deductible, explained Stuart Robertson, head of ShareBuilder 401k, a provider of small business 401(k) plans.

“Small business owners benefit from having the safe harbor plan,” he said. “They're trying to get it for their own tax benefits, and they also want to help the most valuable employees benefit.”

For those who are either self-employed or have a very small number of employees, the SEP IRA or the Solo 401(k) may make sense.

The Simplified Employee Pension Plan, or **SEP IRA**, is set up to take only employer contributions. The employer can make a tax-deductible contribution that's equal to 25% of the worker's pay or $52,000 for 2014, whichever is less. Catch-up contributions and elective deferrals aren't allowed in these plans, according to the IRS. Each of the workers must set up their own individual SEP IRA.

Finally, the **Solo 401(k)** allows the self-employed individual to contribute at up to $17,500 a year, plus $5,500 if he or she is over age 50. That individual can also include a Roth option for the plan, and he or she can maximize savings by adding a profit-sharing component.

“The most you can put into a SIMPLE IRA or SIMPLE 401(k) is $12,000 and the match, but with a Solo 401(k), you can defer more money than with either the SIMPLE IRA or SIMPLE 401(k),” said Mr. Bishop.