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AEPS Pension Update

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Does Your Retirement Plan Solve Your Problems?

The retirement planning process has evolved over the years from transaction oriented to a long-term, consultative process. There is no need to settle for a one-size-fits-all approach. Today's plans can be tailored to meet the goals and solve the unique financial, tax, and employee benefit concerns of each business owner. The plan for your business should be no exception. In today's *Pension Update*, I'll explain how safe harbor plans can provide solutions to many of the common problems experienced by business owners like you.

The first step in the process is to articulate the problems you'd like your retirement plan to address. Most commonly, the issues are as follows:

- Tax management – with marginal tax rates set to increase in January, the ability to defer current taxes and/or receive tax-free retirement income becomes increasingly important
- Managing the cost of employee contributions
- Liquidity – pre-retirement access to savings
- Protecting assets from creditors

Once your planning concerns are prioritized, we begin looking for the best fit.

IRA-based plans – A mismatch with common goals

IRA-based plans are a natural place for the retirement planning process to begin. These plans are easy to understand, inexpensive, and straightforward to administer. However, IRA-based plans are not all things to all people, and often fail to provide solutions to planning needs. The contributions limits – and therefore the deduction opportunity – can be too low, the creditor protection insufficient, the employee cost too high, and the access to assets too restricted.

Limitations of SIMPLE IRAs are a deferral limit of $11,500 ($14,000 if over 50), maximum employer contribution of 3% of compensation, and an exclusive plan rule precludes use of a supplemental plan to increase contribution potential.

SEP IRAs are limited by the fact that they are funded exclusively by your company contributions. In other words, your employees don't bear any responsibility for funding the plan. When several employees become eligible for the plan, the amount of employee contributions can easily exceed your tax savings. Neither the SEP nor the SIMPLE can offer a Roth feature which provides access to tax-free retirement income, a loan or in-service distribution feature, or the robust creditor protection under Title I of ERISA.

Traditional 401(k) – A step in the right direction

A traditional 401(k) often forms a better fit than IRA-based plans. For example, a traditional 401(k) provides a deferral limit of $16,500 ($22,000 if over 50). These plans offer Roth treatment of deferrals, which allows you to forego the current year deduction on deferrals in favor of tax-free retirement income. A loan feature, in-service distribution feature, and creditor protection under Title I of ERISA are also available. Unfortunately, contributions to traditional 401(k) plans are required to go through a compliance testing process. The outcome of this process could lead to reduced contribution potential for the owner and family members, unexpected employee costs, or contribution refunds.

Safe Harbor 401(k) – A fit with common planning concerns

To address these issues, a traditional 401(k) can be enhanced with safe harbor features. Safe harbor features require you to make a small contribution to employee accounts. In a safe harbor plan, you would have to agree to make a contribution equal to 3% of compensation for all eligible employees, or match the contributions of employees who choose to defer their salaries to the plan up to 4% of their compensation. By making this commitment to contribute to employee accounts, you in return are assured the ability to maximize your deferrals.

Safe harbor 401(k) plans also receive creditor protection under Title I of ERISA, can contain a loan feature which provides access to up to $50,000 of retirement savings. Hardship and in-service distribution features can expand the accessibility of retirement savings. A Roth feature can be included as a vehicle to provide tax-free retirement income.

Safe harbor plans also allow you to increase tax savings by making deductible Profit Sharing contributions above the safe harbor minimum. Taken together, the features of safe harbor plans fit neatly with the common planning concerns. The grid below highlights the availability of features among common retirement plans.

Plan ⇩	Features ⇨					
	Salary Deferrals	Mandatory Employer Contribution	Discretionary Employer Contribution	Roth Feature	ERISA Title I Creditor Protection	Loan, In-service, & Hardship Distributions
SEP	Not available	No mandatory employer contributions	Discretionary employer contributions up to 25% of compensation	Not available	Not available	Not available
SIMPLE	Capped at $11,500 (+$2,500 catch up if over age 50)	Mandatory 2% non-elective contribution or 3% match	Additional employer contributions not available	Not available	Not available	Not available
Traditional 401(k)	Capped at $16,500 (+$5,500 catch up if over age 50). Deferrals subject to compliance testing.	No mandatory employer contributions	Total employer contributions capped at 25% of payroll. Total contribution limit from all sources: $49,000 or $54,500 if 50+.	Available	Available	Loans: Yes, lesser of 50% of vested balance or $50,000. Hardship: Yes In-service distributions: Yes
Safe Harbor 401(k)	Capped at $16,500 (+$5,500 catch up if over age 50) Deferrals automatically pass ADP testing.	Mandatory employer contributions of 3% non-elective or 4% match. Can be discontinued, which activates traditional 401(k) compliance testing.	Total employer contributions capped at 25% of payroll. Total contribution limit from all sources: $49,000 or $54,500 if 50+.	Available	Available	Loans: Yes, lesser of 50% of vested balance or $50,000. Hardship: Yes In-service distributions: Yes

Do you have **at least one employee** and are you willing to make **modest contributions** to employee accounts?
Do you require contribution and deduction opportunities **beyond the limits of traditional and SIMPLE IRAs**?
Do you want to be able to **maximize deferrals** without regard for employee deferral habits?
Would you benefit by having **protection for retirement assets** from judgment creditors?
Would you like the ability to receive Roth treatment on a portion of contributions and **tax-free income in retirement**?

If answers to any of the above are 'yes' your next step is to contact me with your top retirement planning concerns. We'll work together to determine your contribution target amount and gather employee data. This initial step usually requires less than an hour of your time. Within a few days, we'll provide a recommended design plan that fits with your planning concerns.

Timing constraints
Safe harbor plans must be in place by October 1 to be effective for 2010 for calendar year businesses. To stay ahead of deadlines, and begin designing your plan to solve your unique planning concerns, I invite you to contact me today.