

Retirement Plan Options

In recent years there has been a lot of talk in Washington about the need to "fix" social security so that it remains fiscally solvent well into the next century. While that's certainly a worthy goal, even if the effort is successful, people still need to take charge of their own retirement planning.

Social security was never intended to provide more than a minimal safety net. Thus, assuming people want a financially comfortable retirement they need to have other sources of income to draw upon during what could be a 20 to 30+ year period of their life.

One of the best sources of additional income is a company retirement plan. Not only does it generally offer tax deductions to the sponsoring employer, it also allows employees covered by the plan to build retirement benefits without currently paying taxes on the increasing value of those benefits.

Unfortunately, dealing with retirement plans can often leave employers confused about the choices available or concerned about the costs of each of the options. Perhaps they'd like to help their employees (and themselves) save more for retirement but they don't know where to start. If this describes your situation, you'll want to explore the chart below. It describes the key characteristics of the most common retirement planning options. The chart moves from the simplest option on the left side (a payroll deduction IRA which is really nothing more than a way to assist employees in setting up their own IRAs) to the most complex choice on the right (the traditional defined benefit plan that guarantees employees a certain specified benefit at retirement).

Summary of Retirement Plan Options

Issues	Payroll Deduction IRA (or Roth IRA)	SEP-IRA	SIMPLE-IRA	Defined Contribution			Defined Benefit Plan
				401(k)	Profit Sharing	Money Purchase Plan	
Key Advantage	Easy to set up and maintain.	Easy to set up and maintain.	Salary reduction plan with little administrative paperwork.	Permits employee to contribute more than in other options.	Permits employer to create large account balances for employees.	Permits employer to make a larger contribution than through other Defined Contribution Plans.	Provides a fixed, pre-established benefit for employees.
Employers Who Can Provide This Option	Any business.	Any business. ¹	Any business with 100 or fewer employees	Any business.	Any business.	Any business.	Any business.

			that does not currently maintain any other retirement plan.				
Employer's Responsibilities	Set up arrangements for employees to make payroll deduction contributions. Transmit contributions for employees to funding vehicle. No employer tax filing required. Employer likely is subject to ERISA rules if the employer, rather than employees, chooses the funding vehicle.	Set up plan (generally by completing IRS Form 5305-SEP). No employer tax filing required.	Set up plan (generally by completing IRS Form 5304-SIMPLE or 5305-SIMPLE.) No employer tax filing required. Bank or financial institution does most of the paperwork.	There is no model form to establish a plan. Advice from a financial institution or employee benefit advisor is necessary. Annual filing of IRS Form 5500 series return is required. Also requires special testing [unless a SIMPLE 401(k) plan is used] to ensure plan does not discriminate in favor of highly compensated employees.	There is no model form to establish a plan. Advice from a financial institution or employee benefit advisor is necessary. Annual filing of IRS Form 5500 series return is required.	There is no model form to establish a plan. Advice from a financial institution or employee benefit advisor is necessary. Annual filing of IRS Form 5500 series return is required.	There is no model form to establish a plan. Advice from a financial institution or employee benefit advisor is necessary. Annual filing of IRS Form 5500 series return is required. Actuary must determine funding obligations.
Funding Responsibility	Employee contributions remitted through payroll deduction.	Employer contributions only. ²	Employee salary reduction contributions and employer contributions.	Employee salary reduction contributions and employer contributions.	Employer contributions only, unless 401(k) feature is included (see previous column).	Employer contributions only.	Primarily employer; may require or permit employee contributions.
Contributor's Options	Employee can decide how much to contribute at any time. ³	Employer can decide whether or not to make contributions year to year.	Employee can decide how much to contribute. Employer must make matching contributions or contribute 2% of each employee's salary up to the set	Employee makes contributions as set by plan option. The employer may match.	Employer makes contributions as set by plan terms. Level of contributions can be redetermined each year.	Employer makes contributions as set by plan terms. Such contributions are mandatory.	Employer makes contributions as set by plan terms.

			maximum.				
Maximum Annual Contribution Per Participant	\$2,000.	Up to 15% of compensation or maximum of \$24,000 (indexed). ⁴	<i>Employee:</i> \$6,000 per year (indexed). ⁵ <i>Employer:</i> Either match employee contributions dollar for dollar up to 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. ⁶	<i>Employee:</i> \$10,000 (indexed). ⁷ <i>Employer/Employee combined:</i> Up to a maximum of 15% of compensation or a maximum of \$24,000. ⁴	Up to a maximum of 15% of salary or a maximum of \$24,000. ⁴	Up to a maximum of 25% of salary or a maximum of \$30,000. ⁴	Per plan terms, employer may permit or require employee contribution.
Minimum Employee Coverage Requirements	No requirement. This is merely a convenience that can be offered to any or all employees.	Must be offered to all employees who are at least 21 years of age, employed by the business for 3 of last 5 years and who earn at least \$400 during 1998 with the employer.	Must be offered to all employees who have earned at least \$5,000 in any previous 2 years and are reasonably expected to earn this amount in current year.	Generally must be offered to all employees at least 21 years of age who worked at least 1,000 hours in previous year.	Generally must be offered to all employees at least 21 years of age who worked at least 1,000 hours in previous year.	Generally must be offered to all employees at least 21 years of age who worked at least 1,000 hours in previous year.	Generally must be offered to all employees at least 21 years of age who worked at least 1,000 hours in previous year.
Withdrawals, Loans & Payments	Withdrawals at any time; subject to current federal income taxes and a possible 10% penalty if the participant is under age 59½.	Withdrawals at any time; subject to current federal income taxes and a possible 10% penalty if the participant is under age 59½.	Withdrawals at any time; subject to current federal income tax and, if employee is under age 59½, may be subject to a 25% penalty if taken within the first two years of	Cannot withdraw employee elective contributions until a specified event, such as reaching 59½, death, separation from service, or other event as identified in plan. May permit loans and hardship	May permit loans and hardship withdrawals. Hardship withdrawals subject to current federal income tax and, may be subject to a possible	Payment of benefits generally at retirement, may offer participant loans.	Payment of benefits generally at retirement, may offer participant loans.

			participation and a possible 10% penalty if taken afterwards.	withdrawals. Withdrawals subject to current federal income tax and, may be subject to a possible 10% penalty if participant is under age 59½.	10% penalty if participant is under age 59½. Payment of benefits generally at retirement.		
Vesting	Immediate 100%.	Immediate 100%.	Employee and employer contributions vested 100% immediately.	Employee contributions vested immediately. Within specified limits, employer contributions may vest over time according to plan terms.	Within specified limits, may vest over time according to plan terms.	Within specified limits, may vest over time according to plan terms.	Within specified limits, may vest over time according to plan terms.

Notes:

1. If the employer also maintains a qualified plan [such as a 401(k), profit sharing plan, or defined benefit plan] or has ever maintained a defined benefit plan, special language must be contained in the SEP document to limit contributions.
2. If employer set up a salary reduction SEP (SARSEP) prior to 1997, such a plan can continue in operation after 1996 and employees (even if hired after 1996) can continue to make elective deferrals to such a plan.
3. Roth IRA contributions are not allowed if income exceeds \$95,000 to \$110,000 for singles or \$150,000 to \$160,000 for married couples filing a joint return. (The \$2,000 contribution limit phases out proportionately within these income ranges.)
4. Maximum compensation on which 1997 and 1998 contributions can be based is \$160,000.
5. Maximum for 1998 is \$6,000.
6. Maximum compensation on which 1998 employer 2% non-elective contributions can be based is \$160,000.
7. Maximum for 1998 deferrals is \$10,000.