



Simplify your retirement plan

SIMPLE IRA plans for small businesses



What is a SIMPLE IRA plan?

A Savings Incentive Match Plan for Employees (SIMPLE) is designed exclusively for small businesses as a way to offer a low-cost, easy-maintenance retirement plan. A SIMPLE IRA plan is a written salary reduction arrangement that allows small businesses to make elective contributions into Individual Retirement Accounts (IRAs) set up for the benefit of each eligible employee. SIMPLE IRAs are also available to self-employed individuals.

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Why does your small business need a SIMPLE IRA plan?



Some individuals may need as much as 70% of their pre-retirement income to maintain their current lifestyle during retirement. Savings from pensions and other retirement plans will have to make up a large percentage of their retirement income. Saving through an employer plan may help your employees (and you) achieve this goal.

Tax deduction

Employer contributions and employee salary deferral contributions made to an employee's SIMPLE IRA may be tax deductible as a business expense.

Tax savings

The amount employees contribute through salary reduction to their SIMPLE IRAs will help reduce their taxable income each year.

Tax deferral

The money contributed to a SIMPLE IRA will continue to accumulate on a tax-deferred basis until money is withdrawn. Withdrawals are subject to ordinary income tax and, if taken before age 59½, may be subject to an additional 10% federal income tax. This percentage increases to 25% for distributions taken within the first two years of participation in the plan.

Compete for talent

Providing a retirement plan will help you compete for the talent you need and retain the skilled workers you have.

ESTABLISHING A SIMPLE IRA PLAN

There are three basic steps:

Step 1 – Execute a formal written agreement.

A SIMPLE IRA plan is adopted when a business creates a written agreement authorizing it and eligible employees are informed. You may use the Internal Revenue Service's (IRS) Form 5304-SIMPLE. Each eligible employee who wishes to make salary reduction contributions to a SIMPLE IRA should complete a Salary Reduction Agreement.

Step 2 – Give all eligible employees information about the plan.

Information about the plan must be provided to each eligible employee. Sample forms and communications are available from financial institutions.

Step 3 – Make sure a SIMPLE IRA is set up for each eligible employee.

A SIMPLE IRA must be set up for each eligible employee. If an eligible employee does not set up a SIMPLE IRA, the employer is required to set it up on the employee's behalf. Each SIMPLE IRA is individually owned and controlled.

The simple facts

Employers who are eligible to establish a SIMPLE IRA plan

These include, but are not limited to:

- Corporations
- Sole proprietorships
- Partnerships
- Tax-exempt organizations
- Government entities

Likely candidates for a SIMPLE IRA plan

An employer who:

- Has no more than 100 employees who received at least \$5,000 in compensation for the previous year.
- Would like a plan that is easy to communicate to employees and relatively inexpensive to operate.
- Does not sponsor another qualified plan (this includes a 401(k) plan, pension plan, profit-sharing plan, a 403(b) annuity plan, or a Simplified Employee Pension plan (SEP).
- Wishes to establish a plan with an employee contribution component.

Advantages of a SIMPLE IRA plan

SIMPLE IRA plans are not subject to complex discrimination testing and annual reporting requirements like many other employer-sponsored plans. By following the guidelines in IRS Form 5304-SIMPLE, you will ensure your SIMPLE IRA plan is in compliance with minimal administrative burden.

Economical

The cost to maintain a SIMPLE IRA plan is minimal compared to other plan types that require annual compliance testing and government reporting.

Choice of employer contribution component

- An employer may choose to match, dollar-for-dollar, employee contributions up to 3% of compensation.
- Or, an employer may choose a non-elective contribution equal to 2% of compensation for each eligible employee, up to IRS limits.
- The employer contribution election may change each year.

Ability to exclude certain employees

Employers may wish to exclude part-time employees. With a SIMPLE IRA plan, employers may exclude employees from the plan who have not earned at least \$5,000 in two previous years and who are not reasonably expected to earn as much in the current year.

Limited fiduciary responsibility

Because employer contributions are invested directly into each eligible employee's IRA, investment decisions are the responsibility of the employee. Generally, this aspect of a SIMPLE IRA reduces the amount of fiduciary responsibility incurred by the employer.

SIMPLE IRA contributions

Employee contributions (salary deferral)

All employees, including highly compensated employees, can participate in the plan and defer up to the maximum dollar limits or 100% of compensation, whichever is less, for the corresponding year. In addition, individuals age 50 and above may also make “catch-up contributions” to their SIMPLE IRA plan.

Year	Contribution Limit	Catch-Up Contribution Limit
2020	\$13,500	\$3,000

Employer contributions

Matching contributions: You must match your employee’s contributions dollar-for-dollar, up to a 3% cap of their compensation for the calendar year (or \$13,500 for 2020, whichever is less). You may elect a lower percentage (not lower than 1% of compensation) for the cap, but only in two years of any five-year period.

OR

Non-elective contributions: A contribution of 2% of compensation will be made for all eligible employees who have at least \$5,000 in compensation from you during the year. Non-elective contributions may not be based on more than \$285,000 of compensation in 2020 (may be indexed for inflation in subsequent years). Note: Although the 2% non-elective contribution is mandatory for every eligible employee, matching contributions are only required for those employees who elect to contribute to the SIMPLE IRA plan.

The advantage is a SIMPLE IRA plan

A SIMPLE IRA plan can help you and your employees save for retirement. In addition, offering a SIMPLE IRA plan can make good business sense because it allows you to offer benefits to all employees, including those who are highly compensated. As a result, you may be better able to attract and retain the talent you need to grow your business.



Case study

Curtain Call Custom Drapes and Upholstery Company

For the year 2020, business owners and sisters Sue and Lori Cole decide to maximize contributions to their SIMPLE IRA plan by electing a 3% matching contribution. Sue and Lori decide to exclude Ellen Cole, who works part-time for her sisters during the summer, from the plan because she only earns \$4,700, failing to meet the \$5,000 compensation requirement.

CONTRIBUTION EXAMPLE

Name	Compensation	Employee Contribution	Employer Contribution	Total Contributions
Sue Cole	\$70,000	\$13,500	\$2,100	\$15,600
Lori Cole	\$70,000	\$13,500	\$2,100	\$15,600
Ellen Cole	\$4,700	\$0	\$0	\$0
Julia Taylor	\$25,000	\$1,300	\$750	\$2,050
Total employee contributions:		\$28,300		
Total company matching contributions:		\$4,950 (\$2,100 + \$2,100 + \$750)		
Tax savings on matching contributions @ 35% tax rate:		\$1,733 (\$4,950 x 35%)		
Net cost of employer matching contributions:*		\$3,217 (\$4,950 - \$1,733)		

* Example does not include fees that may be incurred for professional tax services and record keeping.

How a SIMPLE IRA plan benefits the Cole sisters

- Sue and Lori Cole were each able to put aside \$15,600 toward retirement.
- All contributions to the plan will continue to accumulate on a tax-deferred basis.
- The Cole sisters were able to exclude Ellen, who only worked part time for the company, thereby reducing the cost to maintain the plan.
- Julia elected to put aside \$1,300 toward her retirement through salary reduction. In addition, Julia sees the plan as another reason to stay with the company, because she also receives a 3% matching contribution, or an additional \$750.
- Ellen plans on working full time for her sisters once she graduates from design school. At that time, she will be able to participate in the plan and start saving for her retirement years.
- Employer contributions and employee salary deferrals to the plan are a tax-deductible business expense.

SIMPLE IRA distributions

Distributions

An employee may take a distribution from their SIMPLE IRA at any time. Distributions from a SIMPLE IRA are subject to ordinary income tax and, if taken prior to age 59½, may also be subject to a 25% federal income tax if the distribution is taken within the two-year period beginning on the date the employee first participates in the plan. Distributions after this two-year period but prior to age 59½ may be subject to an additional 10% federal income tax.

Indirect rollovers

An employee receiving a distribution from their SIMPLE IRA may roll over that distribution within 60 days of receipt to a qualified retirement plan without incurring income taxes or penalties. Rollovers from a SIMPLE IRA to a Traditional IRA may only be made if the rollover distribution is taken after the two-year period beginning on the date the employee first participated in the plan. An eligible employee can also roll over funds from another SIMPLE into the new SIMPLE plan at any time, and can roll over funds from another eligible retirement plan or IRA once the two-year period has been satisfied. Only one indirect IRA to IRA rollover may be made within any 12-month period, regardless of how many IRAs your employee owns.

Trustee-to-trustee transfer (direct rollovers)

There are no restrictions on the number of trustee-to-trustee transfers that may be completed during a year. A trustee-to-trustee transfer occurs when an employee moves their SIMPLE IRA assets from one qualified retirement plan to another without taking physical receipt of the funds. There is no waiting period for trustee-to-trustee transfers.

Additional information

To learn more about SIMPLE IRAs, **visit the IRS** at [irs.gov](https://www.irs.gov). IRS publications 560, 590-A, 590-B and IRS Notice 98-4 are essential SIMPLE IRA plan resources.

Your financial professional can help you to evaluate your choices for funding a SIMPLE IRA plan.



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