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APRIL 2000

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Retirement Plans For Small Businesses? Think SIMPLE!

By M. Christopher Zinser

Q. As a small business owner trying to provide an employee retirement program, I find 401(k) plans expensive and time-consuming to administer. Are there other options?

a. The administrative red tape and costs associated with providing most employee benefits have made it difficult for small business owners to consistently attract, reward, and retain the best and brightest workers. This is particularly true of 401(k) plans because of their time-consuming testing, disclosure, and complex reporting requirements. IRS rules give small business owners an excellent opportunity to offer a retirement savings plan without such burdens.

As part of the Small Business Job Protection Act, Congress authorized SIMPLEs – Savings Incentive Match Plans for Employees. This IRS-approved retirement plan offers employees and business owners advantages that 401(k) participants enjoy, including savings on current income taxes, plus tax-deferred and compounded growth on their earnings. The legislation also repealed SARSEPs (Salary Reduction Simplified Employee Pension) plans, the government's prior attempt at simplifying retirement plans for employers with 25 or fewer eligible employees.

Both profit and non-profit companies with up to 100 eligible employees qualify to adopt one of two plan variations – SIMPLE IRA or SIMPLE 401(k). Employers may cover all employees or limit eligibility to employees who have earned at least $5,000 annually in any two prior years and are expected to earn at least that amount in the current year.

In addition to providing small businesses with an attractive employee benefit, SIMPLE plans give employers a tax break. Any contribution an employer makes to the plan qualifies as a tax deduction for the business.

SIMPLE IRAs are truly simple because employees "own" their IRA within the plan. This has a number of specific benefits for employers. Each participant bears the investment responsibility and risk, so employers avoid any fiduciary re-sponsibility. Also, unlike 401(k) and other salary reduction plans, maintaining a SIMPLE IRA does not require testing as a basis for contribution limits. As a result, small business owners and their highly compensated employees can elect to defer up to $6,000 – even if no other employees enroll in the plan.

While SIMPLE plans require employers to contribute to the plan, they are allowed some flexibility. In brief, an employer may choose to make a 3 percent matching contribution to participating employees or a 2 percent non-elective contribution to all eligible employees. The matching contribution may be reduced to as low as one percent in two of five years. In either case, employee notification is required in advance of a 60-day enrollment period.

To make small company plans easier to administer, the IRS eliminated the top-heavy and non-discrimination testing for SIMPLEs. These requirements – along with related disclosure and reporting – characterize 401(k)s and typically require third-party administration.

Reporting requirements for SIMPLE IRAs are minimal. Employers must notify the IRS which eligible employees are active participants in the plan and the amount of employees' salary reduction contributions to the plan on Form W-2. In general, this makes SIMPLE IRAs even more convenient than SIMPLE 401(k)s, since the latter requires the same reporting and disclosure conditions of a traditional 401(k).

In a world that appears to be getting more complicated and competitive by the minute, SIMPLE IRAs are sure to be a hit with small business owners. TW

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