SEP

Employers establish retirement plans for many reasons. First, the employer may want to provide retirement benefits for him or herself. Second, offering a retirement plan may serve to reward and retain quality employees. And third, a retirement plan may help attract competent new employees to the business. If any of these motivations apply to you, and if the idea of a plan that is extremely easy to establish and operate attracts you, then the simplified employee pension – better known as the "SEP" – may be the plan for you.

WHAT MAKES A SEP PLAN UNIQUE?

SEP plans deliver on the promise of simplicity.

A SEP plan eliminates

- Virtually all of the administrative complexity found in many retirement plans,
- Lengthy and detailed government reporting,
- Numerous nondiscrimination tests, and
- Complicated, restrictive contribution formulas associated with many retirement plans.

MUST ALL EMPLOYEES PARTICIPATE?

Generally, all employees are eligible, though the employer may exclude

- Employees under age 21 (or the employer may select a lower age),
- Employees who have not worked in (up to) three of the prior five years,
- Certain union or nonresident alien employees, and
- Employees not earning the minimum annual amount (indexed at $500 for 2008.)

(Employees meeting the plan's eligibility requirements may not choose to be excluded from a SEP plan, and an employer must contribute for them.)

HOW ARE SEP CONTRIBUTIONS MADE?

The manner in which SEP plan contributions are made is just as easy as the rules governing SEPs.

Under a SEP plan,

- An employer generally has discretion whether or not to make a contribution in any year,
- Contributions are directed into a Traditional IRA held by each employee,
- Investment decisions and performance are the responsibility of each employee,
- Contributions are the same percent of all employees' compensation (maximum of 25 percent of $230,000 compensation cap), or the employer may instead specify a fixed dollar amount for all employees.

What are the tax benefits of a SEP?

In addition to providing a means to save for retirement, SEP plans also can provide immediate tax benefits, because

- SEP plan contributions to the business owner and employees are tax deductible,
- Amounts contributed remain tax-deferred, as do their earnings, until withdrawn,
- Withdrawals (distributions) are taxed as ordinary income under the Traditional IRA rules.

Do SEP plans allow employee deferrals?

Some SEP plans allow employee salary deferrals, which means that employees elect to have some compensation withheld and contributed to the plan. But such deferrals are only permitted in certain SEP plans that were properly established by December 31, 1996. SEP plans opened after that time do not allow employee deferrals. (The SIMPLE IRA plan does allow employee salary deferrals).

Does SEP plan participation affect Traditional IRA contributions?

Employees who participate in a SEP plan are considered "active participants" in an employer retirement plan. As such, the deductibility of their Traditional IRA contribution may or may not be affected, depending on their income. SEP plan participation does not, however, reduce or eliminate an employee's ability to fund a Traditional IRA, and all Traditional IRA earnings are tax-deferred, regardless of SEP plan participation. But more important, a SEP plan offers the advantage of a contribution which is potentially much larger than a Traditional IRA contribution.

When must a SEP plan be established and funded?

A SEP plan may be set up and funded at any time prior to the business's tax return due date, plus extensions.

For more information…

For more information on how your business and employees can benefit from establishing a SEP plan, contact the experts at Salem Five. Call Louise A. Mallett, CISP, Vice President at 978-720-5255. Start today on the road to a secure financial future.