

# Choosing a Retirement Plan

A tax-favored retirement plan is a highly valued employee benefit. Most employers recognize that offering a retirement plan can increase satisfaction and productivity. It can also help businesses attract and retain qualified employees. Choosing the right plan, however, requires careful consideration. Each option has its advantages.

## 401(k) Salary Deferral Plan

A 401(k) plan gives employees the opportunity to save for retirement by deferring a portion of their pay to the plan. Employers may choose to contribute, often by matching a portion of employees' plan contributions. Assuming tax law requirements are met, employer contributions are tax deductible. As with other "defined contribution" plans, retirement benefits are based on the balances in employees' individual plan accounts.

Salary deferrals are made *before* taxes are taken out — a tax benefit for employees who participate. Any investment earnings generated by employee or employer contributions are also not immediately taxed. Generally, income taxes are due only when employees receive distributions from their accounts. However, you have the option of adding a Roth feature to your 401(k) plan, which would allow participants to make after-tax contributions. As long as certain tax law requirements are met, qualifying distributions of Roth amounts (including earnings) are tax free.

## Profit Sharing Plan

Profit sharing plans offer employers a great deal of flexibility. Contributions may be made according to a formula written into your plan, or they may be made at your company's discretion. If you wish, the plan may be structured to allow contributions in years with low or no profits. Employees are not permitted to contribute. If employee contributions are desired, a 401(k) option may be added to the plan.

Profit sharing contributions are generally allocated to employees' plan accounts based on compensation. Since your company's tax deduction for plan contributions is limited to 25% of the total yearly compensation paid to your participating employees, employers often limit profit sharing contributions to 25% of compensation. Other tax law limits also apply.

Retirement benefits are based on each participant's account balance, which reflects the employee's years of service, your company's contributions, and your plan's investment performance. Since company contributions generally are dependent on profitability, a profit sharing plan can be a strong incentive for employees to perform well.

## Money Purchase Pension Plan

A money purchase pension plan is similar to a profit sharing plan with one notable difference: Employers are *required* to contribute to employee accounts annually, regardless of profitability. The required contribution is inflexible and is generally stated as a specific percentage of each participating employee's compensation.

As with a profit sharing plan, an employee's account balance depends on years of participation, the amount your company has contributed, and your plan's investment performance. Various tax law limits apply.

## Simplified Employee Pension (SEP) Plan

Simple is the theme of this retirement plan. SEPs are relatively simple to implement and have fewer administrative requirements than many other retirement plans. For these reasons, SEP plans are appealing to smaller companies.

With a SEP, you establish individual retirement accounts (IRAs) for each of your eligible employees. All employees who earn at least \$550 (in 2012), are age 21 or older, and have worked for the employer during at least three of the immediately preceding five years are eligible for participation. Employer contributions are discretionary and tax deductible (within limits). Employees are not permitted to contribute to newly established SEP plans.

## Savings Incentive Match Plan for Employees (SIMPLE)

The SIMPLE plan is another attractive option for smaller employers.\* It can be structured as a SIMPLE 401(k) plan or as a SIMPLE IRA plan. All employees who received at least \$5,000 in compensation from the employer during any two preceding years and who

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are expected to earn at least \$5,000 during the current year are eligible for participation in a SIMPLE IRA plan.

Unlike a SEP plan, a SIMPLE plan<sup>®</sup> allows employees to contribute. Your company must make a minimum matching contribution or contribute a minimum percentage of compensation on behalf of each eligible employee, whether or not the employee contributes. Contributions are tax deductible.

Benefits are based on each participating employee's account balance. As the name implies, setup and administration are simplified. Recordkeeping and reporting requirements are also minimal.

### Defined Benefit Pension Plan

Defined benefit plans — often regarded as “traditional” pension plans — are so named because they pay fixed retirement benefits. Benefit amounts are based on a formula written in the plan. The formula may direct that employees be paid a percentage of their average compensation over a particular number of years, or it

may call for a flat monthly payment based on months or years of service. Or you may develop another formula that better meets your needs. A defined benefit plan is funded entirely by your company. Annual funding amounts are based on actuarial calculations and are tax deductible.

### Employee Stock Ownership Plan (ESOP)

With an employee stock ownership plan, plan assets are invested in your company's stock. Retiring employees receive retirement benefits as cash or employer stock. If the stock is not readily marketable, employees must have the option of selling the stock back to the ESOP or to your company.

**These are just brief “snapshots” of several popular retirement plans. Your professional advisors can provide you with the additional information you'll need to make an informed decision.**

HOW RETIREMENT PLANS COMPARE					
	401(k)	Profit Sharing	Money Purchase	SEP	SIMPLE
<b>Which employers should consider this plan?</b>	All employers	All employers	All employers	All, but typically appeals to small employers	Limited to employers with 100 or fewer eligible employees and no other retirement plan
<b>May employees contribute to this plan?<sup>1</sup></b>	Yes — elective deferrals of up to \$17,000 plus catch-up contributions of \$5,500 for participants age 50 or older	No	No	No <sup>2</sup>	Yes — deferrals of up to \$11,500 plus catch-up contributions of \$2,500
<b>Must employers contribute to this plan?</b>	No — however, employer contributions are allowed	Yes — contributions can be discretionary	Yes — mandatory contributions	Yes — discretionary contributions	Yes — must match employee contributions up to 3% of pay or contribute 2% of pay for all eligible employees
<b>What is the maximum annual contribution?<sup>3</sup></b>	Smaller of \$50,000 or 100% of participant's compensation <sup>3</sup>	Same as 401(k)	Same as 401(k)	Smaller of \$50,000 or 25% of participant's compensation	\$11,500 (plus \$2,500 catch-up) deferral plus employer contribution (see above)
<b>What is the maximum deduction?</b>	25% of all participants' compensation plus employee deferrals	25% of all participants' compensation	Same as profit sharing plan	Same as profit sharing plan	Same as maximum contribution

<sup>1</sup> Dollar amounts are the 2012 tax law limits. The IRS adjusts the annual limits for inflation.  
<sup>2</sup> Elective deferrals are allowed if the plan is a salary reduction SEP (SAR-SEP) established before 1997.  
<sup>3</sup> Compensation is generally limited to \$250,000 in 2012.

\* Employers with 100 or fewer employees who received \$5,000 or more in compensation from the employer for the preceding year

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