



What are the costs of offering a company retirement plan?

The good news is that there are several plans available to small-business owners from IRAs to SIMPLE's and SEP's; from 401(k)s to cash balance plans and pensions. And you could get a tax credit of up to \$500 just to set up the plan! But where do you start¹?

- **Is it just you or employees too?** The first thing is to decide who you want to cover. Is it just you and your spouse? Do you have a business partner? Or do you also plan to offer the plan to employees? How many employees?
- **Cost.** The cost of setting up a plan can be minimal, such as a Payroll-Deducted IRA or SEP IRA, or a few hundred dollars or more to establish and maintain a 401(k) or a pension.
- **Contributions.** Do you, as the employer, plan to make all the contributions to the retirement plan, or do you want the employees to contribute, or do you want to share the contributions between the company and the employee?
- **Motivation.** Why are you setting up a retirement plan in the first place? Is it to reduce your tax liability? Or is it to attract new employees and offer a retirement benefit to existing employees?

Below is a list of the six most popular company-sponsored retirement plans, ranked in order from the simple and least costly to the more complex and expensive:

- **SEP IRA:** For small-business owners and for self-employed people, the SEP IRA is a no-cost, easy-to-set-up retirement plan. You can contribute any amount each year – up to \$57,000 in 2020 – but you must contribute the same percentage amount to yourself and to other employees as well. Contributions are made by the employer only and are tax-deductible as a business expense.
- **SIMPLE IRA:** For businesses with less than 100 employees, these plans are designed for both the employer and the employee to contribute to the employee's retirement. As with SEP IRAs, employer contributions are tax-deductible, and employees' contributions can be made pretax and in 2020 are limited to \$13,500. Costs and paperwork are minimal.
- **Solo 401(k):** Also known as the Self-Employed 401(k), this plan is just for the business owner/spouse, but not for your employees. The paperwork is more intense than the above plans. You'll have to file a Form 5500 with the IRS if your plan assets exceed \$250,000. The good thing is that many financial service firms will not charge a setup or maintenance fee other than on the account itself. Plus, you can contribute salary deferrals of \$19,500 and total contributions of \$57,000 in 2020.
- **401(k):** These are a flexible type of company-sponsored retirement plan. You will pay for a plan document to be created, the Form 5500 to be filed with the IRS each year, and for annual administration to ensure that your plan remains in compliance with the current laws. You may be hiring a Third-Party Administrator (TPA) and/or a Recordkeeper to accomplish these tasks. Depending on the number of employees, you could spend less than \$1,000/year. You and your employees can contribute salary deferrals of \$19,500 and total contributions of \$57,000 in 2020.
- **Pension/defined benefit:** The old-fashioned pension plan may be a suitable plan to help ensure a comfortable retirement and for attracting job applicants to your firm. The problem with these plans is

the cost and paperwork involved. For a small firm, you may pay \$1,000 to set up the account plus an annual fee of \$3,000. The benefits of this plan for the employee is that the employer takes on all the investment risk.

- **Cash balance plan with 401(k):** The cash balance plan is a type of defined benefit plan, but when combined with a 401k this retirement plan could be beneficial to small business owners who can afford the costs of both. It offers both employer contributions as well as employee contributions, and it allows both parties to manage the investments.

The key is to know what is suitable for you and your firm. Is ease of administration an important consideration? Is it critical that employees be able to contribute to the plan? Knowing what you want and need ahead of time is a key component because each plan has its advantages and disadvantages.


1 October 9, 2018, <https://www.irs.gov/retirement-plans/retirement-plans-startup-costs-tax-credit>

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