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RETIREMENT SAVINGS OPTIONS FOR SMALL BUSINESS OWNERS



At Flourish Financial Planning, we specialize in working with small business owners. It always amazes me how often we will see someone come in with a permanent life insurance policy and the reason for the policy being, "I don't have a retirement plan offered through my work." I can only assume this has been a scripted sales pitch by insurance professionals for some time, now, but the truth is, there are many other options available to small business owners when it comes to deferring taxes and saving for retirement. **In fact, there are MORE options available to small business owners than W-2 workers who have a 401(k).** Not to mention most will be more affordable than a permanent life insurance policy.

What Types of Plans are Available?

Traditional & ROTH IRAs

Yes, these aren't options that are solely available for business owners, but I need to bring them up. Setting up an IRA or ROTH IRA are certainly the easiest options for retirement savings. And, if you are below the income limitations, and not looking to save more than \$12,000, it should work just fine for accomplishing your goals.

SIMPLE IRAs

Ironically, this plan is not as simple to set up as a SEP IRA, but it is still a little easier than setting up a 401(k). SIMPLE IRAs are typically good options for employers with a couple of employees. Employees can contribute \$13,500 in 2020 to their SIMPLE IRA account, but employers can set up a 2% contribution to all employee accounts or a 3% matching contribution. Additionally, employees over age 50 can add an additional \$3,000 in their employee contributions.

SEP IRAs

This would be the second easiest option (administratively) for retirement savings. A SEP IRA is typically a good option for business owners that do not have other employees (or can exclude all or most of their other employees). If you are a self-employed individual or have 1099 income, this option is also available for you. Generally, employees can contribute 25% of their gross income and business owners can contribute 20% of their net income up to \$57,000 in 2020.

This type of plan is almost as easy to set up as a Traditional IRA if you don't have other employees.



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Solo 401(k)

As you may have been able to tell, we are increasing in complexity as you go through the available options. As the complexity of the plans increase, often the administrative costs increase as well.

The Solo 401(k) is only available for business owners with no other employees. You can contribute up to \$57,000 with a \$6,500 catch up contribution for employees over age 50. This \$57,000 amount is split between employee and employer contribution calculations.

Another great benefit of a Solo 401(k) plan is that you can set it up to have ROTH provisions (like a ROTH IRA). Also, if your spouse works for your business, you can cover them through this plan as well.

401(k)

If you have quite a few employees and some of these other plans aren't great options for your needs, you can look into setting up a 401(k) for your company. Many employers think that the administrative costs and complexities to set up a 401(k) are cost prohibitive to set up. While it is more costly than some of these other options, there are boxed 401(k) solutions that are able to keep the costs down. With a 401(k), you will have the same contribution requirements as a Solo 401(k), but you will set up rules on your contributions to employees accounts. There are some requirements and testing for 401(k) plans, but if you are not looking for a customizable plan, you can stick with a Safe Harbor 401(k) plan which is a standard plan that allows you to not worry about the compliance testing and helps you keep costs down.

Which Plan is Right For You?

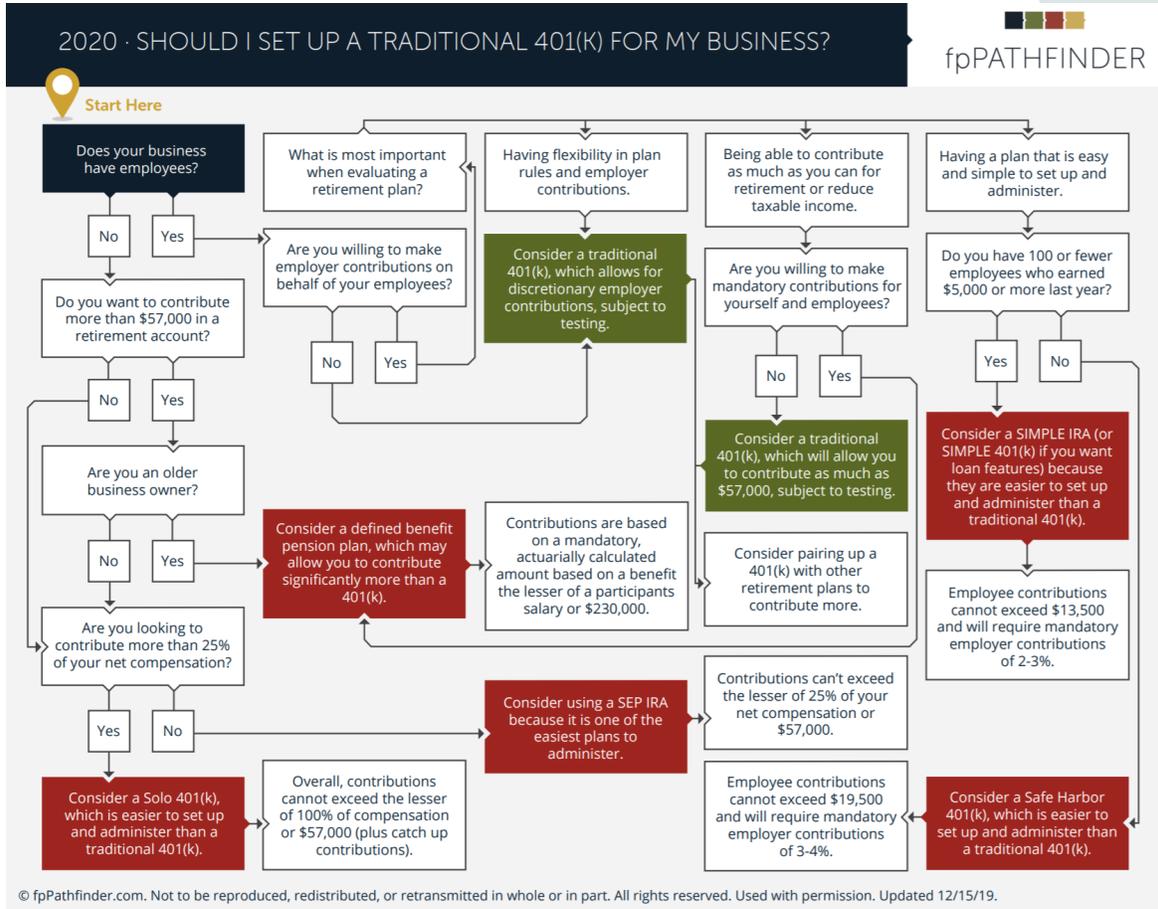
There are a lot of ins and outs to these plans, so it is important to understand what you are getting in to. Our financial planners or tax advisors at Flourish Financial Planning can help you run the numbers. For example, one advanced consideration is that **sometimes when you contribute to a retirement account on behalf of the business, you will be reducing the QBI Deduction** (20% Qualified Business Income Deduction), which may make that contribution less beneficial.

What are your all-in costs? How much will you spend in admin costs and additional personnel costs (contributing to other employees plans)?

How much are you hoping to contribute to a retirement plan? If you are looking to contribute \$12,000 or less, and you are under the income limitations - Traditional and ROTH IRAs are easy answers.

Consider your long-term goals and if you should be making ROTH (tax-free contributions) vs Tax-deferred contributions. If tax-free contributions are more advantageous for you, then a SIMPLE IRA or SEP IRA may not be good options.

Finally, here is one of the flow charts we use with clients to help them use.



We hope that you find this article and all the other articles in this guide helpful. You are always welcome to contact us if you have questions about this or any other personal finance question. Our first call is always free.

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