

# Creating Retirement Plans for Small Businesses

**M**ore so than previous generations, the burden is on today's Americans to financially plan for retirement. Unfortunately, small businesses are much less likely to offer a retirement plan than employers with 100 or more employees. A quality retirement plan helps motivate and retain good employees. Therefore, retirement planning represents an opportunity for accountants to work with their existing client base during tax season, or at other times of the year, to fulfill this need.

In 1999, the Department of Labor (DOL) concluded from its analysis that "about 30 million employees of small businesses do not have access to employment-based retirement coverage. Furthermore, only about 12 percent of these employees choose to close this gap in retirement coverage with an individual retirement account."

Significantly, small employers stated that they avoid making retirement plans because of the risk of commitment to expense, and the administrative costs of a plan. Certain types of retirement plans that accountants can introduce to their clients address these concerns.

For example, Simplified Employee Pension (SEP) and Savings Incentive Match Plan for Employees (SIMPLE) plan formats are designed to benefit small businesses. These plans have clear rules for funding employee accounts. Less reporting or complex limitations are imposed on the employer. SEPs and SIMPLEs include flexibility as to how much an employer must contribute in a year.

Payroll deduction IRAs are a savings service the employer can provide to employees with no contributions from the employer. Keogh plans for self-employed individuals also are designed for small businesses. While standard defined benefit or defined contribution qualified plans are also possible, and provide the maximum contribution potentials, these impose complex limitations and reporting rules.

## Payroll Deduction IRA

The payroll deduction IRA is a service the employer can offer to make deductions from after-tax pay, and direct them, as the employee indicates into an IRA. The employer makes no additional contribution with this service. The employer makes no plan document and files nothing with the IRS. Depending on the nature of the plan the employee chooses, the amount deposited can be a tax deduction to the employee.

## SEP

A unique feature of the SEP is that the employer can vary the percentage of deductible employer contributions from zero to the maximum of 25 percent of employee salary each year. This is ideal for cyclical industries in which employers can contribute more in one year than another.

Annually, eligible employees must receive the same percent-



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## BUSINESS TAX STRATEGIES ADVISOR

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age of their salary in their SEP IRA account. Every eligible employee must be included in the plan. See IRS Pub. 560 for the relevant eligibility criteria.

A bank, mutual fund, insurance company issuing annuities or other approved financial institution acts as a trustee and manages the employee's IRAs. Generally, no paperwork needs to be filed with the government by the employer. The SEP agreement on Form 5305-SEP is distributed to employees, but not sent to the IRS.

## SIMPLE IRA or SIMPLE 401(k)

Compared to the SEP, a SIMPLE is better suited for "larger" small businesses. A SIMPLE plan is distinguished by employee salary reduction contributions that the employer matches. Employees take more control by setting the amount they contribute, and can decide what financial institution will hold the IRA or 401(k) that is built up by the contributions. The employer must contribute only if employees contribute. The employer also has the option of setting a fixed two-percentage contribution for any given year, instead of matching employee contributions.

Only employers of 100 employees or fewer are eligible for a SIMPLE. An employer cannot start a SIMPLE if it has another plan.

Every year, employees have an election period to choose whether, and in what amount, they will participate in salary reduction. Election periods must be at least 60 days and immediately precede January 1 of that calendar year (i.e., November 2 to December 31). Employees must receive notice of the upcoming period. More flexibility is allowed for the first year of a plan.

Sufficient notice also must be given if an employer wishes to make a 2 percent non-elective contribution instead of matching employee salary reductions for a year. Notice is sufficient if it is given a reasonable time before the commencement of the election period.

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our success depends upon our advocacy skills in working with individual decision-makers at the IRS, we are often able to deliver more than our clients anticipate.

I usually leave my schedule fairly flexible so that I can spend two to three hours with the client, if necessary. During this time, multiple tasks may be taking place at one time. I may have one staff member copying documents, while another prepares an engagement letter and a third prepares powers of attorney forms. While they are doing this, I am putting together a list of additional documents or information required of the client, doing a budget with the client and/or putting together the Plan of Action.

### The Engagement Letter

This is the contract between your client and you. After the initial consultation, I perform no work until the client executes the engagement letter and provides the agreed-to retainer. As you develop your standard engagement letter, keep the following points in mind:

- I will state, usually in general terms, that I will be representing the taxpayer before the tax agency for certain years with respect to particular taxes. If I anticipate submitting an offer in compromise to resolve a collection matter, I will include that information. (It should be noted that most of my collection engagements do not result in submissions of offers in compromise.) I also add the following wording: "I may also provide other services which you request." This ensures I am covered if the scope of the engagement expands.
- If the Taxpayer is married, I insist that the spouse sign the engagement letter and be fully responsible for my fees.
- I ask for a retainer in advance. The client will receive interim billings. The funds held as a retainer are applied to the last invoice.
- Since my rates increase annually, I include the following

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Form 5304-SIMPLE is used if the employee chooses the financial institution and Form 5305-SIMPLE if the employer chooses. Either of these forms establishes the SIMPLE, and is not filed with the IRS.

### Summary

The chief concerns that stop a small business client from establishing a retirement plan are being required to contribute annually and the administrative burdens. SEP and SIMPLE plans can overcome these concerns. These plans do away with the complex fiduciary and reporting requirements associated with managing a standard deferred compensation plan; top-heavy rules and eligibility criteria are built into the structure of the plans. These plans offer flexibility as to how much an employer must contribute in the year. They can be presented to clients with the assurance that they will adequately address their employee's retirement concerns. ☺

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language: "All rates will increase from time to time consistent with rates charged generally to the firm's clients."

•I provide that work will cease, at my option, if invoices are not paid within a set timeframe, usually 20 days. In addition, I will often issue stop-work letters if the deadline is not met. This is a tremendous tool in getting clients to pay. It really works!

•If I am providing services for a corporation, my letter includes provisions that will make the owner individually liable for any invoices issued to the corporation or the individual.

•The engagement letter provides that the costs of collecting my fees from the taxpayer are his or her responsibility, including my time. While I have not usually collected this, it does bring us to more satisfying resolution on the few times I have had a financial dispute with a client.

•We occasionally include a provision that clients may pay me on a monthly basis, ranging from \$300 to \$750 per month. By doing so, a portion of the payment will often be included by the IRS in determining the client's necessary expenditures. However, it is important to provide an end date to such an arrangement. I use three years, at which point any remaining balance becomes due.

In spite of all the provisions that our firm includes, our engagement letters for tax representation work are never longer than two pages. When presenting the engagement letter to the client, I take time to clearly explain its provisions. I pay particular attention to the retainer, which many clients think will be applied to the initial invoice, not the last.

With an office staff attuned to landing the prospect and serving the client, you can develop a profitable tax representation practice, providing cost-effective services to those in need. ☺

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