Offset Your Costs with a Tax Credit

The Further Consolidated Appropriations Act of 2020 included a provision from the Setting Every Community Up for Retirement Enhancement Act of 2019 (SECURE Act) that modifies the amount of tax credit an employer may receive for qualified costs incurred as a result of setting up a new retirement plan for 2020 and later years.

Eligible employers may be able to qualify for up to a $5,000 tax credit for each of the first three years of a plan's existence. Prior to 2020 the tax credit was up to $500.

You're an eligible employer if:

- you had 100 or fewer employees who received at least $5,000 in compensation for the preceding year; and
- you had at least one plan participant who was a non-highly compensated employee (NHCE); and
- in the three tax years before the first year the business is eligible for the credit, you did not maintain any other employer sponsored retirement plan.

The new law increases the credit by changing the calculation of the flat dollar amount limit on the credit to the greater of either:

- $500; or
- The lesser of:
    - $250 multiplied by the number of NHCEs of the eligible employer who are eligible to participate in the plan; or
    - $5,000.

As a result, for each of the first three years, the credit could be at least $500 and up to $5,000, depending on the number of NHCEs covered by the plan. You may claim the credit using Form 8881, Credit for Small Employer Pension Plan Startup Costs.

The term "qualified startup costs" means any ordinary and necessary expenses of an eligible employer which are paid or incurred in connection with the:

- Establishment or administration of an eligible employer plan, or
- Retirement-related education of employees with respect to such plan.

Eligible plans include a Profit Sharing 401(k) Plan, a Defined Benefit Plan, 403(a) annuity plan, a simplified employee pension (SEP) plan or a savings incentive match plan for employees of small employers (SIMPLE) IRA plan.

In addition, there is a new tax credit for the first three years of up to $500 for an employer that adds an automatic enrollment feature to a 401(k) arrangement or SIMPLE IRA plan.

Case Study:

Mary operates a successful manufacturing business employing 25 individuals. Mary's business has turned profitable in the last several years and she also sees the need to provide her employees with a retirement plan. The cost to set up the plan is $3,000 ($1,000 one-time set up charge plus $2,000 for the first year administration).

Mary will incur no administrative cost to establish the plan.

Conclusion

For 2020 and later years, the incentive for small businesses to establish new retirement plans for their workers has become more lucrative from a tax perspective. Potentially, the credit may be up to $5,500.

Contact your local Security Mutual Insurance Life advisor today to determine if this strategy is appropriate for your circumstances and to coordinate your financial plans and help achieve your goals and objectives.

SECURITY MUTUAL LIFE
INSURANCE COMPANY OF NEW YORK
SECURITY MUTUAL BUILDING • 100 COURT ST.
P.O. BOX 1625 • BINGHAMTON, NY 13902-1625
607-723-3551 • www.smlny.com

The Company That Cares.®

LinkedIn YouTube