Recruiting and Retaining Great Employees with Retirement Benefits

As the owner of a closely held business, you've worked long and hard to build the business to what it is today and what you have planned for in the future. Owning a business requires the coordination of many moving parts, but one of the most important is the search for and retention of great employees. Often that requires offering a great suite of employee benefits, especially the provision of a retirement savings vehicle. A good retirement savings plan is also beneficial to you, allowing you to convert some of your hard-earned time and money in the business to financial security for yourself and your family.

But what's the right type of plan? There's a virtual alphabet soup of plans that you may have already heard of—from SEPs, SIMPLEs, IRAs, 401(k)s or DB plans. There are probably still more types of plans that you've never heard of, particularly for non-profit entities. There are also numerous considerations such as benefit amounts, employee coverage, contributions to the plan, maximizing tax deductions, controlling investment choices, and more. Choosing the right plan can be complex.

To get you started on this important topic, we're going to describe some of the basic characteristics of various plans that might be available to your business and when those plans might be appropriate based upon the maturity and life stage of your business.

Newer Business

For a newer business or a startup, where cash flow may be limited or unproven, you might not be ready to offer a retirement savings plan to your employees. However, you should still save for your own financial security by using a Traditional IRA ("Individual Retirement Account") or Roth IRA.

Traditional and Roth IRAs are retirement savings vehicles set up by individuals. They are not employer-sponsored retirement plans. The annual contribution limit is only $6,000 for 2021, but those age 50 and over can contribute an additional amount known as a "catch-up provision." For IRAs, it is $1,000. Contributions to a Traditional IRA may be income tax-deductible, but Roth IRA contributions are made on an after-tax basis.

If your business is at the point where you are enjoying some success, steady cash flow and profits, and you have some employees, you may wish to set up a SEP ("Simplified Employee Pension Plan") IRA Plan or a SIMPLE ("Savings Incentive Match Plan for Employees") IRA Plan.

SEPs and SIMPLEs are employer-sponsored retirement plans where the employer is required to make contributions to the accounts of their employees. Both types of plans are relatively simple to establish and maintain. In a SEP, contributions are made by the employer only and can be up to 25 percent of an employee's salary up to $58,000 (for 2021). For a SIMPLE plan, contributions are made by the employees through salary deferrals up to $13,500 per employee (for 2021), with an additional $3,000 catch-up provision. However, the employer must also provide matching contributions up to certain percentages depending upon plan design.

If you are the sole employee of your business and you are enjoying some success and steady cash flow and profits, you may wish to set up an Individual ("Solo") 401(k) Plan. For 2021, you can make salary deferrals of $19,500, with a catch-up provision of $6,500. Since you're also the employer, you can make a profit-sharing contribution to your own plan of up to 20 percent of net self-employment income for a maximum contribution of $58,000 plus the catch-up provision.

Stable Business

If your business has enjoyed a few years of success, continues to grow, has steady cash flow and profits, and you have full-time employees, then a SEP IRA Plan or SIMPLE IRA Plan may still be appropriate. But depending upon your level of success and profitability, you may wish to consider a Traditional 401(k) Profit Sharing Plan or Safe Harbor 401(k) Profit Sharing Plan.

The employee salary deferral limits with catch-up provisions are the same as a Solo 401(k) Plan. In a Traditional 401(k) Plan, discretionary profit-sharing contributions by the employer can be up to 25 percent of employee compensation. 401(k) plans are more complex and typically require the services of a third-party administrator to help run the plan and keep it compliant with various regulations. However, these plans have some flexibility in design characteristics (e.g., different contribution limits for different classes of employees; favoring older, more highly compensated employees; allowing for pre- and post-tax contributions; and more). Nevertheless, 401(k) plans must still meet rigorous qualification and non-discrimination rules established by the federal government.

Safe Harbor 401(k) Plans seek to simplify the administration of 401(k) Plans by removing some of the flexibility of traditional plans and enforcing certain standards upon the employer, including requiring the employer to make matching contributions to employee deferrals up to a certain percentage based upon plan design.

Note that Profit Sharing Plans may allow for the purchase of life insurance inside of the plan. There are various rules that must be complied with, but this can be very useful to participants who need life insurance protection but lack sufficient cash flow outside of the plan to pay for the premiums.

Mature Business

If your business is one that has existed for many years and enjoyed consistent success and profitability, and you are starting to think about your retirement or exit strategy from the business to do other things, then you probably have a mature business. Traditional and Safe Harbor 401(k) Profit Sharing Plans are still viable retirement savings vehicles. However, depending upon the make-up of the company (e.g., number of employees; the business succession plan; demographics of the company; etc.), Defined Benefit

Pension Plans ("DB Plans") may also be options. DB Plans can be in lieu of, or in addition to, a 401(k) Plan. DB Plans can be great tools, particularly if you have not sufficiently saved for retirement or if the savings in a 401(k) Profit Sharing Plan will not allow you to maintain the lifestyle in retirement that you've been accustomed to.

There are several different types of DB Pension Plans (i.e., Traditional, Cash Balance and Fully Insured), but each "defines" the retirement benefit, and therefore, depending upon the participant's current age, retirement age, and promised benefit, the contribution will be actuarially determined in order to fund the defined benefit rather than arbitrarily limited by law. Of course, the defined benefit is also subject to government rules and regulations (e.g., for 2021, the maximum single life annuity that can be solved for is $230,000 per year for life), but contributions can well exceed what can be put into a 401(k) and profit-sharing plan, leading to large tax deductions for the business. Unlike plans relying upon a participant's salary deferrals to fund the plan to meet the participant's retirement goals, the employer bears the burden of achieving the investment returns needed to fund the defined benefit.

DB Plans are particularly useful if you're a business owner who has started late on your retirement savings efforts or if you have few or no employees. In addition, DB Plans often include the ability to purchase life insurance inside of the plan to enhance the investment component of the plan and to provide an enhanced death benefit to the participant's family.

Conclusion

We've very briefly discussed a variety of retirement plans that may help you to recruit and retain top performers to work in your company. These retirement plans may also help you, as the business owner, plan for your own financial security. There are still other types of plans that we did not touch upon and which may apply, particularly if your company is a non-profit or charitable organization.

As you can see, there are many types of plans that may be appropriate for your company. That's why it is important to work with your CPA as well as an experienced financial professional such as your Security Mutual life insurance advisor. Security Mutual offers many retirement plan options. In addition, Security Mutual's wholly owned subsidiary, Security Administrators, Inc., provides third-party actuarial and administrative services to small- and medium-sized companies that sponsor "qualified" pension and profit-sharing plans. This provides you with a full-service, turnkey implementation of your company's retirement plan.

For More Information Contact:

Contact your Security Mutual life insurance advisor today to get the process started. Your advisor will assemble your team and coordinate with your attorney and tax professional to review your situation and help determine which retirement plan is appropriate for you and your business.

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