SIMPLE Retirement Plan

The Small Business Job Protection Act of 1996 created an entirely new type of retirement plan called "SIMPLE," an acronym that stands for Savings Incentive Match Plan for Employees. It is available for any business which:

- Has 100 or fewer employees (including employees of related entities);
- Does not maintain another tax-qualified retirement plan to which contributions are made; and
- Is either an incorporated or unincorporated firm.

How It Works

- Employee has the option of taking cash, or having it contributed to the trust for retirement. This is equivalent to the employee making a pre-tax contribution.
- Mandatory employer contributions are tax-deductible to the business.
- Employer contributions are not taxed currently to the participants.
- Earnings accumulate income tax deferred.
- The employer must deposit participant contributions within 30 days after the end of the month for which the contribution was made.
- There are two different types of SIMPLE plans that, although similar, do have distinct differences. There is an IRA version and a 401(k) version.

Item	IRA Version	401(k) Version
Plan type	Individual IRA for each participant.	Cash or deferred profit sharing plan.
Participation	Any employee who received $5,000 or more of income during any 2 prior years and is expected to earn $5,000 during the current year must be eligible.	Regular qualified plan rules apply, such as: Minimum age of 21 1 year of service 1000 hours

Item	IRA Version	401(k) Version
Do cash or deferred nondiscrimination rules apply? [(401(k), 401(m)]	No	No, unless employer fails to contribute.
Top-heavy rules	They do not apply.	Do not apply unless employer fails to contribute.
ERISA reporting and disclosure rules	Simplified rules apply.	Regular rules apply.
Vesting	Always 100%	Always 100%
Employee contributions	Voluntary up to $12,500[1] (indexed for inflation) per year. May not exceed 100% of compensation. May stop at any time.	Voluntary up to $12,500[1] (indexed for inflation) per year. May not exceed 100% of compensation. May stop at any time.
Minimum participation requirements	There is no minimum number or percentage of eligible employees who must participate.	There is no minimum number or percentage of eligible employees who must participate.
Employer contributions	Employer must satisfy one of two alternatives. Election must be made at least 60 days before the start of the plan year.	Employer must satisfy one of two alternatives. Election must be made at least 60 days before the start of the plan year.
Alternative #1 - Matching contributions	Employer matches employee's elective deferral, dollar for dollar, up to 3.0% of compensation.	Employer matches employee's elective deferral, dollar for dollar, up to 3.0% of compensation.
	For any two years out of five, employer may have a lower match, but not less than 1.0%.	Not available.
	The $265,000 compensation limit does not apply.	The $265,000 compensation limit does apply.
	No conditions may be imposed on the right to the employer match such as minimum hours or end of year employment.	No conditions may be imposed on the right to the employer match such as minimum hours or end of year employment.

[1] This is the 2015 limit. For those age 50 and older, additional "catch-up" contributions of $3,000 may be made.

Item	IRA Version	401(k) Version
Alternative #2 - Nonelective contribution	Employer contribution is 2% of compensation to all eligible employees, whether they defer or not.	Employer contribution is 2% of compensation to all eligible employees, whether they defer or not.
	The $265,000 compensation limit does apply.	The $265,000 compensation limit does apply.
Employer contributions are due by:	Due date of employer's income tax return, plus filing extensions.	Due date of employer's income tax return, plus filing extensions.
Employee in-service withdrawals	These are allowed.	Rules are the same as for 401(k) plans. If plan provides for loans or hardship withdrawals, they are allowed.
Taxation of distributions	Generally, treated in the same fashion as withdrawals from a traditional IRA. Ordinary income. Penalty taxes may apply.	Same as 401(k) plans. Distribution is ordinary income. 10-Year averaging[1] may be available.
Additional employer contributions	Are not permitted.	Are not permitted.
May employer have another plan to which contributions are made or in which benefits accrue?	No	No
Rollovers	Allowed if to another SIMPLE IRA or, after 2 years of SIMPLE participation, to a traditional IRA.	These are allowed when made to a traditional IRA or qualified plan.
Taxation of premature (before age 59½) distributions within first two years of participation	Taxed as ordinary income, plus a 25% penalty, unless an exception applies.	Taxed as ordinary income, plus a 10% penalty, unless an exception applies.
Taxation of premature (before age 59½) distributions after first two years of participation	Taxed as ordinary income, plus a 10% penalty, unless an exception applies.	Taxed as ordinary income, plus a 10% penalty, unless an exception applies.

[1] Those born before 1936 may be able to elect 10-year income averaging or capital gain treatment; these strategies are not available to those born after 1935.

Item	IRA Version	401(k) Version
Reporting requirements	Plan trustee must provide employer with information on basic plan details.	Regular reporting and disclosure requirements apply. 5500 filing, Summary Plan Description and Summary Annual Report.
	Employer must notify employee of right to defer and provide above information.	
	By January 30, employer must give each participant a statement setting forth account balances as of December 31, and all activity during the calendar year.	401(k)-type of participant reports is required. Time limit is 9 months after the close of the plan year with Summary Annual Report.

Advantages to Employer

- Unlike 401(k) plans, the employer knows in advance approximately what the financial commitment will be.
- Employer contribution is tax deductible.
- The plan is easily understood by employees.
- The 401(k) version of the plan can provide employees with permanent life insurance benefits that need not expire nor require costly conversion at retirement age.
- In the 401(k) version, the employer can direct employer investments.
- If former participants do not provide the plan with distribution instructions, the plan may automatically distribute accounts less than $5,000. In the case of a plan that provides for such mandatory distributions, the plan must automatically roll an eligible distribution amount that exceeds $1,000 to a Rollover IRA in the former participant's name. A plan may allow direct rollovers of less than $1,000.

Advantages to Employees

- Participant deferrals are made with pre-tax dollars.
- Employer contributions are not currently taxable to participant.

- In the 401(k) version, distributions may be eligible for 10-year income averaging[1] or, at retirement from the current employer, rolled over to a traditional or a Roth IRA, or to another employer plan if that plan will accept such a rollover.
- Distributions from the IRA version are taxed in the same manner as a traditional IRA, except for a 25% penalty for premature distributions in the first two years.
- In the IRA version, participants have the right to direct investments. In the 401(k) version, participants may have the right to direct investments, depending on plan provisions.
- Federal law allows a qualified plan to establish an "eligible investment advice arrangement" under which individually tailored investment advice is provided to plan participants. Any fees or commissions charged must not vary with the investment options chosen, or else a computer model meeting certain requirements must be used.
- Participants may also have a traditional, deductible IRA, or Roth IRA, subject to certain income limitations based on filing status.
- In the 401(k) version there is the ability to purchase significant permanent life insurance which is not contingent upon the company group insurance program. Purchase of life insurance will generate taxable income to the employee.
- Younger employees can accumulate a larger fund than with a defined benefit plan.
- If the 401(k) plan permits, participants can borrow from the plan, within the requirements of the plan and the law.
- In the 401(k) version, if the plan permits, participants can make hardship withdrawals within the requirements of the plan.
- ERISA and federal bankruptcy law provide significant protection from creditors to participant accounts or accrued benefits in tax-exempt retirement plans. In traditional and Roth IRAs, generally, up to $1,245,475[2] is protected. However, funds in either a SIMPLE IRA or SIMPLE 401(k) are protected without any dollar limitation.

[1] Those born before 1936 may be able to elect 10-year averaging or capital gains treatment
[2] Effective April 1, 2013. This limit is indexed for inflation every three years.

Disadvantages to Employer

- The employer is required to contribute.
- The more highly paid participants may not be able to contribute sufficient funds to build an adequate retirement. This may bring pressure on the employer to provide additional retirement benefits.
- While called a "SIMPLE" plan, in operation it is not nearly as simple as often thought.

Disadvantages to Employees

- There is no guarantee as to future benefits.
- Investment risk rests on the participant.
- There are no forfeitures to reallocate as under other types of defined contribution plans.
- For older employees, there may not be sufficient time to accumulate a decent retirement fund. Other types of defined contribution plans can provide a better retirement benefit for older workers.