

Small Business Retirement Plans

Understanding and Navigating Plan Selection for Your Clients



Small Business Key Facts

- › Nearly half of all workers in the U.S. have less than \$1,000 saved for retirement¹
- › 55 million U.S. workers are not covered by a retirement program because their employer does not sponsor one²
- › Over 70% of small businesses are sole proprietors³
- › Only 21% of workers feel “very confident” that they will have accumulated enough money to live comfortably in retirement⁴

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Close to 9 million self-employed individuals do not have a business retirement plan.¹ One of the most important services you can provide to your small business owner clients is to help them evaluate retirement plan options and establish a retirement program to meet their personal and business needs.

There are various plans, each with different features, administrative responsibilities, legal obligations and costs. Typically you will want to help clients choose the simplest plan that will meet the objectives and priorities of their business, such as a Simplified Employee Pension Individual Retirement Account (SEP IRA), Savings Incentive Match Plan for Employees Individual Retirement Account (SIMPLE IRA) or an Individual 401(k).

Why Focus on Small Business Retirement Plans?

Offering these and other small business retirement plans can help you:

- › Develop long-term relationships with business owners
- › Expand your opportunities to include employees of small businesses
- › Create potentially recurring revenue streams through ongoing contributions

Tools to Help Grow Your Business

Visit retirementpowerplay.com/essentials for tools to help you compare appropriate employer-sponsored retirement plans for your clients.

Use the Small Business Plans calculator in the Retirement Center under Tools in NetX360® to identify appropriate plan options for your client and create customized reports.

¹ Employee Benefits Research Institute, March 2016.

² Employee Benefits Research Institute, October 2012.

³ SBA.gov, “Frequently Asked Questions,” March 2014.

⁴ 2016 Retirement Confidence Survey, Employee Benefit Research Institute.

Employer and Employee Benefits of Establishing a Plan

Small business retirement plans provide employers with tax benefits and may help them to attract and retain employees, but do not require the same level of administration required by a traditional 401(k) or other full-featured retirement plan. Whether clients choose a SEP IRA, SIMPLE IRA or an Individual 401(k) plan, they will enjoy federal tax deductions on contributions and potential federal tax credits for the first three years of the plan.⁵ Additionally:

- › **SEP IRAs** offer business owners maximum flexibility for contributions—providing the ability to scale contributions based on employee wages and to change contributions depending on business conditions.
- › **SIMPLE IRAs** offer many of the same features and benefits of 401(k)s, but with limited employer contribution requirements.
- › **Individual 401(k)** plans offer high contribution limits and a flexible plan design, plus they allow business owners to make tax-deferred contributions as both the employee and employer—increasing their chance of meeting their individual retirement goals.

If available through your firm, a Mutual Fund Only investment option is available for SEP and SIMPLE IRAs for investors who prefer a simplified investment structure and invest only in mutual funds.

Potential Candidates for Small Business Plans

In general, the following types of business owners may be potential candidates for these small business plans:

SEP IRA	Simple IRA	Individual 401(k)
<ul style="list-style-type: none"> › Owns a business of any size without a retirement plan › Wants a plan with minimal administrative and regulatory requirements › Is looking for maximum flexibility for annual contributions › Wants to make employer contributions (or not allow employee contributions) › Is comfortable with contributing the same percentage for all eligible employees 	<ul style="list-style-type: none"> › Has a business with 100 or fewer employees (usually 2-25 employees) › Is looking for a cost-effective retirement solution › Can commit to mandatory annual employer contributions › Is looking to offer employees the opportunity to contribute to the plan › Does not currently offer a retirement plan 	<ul style="list-style-type: none"> › Has a business that employs only the owner(s) and potentially any spouse(s) › Expects to make less than \$265,000 in 2016 and \$270,000 in 2017 in annual compensation › Is 50 years or older and wants to make higher catch-up contributions › Wants a plan that allows for higher employer contributions › Would like to permit plan loans

⁵ A tax credit of 50% of the administrative and retirement education expenses of certain small businesses that adopt a new SEP IRA, SIMPLE IRA, defined benefit or defined contribution plan may be available. Visit irs.gov for more information.

Small Business Retirement Plans At-A-Glance

Plan Details	SEP IRA	Simple IRA	Individual 401(k)
Businesses That Can Offer the Plan	Any business without a retirement plan	Any business with 100 or fewer employees without a retirement plan	Any sole proprietor, partnership or other business structure where the business employs only the owner and potentially the spouse
Key Advantages	Minimal administrative and regulatory requirements Low administrative costs Flexible annual employer contributions	Minimal administrative and regulatory requirements Low administrative costs Employees share responsibility for their retirement savings	Employees share responsibility for their retirement savings Maximizes employee pre-tax contributions Allows for loans and withdrawals Flexible annual contributions Discretionary profit-sharing contributions
Potential Disadvantages	Employer must contribute equally for all eligible employees	Inflexible employer contributions Lower contribution limits than some other qualified plans	Administrative costs may be higher than other plans Withdrawal and loan flexibility adds administrative responsibility
Eligible Employees	Must be offered to all employees who are at least 21 years of age, employed by the business for at least three of the last five years and earned at least \$600 per year	Must be offered to all employees who have earned at least \$5,000 in the previous two years and are reasonably expected to earn at least \$5,000 in the current year	Only business owners and their spouses employed by the business
Types of Contributions Allowed	Employer contributions only	Both employee and employer contributions	Both employee and employer contributions
Form of Contributions	Cash only	Cash only	Cash only

Plan Details	SEP IRA	Simple IRA	Individual 401(k)
Mandatory Annual Employer Contributions	Contributions may vary from year to year	Yes	No, profit-sharing contribution optional
Maximum Employee Contribution⁶	N/A	\$12,500 for 2016 and 2017 plus an additional catch-up contribution of up to \$3,000 for those age 50 or older	\$18,000 for 2016 and 2017 plus an additional catch-up contribution for each year of up to \$5,500 for those age 50 or older
Maximum Employer Contribution⁶	Lesser of 25% of eligible compensation or \$53,000 in 2016 and \$54,000 in 2017	Employers must either match employee contributions dollar for dollar up to 3% of compensation (can be reduced to as low as 1% in any two out of five years) or contribute 2% for each eligible employee's compensation (up to \$5,000)	Employer contributions are not mandatory; however, employee contributions plus employer matching and/or profit-sharing contributions cannot exceed the lesser of 100% of compensation or \$53,000 for 2016 and \$54,000 for 2017 Employer can deduct amounts that do not exceed 25% of the aggregate compensation for all employees
Annual Employee Compensation Limit for Calculating Contributions⁶	\$265,000 in 2016 and \$270,000 in 2017	\$265,000 in 2016 and \$270,000 in 2017	\$265,000 in 2016 and \$270,000 in 2017
Vesting Terms	Immediate	Immediate	Immediate
Administrative and Regulatory Reporting Requirements⁷	Employee notice	Employee contribution notice and a Summary Plan Description (SPD)	IRS Form 5500-EZ filing when plan assets reach \$250,000
Investment Selection	Employees are fully responsible for investment selection	Employees are fully responsible for investment selection	Employees are fully responsible for investment selection

⁶ Adjusted annually by the IRS.

⁷ Additional reporting may be required.

Case Study: Determine Business Needs and Priorities

Julie recently left her full-time corporate job to become a marketing and social media consultant. She regularly contributed to her former employer's 401(k) and wants to establish a retirement plan for her business so she can continue to invest on a pre-tax basis for retirement.

Julie worked with her advisor and tax professional to help choose a plan to meet her needs. One of the first considerations was whether she planned to hire employees other than her spouse. If she did, she might consider a SIMPLE or SEP IRA. However, since she did not plan to hire employees she focused her selection on either an Individual 401(k) or a SEP IRA. She had not always contributed the maximum to her tax-deferred accounts when she was younger, so her top priority was maximizing contributions. As a sole proprietor, she also wanted to consider costs and administrative requirements.

An Individual 401(k) allows her to make contributions as both the employer and employee, so Julie's contribution limits would be higher. However, she was also attracted to the lower costs and minimal regulatory and administrative requirement offered by SEP IRAs. In the end, Julie decided the higher contribution limits of an Individual 401(k) outweighed the potentially higher administrative costs and filing requirements.

Potential contribution for 2017 for a business owner under age 50 who earned \$100,000⁸

	Individual 401(k)	SEP IRA	Simple IRA
Employer contribution or match	\$25,000	\$25,000	\$3,000
Employee contribution	\$18,000	\$0	\$12,500
Total	\$43,000	\$25,000	\$15,500

⁸ Based on 2017 IRS limits and calculations. This example is for illustrative purposes only and clients should consult with their tax or legal advisor before establishing any business retirement plan. Assumes \$100,000 compensation is W-2 income and does not include catch-up contributions. Lower limits may apply if wages constitute self-employment income. Individual 401(k) contributions include an employer contribution of \$25,000 plus an employee contribution of \$18,000. SIMPLE IRA contribution amount reflects a 3% match formula.

Cultivating Small Business Plan Opportunities

Your current and prospective clients may provide new opportunities to grow and deepen your business. You are probably already serving small business owners, entrepreneurs or consultants.

Sole Proprietors

More than 70% of U.S. businesses are owned by sole proprietors, which includes consultants, freelancers and contractors.⁹ That number is expected to rise in coming years, presenting new opportunities for advisors to address the personal financial needs of their clients with employer retirement plans. Many of these new business owners may come from Corporate America and have an understanding of the benefits of employer retirement programs. Here are some ideas for prospecting sole proprietors:

- › **Gauge their interest in funding their personal retirement goals now.** Discuss the personal and tax advantages of establishing a retirement plan. Evaluate whether the business is temporary or something your client is interested in pursuing longer term. Many consider their freelance activities something they are doing on a temporary basis until they find full-time work again. Even still, deferring taxable income can have great appeal, so do not let that stop you from pursuing a conversation. Keep in mind that the self-employed carry the extra burden of fully funding Social Security benefits and, therefore, have a higher overall tax bill. Be sure to advise your clients of maximum contribution restrictions, especially if they re-enter the corporate workforce and receive retirement benefits.
- › **Look for opportunities to assist with assets from former employer relationships.** For clients who have recently left their former employer, did they receive a severance package or a distribution from their retirement plan? If so, explore opportunities to work with your client to develop a strategy that addresses short-term liquidity needs while not sacrificing thoughtful and important long-term retirement planning. Does your client have an old 401(k) or IRA? Offer to create a retirement plan strategy or conduct a portfolio review to uncover opportunities to help your client with retirement matters, including evaluating rollover decisions, asset consolidation or new employer-based savings plan suggestions for future retirement funding needs.
- › **Follow up and continue to position the personal and tax-advantages of funding a retirement plan.** For clients with new businesses, cash flow concerns may be an impediment to prioritizing retirement savings—make a note to re-engage them in a discussion before next year's tax-filing deadline.

Sole Proprietor Tips

- › Every qualified dollar contributed to a sole proprietor employer retirement program represents a personal income tax deduction
- › Sole proprietors have until the federal tax filing date to establish and fund a SEP IRA; Individual 401(k)s must be set up by December 31, but can be funded up to the tax filing date
- › Mid-to-late career job changers may have special needs associated with potential severance arrangements and the unlocking of workplace wealth, such as long-term incentive programs or former corporate retirement plans such as 401(k)s
- › A saver's credit of up to \$1,000 (up to \$2,000 for married couples filing jointly) may also be available to low- and middle-income employees

Note: Refers to federal taxes only. Individuals should consult their tax or legal advisor to confirm that they qualify for the federal tax benefit described.

⁹ SBA.gov, "Frequently Asked Questions," March 2014.

Tips for Businesses With Employees

- › Larger employers tend to need more features and flexibility and may value a 401(k) plan
- › In addition to business deductions for employer contributions, a tax credit of 50% of the administrative and education expenses of certain new businesses may be available for those who establish a SEP IRA, SIMPLE IRA or other qualified retirement program, including 401(k) and profit sharing plans
- › A saver's credit of up to \$1,000 (up to \$2,000 for married couples filing jointly) may also be available to low- and middle-income employees

Note: Refers to federal taxes only. Individuals should consult their tax or legal advisor to confirm that they qualify for the federal tax benefits described.

Businesses With Employees

Clients who have employees and stable businesses may be focused on employee retention and recruiting. Alternatively, their own personal retirement goals may be a higher priority. Getting to know the business owner's personal and business goals is key to building the relationship. Here are some ideas for prospecting businesses with employees:

- › **Look at the business track record.** Has the business been in place for more than two years? Businesses that have beat the odds and are still operating after two years may offer worthwhile opportunities for you.
- › **Evaluate and discuss growth prospects.** Is your client considering expanding or recruiting more employees? You may want to highlight the importance of retirement programs in attracting and retaining talent, particularly if skilled talent is key to the small business. Is your client concerned about employee retention? Retirement programs, particularly employee-funded plans with vesting schedules, can be a valuable tool in building loyalty and sharing the success of the business with employees, while benefiting from business tax deductions.
- › **Understand the dynamics of the industry served.** Knowing the industry your client serves can provide important clues into the considerations that may be important for attracting and retaining employees and establishing an effective plan design.
- › **Examine the makeup of the employee group.** What is the profile (education, salary range, tenure, average age) of your client's employee base? A combination of professionals and mid-career employees with low staff turnover may be optimal for a successful retirement program.
- › **Determine the preferred features of the retirement plan.** Does the business owner want to allow employees to contribute to the plan? Does the business owner want to commit to mandatory or discretionary employer contributions? Are vesting schedules important for employer contributions? Are loans an important feature? Answers to these questions eliminate certain plan types and help influence plan design considerations.
- › **Discuss plan options and recommend an approach for meeting business owner, employee and funding objectives.** There are many choices when it comes to types of retirement plans. Each plan type has different plan features, legal obligations and costs. Typically you will want to help clients select the appropriate plan options that will meet the objectives set out for each business situation.
- › **Do your clients currently offer a retirement program to their employees?** If so, determine the level of satisfaction and look for an opportunity to discuss how you can offer a plan that provides potentially more investment choices, additional employee support or potentially better plan design approaches. Consider offering your services to help educate employees about planning for retirement. This approach may create new opportunities, positioning you to work with employees to evaluate IRA rollovers.

Overcoming Common Objections to Establishing a Plan

The table below outlines the most common objections of small businesses that do not have a retirement plan, along with tips for overcoming these objections.

Objection	Tips to Overcome the Objection
<p>Retirement plans cost too much</p>	<p>In general, small business retirement plans have lower administrative costs than full-featured plans. Plan costs generally come into play in two primary areas with different potential strategies for addressing each:</p> <p>1. Retirement Funding Costs</p> <ul style="list-style-type: none"> › SEP IRAs and Individual 401(k)s allow the employer to decide whether and how much to contribute to the plan each year, however, SEP IRAs require that all eligible employees receive proportionally equal benefits. › Profit sharing programs commonly provide options for targeting benefits to certain employees through eligibility and vesting elections, while more complex programs provide funding models that are weighted by age or other targeted populations. <p>2. Administrative Costs</p> <ul style="list-style-type: none"> › Retirement programs such as SEP and SIMPLE IRAs have minimal administrative responsibilities (except required employee notices) or costs incurred by the employer. › Qualified retirement plans, such as Individual 401(k) and 401(k) plans, typically allow for administrative costs to be deducted from plan assets instead of being paid directly by the employer, although this may be impractical until the plan has sufficient assets to cover expenses. › For clients who invest in mutual funds, Pershing offers a Mutual Fund Only option for SEP and SIMPLE IRAs with a low \$10 annual maintenance fee. › Business owners who hold the majority of plan assets may want to fund as many expenses as possible out of the business to get a tax deduction on those expenses and to avoid using their own tax-deferred dollars to pay plan expenses. New plans have the added benefit of a potential federal tax credit of up to \$500 per year for each of the first three years after establishing the plan.
<p>Retirement plans carry too many regulatory burdens</p>	<p>In general, small business retirement plans have fewer administrative and regulatory requirements than full-featured plans, like 401(k)s. SEP and SIMPLE IRAs do not require complex tax reporting or regulatory testing requirements. Individual 401(k) programs only require tax filings (IRS Form 5500-EZ) when plan assets are \$250,000 or more. The custodian typically handles updates for regulatory changes affecting the operation of these plans and facilitates communication with account holders.</p>

Objection	Tips to Overcome the Objection
I don't want the fiduciary responsibilities associated with offering a plan	Currently, all qualified plans have the same level of fiduciary responsibility. For example, SEP and SIMPLE IRAs and Individual 401(k)s have limited fiduciary responsibility for plan sponsors.
I just don't know enough about sponsoring or setting up a plan	This is an opportunity for you to help educate clients on the benefits and obligations of establishing a plan—along with the assistance you can provide setting up the plan and educating employees.

Full-Featured Retirement Plans

Pershing also makes available full-featured retirement plans, such as 401(k)s and Profit Sharing Plans. These plans can provide more flexibility in plan design and contributions, but can be more complex to administer. Visit retirementpowerplay.com/essentials to help compare and select plans.

How Pershing Can Help

- › Full range of retirement plans for small businesses
- › Robust range of investments including no-transaction-fee mutual funds through the FundVest® platform
- › Low cost mutual fund only option for SEP and SIMPLE IRAs
- › Support tools to help you choose, set up, fund and service small business retirement plans

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*Based on number of broker-dealer clients, *InvestmentNews* August 2013.

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