

SIMPLE IRA PLANS

FOR SMALL BUSINESSES

SIMPLE IRA Plans for Small Businesses is a joint project of the U.S. Department of Labor's Employee Benefits Security Administration (EBSA) and the Internal Revenue Service.

To view this and other EBSA publications, visit the agency's website at:
dol.gov/agencies/ebsa.

To order publications or speak with a benefits advisor, contact EBSA electronically at: **askebsa.dol.gov**.

Or call toll free: **866-444-3272**

This material will be made available in alternative format to persons with disabilities upon request:

Voice phone: **(202) 693-8664**

TTY: **(202) 501-3911**

This publication constitutes a small entity compliance guide for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.



Thinking about a retirement plan? If it seems like the right thing for your business, here's a SIMPLE one.

A SIMPLE (Savings Incentive Match Plan for Employees of Small Employers) IRA plan offers great advantages for businesses that meet two basic criteria. First, your business must have 100 or fewer employees (who earned \$5,000 or more during the preceding calendar year). In addition, you cannot currently have another retirement plan. If you are among the thousands of business owners eligible for a SIMPLE IRA plan, read on to learn more.

A SIMPLE IRA plan provides you and your employees with a simplified way to contribute toward retirement. It reduces taxes and, at the same time, attracts and retains quality employees. And compared to other types of retirement plans, SIMPLE IRA plans offer lower start-up and annual costs ... they are just *simpler* to operate.

Other Advantages of a SIMPLE IRA plan

- SIMPLE IRA plans are easy to set up and run – your financial institution handles most of the details.
- Employees can contribute, on a tax-deferred basis, through convenient payroll deductions.

- You can choose either to match the employee contributions of those who decide to participate or to contribute a fixed percentage of each eligible employee's pay.
- You may be eligible for a tax credit of up to \$500 per year for each of the first 3 years for the cost of starting a SIMPLE IRA plan. (IRS Form 8881, *Credit for Small Employer Pension Plan Startup Costs*).
- Administrative costs are low.
- You are not required to file annual financial reports.

Establishing the Plan

Starting a SIMPLE IRA plan is easy to do!

Step 1: Contact a retirement plan professional or a representative of a financial institution that offers retirement plans. Many financial institutions will probably have a pre-approved SIMPLE IRA plan form that you can review.

Step 2: Choosing a financial institution to maintain employees' SIMPLE IRAs is one of the most important decisions you will make, since that entity becomes a trustee to the plan. (Alternatively, you can decide to let employees choose the financial institution that will receive their contributions.)

Regardless of who makes the choice, only the following institutions can be designated as trustees of SIMPLE IRA plans: banks, mutual funds, insurance companies that issue annuity contracts, and certain other financial institutions that have been approved by the IRS. Trustees work with employers and agree to:

- Receive and invest contributions, and
- Provide the employer with a summary description of the plan features each year.

Step 3: Choose a model form or other plan document offered by your financial institution. If your financial institution offers a model SIMPLE IRA plan document, you will have a choice of two forms to use:

- **IRS Form 5304-SIMPLE**, *Savings Incentive Match Plan for Employees of Small Employers (SIMPLE) – Not for Use with a Designated Financial Institution*, if employees are allowed to select the financial institutions that will receive their SIMPLE IRA plan contributions; or
- **IRS Form 5305-SIMPLE**, *Savings Incentive Match Plan for Employees of Small Employers (SIMPLE) – for Use with a Designated Financial Institution*, if you require that all contributions under the SIMPLE IRA plan be initially deposited with a designated financial institution.

Your choice of the employees covered will be set out in your selected plan document. You can choose to cover all employees without restriction. Alternatively, you can limit the employees covered to those who received at least \$5,000 in compensation during any 2 years prior to the current calendar year and who are reasonably expected to receive at least \$5,000 during the current calendar year.

Step 4: Complete and sign the selected IRS form (or other plan document, if not using the IRS model form). When it is completed and signed, this document becomes the plan's basic legal document, describing your employees' rights and benefits. Do not send it to the IRS; instead, use it as a reference since it sets out the plan terms (for example, eligible employees, compensation, and employer contributions). You will need to ensure that your plan is kept current with the law.

Operating the Plan

A SIMPLE IRA plan is true to its name when it comes to plan operation. Contributions under the plan (employees' and yours) are simply deposited into IRAs.

Participants in a SIMPLE IRA Plan

Employees who elect to contribute or to whose accounts you deposit contributions are participants. Your obligation is to provide information to your financial institution on those employees who can participate as described in your plan document. You will want to keep your financial institution aware of any changes in the status of those employees who can participate (for example, new employees).

Enrolling Employees in a SIMPLE IRA Plan

SIMPLE IRA plans operate on a calendar-year basis. An employer may initially set up a SIMPLE IRA plan as late as October 1.

A SIMPLE IRA must be set up for each employee with contributions under the plan. Employees must receive notice of their right to participate, to make salary reduction contributions, and to receive employer contributions. In addition, employees must receive information about the plan, including a copy of the summary description. The required notice also informs employees of the plan's election periods during which eligible employees can decide to contribute to the plan. For employers that use one of the model forms, a model notice is on page 3 of both Form 5304-SIMPLE and Form 5305-SIMPLE.

If the plan provides for automatic enrollment, the employer can choose to automatically enroll employees in the SIMPLE IRA plan as long as the employees are allowed to choose not to have salary reduction contributions made to their SIMPLE IRAs or to have salary reduction contributions made in a different amount.

Employee Contributions

Employees can make salary reduction contributions in any amount to a SIMPLE IRA plan up to the legal limits. The maximum amount that an employee can contribute is \$12,500 in 2016 and in 2017. (This amount is subject to cost-of-living adjustments for years after 2017.) Additional employee contributions (known as catch-up contributions) are allowed for employees age 50 or over. The additional contribution limit is \$3,000 in 2016 and in 2017. (This amount is subject to cost-of-living adjustments for years after 2017.)

Each year, employees can change their contribution levels during the plan's election period. This election period must be at least 60 days long, and employees must receive prior notice about an upcoming election opportunity. SIMPLE IRA plans that have already been established must have an annual election period that extends from November 2 to December 31. A plan can have more election periods each year in addition to this 60-day election period.

Employer Contributions

You have two choices in determining your contributions to the SIMPLE IRA plan:

- A 2 percent nonelective employer contribution, where employees eligible to participate receive an employer contribution equal to 2 percent of their compensation (limited to \$265,000 for 2016 and \$270,000 for 2017 and subject to cost-of-living adjustments for later years), regardless of whether they make their own contributions.
- A dollar-for-dollar match up to 3 percent of compensation, where only the participating employees who have elected to make contributions will receive an employer matching contribution.

Each year, you can choose which one you will use for the next year's contributions. This choice is part of the information you are required to communicate to employees before the beginning of the 60-day election period.

Rollovers to a SIMPLE IRA Plan

You and your employees also can roll over amounts into a SIMPLE retirement account from a qualified retirement plan or an IRA. During the first 2 years of participation in a SIMPLE IRA plan, you may roll over amounts from another SIMPLE retirement account. After 2 years of participation, you also may roll over amounts from a qualified retirement plan or an IRA.



Depositing and Investing Plan Contributions

Employee contributions must be deposited in the financial institution serving as trustee for the plan as soon as reasonably possible, but no later than 30 days after the end of the month in which the amounts would otherwise have been payable to the employee in cash. For plans with fewer than 100 participants, salary reduction contributions deposited with the plan no later than the 7th business day following withholding by the employer will be considered contributed in compliance with the law. Your employer contributions must be made by the due date (including extensions) for filing your business's Federal income tax return for the year.

After forwarding the SIMPLE IRA plan contributions to the trustee, the trustee will invest the funds, in many cases at the direction of the participants. SIMPLE IRAs can be invested in stocks, bonds, mutual funds, and similar types of investments. Employee and employer contributions are always 100 percent vested—that is, the money an employee has put aside plus employer contributions and earnings from investments cannot be forfeited. Employees can move their SIMPLE IRA assets from one SIMPLE IRA plan to another in accordance with the procedures of the financial institution.

How does a SIMPLE IRA plan work?

Example 1:

Elizabeth works for the Rockland Quarry Company, a small business with 50 employees. Rockland has decided to establish a SIMPLE IRA plan for its employees and will match its employees' contributions dollar-for-dollar up to 3 percent of each employee's salary. Under this option, if a Rockland employee does not contribute to his or her SIMPLE IRA, then that employee does not receive any matching employer contributions from Rockland.

Elizabeth has a yearly salary of \$50,000. If she decides to contribute 5 percent of her salary to her SIMPLE IRA, Elizabeth's yearly contribution will be \$2,500 (5 percent of \$50,000). The Rockland matching contribution will be \$1,500 (3 percent of \$50,000). Therefore, the total contribution to Elizabeth's SIMPLE IRA that year will be \$4,000 (her \$2,500 contribution plus the \$1,500 contribution from Rockland). The financial institution holding Elizabeth's SIMPLE IRA has several investment choices and Elizabeth is free to choose which ones suit her best.

Example 2:

Austin works for the Skidmore Tire Company, a small business with 75 employees. Skidmore has decided to establish a SIMPLE IRA plan for its employees and will make a 2 percent nonelective contribution for each of them. Under this option, even if an eligible Skidmore employee does not contribute to his or her SIMPLE IRA, that employee would still receive an employer nonelective contribution to his or her SIMPLE IRA equal to 2 percent of salary.

Austin has a yearly salary of \$40,000 and has decided that this year he simply cannot contribute to his SIMPLE IRA. Even though Austin will not contribute this year, Skidmore must make a nonelective contribution of \$800 (2 percent of \$40,000). The financial institution holding Austin's SIMPLE IRA has several investment choices, and Austin has the same investment options as the other plan participants.

Employee Communications

There are two key disclosure documents that keep participants informed about the basics of how the plan operates, inform them of changes in the plan's structure and operation, and provide them a chance to make decisions and take timely action about their accounts.

The **summary description** is a plain-language explanation of the plan and is comprehensive enough to inform participants of their rights and responsibilities under the plan. It also informs participants about the features of the plan. This document is usually provided by the financial institution and is given to participants at the plan's inception, when employees first join the plan, and annually thereafter.

A summary description must include:

- The names and addresses of the employer and trustee,
- A description of the requirements for eligibility to participate,
- The benefits provided,
- The time and method of making salary elections, and
- The procedure for, and effects of, withdrawals and rollovers (including the penalties for early withdrawals).

You can satisfy the summary description requirement by providing employees with the most recent copy of IRS Form 5304-SIMPLE or 5305-SIMPLE provided by the financial institution (if one of these model forms is used to establish the SIMPLE IRA plan), along with the financial institution's procedures for withdrawals and transfers.

Each year, in addition to the information above, employees must receive an **annual election notice** describing their right to make salary reduction contributions and your decision to make either matching or nonelective contributions for the following year. For employers that use one of the model forms, page 3 of both Form 5304-SIMPLE and Form 5305-SIMPLE contain a *Model Notification to Eligible Employees* that can be used to provide this information to employees.

Every year, during the 60-day election period at the end of the year, employees must be given the opportunity to enter into a salary reduction agreement or to modify an existing agreement.

Reporting to the Government

SIMPLE IRA plans are NOT required to file annual financial reports with the government.

Distributions from the plan are reported by the financial institution making the distribution to both the IRS and the recipients of the distributions on Form 1099-R, *Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.*

The financial institution handling the SIMPLE IRAs provides the IRS and participants with an annual statement containing contribution and fair market value information on Form 5498, *Individual Retirement Arrangement Contribution Information*.

SIMPLE IRA contributions are not included in the “Wages, tips, other compensation” box of Form W-2, *Wage and Tax Statement*. However, salary reduction contributions must be included in the boxes for Social Security and Medicare wages.

When Employees Want to Stop Contributions

Employees may elect to terminate their salary reduction contributions to a SIMPLE IRA plan at any time. If they do so, the SIMPLE IRA plan may preclude them from resuming salary reduction contributions until the beginning of the next calendar year. Employers making nonelective employer contributions must continue to make them for these employees.

Distributions

Participants cannot take loans from their SIMPLE IRAs.

SIMPLE IRA contributions and earnings can be withdrawn at any time. When participants take a distribution, they typically can elect to:

- Take a lump sum distribution of their account, or
- Roll over their account to an IRA or another employer’s retirement plan.

Distributions from a SIMPLE IRA are generally subject to income tax for the year in which they are received. If a participant takes a withdrawal from a SIMPLE IRA before age 59½, generally a 10 percent additional tax applies. If the withdrawal occurs within 2 years of beginning participation, the 10 percent tax is increased to 25 percent.

SIMPLE IRA contributions and earnings may be rolled over tax free from one SIMPLE IRA to another. A tax-free rollover may also be made from a SIMPLE IRA to another type of IRA, or to another employer’s qualified plan, after 2 years of beginning participation in the original plan.

A specific minimum amount of SIMPLE IRA contributions and earnings is required to be distributed by April 1 of the year following the year the participant reaches age 70½. After this initial year, the participant must receive a required minimum distribution for each year by December 31 of that year. (For further details regarding the required minimum distribution amount, see IRS Publication 590-B, *Distributions from Individual Retirement Arrangements (IRAs)*.)

Monitoring the Trustee

As the plan sponsor, you should monitor the financial institution/trustee to assure that it is doing everything it is required to do. You should also ensure that the trustee’s fees are reasonable for the services it is providing. If the trustee is not doing its job properly, or if its fees are not reasonable, you should consider replacing the trustee.

Terminating the Plan

Although SIMPLE IRA plans are established with the intention of continuing indefinitely, the time may come when a SIMPLE IRA plan no longer suits the purposes of your business. When that happens, consult with your financial institution to determine if another type of retirement plan might be a better alternative.

To terminate a SIMPLE IRA plan, notify the financial institution that you will not make a contribution for the next calendar year and that you want to terminate the contract or agreement.

You must also notify your employees that the SIMPLE IRA plan will be discontinued.

You do not need to give any notice to the IRS that the SIMPLE IRA plan has been terminated.

Mistakes ... and How to Correct Them

Even with the best intentions, mistakes in plan operation can happen. The U.S. Department of Labor and the IRS have correction programs to help employers with SIMPLE IRA plans correct plan errors, protect participants' interests, and keep the plan's tax benefits. These programs are structured to encourage you to correct the errors early.

Periodically reviewing the plan makes it easier to spot and correct mistakes in plan operation. See the *Resources* section for further information.

Your SIMPLE IRA Plan – A Quick Review

- Choose a financial institution to set up your SIMPLE IRA plan.
- Enroll your employees and start salary reduction contributions.
- Deposit contributions timely.
- Tell your employees about their rights under the plan.
- Monitor your financial institution/trustee.

Resources

The U.S. Department of Labor’s (DOL’s) Employee Benefits Security Administration and the IRS feature this publication and additional information on retirement plans on their websites:

dol.gov/agencies/ebsa – Go to the Saving Matters website at savingmatters.dol.gov or the “Small Business” section under “Employers & Advisers” for additional information to help you understand and operate your SIMPLE IRA plan. This website also has information to help your employees understand the importance of saving for retirement through an employer-sponsored plan.

irs.gov/retirement – Go to “Choosing a retirement plan” to view plain-language information that will help you properly maintain your SIMPLE IRA plan. All the IRS forms and publications mentioned in this booklet are available here.

In addition, the following jointly developed publications are available on the DOL and IRS websites or can be ordered through the DOL toll-free number listed below:

- *Choosing a Retirement Solution for Your Small Business*, Publication 3998, provides an overview of retirement plans available to small businesses.
- *401(k) Plans for Small Businesses*, Publication 4222, provides detailed information about the establishment and operation of a 401(k) plan.
- *Adding Automatic Enrollment to Your 401(k) Plan*, Publication 4721, explains how to add automatic enrollment to your existing 401(k) plan.
- *Automatic Enrollment 401(k) Plans for Small Businesses*, Publication 4674, explains a type of retirement plan that allows small businesses to increase plan participation.
- *Payroll Deduction IRAs for Small Businesses*, Publication 4587, describes an arrangement that is an easy way for businesses to give employees an opportunity to save for retirement.
- *Profit Sharing Plans for Small Businesses*, Publication 4806, describes a flexible way for businesses to help employees save for retirement.
- *SEP Retirement Plans for Small Businesses*, Publication 4333, describes a low-cost retirement savings option for small businesses.

For business owners with a plan

- *Retirement Plan Correction Programs*, Publication 4224, briefly describes the IRS and DOL voluntary correction programs.

Order electronically at askebsa.dol.gov or by calling 866-444-3272.

Related materials available from DOL

DOL sponsors an interactive website – the Small Business Retirement Savings Advisor, available at webapps.dol.gov/elaws/ebssaplan.htm – that encourages small business owners to choose the appropriate retirement plan for their businesses and provides resources on maintaining plans.

Related materials available from the IRS

- *Retirement Plans for Small Business (SEP, SIMPLE, and Qualified Plans)*, Publication 560
- *Contributions to Individual Retirement Arrangements (IRAs)*, Publication 590-A
- *Distributions from Individual Retirement Arrangements (IRAs)*, Publication 590-B
- *Have you had your Check-up this year? for Retirement Plans*, Publication 3066
- *SIMPLE IRA Plan Checklist*, Publication 4284
- *Lots of Benefits*, Publication 4118 (also in Spanish, Vietnamese, Korean, Chinese and Russian)
- *The IRS Retirement Guide*, Publication 4460

To view these related publications, go to irs.gov/retirement and click on “Retirement Plans A-Z” and then “Forms & Publications.”



EMPLOYEE BENEFITS SECURITY ADMINISTRATION
UNITED STATES DEPARTMENT OF LABOR



Publication 4334 (Rev. 10-2016) Catalog Number 38508F
Department of the Treasury **Internal Revenue Service** www.irs.gov