SIMPLE IRA Plans

The Small Business Job Protection Act (SBJPA) of 1996 created a new type of simplified retirement plan for smaller employers called the Savings Incentive Match Plan for Employees or "SIMPLE" Plan. These plans are available only to employers with 100 or fewer employees who received at least $5,000 in compensation during the preceding calendar year. All employees must be counted towards the 100 limit except for employees who earned less than $5,000.

A SIMPLE IRA Plan is a retirement plan that permits all eligible employees to make pre-tax contributions to a specified limit. The contribution limit in 2020 is $13,500 and there is also an age 50+ catch up contribution permitted of up to $3,000. Originally these limits were much lower, but after the Economic Growth and Tax Reconciliation Relief Act of 2001 (EGTRRA), the contribution limits to SIMPLE IRA Plans were significantly increased.

The following chart provides some historical information on the SIMPLE IRA limits:

Year	Maximum Contribution	Age 50+ Catch-up
2003	$8,000	$1,000
2004	$9,000	$1,500
2005	$10,000	$2,000
2006	$10,000	$2,500
2007-2008	$10,500	$2,500
2009-2012	$11,500	$2,500
2013-2014	$12,000	$2,500
2015-2018	$12,500	$3,000

2019	$13,000	$3,000
2020	$13,500	$3,000

As with 403(b), 457(b) and 401(k) plans, EGTRRA introduced the “age 50+ catch up” concept. This provision permits individuals who have attained age 50 or greater at any time during the applicable tax year to increase their deferral limits by an additional amount. The previous chart describes the age 50+ catch up limit for SIMPLE IRA Plans since 2003.

In a SIMPLE Plan, the employer must also make a contribution to the SIMPLE Plan. The employer can elect to make either a $1.00 for $1.00 matching contribution up to 3% of pay (total pay, no limit) or a contribution equal to 2% of pay (capped at $280,000 for 2019) for all eligible employees. Neither the employee nor employer may make additional contributions other than rollovers into the SIMPLE, as long as the Employer’s SIMPLE Plan was amended to accept such rollover contributions. The employer must make the contribution every year, except for a special rule that permits the matching contribution to be dropped to 1% in the event of the employer’s occasional financial hardship. There are no nondiscrimination, coverage or participation tests because all employees who have earned at least $5,000 in any two (2) preceding years, and if expected to earn at least $5,000 in the current year, must be included in the plan. Employees covered by a collective bargaining unit may be excluded from participation.

SIMPLE IRA Plans are funded through IRAs. IRA rules apply (except for the contribution limits). The employer has the option of selecting one financial organization to act as the IRA custodian (“DFI” or Designated Financial Institution”) or provide employees the option of selecting their own IRA custodian (“non-DFI” or non-designated Financial Institution); the employer will send all contributions directly to the IRA custodian(s). The employer is relieved of fiduciary obligations (other than for selecting the IRA depository as a DFI) if the participant selects a different IRA product and moves his SIMPLE account into that IRA. The rules here are a little more complex where if there is a DFI, then no fees, penalties or any charges can be made to the participant’s IRA and they are permitted to move the assets at least once a month. If the participant does not move his IRA to another custodian, then one year after the employee established the IRA for the participant the employer will be relieved of fiduciary liabilities for selecting the IRA. There are no Form 5500 filings with the IRS or DOL. A SIMPLE Plan must be the only plan that an employer offers. Therefore, an employer may not offer a 403(b) program even a supplemental 403(b) plan if the employer offers a SIMPLE Plan. For this reason, many 403(b) agents, sales representatives and product providers have not shown interest in entering the SIMPLE market. However, a SIMPLE IRA Plan may be an excellent option for smaller employers who wish to make a contribution to a retirement program, but are reluctant to commit to the normal administrative and fiduciary obligations inherent in offering a regular qualified plan or ERISA 403(b) Plan. Most mutual funds and many banks, brokerage houses and insurance companies have SIMPLE IRA package products available for immediate adoption.

Advantages of SIMPLE IRA Plans

1. **They are Simple.** These plans truly are very easy to implement and administer. The custodian or trustee is responsible for all recordkeeping, distributions and tax reporting. The employer’s duties are generally restricted to providing notice of the plan to employees, making timely contributions and transmitting the contributions.

2. **They are Inexpensive**. SIMPLE IRA plans are relatively inexpensive. If the employer wishes to ensure that all employees have a minimum retirement benefit, then the 2% of pay contribution may be made. The total potential contribution can be calculated based on current payroll numbers. However, the matching SIMPLE IRA Plan will probably be even less expensive because employees who don’t participate will cost the employer nothing. Even if the only employees that participate are highly compensated employees (HCEs), the

employer will not have to make a contribution for any other employee. In any other contributory plan, this would be discriminatory and the employer would either have to return the HCE contributions or make contributions for the non-HCEs.

3. **Good Starter Plan.** For employers who are reluctant to have a retirement plan, a SIMPLE IRA Plan is a good starter plan. It introduces some of the concepts related to employer sponsored plans, but does not overwhelm the employer with burdensome testing, reporting, accounting, recordkeeping or fiduciary responsibilities. The plan is funded through an IRA, the employer can terminate the plan at any time and “graduate” to a more sophisticated plan, if necessary.

Disadvantages of SIMPLE IRA Plans

1. **Not Much Flexibility.** These plans may not be modified, customized or amended in any way. The employer must adopt and maintain the plan according to the closely defined parameters of the statute. In exchange for easy administration, the employer must give up design flexibility.

2. **Lower Contributions.** Most deferral plans permit employees to defer larger amounts than permitted under a SIMPLE Plan. For example, in 2019, the deferral limit applicable to 401(k) and 403(b) plans is $19,000, plus the age 50+ catch up (if applicable) versus $13,000 in the SIMPLE. The age 50+ catch up is only $3,000 in the SIMPLE contrasted with $6,000 in the other plans. Employers may make additional contributions to 401(a), 403(b) or 401(k) plans. However, employee contributions to SIMPLE IRA Plans are limited to the deferral limits outlined in the chart on the previous page and employers may contribute no more than either the 2% (nonelective contribution) or 3% (matching contribution). For employees who want to take advantage of the maximum elective deferral limits, SIMPLE IRA Plans are not the best plans.

3. **Employer Eligibility May Change.** Since these plans are only available to smaller employers, any employer that grows beyond the 100 employee maximum limit will no longer be eligible to sponsor a SIMPLE IRA Plan. This can also become a problem where employers merge or are acquired by another employer. If the new entity exceeds 100 employees, then the SIMPLE IRA Plan must also be discontinued. There is a two (2) year grace period that permits employers to continue to maintain SIMPLE IRA Plan if they exceed the 100 employee limit. However, once the grace period has ended, such employers must discontinue their SIMPLE IRA Plan. Therefore, these plans may not be recommended for any employer that expects to expand beyond 100 employees either by growth or acquisition.

4. **Too Limited.** The employer is not permitted to sponsor any other type of retirement plan. Thus, a 403(b) eligible employer would be limited only to the SIMPLE IRA plan.