

## CHECKLIST

# ARE YOUR QUALIFIED RETIREMENT PLANS UP TO DATE?

Various changes in tax law have had a positive impact on how much Business Owners and Professionals can save in qualified retirement plans. By reviewing the different types of plan designs, advisors and their clients may be better able to capitalize on some of these changes. Here are some points to consider:

- Elective 401(k) deferrals.* The maximum elective contribution per employee in the 2008 calendar year is \$15,500, even if the plans are from different employers.
- Catch-up contributions.* Employees who will reach age 50 or older by the end of the plan year can add a catch-up contribution of \$5,000 to their elective deferrals.
- Annual additions limit for defined contribution plans.* Annual additions – including employer contributions, employee contributions and forfeitures – are limited to the lesser of 100% compensation or \$46,000. The catch-up contribution is not included in this limit.
- Annual compensation limit.* The eligible compensation limit in 2008 is \$230,000. If services are rendered by a husband and wife, consider balancing their compensation (as long as it is reasonable and customary) to increase their overall retirement contribution.
- Highly compensated employee limit.* Employees earning \$105,000 or more may be excluded from the plan. This may work well in a professional organization, which could cover non-highly-compensated employees along with the partners, leaving out highly-compensated managers or supervisors.

*Maximum annual retirement benefit.* The annual limit for defined benefits is \$185,000 for retirement ages 62-65.

*Tax credit for new plans.* A three-year tax credit of 50% of the first \$1,000 of start-up costs (\$500 maximum) is available to employers with fewer than 100 employees that cover at least one non-highly compensated employee. Eligible expenses include fees to establish the plan, administrative fees and costs incurred to educate employees about the plan.

*The Roth 401(k).* A Roth 401(k) plan may be added to a traditional 401(k) plan, allowing participants to make after-tax contributions. Income limits do not apply. Employer matching contributions must continue to be made on a pre-tax basis. Plan sponsors must amend the plan to include the provision.

*One-person plans.* Employee deferrals are not included in the deduction limit, though they are included in the annual addition limit. Consider a uni-401(k) plan or a defined benefit plan with a 401(k) to maximize contributions. For example, in 2008 a 50-year-old business owner earning \$50,000 of W-2 compensation could contribute \$33,000 to a uni-401(k) plan (25% x \$50,000 = \$12,500, plus \$15,500 employee deferrals, plus \$5,000 catch-up for age 50+). The same business owner making \$225,000 could contribute only \$49,000 to a uni-401(k) plan (annual addition limit of \$45,000 plus catch-up of \$5,000). A defined benefit plan with retirement age 60 would allow for contributions of \$160,000 or more, plus \$20,500 for 401(k) with catch-up.

*Comparability profit-sharing plans.* Consider a comparability plan for clients who would like to keep the contribution discretionary and to have different contribution percentages for different categories of participants. This plan allows the business owner to maximize both tax deductions and contributions to the plan.

*Safe-harbor plans.* These plans have eliminated many of the issues with testing associated with 401(k) plans. Consider them if you have bumped into limits to the levels of contributions of highly-compensated participants. Certain structures permit a double use of a safe-harbor contribution, enabling reduced levels of profit-sharing dollars to achieve maximum contribution levels.

# RETIREMENT PLAN LIMITS 2008

The Internal Revenue Service has announced cost of living adjustments to the retirement plan limits. The new limits are effective January 1, 2008.

Type of Limitation	2007	2008
Annual Compensation Limit	\$225,000	\$230,000
Defined Benefit Annual Limit	\$180,000	\$185,000
Defined Contribution Annual Limit	\$ 45,000	\$ 46,000
401(k), 403(b), 457(b) Deferral Limit	\$ 15,500	\$ 15,500
401(k), 403(b), 457(b) Catch-Up Limit (Age 50)	\$ 5,000	\$ 5,000
SIMPLE Contribution Limit	\$ 10,500	\$ 10,500
SIMPLE Catch-Up Limit (Age 50)	\$ 2,500	\$ 2,500
Highly Compensated Employee (Compensation in the prior year exceeding)	\$100,000	\$105,000
Officer as Key Employee	\$145,000	\$150,000
Social Security Taxable Wage Base	\$ 97,500	\$102,000
SEP Minimum Compensation	\$ 500	\$ 500

Source: IRS News Release  
IR-2007-171, Oct. 18, 2007

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# UNDERSTANDING NEW COMPARABILITY AND CROSS-TESTED PLANS

IRS regulations have come to the rescue of the small business! Owners have more flexibility with retirement plans than in the past.

Profit sharing plans have long been the retirement plan of choice for the small business. However, with “traditional” plans, flexibility exists only in the contribution level. Typically, each employee’s share of the firm’s contribution is identical. If one employee receives an allocation of 10 percent of salary, all employees receive an allocation of 10 percent of salary.

Most small business owners would like more options in the amount of their contribution to employees. Flexibility is now available. Section 401(a)(4) of the Internal Revenue Code allows profit sharing allocations to be divided differently among employees based upon identifiable classification groups. Not only is the amount of contribution flexible, but there is flexibility in the way it is divided among the employees.

The New Comparability profit sharing plan allows the owner to decide who will benefit more from the firm’s profit sharing contribution based upon objective criteria. For example, the owner may divide employees by job classification, salary level, length of service or each employee may be deemed their own class.

Under IRS regulation 1.401(a)(4) – 8(b)(3) and IRS regulation 1.401(a)(4) – (b)(1)(vi) (A) and (B), the Gateway Safe Harbor rule is introduced which states that the discrimination rule will be satisfied if each non-highly compensated employee allocates a minimum of 5% of compensation. This will allow the employer to contribute the maximum amount to the highly compensated employee which is \$46,000 in 2008.

The options for classification groups and contribution amounts maximize the effectiveness of the firm’s retirement plan using a New Comparability plan design. To find out more about how New Comparability and Cross-Testing plans can benefit your business, contact Willow Financial Services today at 800-662-9847.

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# UNDERSTANDING 401(k) PLANS

Many of us are familiar with or participate in an employer-sponsored 401(k) plan, but what is it and how does it work?

A 401(k) plan is a type of defined contribution plan known as a profit sharing plan. The profit sharing plan, in addition to allowing employer contributions, has a 401(k) feature that allows eligible participants to defer a portion of compensation into an investment account. These employee contributions, also called salary deferrals or elective contributions, reduce the employee's current federal income tax, and in most states, state income tax. The taxes on elective contributions are deferred until distribution. The employee contribution does not reduce compensation for the purpose of social security taxes (FICA) or federal unemployment taxes (FUTA.)

Employees can contribute up to 100 percent of compensation to the individual maximum. The individual maximum for 2008 is \$15,500 per participant. For participants who will be age 50 or older by the end of 2008, a \$5,000 catch-up contribution may also be made. These limits are adjusted or indexed annually for cost-of-living increases.

The employer has the option to match a portion of its participants' elective contributions to reward those employees who are participating in the 401(k) plan. This is usually quoted as a percent of the contribution up to a stated maximum. For example, the employer might match 25 percent of elective contributions up to the first three percent of compensation.

Salary deferrals are always 100 percent vested and are typically invested at the participant's direction.

Employer profit sharing and employer matching contributions are subject to the vesting schedule stated in the plan document. The employer may choose to direct the investments of these funds or it can leave that responsibility to its employees.

401(k) plans, if handled properly, make a nice addition to an employer's profit sharing plan. To find out more about how a 401(k) plan can benefit your business, contact Willow Financial Services today at 800-662-9847.

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# UNDERSTANDING 412(E)(3) DEFINED BENEFIT PLANS

Wealth accumulation and retirement savings become more important as businesses prosper and owners begin dreaming of retirement. Adopting a 412(e)(3) plan is an important financial tool for retirement planning. It provides you an opportunity to achieve retirement goals without stock market risk to the owner.

412(e)(3) plans are retirement plans funded solely with insurance products. Plans can be funded with life and annuity products or annuity only. Funding begins when a participant enters the plan and ends at the participant's retirement date.

<b>Advantages</b>	<b>Considerations</b>
Guaranteed Benefits - <i>provided that annual, level premiums have been paid</i>  Tax Deductions  Larger contributions for older employees  Life Insurance available with tax-deductible premium	Annual Funding requirement  Plan Sponsor must have cash flow to fund at the beginning of each plan year  Participant Loans are not permitted

To find out more about how a 412(e)(3) Defined Benefit Plan can benefit your business, contact Willow Financial Services today at 800-662-9847.

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# UNDERSTANDING CREATIVE DESIGN PLANS

A Hybrid Defined Benefit Plan has combined characteristics from both Defined Benefit and Defined Contribution Plans. There are two types of Hybrid Defined Benefits Plans. The first type is the Floor Offset Plan.

## FLOOR OFFSET

A **Floor-Offset Plan** is a combination of two plans:

1. Defined Benefit Plan.
2. Defined Contribution Plan  
(typically a safe-harbor Profit Sharing Plan)

Floor Offset Plans work by:

1. Projecting the Profit Sharing Contribution and Account Balance to Normal Retirement at an assumed rate of return no greater than 8 ½ % and continuing contributions to the Profit Sharing Plan of 5 % - 7 ½ %.
2. Then this is converted by the Annuity Purchase Rate.
3. If calculated properly this “offset” amount will always be greater than the Defined Benefit Plan resulting in only a contribution to the Profit Sharing Plan.

## CASH BALANCE

A Cash Balance plan is a Hybrid plan with Defined Benefit plan with Defined Contribution features. From the employee’s perspective a Cash Balance Plan mirrors a Money Purchase Plan .

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# UNDERSTANDING SAFE HARBOR 401(K) PLANS

Many of us are familiar with 401(k) plans, but what is a safe harbor 401(k) plan and why would an employer choose one over a traditional 401(k) plan?

Safe harbor 401(k) plans also allocate either an employer contribution of three percent or a matching formula of 100 percent of the first three percent of compensation and 50 percent on salary deferrals between three percent and five percent of compensation to all eligible participants. These funds are immediately 100 percent vested. In exchange for these employer contributions, the highly compensated employees (usually the owners) are allowed to defer up to the individual maximum salary deferral limits, without discriminating against the non-highly compensated employees\*.

It is important to note that safe harbor 401(k) plans must follow the IRS guidelines to be considered a safe harbor plan. Failure to follow these rules, such as failing to provide adequate notice to its employees, may disqualify a plan. However, when the rules are followed, this plan can be a win-win situation for the employer and its employees.

To find out more about how a Safe Harbor 401(k) plan can benefit your business, contact Willow Financial Services today at 800-662-9847.

\* Refer to PPA06 for changes beginning in 2008.

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# UNDERSTANDING SIMPLE IRA PLANS

A SIMPLE (Savings Incentive March Plan for Employees of Small Employers) IRA provides employers and their employees with a simplified way to contribute toward retirement. It reduces taxes and attracts and retains quality employees.

A SIMPLE IRA plan offers great advantages for businesses that meet two basic criteria. First, your business must have 100 or fewer employees who each received at least \$5,000 in compensation during any 2 years preceding the current calendar year and is reasonably expected to receive at least \$5,000 during the current calendar year is eligible to participate. In addition, you cannot currently have another retirement plan.

Employer and employee contributions under this plan are simply deposited into individual retirement accounts or annuities.

Contributions are made up of salary reduction contributions and employer contributions. You, as the employer, must make either matching contributions or non-elective contributions within certain time restrictions. The maximum amount that an employee can contribute is \$10,500 in 2008. Additional employee contributions (known as catch-up contributions) are allowed for employees age 50 or over. The catch-up contribution is \$2,500 in 2008.

To find out more about how a SIMPLE IRA plan can benefit your business, contact Willow Financial Services today at 800-662-9847.

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