SIMPLE IRAs

SIMPLE IRAs (Savings Incentive Match Plan for Employees) are employer-sponsored plans that allow contributions by the employees and employer. Contributions are made with pre-tax dollars, earnings grow tax-deferred, and distributions are taxable. SIMPLE IRAs have much lower administrative costs than a traditional qualified plan, but they also require employer contributions be made in employees' accounts. For those employers with SIMPLE IRAs, they cannot maintain another qualified plan.

FEATURES

CONTRIBUTION LIMITS

For 2015, employees can contribute up $12,500 and for those who are age 50 and older at the end of the calendar year, they are eligible to make a catch-up contribution of up to $3,000. Deferrals are made through payroll deduction.

Employer contributions are also required but can be made in one of two ways. Employers are generally required to match up to 3% of employees' elective deferrals. This percentage can be as low as 1%, but cannot be below 3% for more than two years during a five year period that ends with the current year. Employers can also make non-elective contributions of 2% of compensation for all eligible employees, regardless of whether the employee contributed. Only $265,000 of the employee's compensation can be taken into account in calculating these non-elective contributions.

ELIGIBLE EMPLOYEES

An employer can set up and maintain a SIMPLE IRA if they have 100 or fewer eligible employees (those who received at least $5,000 in compensation the last two prior calendar years and is reasonably expected to earn at least $5,000 in the current year). Employers can use less restrictive eligibility requirements but cannot make them more restrictive.

CONTRIBUTION DEADLINE

Employee deferral contributions must be deposited to each employee's SIMPLE IRA by the 30th day following the month for which the deferral applies. Employers have until their tax-filing deadline, including extensions, to deposit matching or non-elective contributions to the employees' SIMPLE IRAs.

DISTRIBUTIONS

SIMPLE IRA distributions are the same as normal IRA distribution rules, which are subject to income taxes for any pre-tax contributions and earnings. However, there is a "2-year period" rule that is unique to these plans. This begins on the date on which the employee first participated in a SIMPLE IRA. If an employee takes an early distribution within this 2-year period, the additional tax penalty is 25%, excluding exceptions. These exceptions include death, total disability, SEPP (discussed below), or a distribution that meets certain requirements in purchasing a first home.

REQUIRED MINIMUM DISTRIBUTIONS (RMD)

To ensure that IRAs are used for retirement income and not for estate planning purposes, IRA holders must begin making withdrawals by April 1st of the year after reaching age 70½ (the required beginning date). The minimum amount that must be withdrawn (RMD) is calculated by dividing the account balance on December 31st of the year preceding the distribution by the IRA owner's life expectancy as found in IRS Publication 590. Failure to withdraw the RMD before December 31st results in 50% excise tax on the amount not distributed as required.

SUBSTANTIALLY EQUAL PERIODIC PAYMENTS (SEPP)

Substantially equal periodic payments (SEPP) are one of the exceptions in the United States IRS Code that allows individuals under age 59 ½ to start receiving payments without incurring a 10% early distribution penalty. The individual must be at least 55 to take SEPP and the rules for SEPPs are set out in IRS code section 72(t). It allows for three specific methods of calculating the allowed withdrawal amounts and SEPP payments must continue for the longer of five years or until the account owner reaches age 59 ½.