SOLO 401(k) PLANS

These tax-favored accounts are one strategy for business owners to set aside funds for retirement. There are two parts to this plan – salary deferral as well as the profit sharing component in which the business can contribute up to 25% of the participant's compensation. Contributions are tax-deductible, earnings grow tax-deferred, and distributions are taxable.

Solo 401(k) plans were first introduced in 2002 as a way for eligible business owners to make larger contributions to a retirement plan than what they would be able to contribute in a SEP IRA or Keogh plan. These plans are also commonly referred to as an Individual 401(k) plan and a Uni-K plan.

FEATURES

ELIGIBILITY

Solo 401(k) plans are available to those that are self-employed and to business owners with no full-time employees other than a spouse. Sole proprietorships, partnerships, limited liability companies (LLC), S corporations, and C corporations qualify for Solo 401(k) plans. Those businesses employing independent contractors (1099 employees) would not disqualify the business owner from being able to contribute to a solo 401(k) plan.

The plan must be established by December 31st of the year in which the business owner would like to receive the tax deduction or the end of fiscal year for incorporated businesses.

CONTRIBUTION LIMITS

With an individual 401(k) plan, the business owner can elect to defer up to $18,000 (or $24,000 if age 50 and over by the end of the calendar year) of their compensation to the plan for 2015. The deferral amount can be allocated towards the traditional account (pre-tax), Roth account (after-tax), or a combination of the two. In addition, as with a traditional profit-sharing plan, the business can make a maximum tax-deductible contribution to the plan of up to 25% of the owner's compensation (20% for sole proprietorships and single member LLCs).

For this year, the total maximum contribution is $53,000 or if age 50 and over, $59,000 due to the $6,000 catch-up contribution. Solo 401(k) plan contributions can be increased or decreased or stopped on a year by year basis.

CONTRIBUTION DEADLINE

The deadline for salary deferrals is dependent on how the business is structured. For unincorporated businesses, the deadline is the tax filing deadline of the following year plus extensions. For incorporated businesses, the deadline is within 15 days after the close of the fiscal year.

For the profit sharing contributions made by the business, it is the tax filing deadline plus extensions for unincorporated businesses and for incorporated businesses, they are the corporate tax filing deadline plus extensions.

LOANS

These are allowed in solo 401(k) plans for up to 50% of the account balance with a maximum loan amount of $50,000. They typically have a 5-year term where principal and interest is repaid back to the account.

DISTRIBUTIONS

Once the account holder turns age 59 ½, they are able to withdraw funds with no penalties but these distributions are subject to federal and state income taxes. At age 70.5, the individual must begin taking required minimum distributions (RMD) unless they are still actively contributing to the plan. For those under age 59 ½, distributions are subject to a 10% penalty in addition to income taxes in the year the distribution is made. There are exceptions to the 10% early withdrawal penalty and these include death, total disability, or SEPP (discussed below).

SUBSTANTIALLY EQUAL PERIODIC PAYMENTS (SEPP)

These 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.