Why Sponsor a Retirement Plan?

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Plan Consulting • Administration • Design

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As the owner of your business, you may have wondered if you should implement an employer sponsored retirement plan. Do the pros outweigh the cons? There are several reasons to establish an employer sponsored plan. These plans not only benefit employees, but benefit the company as well.

Retirement can last 30 years or more and many people will need up to 80% of their annual pre-retirement income to live comfortably once they retire. By making an employer sponsored plan available, you give your employees the tools they need to start preparing for their futures. Because the employer controls payroll processing, it is best suited to direct payroll deductions straight into the plan from the employee's paychecks. By contributing some of the employee's pay directly to the plan, employers are able to provide a systematic, disciplined savings opportunity for employees who might not otherwise be as disciplined if they were left to invest on their own with after-tax dollars.

Many plan participants have a limited understanding of important investment topics such as risk tolerance, portfolio diversification, or mutual fund selection. The employer can aid the participants in the plan by providing a qualified default investment alternative (QDIA) as the default fund. QDIA's are typically target date funds, life-cycle funds, balanced funds or managed portfolios. Employees who are not investment savvy and are defaulted into the QDIA have the benefit of knowing that their contributions have been invested in a fund that is specifically designed to provide a diversified savings vehicle for their money.

Plan participants also receive the benefit of reducing their taxable income and the potential to claim the Savers Credit when filing their taxes. In addition, contributions and earnings will never be taxed until the participant takes a distribution. Most importantly, compounding interest can turn small contributions into an account the employee can comfortably carry into retirement. If the employee terminates, the retirement account balance can be easily moved from employer to employer or to an individual retirement account (IRA).

Employers also receive the benefit of tax savings by implementing a retirement plan. Not only do plan assets accumulate tax free, but all contributions to the plan are tax-deductible for the company. This can result in significant savings for the employer. The initial process of setting up a brand new plan may seem daunting, but the IRS offers tax credits that help offset some of the expense. Other features, such as revenue sharing from the investment provider, can also be available to reduce the cost to the employer even more.

Business owners should give careful consideration to the type of plan that they select. For example, a newer business may want to consider a plan with a discretionary contribution, whereas a more established business may be comfortable with a mandatory contribution. As the owner of the business, you are afforded significant flexibility when choosing the features for the plan. Whether your goal for the plan is to encourage plan participation, increase employee retention, or maximize contributions for the owners of the company, the specifications can be written to ensure your objectives are satisfied.

There can be significant value found in establishing an employer sponsored plan. When businesses offer a plan, they get significant tax savings and the employees get the benefit of knowing that their retirement is secure. Consult with your Third Party Administrator about implementing a new plan and what features would work best for your business.