

CREDIT FOR SMALL EMPLOYER RETIREMENT PLAN START UP COSTS

Updated July, 2006

For small employer retirement plans, a tax *credit* of up to 50% of the first \$1,000 in “qualified start up costs” may be available to offset establishment and maintenance costs. This credit would be available for each of the first three years a new plan is in existence.

Eligible Employer:

- Employs 100 or fewer employees who received at least \$5,000 in prior year compensation.
- Has not established or maintained a retirement plan (qualified plan, SIMPLE, or Simplified Employee Pension plan) in the preceding three years. (Example: For a credit available in 2006, the three year period is 2003, 2004, and 2005.)

Eligible New Plans:

- Qualified defined contribution plans, qualified defined benefit plans, SEPs, and SIMPLEs. This would also include 401(k) plans and ESOPs.
- Must cover at least one non-highly compensated employee.

Eligible Expenses:

- Include any ordinary and necessary expenses paid or incurred in connection with the establishment and administration of an eligible employer plan, or the retirement-related education of employees with respect to the eligible employer plan.
- Eligible expenses may be incurred and credited in the year preceding the actual effective date of the plan.

Tax Credit:

- Maximum credit is \$500 for the first credit year and each of the two tax years immediately following the first credit year.
- No *deduction* is allowed for the portion of startup costs taken as a *credit*. (Example: If an employer’s eligible costs are \$1,750 and the maximum credit of \$500 is used, \$1,250 remains as a deductible expense.)
- This credit is subject to the general business credit rules. Those rules allow a carryback of unused credits.