

**A Retirement Planning Strategy**  
for Business Owners

# Small business retirement planning stems from a simplified approach – SEP-IRA



We'll help you get there.®



## A simplified approach to small business retirement planning

Congratulations. Your dedication and hard work have taken your company to where it is today. You've made good, solid decisions over the years, as evidenced by your success. Now is a good time to make other important decisions – such as determining how your business can help you and your employees save for retirement.

### What is a Simplified Employee Pension Plan (SEP)?

A SEP is a written plan designed to allow your company to make contributions toward retirement for you and your eligible employees. The contributions are made directly into individual retirement arrangements set up by, or for, each individual, called Simplified Employee Pension Plan Individual Retirement Account, or Individual Retirement Annuity (SEP-IRA). These SEP-IRAs are individually owned and controlled.

### Why consider a SEP-IRA plan?

#### By establishing SEP-IRAs, you can:

- Save more for your retirement and contribute toward your employees' retirement.
- Realize a tax deduction for your business.
- Have the flexibility to not make contributions every year.
- Attract, retain and motivate employees.

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# Advantages of a SEP-IRA plan

## Easy to set up

A business owner can set up a SEP-IRA plan using Internal Revenue Service (IRS) form 5305-SEP. The completed form becomes the SEP-IRA plan’s basic legal document and ensures the plan is in compliance.

## Cost efficient

Administrative costs related to a SEP-IRA plan are generally low because there are no complex compliance testing requirements and limited government reporting.

## Longer eligibility requirements

A SEP-IRA plan imposes relatively long service requirements compared to other types of plans. This allows employers to exclude certain employees which may also help control costs.

## Discretionary contributions

Employers are not required to make contributions every year. When contributions are made, however, they must be allocated to all eligible employees’ individual retirement arrangements according to the SEP-IRA agreement. Employers may discontinue the plan at any time.

## Limited fiduciary responsibility

Employer contributions are sent to the financial institutions where the eligible employees have set-up individual retirement arrangements. Investment decisions are the responsibility of each employee which helps limit the fiduciary responsibility of the employer.

## SEP-IRA plan participation

Any type of business can establish a SEP-IRA plan, including sole proprietorships, corporations (including S-corporations) and non-profit organizations. All eligible employees of a business with a SEP-IRA plan must participate. An eligible employee is an individual who meets the following requirements:

- Age 21 or older
- Worked for the company during three of the last five years
- Received at least \$550\* in compensation from the company for the year

An employer may use less restrictive eligibility requirements, but not more restrictive than what is shown above.

\* Minimum as of 2013. Amount may be indexed for inflation in subsequent years.

## Establishing a SEP-IRA plan

There are three basic steps:

### Step 1 – Execute a formal written agreement.

A SEP-IRA plan is adopted when a business creates a written agreement authorizing it and eligible employees are informed. The Internal Revenue Service’s (IRS) model agreement Form 5305-SEP may be used. Other SEP-IRA forms are available through financial institutions.

### Step 2 – Give all eligible employees information about the plan.

Information about the plan must be provided to each eligible employee. Sample forms and communications are available from financial institutions.

### Step 3 – Make sure a SEP-IRA is set up for each eligible employee.

A SEP-IRA must be set up for each eligible employee. If an eligible employee does not set up a SEP-IRA, the employer is required to set it up on his/her behalf. Each SEP-IRA is individually owned and controlled.

NOT FDIC/ NCUA INSURED	NO BANK/ CREDIT UNION GUARANTEE	MAY LOSE VALUE	NOT INSURED BY ANY GOVERNMENT AGENCY	NOT A BANK/CREDIT UNION DEPOSIT OR OTHER OBLIGATION
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### Consider a SEP-IRA plan if you are a business owner who wants:

- A simplified method to make contributions toward your own retirement and your employees' retirement;
- Maximum eligibility requirements in order to exclude certain employees;
- The flexibility to choose when contributions are made and not be required to contribute every year.



## Contributions to SEP-IRAs

Contributions are made by an employer; employees cannot contribute. The company contributions are made to an individual retirement account or individual retirement annuity (SEP-IRA) and are sent directly to the financial institutions where the IRAs are maintained.

The employer determines the amount that will be contributed to the SEP-IRAs. The contributions must be uniform (i.e., a percentage of compensation) for every eligible employee – including the owner(s). Contributions are not required, however, and in any given year they can be as low as zero.

If an annual contribution is made, it must be made for all eligible employees. Employees are eligible even if they:

- Don't want to have a SEP-IRA;
- Are age 70½ or older and are subject to IRA minimum distribution requirements;
- Are no longer employed by the company prior to the last day of the year;
- Die, become disabled or take a leave of absence.

## Contribution limits

The contribution amount is limited and cannot exceed a certain dollar amount each year. There is a cap on the amount of annual compensation that can be considered. Compensation is generally based on W-2 wages. (Note: These contribution limits apply to self-employed individuals also. The IRS has special rules that apply to determine the maximum deductible contribution. Refer to IRS Publication 560 for details.)

Maximum Contribution	25% of compensation
Compensation Cap	\$255,000*
Maximum Contribution	\$51,000*

\* Maximum as of 2013. Amount may be indexed for inflation in subsequent years.



## Hypothetical example: Leigh & Watson Creative Designs, Inc.

### A small business with two owners and two employees

Janet Leigh and Angela Watson are equal owners in a design firm that was established in 2002. They have two full-time employees – Robert joined the company four years ago and Gabriel was hired this year. In the written SEP-IRA plan, the owners elected to contribute 25% of each eligible employee's annual compensation to SEP-IRAs.

**A SEP-IRA plan allows an employer to contribute to individual retirement arrangements that are owned and controlled by each eligible employee.**

### Example: Leigh & Watson Creative Designs, Inc.

Name	Annual Compensation	Company Contribution to SEP-IRA (25% of annual compensation)
Janet	\$100,000	\$25,000
Angela	\$100,000	\$25,000
Robert	\$48,000	\$12,000
Gabriel (not eligible)	\$23,000	n/a

The company contributed a total of \$62,000 to the SEP-IRAs. The total contribution for both owners is \$50,000. The contribution for the one eligible employee is \$12,000. That resulted in more than 80% of the overall contribution being directed to the owners' SEP-IRAs.



## Tax advantages of SEP-IRAs

SEP-IRAs offer tax benefits for both the company and its eligible employees.

### **Contributions are tax-deductible as a business expense.**

As long as they are made by the business' tax-filing deadline, including extensions, contributions within limits can be deducted on a company's tax return.

### **Contributions are not included in gross income.**

As long as they are made within the annual limits, employer contributions are not included in an eligible employee's gross income for federal income tax purposes.

### **Earnings within a SEP-IRA accumulate on a tax-deferred basis.**

Gains and investment income are not reported to the IRS until withdrawals are taken.

### **Transfer to another IRA or qualified retirement plan is tax-free.**

This portability feature allows individuals to transfer their SEP-IRA assets when they take a new job or retire.

## Distributions from SEP-IRAs

SEP-IRA account owners (employer and eligible employees) can request distributions from their IRAs. The amount of a distribution is not limited.

An account owner can withdraw funds from a SEP-IRA at any time. Withdrawals are subject to income tax and if taken prior to age 59½, a 10% federal income tax penalty may apply.

Assets from a SEP-IRA can be rolled-over or transferred to another IRA or type of qualified plan. In a rollover, the account owner receives the distributed funds and must move them to a new qualified plan within 60 days. A direct transfer moves the SEP-IRA assets directly from one financial institution to another.

Eligible employees may continue to receive employer contributions in their SEP-IRAs regardless of taking a distribution. Individuals should consult their financial professional and tax advisor prior to taking distributions from a SEP-IRA.





## Funding your SEP-IRA plan

When it comes to funding your SEP-IRA plan, there are a number of alternatives to choose from. Individual deferred annuities are an important option to consider because they are specifically designed to help employees accumulate and protect assets for retirement.

Individual deferred annuities may be variable (subject to stock market performance) or fixed (with interest rates guaranteed by the insurer for a specific period of time). Advantages may include asset accumulation potential, tax deferral, death benefit protection and guaranteed income for life.

Whether variable or fixed, a deferred annuity is a contract between the individual contract owner (your employee) and the insurance company. Because deferred annuities are designed to help employees save for retirement, they should be considered a long-term investment.

## For additional information

Massachusetts Mutual Life Insurance Company (MassMutual) offers individual retirement annuities that can help you meet your SEP-IRA plan objectives while helping your employees enhance their future financial security in retirement. Contact your financial professional for additional information and guidance in choosing the solution that's right for your company.

Guarantees and payment of lifetime income are based on the claims-paying ability of the issuing company.

This brochure provides a summary of certain tax advantages of SEP-IRAs. It is not intended to be used as a basis for tax or legal advice. Employers are encouraged to seek specific advice from their own tax or legal counsel prior to setting up a SEP plan and SEP-IRAs.

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