Advisor Connect | New Plan Tax Credits

MAKING IT ACTIONABLE

Discussion about new retirement plans usually focuses on the savings advantages they grant to business owners, or the big-picture advantages of helping employees achieve ongoing financial wellness. Tax credits granted to plan sponsors are another important, but sometimes opaque, piece of this puzzle. When your client starts a new qualified retirement plan, SEP, or SIMPLE IRA, they may be eligible to claim tax credits for the first three years of the plan.

How Is Eligibility Determined?

A plan sponsor is eligible to claim this tax credit if three conditions are met:

1. They had ***no more than*** 100 employees who received $5,000+ in compensation in the previous year
2. They had ***at least one*** plan participant who was a "non-highly compensated employee" in the previous year
3. They were not ***already*** sponsoring a different qualified retirement plan that was benefiting the same group of plan participants in the last three years.

   In other words, a plan sponsor can't change to a new plan every three years and get a new tax credit every time.

What Is the Value of the Tax Credit?

The tax credit a new plan sponsor can claim is equal to half of their **eligible startup costs**, but it caps at $500 each tax year.

An **eligible startup cost** refers to any ***typical*** expense that's necessary to:

- Set up a new qualified retirement plan
- Perform ongoing administration for that plan
- Educate employees about their new options

A quick note: *a plan sponsor can claim this tax credit for those eligible startup costs OR deduct them as business expenses on their tax return, but NOT both. Work with your client to determine which strategy is most effective for their situation.*

When Can a Plan Sponsor Claim These Tax Credits?

A plan sponsor may begin claiming the credit in the tax year before the plan becomes effective.

EXAMPLE:

Your client's business decides to enact a qualified retirement plan that begins to take effect in 2021. Your client may claim the credit when completing their tax return for 2020.

Your client is also allowed to carry that credit forward to future tax years if they can't use it effectively in 2020 or 2021.

ACTION TO TAKE NOW

Become familiar with these tax credit opportunities; they can be an important tool in helping your clients offset the costs of setting up a new retirement plan for their business. Review the information laid out above until you're familiar with these basic details and then, if you have any questions about new plan tax credits, don't hesitate to reach out to chat.

As with many of our previous topics, it's essential to understand your client's unique needs and circumstances so that you can guide them toward the financial decisions most prudent to their specific situation.