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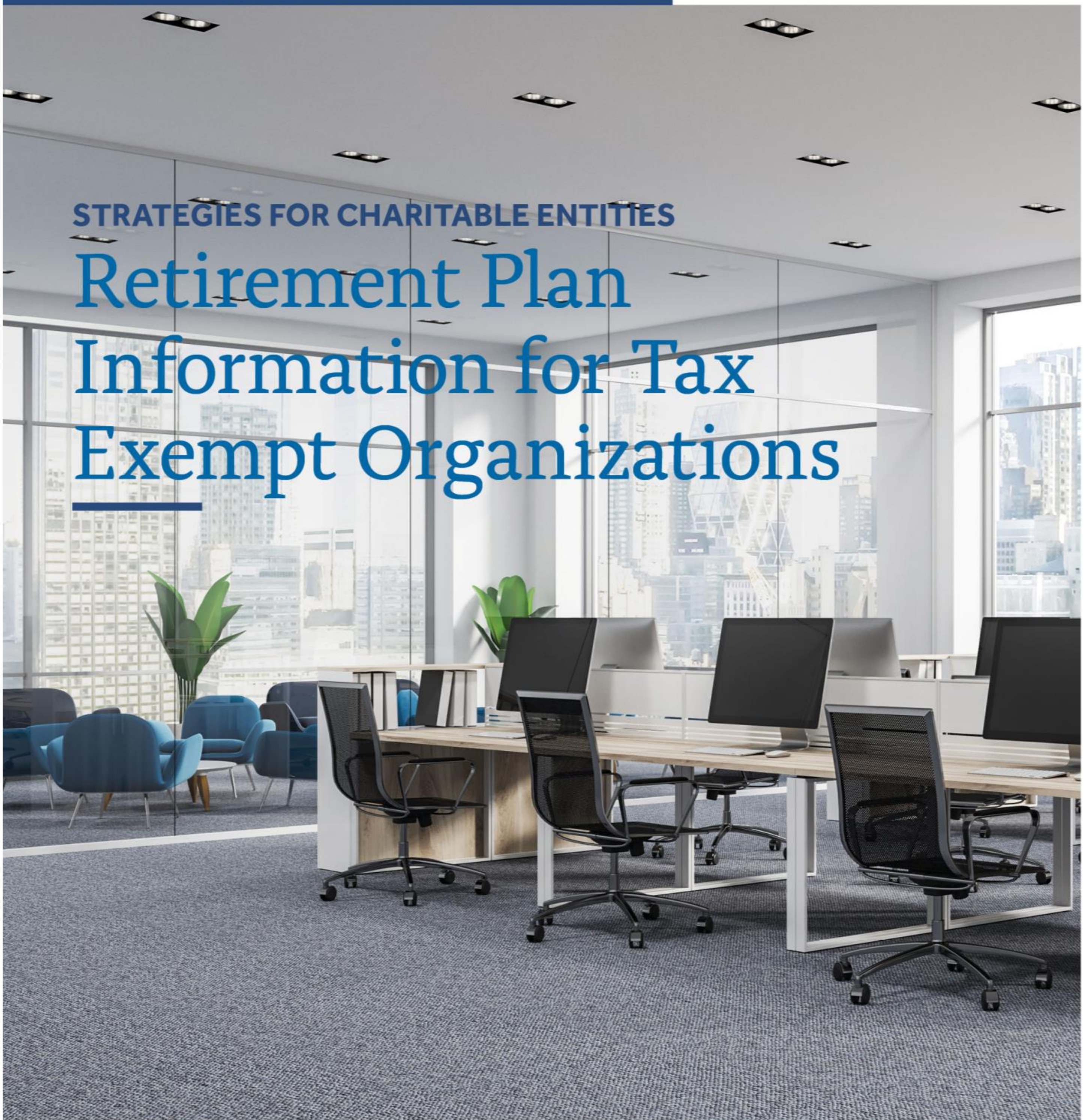
STRATEGIES FOR CHARITABLE ENTITIES

Retirement Plan Information for Tax Exempt Organizations



Retirement Plan Information for Tax-Exempt Organizations

By starting a retirement plan for its employees, a tax-exempt charitable organization will help those employees save for their futures. Also, retirement plans may help a charitable organization attract and retain better qualified employees. Non-profit organizations can provide traditional benefits like retirement plans. Eventually, all employees will retire, and a retirement plan is one of the most powerful tools for building savings for retirement. Furthermore, such retirement plans may provide significant tax advantages that employees are not able to find outside of the workplace.

Retirement plans for non-profit organizations

Non-profit organizations often use a combination of 403(b) plans, 401(k) plans, SIMPLE IRA plans, and other retirement plans for employees. Traditionally, 403(b) plans were the default option for non-profit organizations, but 401(k) plans can be a viable option for some organizations, and SIMPLE IRA plans may make sense where employers prefer a basic retirement plan but with minimal costs.

Various qualified plans available to non-profit organizations

Traditionally, non-profit organizations primarily utilized 403(b) plans for employees' retirement savings, and many non-profit organizations still use those plans. The rules governing retirement savings have morphed over several years, and now private non-profit organizations may elect 401(k) plans for the following reasons:

- Regulations under the Employee Retirement Income Security Act of 1974 (commonly referred to as ERISA) now require many 403(b) plans to function similar to 401(k) plans and maintain a written plan document and provide a summary plan document to employees.
- There are more 401(k) plan providers than 403(b) plans providers from which to choose so 401(k) plans have more investment options available and greater competition to keep pricing competitive.
- Some tax-exempt organizations, such as 501(c)(6) business leagues and 501(c)(7) fraternal organizations, are not permitted to use 403(b) plans.

SIMPLE IRA plans

Non-profit organizations often need to minimize costs. Funding may be minimal, and the organization's directors may be unwilling to be spend donor money on much other than its charitable purpose. Paying for retirement plan administration and contributing to employee accounts may be uncomfortable for the organization's directors, who may believe the non-profit organization exists primarily to serve its charitable purpose.

A SIMPLE IRA plan may be a less expensive option. For a basic retirement account that allows employees to save meaningful amounts each year [albeit less than the amounts that can be contributed to 401(k) and 403(b) plans], a SIMPLE IRA will be sufficient, providing the following advantages:

- Unlike 401(k) plans and 403(b) plans, SIMPLE plans do not require employers to pay annual administration or other costs typical of larger retirement plans.
- SIMPLE plans are somewhat rigid, and that makes them inexpensive and typically easier to administer.
- SIMPLE plans allow for pre-tax contributions only; there is no post-tax savings mechanism such as is available through a Roth 401(k) plan and a Roth 403(b) plan. If non-profit organization employees wish to make post-tax savings contributions, they will need to do so via a Roth IRA (if applicable income tax laws permit).

- SIMPLE plans provide for immediate vesting of contributions. Once funds are contributed to the SIMPLE account (even if it's employer money), those funds are available for immediate withdrawal by the employee, even where it was the non-profit organization/employer that contributed the funds.

There are some disadvantages to SIMPLE plans:

- While taking distributions from a retirement account earlier than permissible often results in income taxes and an early withdrawal penalty, with SIMPLE IRA plans the early withdrawal penalty is 25% of the amount distributed as opposed to 10% for traditional IRAs.
- SIMPLE plans may limit the employer's ability to start other types of retirement plans during the same year.

The costs to a non-profit organization/employer are primarily the required employer contribution and the administrative expenses of operating the plan. The non-profit organization/employer must choose between:

- 3% of pay: Employees receive 3% of their earnings each year; or
- 2% match: Employees receive a 100% match on their contributions, up to 2% of their pay.

  (In very limited circumstances, a non-profit organization can reduce that contribution.)

For most nonprofit organizations, a SIMPLE IRA plan is one of the least expensive and simplest retirement plans to manage and is especially attractive for infant non-profit organizations. If a non-profit organization has outgrown its SIMPLE plan, then it can always transition to a 401(k) plan or a 403(b) plan at some later date.

Payroll deduction IRA

Payroll deduction IRAs are even less expensive and less restrictive than SIMPLEs. The non-profit organization need not make any contribution to employer accounts, so the cost is simply the administrative time it takes to help employees save money.

With a payroll deduction IRA, employees establish individual retirement accounts and the employer makes contributions directly to those employees' accounts. Furthermore, employees can elect to contribute on a pre-tax or post-tax basis. Employees need to be eligible, however, to use certain tax features such as Roth IRAs or taking a deduction for contributions to traditional IRAs. Unlike a 401(k) plan or a 403(b) plan, which allow for contributions regardless of the employee's income, IRAs can be limited; therefore, employees should verify their ability to make contributions with their own tax advisors.