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The Many Benefits of a SEP

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One of the most common questions on business owners' minds is what they can do to reduce their taxes. While there are many possible responses to this question, there is one that stands out. Just as employees may contribute some of their wages to a 401(k) to defer their taxes, small business owners have similar options. One such option is the Simplified Employee Pension, or more commonly referred to as a SEP.

Contributing to a SEP is a great way for small business owners to receive a tax deduction and put money away for the future. The SEP is also incredibly easy to set up, requiring the completion of Form 5305-SEP and setting up an account with any qualified financial institution (broker, bank, insurance company). Not to mention, this can be done at any time prior to the extended due date of the self-employed person's or business' tax return. This means that you could potentially open and contribute to a SEP in October of 2015, and still deduct the contribution in 2014. Also, the Form 5305-SEP is very easy to complete and does not need to be filed with the IRS. However, if your small business has any employees, then each employee should receive a copy, as well. Once the SEP has been opened there is very little work required to keep it going, since it does not have any separate reporting requirement with the IRS.

Businesses eligible for SEPs include sole proprietorships, partnerships, and corporate employers that do not already have another retirement plan in place. If the business is part of an affiliated group or commonly controlled entity then all qualified employees of all affiliated members or controlled groups **must** be covered by the SEP. Also, SEP contributions are not required to be made each year. This can be a major benefit to small business owners who want the flexibility to decide whether or not they want to make a contribution.

Now let's talk about how much small business owners can contribute to the plan each year. For 2014, the maximum contribution allowed to a SEP is the lesser of 20% of self-employed earnings or 25% of an employee's wages up to a maximum of $52,000. This means that you could potentially get a $52,000 deduction on your 2014 tax return. In addition, for any small business owners having employees (who qualify for the plan), they must receive uniform contributions. For example, if you contribute 20% of your compensation to a SEP then you must contribute 20% of **each** employee's compensation to **their** SEP. This requirement is one of the few negatives of SEPs. In addition, the contribution to an employee's SEP is considered immediately vested. Finally, both the employer and employees can still potentially contribute to their individual IRAs up to the $5,500 ($6,500 if 50 and older) limit for 2014.

For more information on SEPs and other tax planning strategies contact one of the tax professionals at Zinner & Co. LLP.

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