SIMPLE IRA PLAN CHECKLIST

This Checklist is *not* a complete description of all plan requirements, and should *not* be used as a substitute for a complete plan review.

For Business Owner's Use

(DO NOT SEND THIS WORKSHEET TO THE IRS)

Every year it is important that you review the requirements for operating your Savings Incentive Match Plan for Employees of Small Employers (SIMPLE) IRA plan. This Checklist is a "quick tool" to help you keep your plan in compliance with many of the important tax rules. Underlined text below will link you to Internet information.

1. Does your business have 100 or fewer employees? Yes ☐ No ☐

Businesses with more than 100 employees (including full-time, part-time, and seasonal employees) with individual earnings of at least $5,000 yearly cannot establish a SIMPLE IRA plan.

2. Is this SIMPLE IRA plan your business's only retirement plan? Yes ☐ No ☐

A business with a SIMPLE IRA plan generally cannot also sponsor any other retirement plan, such as a 401(k) plan.

3. Do you know how to, and did you, identify your eligible employees? Yes ☐ No ☐

An eligible employee is one with compensation of at least $5,000 per year in any 2 prior years, who is expected to earn at least $5,000 this year.

4. Is the business that the SIMPLE IRA plan covers the only business that you and/or your family members own? Yes ☐ No ☐

Employees of other businesses you and/or your family members own may have to be considered when determining who is an eligible employee under this SIMPLE IRA plan.

5. Did you notify your eligible employees of their right to elect salary reduction or modify a prior salary reduction agreement? Yes ☐ No ☐

Each year, you must give your employees notice before November 2 of their right to participate in the retirement plan for the next year and to change a prior salary reduction agreement.

6. Do you give your employees an annual notice, before November 2 of each year, of plan provisions and employer contribution levels for the upcoming year? Yes ☐ No ☐

You must give your employees notice of the plan provisions and employer contribution levels, including any plan changes, at least 60 days prior to the start of the next calendar year.

7. Have you allowed employees to terminate their salary reduction election? Yes ☐ No ☐

You must allow your employees, *at any time,* to stop making deferrals.

8. Have you deposited employee deferrals timely? Yes ☐ No ☐

You must deposit an employee's deferral in the IRA as soon as possible, but no later than 30 days following the month in which the employee would have otherwise received the money.

9. Have you deposited employer contributions timely? Yes ☐ No ☐

As an employer, you have until the due date, including extensions, of your tax return to deposit matching contributions or nonelective contributions.

10. Are employee deferrals to SIMPLE IRAs limited as required by law? Yes ☐ No ☐

The deferral limit to a SIMPLE IRA is $8,000 for 2003, $9,000 for 2004, and $10,000 for 2005. Catch-up contributions of participants, aged 50 or over, are limited to an additional $1,000 for 2003, $1,500 for 2004, and $2,000 for 2005.

If you answered "No" to any of the above questions, you may have a mistake in the operation of your SIMPLE IRA plan. Many mistakes can be corrected easily, without penalty and without notifying the IRS.

- **contact your benefits professional**
- **visit the IRS at www.irs.gov/ep**
- **call the IRS at (877) 829-5500**

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SIMPLE IRA Plan

A Savings Incentive Match Plan for Employees of Small Employers (SIMPLE) IRA plan is a written arrangement that provides you and your employees with a simplified way to make contributions to provide retirement income. Under a SIMPLE IRA plan, employees can choose to make salary reduction contributions to the plan rather than receiving these amounts as part of their regular pay. In addition, you contribute matching or nonelective contributions. All contributions to a SIMPLE IRA plan are deposited in SIMPLE IRAs that are set up for each eligible employee.

Credit for startup costs: You may be able to claim a tax credit for part of the ordinary and necessary costs of starting a SIMPLE IRA plan. (See Form 8881, *Credit for Small Employer Pension Plan Startup Costs*.)

Deadline for setting up a SIMPLE IRA plan: You can set up a SIMPLE IRA plan effective on any date between January 1 and October 1 of a year, provided you did not previously maintain a SIMPLE IRA plan. This requirement does not apply if you are a new employer that comes into existence after October 1 of the year and you set up a SIMPLE IRA plan as soon as administratively feasible after you come into existence. If you previously maintained a SIMPLE IRA plan, you can set up a SIMPLE IRA plan effective only on January 1 of a year. A SIMPLE IRA plan cannot have an effective date that is before the date you actually adopt the plan. SIMPLE IRA plans can only be maintained on a calendar-year basis.

Setting up a SIMPLE IRA plan: You can use Form 5304–SIMPLE, *Savings Incentive Match Plan for Employers of Small Employers (SIMPLE) – Not for use With a Designated Financial Institution* or Form 5305–SIMPLE, *Savings Incentive Match Plan for Employees of Small Employers (SIMPLE) – for Use With a Designated Financial Institution* to set up a SIMPLE IRA plan. Each form is a SIMPLE IRA plan document. Which form you use depends on whether you select a financial institution or your employees select the institution that will receive the contributions.

Use Form 5304–SIMPLE if you allow each plan participant to select the financial institution for receiving his or her SIMPLE IRA plan contributions. Use Form 5305–SIMPLE if you require that all contributions under the SIMPLE IRA plan be deposited initially at a designated financial institution.

The SIMPLE IRA plan is adopted when you have completed all appropriate boxes and blanks on the form and you (and the designated financial institution, if any) have signed it. Keep the original form. Do not file it with the IRS.

Additionally, a SIMPLE IRA plan may be established through the adoption of a prototype SIMPLE IRA plan document (usually through a mutual fund, insurance company, bank or other qualified financial institution).

Other uses of the forms: If you set up a SIMPLE IRA plan using Form 5304–SIMPLE or Form 5305–SIMPLE, you can also use the form to:

- Meet the employer notification requirements for the SIMPLE IRA plan. Page 3 of Form 5304–SIMPLE and page 3 of Form 5305–SIMPLE contain a *Model Notification to Eligible Employees* that provides the necessary information to the employee.
- Provide employees with a salary reduction agreement. Page 3 also contains a *Model Salary Reduction Agreement*.

Setting up SIMPLE IRAs: SIMPLE IRAs are the individual retirement accounts or annuities into which the contributions are deposited. A SIMPLE IRA must be set up for each eligible employee. Forms 5305–S, *SIMPLE Individual Retirement Trust Account,* and 5305–SA, *SIMPLE Individual Retirement Custodial Account,* are model trust and custodial account documents the participant and the trustee (or custodian) can use for this purpose.

A SIMPLE IRA cannot be designated as a Roth IRA. Contributions to a SIMPLE IRA will not affect the amount an individual can contribute to a Roth IRA or a traditional IRA. However, contributions to a SIMPLE IRA may preclude an individual from receiving a tax deduction for contributions to a traditional IRA.

Deadline for setting up a SIMPLE IRA: A SIMPLE IRA must be set up for an employee before the first date by which a contribution is required to be deposited into the employee's IRA.

The Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) changed many of the Internal Revenue Code's requirements and limits for qualified plans and IRAs. In order to maintain tax-advantaged status and to benefit under these new provisions, SIMPLE IRA prototype plans must be amended for current law. In order for employers with model SIMPLE IRA plans to maintain tax-advantaged status and to avail themselves of new law changes they must adopt the current version of the models (Form 5304-SIMPLE or 5305-SIMPLE). These model forms have a revision date of March 2002. The current model forms for SIMPLE IRAs (Form 5305-S or Form 5305-SA) also have a revision date of March 2002.

1. 100 or Fewer Employees

You can set up a SIMPLE IRA plan only if you had 100 or fewer employees who received $5,000 or more in compensation from you for the preceding year. Under this rule, you must take into account ***all*** employees employed at any time during the calendar year regardless of whether they are eligible to participate. Employees include self-employed individuals who received earned income, business owners who work in the business and leased employees. Once you set up a SIMPLE IRA plan, you must continue to meet the 100-employee limit each year you maintain the plan.

Grace period for employers who cease to meet the 100-employee limit*:* If you maintain the SIMPLE IRA plan for at least 1 year and you cease to meet the 100-employee limit in a later year, you will be treated as meeting it for the 2 calendar years immediately following the calendar year for which you last met it.

A different rule applies if you do not meet the 100-employee limit because of an acquisition, disposition, or similar transaction. Under this rule, the SIMPLE IRA plan will be treated as meeting the 100-employee limit for the year of the transaction and the 2 following years if both the following conditions are satisfied:

- Coverage under the plan has not significantly changed during the grace period.
- The SIMPLE IRA plan would have continued to qualify after the transaction if you had remained a separate employer.

The grace period for acquisitions, dispositions, and similar transactions also applies if, because of these types of transactions, you do not meet the rules explained under *Only Employee Retirement Plan* or *Eligible Employees*, below.

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2. Only Employee Retirement Plan

The SIMPLE IRA plan generally must be the only retirement plan to which you make contributions, or to which benefits accrue, for service in any year beginning with the year the SIMPLE IRA plan becomes effective.

Exception: If you maintain a qualified plan for collective bargaining employees, you are permitted to maintain a SIMPLE IRA plan for other employees.

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3. Eligible Employees

Any employee who received at least $5,000 in compensation during any 2 years preceding the current calendar year and who is reasonably expected to receive at least $5,000 during the current calendar year is eligible to participate. The term "employee" includes a self-employed individual who received earned income. Note: An individual cannot be required to attain a certain age or earn a certain number of hours of service to become eligible.

Your SIMPLE IRA plan can provide less restrictive eligibility requirements (but not more restrictive ones) by reducing or eliminating the prior year compensation requirements, the current year compensation requirements, or both.

For example, you can allow participation for employees who received at least $3,000 in compensation during any preceding calendar year. However, you cannot impose any other conditions for participating in a SIMPLE IRA plan.

Excludable employees: The following employees do not need to be covered under a SIMPLE IRA plan:

- Employees covered by a union agreement whose retirement benefits were bargained for in good faith by you and their union.
- Nonresident alien employees who did not earn U.S. source income from you.

4. Only Business

Including Employees of Related Employers: "Employees" for purposes of determining who is an eligible employee under your SIMPLE IRA plan includes all employees of all related employers. Related employers include controlled groups of corporations that include your business, trades or businesses under common control with your business, and affiliated service groups that include your business. This means, for example, that if you and/or your family members own a controlling interest in another business, employees of that other business are "employees" for purposes of determining who is eligible to participate in a SIMPLE IRA plan.

Example. Individual P owns Business A, a computer rental agency that has 40 employees who received more than $5,000 in compensation. Individual P also owns Business B, which repairs computers and has 30 employees who received more than $5,000 in compensation. For purposes of the SIMPLE IRA plan rules, all 70 employees are treated as employed by a single employer.

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5. & 6. Notification Requirements

You must notify each employee of the following information before the beginning of the election period:

1) The employee's opportunity to make or change a salary reduction choice under the SIMPLE IRA plan.
2) Your decision to make either matching contributions or nonelective contributions.
3) A summary description including the basic features of the plan, information about the employer, trustee, eligibility requirements, etc. The financial institution should provide you with this information.
4) If you use a designated financial institution, written notice that the employees' SIMPLE IRA balance can be transferred without cost or penalty.

Election period: The election period is generally the 60-day period immediately preceding January 1 of a calendar year (November 2 to December 31 of the preceding calendar year). However, the dates of this period are modified if you set up a SIMPLE IRA plan during a year (for example, on July 1) or if an employee first becomes eligible to participate in the SIMPLE IRA plan after January 1 of the year. A SIMPLE IRA plan can provide longer periods for permitting employees to enter into salary reduction agreements or to modify prior agreements. For example, a SIMPLE IRA plan can provide a 90-day election period instead of the 60-day period. Similarly, in addition to the 60-day period, a SIMPLE IRA plan can provide quarterly election periods during the 30 days before each calendar quarter, other than the first quarter of each year.

General Reporting Requirements:

In addition to the employee notification requirements above, the bank, insurance company or other trustee or issuer of the SIMPLE IRAs must comply with the following general reporting requirements:

1) Form 5498, *IRA Contribution Information,* must be submitted to the IRS by the trustee or issuer of a SIMPLE IRA to report contributions to the SIMPLE IRA. A separate Form 5498 must be submitted for

each participant. This form or other statement of fair market value and account activity must also be given to participants.

2) Form 1099-R, *Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.*, is used to report distributions from a SIMPLE IRA. Distributions from a SIMPLE IRA are subject to the same withholding rules that apply to distributions from traditional IRAs. See Publication 590, *Individual Retirement Arrangements (IRAs)*, for details on IRA distribution rules.

3) The Form 5500, *Annual Return/Report of Employee Benefit Plan,* that is required to be filed by most qualified retirement plans is not required for SIMPLE IRA plans.

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7. Stopping Deferrals

You must permit each employee to stop – at any time – making salary reduction contributions.

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8. Depositing Employee Deferrals

Employee deferrals are amounts that employees elect to contribute to the SIMPLE IRA plan by salary reduction. In accordance with Department of Labor ("DOL") rules, an employer must forward employee deferrals to the financial institution that holds the plan's SIMPLE IRAs as soon as they can reasonably be segregated from the employer's general assets, but in no event later than 30 days following the month in which they were withheld from the employees' paychecks. For more information on the DOL rules, go to their web site at www.dol.gov/ebsa.

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9. Depositing Employer Contributions

An employer's matching or nonelective contributions must be made to the financial institution that holds the plan's SIMPLE IRAs no later than the due date for filing the employer's tax return (including extensions) for the employer's tax year with or within which the calendar year for which the contribution was made ends. See examples under *When to Deduct Contributions,* later.

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10. Contribution Limits

Contributions are made up of salary reduction contributions and employer contributions. You, as the employer, must make either matching contributions or nonelective contributions, defined later. No other contributions can be made to the SIMPLE IRA plan. These contributions, which you can deduct, must be made timely. See *Depositing Employee Deferrals* and *Depositing Employer Contributions* above. Once you make the SIMPLE IRA contribution, it is owned by the employee and cannot be made subject to a vesting schedule or taken back by you.

Employee Deferrals: The amount the employee chooses to have you contribute to a SIMPLE IRA on his or her behalf cannot be more than $8,000 for 2003 ($9,000 for 2004, $10,000 for 2005, and subject to cost-of-living adjustments for later years). These contributions must be expressed as a percentage of the employee's compensation unless you permit the employee to express them as a specific dollar amount. You cannot place restrictions on the contribution amount (such as limiting the contribution percentage), except to comply with this dollar limit.

If an employee is a participant in another employer's retirement plan during the year and has elective salary reductions or deferred compensation under that plan, the salary reduction contributions under the SIMPLE IRA plan and the elective deferrals under the other employer's retirement plan are subject to an overall annual limit. This limit is $12,000 for 2003, $13,000 for 2004, $14,000 for 2005, $15,000 for 2006 and subject to cost-of-living adjustments for later years.

Catch-up contributions: A SIMPLE IRA plan can permit participants who are age 50 or over at the end of the calendar year to also make catch-up contributions. The catch-up contribution limit for 2003 is $1,000 ($1,500 for 2004, $2,000 for 2005, $2,500 for 2006 and subject to cost-of-living adjustments for later years). Salary reduction contributions are not treated as catch-up contributions for 2003 until they exceed $8,000. However, the catch-up contribution a participant can make for a year cannot exceed the lesser of the following amounts:

- The catch-up contribution limit.
- The excess of the participant's compensation over the salary reduction contributions that are not catch-up contributions.

Employer matching contributions: You are generally required to match each employee's salary reduction contributions on a dollar-for-dollar basis up to 3% of the employee's annual compensation. This requirement does not apply if you make nonelective contributions as discussed later.

Lower percentage: If you choose a matching contribution less than 3%, the percentage must be at least 1%. You must notify the employees of the lower match within a reasonable period of time before the 60-day election period (discussed earlier) for the calendar year. You cannot choose a percentage less than 3% for more than 2 years during the 5-year period that ends with (and includes) the year for which the choice is effective.

Nonelective contributions: Instead of matching contributions, you can choose to make nonelective contributions of 2% of annual compensation on behalf of each eligible employee who has at least $5,000 (or some lower amount you select) of compensation from you for the year. If you make this choice, you must make nonelective contributions whether or not the employee chooses to make salary reduction contributions.

For 2003, only $200,000 of the employee's compensation can be taken into account to figure the nonelective contribution. In 2004, the compensation limit is $205,000, and it is subject to cost-of-living adjustments for later years.

Whether you choose this 2% contribution formula or matching contributions, you must notify the employees of your choice within a reasonable period of time before the 60-day election period (discussed earlier) for the calendar year.

When to Deduct Contributions

Contributions to a SIMPLE IRA plan are deductible in the tax year containing the end of the calendar year for which contributions are made. Contributions will be treated as made in a particular tax year if they are made for that year and are made by the due date (including extensions) of your federal income tax return for that year.

Example 1. Your tax year is the fiscal year ending June 30. Contributions under a SIMPLE IRA plan for the calendar year 2003 (including contributions made in 2003 before July 1, 2003) are deductible in the tax year ending June 30, 2004.

Example 2. You are a sole proprietor whose tax year is the calendar year. Contributions under a SIMPLE IRA plan for the calendar year 2003 (including contributions made in 2004 by April 15, 2004) are deductible in the 2003 tax year.

Where to Deduct Contributions

Deduct the contributions you make for your common-law employees on your tax return. For example, sole proprietors deduct them on Schedule C (Form 1040), *Profit or Loss From Business,* or Schedule F (Form 1040), *Profit or Loss From Farming,* partnerships deduct them on Form 1065, *U.S. Return of Partnership Income,* and corporations deduct them on Form 1120, *U.S. Corporation Income Tax Return,* Form 1120–A, *U.S. Corporation Short-Form Income Tax Return,* or Form 1120S, *U.S. Income Tax Return for an S Corporation.*

Sole proprietors and partners deduct contributions for themselves on line 30 of the 2003 Form 1040, *U.S. Individual Income Tax Return.* (If you are a partner, contributions for yourself are shown on the Schedule K-1 (Form 1065), *Partner's Share of Income, Credits, Deductions, etc.,* you get from the partnership.)

Tax Treatment of Contributions

You can deduct your contributions and your employees can exclude these contributions from their gross income. SIMPLE IRA contributions are not subject to federal income tax withholding. However, salary reduction contributions are subject to social security, Medicare, and federal unemployment (FUTA) taxes. Matching and nonelective contributions are not subject to these taxes.

Reporting on Form W–2: Do not include SIMPLE IRA plan contributions in the "Wages, tips, other compensation" box of Form W–2. However, employee deferrals must be included in the boxes for "Social security wages" and "Medicare wages and tips". Also include the proper code in box 12. For more information, see the instructions for Form W–2.

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