

What's New for Breakfast in Retirement Plans?

“Solo K!”



“SOUNDS TASTY! HOW BIG IS THE BOWL?”

A **Solo K** retirement plan is a flexible and easy way to maximize retirement savings for small, single owner businesses. The name comes from the often used popular name of an individual retirement plan commonly offered by large employers. The plan takes advantage of existing 401 (K) plans and adds a touch of spice to your breakfast meal.... profit sharing! That's right, you can not only maximize your 401 (K) contribution (\$13,000 for 2004 if under age 50, \$16,000 if over age 50), and you can now



pay yourself a tax deductible profit sharing portion based on net earnings. **Solo K** plans allow you to contribute up to 20% of your modified net profit (net profit minus $\frac{1}{2}$ SE tax). In certain circumstances you can contribute almost dollar for dollar of your earnings.

Example: With a net income of \$20,000 an over age 50 self employed person can contribute \$19,717 for 2004, almost dollar for dollar of earnings! Here's the math:

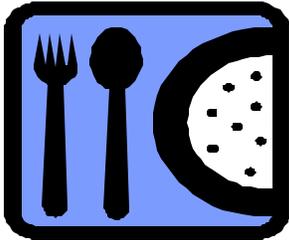
	Maximum 401 (k) deferral:			\$16,000
	Modified Net Profit:			
	Net Income	20,000		
	½ SE Tax	<u>(1,413)</u>		
	Profit Sharing	18,587	x 20%	<u>3,717</u>
	Total Contribution Amount			<u>\$19,717</u>

The entire contribution amount of \$19,717 can be made at the time of filing your tax return (April 15th of the following year with extensions up to October 15th). This is not the case for S or C Corporations. S & C Corporations must contribute the 401 (k) portion as they pay themselves (within 15 days), in other words, during the calendar year in which monies are earned.

Additional benefits include:

- Access to tax-free loans.
Loans are not permitted with Traditional or Roth IRAs, and SEP IRAs
- Minimal administration/cost effective.
The Solo K plan is inexpensive to maintain. Fees for administration can range from \$30 annually to \$200 annually.
- Flexible Contribution Amounts.
Each year funding is up to you. You can increase or decrease funding accordingly.
- Consolidate your existing plans into this one for an all in one meal!
This includes IRAs, SEP Plans, etc.

**Setting the table (or in technical parlance-
who is eligible for this unique
new retirement plan)**



Like any choices for breakfast, **Solo K** is not for everyone. In fact, it is a retirement plan ideal for the following type situations:

- 1) The full time employee (not covered by employer 401 (k) plan) who moonlights on weeknights and weekends earning upwards of \$50,000 of self employment income.
- 2) The distaff spouse who after the kids are out of the house (and she stops making their breakfast everyday) works part time as a self employed person and makes upward of \$50,000. A classic example is a real estate mom or self employed artist.
- 3) A family business that employs owners and their immediate family such as spouses and children.
- 4) Sole proprietorships, partnerships and corporations (including subchapter S and C corporations) would qualify as long as it is for owner-only businesses or those with part-time employees only (employees who work less than 1,000 hours per year).

ENJOYING THE REPASTE (OR HOW DO YOU SET THESE UP?)

Actually this may be the hardest part of all. The pension actuaries we deal with don't want to bother with what is essentially single member plans. The



banks have no clue as to how **Solo K** plans work. Some brokerage firms are aware but usually it is tough work to find someone to help (sort of like dry Solo K-not appealing without milk). There are a few rules to follow, they are:

- The plan must be opened during the calendar year the income is earned. Thus, unlike a traditional IRA you cannot wait until April 15 after the year end to decide to open a **Solo K** plan.
- The 401 K piece of the contribution (\$13,000, \$16,000 if you are over age 50) must be made as you pay yourself. For example, if you make \$1,000 per month in earnings, that amount should be placed in the **Solo K** account. **HOWEVER**, if you are a sole proprietor versus a S Corporation shareholder, you may fund **BOTH** your 401 (k) portion and profit sharing portion at the time of filing your personal return including extensions (up to October 15 of the following year)
- The profit sharing piece (20% of net earnings after SE tax) can be contributed at the time of the normal filing of your personal income tax return including extensions.

There you have it, a nutritious blend of savings and tax deductions that are sure to satisfy the cash starved retirement cravings of the workforce who are most in need of a balanced diet.

Savor the flavor of providing retirement dollars and beating the tax man at the same time. Enjoy! See below for some examples of tax savings that are sure to please.

Michael J. Knight, CPA

Email: mjk@mjkcpas.com

Website: www.mjkcpas.com

5/6/2004

Copyright pending, Michael J. Knight & Company CPAs

(Special thanks to Ryan C. Sheppard who assisted in the preparation of this article)

2004

AGE 50 AND OVER

Self Employed Net Earnings	\$ 20,000	\$ 40,000	\$ 75,000	\$ 125,000	\$ 200,000
Minus 1/2 SE Tax	1,413	2,826	5,299	14,247	16,256
Modified Net Profit	18,587	37,174	69,701	110,753	183,744
Profit Sharing %	<u>20%</u>	<u>20%</u>	<u>20%</u>	<u>20%</u>	<u>20%</u>
Maximum Profit Sharing Contribution	<u>3,717</u>	<u>7,435</u>	<u>13,940</u>	<u>22,151</u>	<u>36,749</u>
Maximum Employee Deferral	16,000	16,000	16,000	16,000	16,000
Maximum Retirement Contribution	<u>\$ 19,717</u>	<u>\$ 23,435</u>	<u>\$ 29,940</u>	<u>\$ 38,151</u>	<u>\$ 44,000</u>
Percentage of Earnings Saved	99%	59%	40%	31%	22%

AGE 49 AND UNDER

Self Employed Net Earnings	\$ 20,000	\$ 40,000	\$ 75,000	\$ 125,000	\$ 200,000
Minus 1/2 SE Tax	1,413	2,826	5,299	14,247	16,256
Modified Net Profit	18,587	37,174	69,701	110,753	183,744
Profit Sharing %	<u>20%</u>	<u>20%</u>	<u>20%</u>	<u>20%</u>	<u>20%</u>
Maximum Profit Sharing Contribution	<u>3,717</u>	<u>7,435</u>	<u>13,940</u>	<u>22,151</u>	<u>36,749</u>
Maximum Employee Deferral	13,000	13,000	13,000	13,000	13,000
Maximum Retirement Contribution	<u>\$ 16,717</u>	<u>\$ 20,435</u>	<u>\$ 26,940</u>	<u>\$ 35,151</u>	<u>\$ 41,000</u>
Percentage of Earnings Saved	84%	51%	36%	28%	21%