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For The Self-Employed: 4 Retirement Plan Choices

When you're self-employed, it's often difficult to set aside money for retirement because every dollar is coming out of your own pocket. Yet if you don't invest in your future, no one else will, so it's important to make retirement saving a top priority. You can use one of several saving and investment vehicles whose features can help you gradually build a substantial nest egg. Consider these four retirement plans that are specifically geared to the self-employed.

1. Simplified Employee Pensions (SEPs): The main attraction of SEPs is that they are, indeed, simplified. For one thing, SEPs are generally exempt from stringent tax reporting requirements that apply to most other plans. As a "defined contribution" plan, deductible contributions for the 2011 tax year are limited to 25% of your compensation or to $49,000 ($54,500 if you're age 50 or over), whichever is less. The maximum compensation taken into account for these purposes is $245,000.

Contributions to an SEP are discretionary, so you're not locked into a specific amount for any year. However, if you have other employees, you have to make contributions on their behalf if they have worked for you for at least three out of the previous five years and earn more than a minimum level of compensation ($550 for 2011).

Like other tax-advantaged retirement plans, SEPs generally don't permit distributions before you reach age 59½ (you'll be assessed a 10% penalty and owe income tax on early withdrawals) and you must begin taking annual required minimum distributions, or RMDs, after age 70½.

2. Savings Incentive Match Plans for Employees (SIMPLEs): Many tax rules for SEPs also apply to SIMPLEs, which are likewise exempt from the usual tax reporting rules. But unlike SEPs, which let you contribute even if your business has another retirement plan, a SIMPLE must be your sole retirement savings vehicle, and SIMPLEs also have lower ceilings for tax-deferred contributions. For 2011, the maximum is $11,500 ($14,000 if you're age 50 or older). But your business can elect to provide matching contributions to the plan, subject to nondiscrimination rules. You'll have to contribute on behalf of any employee who has earned at least $5,000 during the preceding two years and who is expected to earn at least that much during the current year.

The general tax rules for early withdrawals and RMDs also apply to SIMPLEs. But there's a 25% penalty on withdrawals made within the first two years of participation.

3. Keogh plans. At one time, if you were self-employed, the Keogh was the only retirement plan in town, but its popularity has waned now that there are other, generally simpler alternatives. The amount you can put into a Keogh each year depends on

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Retirement Saving Takes Time And Must Be A Priority

The bad news: If you're like most people, you haven't made adequate plans to ensure a comfortable lifestyle throughout retirement. The good news: You may still have time to do something about it.

According to a new study of almost 1,500 Americans by the National Bureau of Economic Research (NBER), many people lack essential financial literacy, and for most, prospects for a secure retirement may be even dimmer than feared. According to NBER:

- Fewer than one in 10 respondents was able to answer basic financial questions correctly.
- About 50% said they had trouble keeping up with monthly bills.
- Only about half had "rainy day" funds large enough to cover expenses for three months in case of lost income.
- Almost a third had done something resulting in an interest charge or fee for credit card charges.
- Only 42% said they have tried to figure out how much to save for retirement. Of those between the ages of 45 and 59, more than half said they hadn't calculated how much they'll need for retirement.
- Only 51% had a retirement account with an employer, and just 28% had another retirement account such as an IRA.
- During the past year, 9% of those with a 401(k), IRA, or another retirement account tapped the account prematurely.

The takeaway? Start now, during your working years, to get up to speed on financial matters and take steps to protect your future.

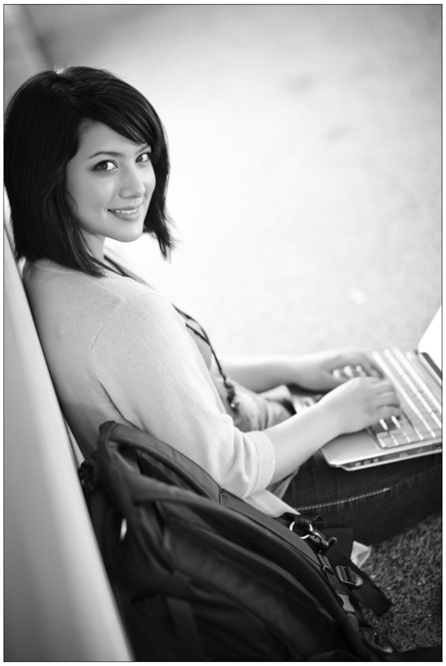
Robert J. Pyle, CFP, CFA

Start Estate Planning For Your Child Now

You may already have had a power of attorney drafted that lets you act on behalf of elderly parents. And it's possible you have estate planning documents dealing with the possibility that you or your spouse could become incapacitated. But what about your college-age children?

That's not as crazy as it may sound. Once a child becomes an adult under state law, you may have to rely on the following documents to enable you to make important medical and financial decisions for your son or daughter.

Health care proxy. Under the landmark Health Insurance Portability and Accountability Act (HIPAA), parents may not have access to their children's medical records even in the case of a serious accident or illness. HIPAA generally prohibits medical providers from revealing confidential information about their patients. However, a health care proxy can give parents the access they need. This document allows a child to designate someone—usually a parent—to make health care decisions on the child's behalf in case of physical or mental incapacitation. Such decisions may include approving treatment options and medications. If you establish a health care proxy with your child, be sure to provide copies to the college health services and to the child's primary physician.



Durable power of attorney. This document ensures ongoing management of the financial affairs of a child who's unable to take care of those matters. Typically, such a document designates a parent as "attorney-in-fact," so that if a child becomes incapacitated, the parent can step right in. For example, you might need to take action relating to investments, bank and credit card accounts, leases, student loans, tax filings, and the like. A durable power of attorney could also let you take care of things stateside while your child goes abroad for education. Be sure to give copies to your child's school, the financial aid office, and other relevant parties.

Wills and trusts. Though many college-age children may have no need for a will, it's a sensible precaution for those with substantial assets. A will and perhaps a trust can help avoid having assets revert to the parents if a child should die—a transfer that could complicate the parents' estate plans. Trusts can be efficient tools for sending wealth directly to a sibling or to another relative, and assets held in trust are also exempt from probate. Finally, a will and trusts could be structured to minimize potential estate taxes.

If a child becomes incapacitated without a health care proxy or durable power of attorney in place, the family may be forced to pursue a guardianship or conservatorship arrangement. That can be costly and time-consuming—and easily avoided by establishing these few essential estate planning documents. ●

Most Boomers Fear Outliving Money

If you are concerned about your retirement nest egg, you are certainly not alone. A new survey shows that nine out of 10 baby boomers believe there is a retirement crisis and almost six out of 10 are worried they haven't saved enough.

Among the more striking results: 61% of boomers say they are more afraid of outliving their money than they are of dying.

The second annual "Reclaiming the Future" survey by Allianz Life Insurance Co. shows the economic downturn of 2008-2009 took a big toll on boomers: 53% saw their net worth drop significantly, 43% lost value on their homes, and 41% realized they are not as in control of their financial future as they had thought they were.

More respondents this year than in past surveys said they would like to work with a financial advisor, and more expressed interest in products that guarantee income. In fact, 69% said they prefer a product that is "guaranteed not to lose value" rather than a product whose goal is "providing a high return."

In addition, 56% prefer an annuity-like product (moderate growth opportunity, guaranteed monthly income for life, but limited access) to a product that risks running out of money while providing access to potentially higher returns.

This year's survey polled 439 people between the ages of 44 and 75 in March, at about the time the Dow Jones Industrial Average hit a two-year high. Despite the ongoing economic recovery, most respondents remain pessimistic about investment returns. In fact, the average respondent now expects to retire at age 66.5, up from age 63 just a year earlier.

Indeed, there are several factors today that make all of these concerns valid. Pensions provided by employers are rapidly becoming a thing of the past, replaced by 401(k) and other

Big New Tax Breaks For Small Biz Owners

Recent federal tax legislation, designed to stimulate the economy, has created several significant tax breaks for business owners during the past few years. Consider these key provisions.

Section 179 deductions. Under Section 179 of the tax code, you can claim a current deduction for qualified business property placed in service during the year, within certain limits. Prior to 2010, the maximum Section 179 deduction had been increased from $125,000 to $250,000, with deductions phased out for purchases exceeding an $800,000 threshold. For businesses' tax years beginning in 2010 and 2011, the Small Business Jobs Creation Act of 2010 doubles the maximum annual write-off to $500,000, with a $2 million phase-out threshold. It also authorizes a maximum Section 179 deduction of $250,000 for qualified real estate.

These figures had been scheduled to revert to a maximum $25,000 deduction, with a $200,000 phase-out threshold, but the mammoth Tax Relief, Unemployment Insurance Reauthorization and Jobs Creation Act of 2010, passed in December during a lame-duck session of Congress, preserves a $125,000 maximum Section 179 deduction, with a $500,000 phase-out threshold, for tax years beginning in 2012.

Bonus depreciation. The 2010 small business law retroactively extended the 50% "bonus depreciation" tax break, which had expired after 2009, through 2010, and the 2010 Tax Relief Act authorizes 100% bonus depreciation for qualified business property placed in service after September 8, 2010 and before January 1, 2012. (Certain property with a long "useful life" qualifies if placed in service before January 1, 2013.) The 50% bonus depreciation break is generally reinstated for qualified business property placed in service during 2012.

Building improvements. Normally, write-offs for improvements to business real estate must be spaced out over 39 years. However, under a special tax law exception, a business building owner could depreciate qualified leasehold improvements, restaurant improvements, and retail building improvements during a 15-year period. This tax break, which had expired after 2009, is retroactively reinstated for 2010 and extended through 2011 by the 2010 Tax Relief Act.

Qualified small business stock. Previously, an investor in "qualified small business stock" (QSBS) could exclude up to 50% of the gain from a sale of the stock if the QSBS was held at least five years. The maximum exclusion was temporarily raised to 75% for sales of QSBS acquired after February 17, 2009 and before January 1, 2011. For sales of QSBS bought after September 27, 2010 and before January 1, 2011, the small business law hiked the maximum exclusion to 100%, and the Tax Relief Act extended that tax break through 2011.

Research credits. A business that engages in qualified research and development may qualify for a special tax credit. This credit, which had been extended several times, expired after 2009, but the 2010 Tax Relief Act retroactively reinstated it for 2010 and extended it through 2011. The research credit is generally equal to 20% of the qualified expenses that exceed a base amount.

Roth rollovers. Effective September 27, 2010, participants (including business owners) in 401(k) and 403(b) retirement plans could roll over those accounts to a designated Roth account that will provide tax-free distributions during retirement. The rollover amount, minus any after-tax contributions, is taxable as ordinary income.

BIG tax on S corporations. The built-in gains (BIG) tax may apply if a corporation sells assets after converting to S corporation status. Normally, the holding period for BIG tax purposes is 10 years, but it was temporarily reduced to seven years for asset dispositions in fiscal years beginning in 2009 and 2010. The small business law reduces the holding period to just five years for dispositions in tax years beginning in 2011.

Electronic devices. Previously, employees had to meet tough substantiation requirements regarding the business use of employer-provided cell phones and similar electronic devices. For tax years beginning after 2009, these difficult-to-enforce requirements have been dropped and as an employer, you can now treat personal use of company-owned electronic devices by your employees (and by you) as a tax-free fringe benefit. ●

retirement plans that require research and planning by account holders. The growing dependence on such plans also makes retirement savers more vulnerable to market downturns such as the 2008 crisis. Meanwhile, life expectancy is increasing, stretching the number of years that your retirement income needs to last.

Are You Prepared For Retirement?

Percentage who say they are "totally unprepared for retirement" financially:

Total:	35%
Men:	35%
Women:	43%
Late 40s:	54%
Lower wealth:	77%

Source: Allianz Life Insurance Co.

More than half the respondents said the economic crisis has made them realize that a secure retirement is by no means guaranteed, and 46% said protecting their assets has become more important to them. Nearly a third said they want to achieve a higher level of security regarding their retirement years.

Do you share these worries? Has the economic crisis caused you to rethink your prospects for a financially secure retirement? We're here to address your concerns and help you create a solid retirement plan for you and your family. Call us to begin discussing your future today. ●

Estate Tax Exemptions Survive Longer

Maybe you can't take it with you, but under the Tax Relief Act of 2010, you can give it to your spouse. In this case, "it" isn't your assets but rather the portion of your federal estate tax exemption that's not needed to shield your property from estate tax. Under the old rules, any part of your exemption not used at your death would be lost. Now, the exemption is "portable," and that creates estate-planning opportunities—at least through 2012, after which this new tax break is scheduled to expire.

Under the old estate tax law, the size of the individual exemption grew from $1 million in 2001 to $3.5 million in 2009, and the top tax rate on assets exceeding the exempt amount fell gradually from 55% to 45%. The estate tax then disappeared entirely in 2010 but was scheduled to return in 2011 with the 2001 exemption and tax rate. The Tax Relief Act, passed at the 11th hour, instead brings a whole new set of rules.

Now, there's a $5 million exemption (the highest ever) and a flat 35% estate tax rate. And, assuming an estate makes an election before a deadline, a surviving spouse can take any unused portion of the exemption from the estate of the first spouse to die. This enables a married couple to shelter up to $10 million of assets from estate tax, regardless of which spouse dies first.

Suppose John Smith owns assets currently valued at $3 million and his wife Mary owns $6 million. John dies in 2011, so his exemption shelters the entire amount. The excess $2 million of the exemption can be carried over to Mary's estate. Let's assume she dies in 2012, and that her assets have increased in value by then to $7 million (or $2 million above the $5 million individual exemption amount). With the benefit of John's unused $2 million exemption, her estate also owes no estate tax. (The $5 million exemption will be indexed for inflation in 2012, so the total exemption for couples could exceed $10 million.)

If a surviving spouse outlives more than one spouse, the exemption that can be carried over is limited to the lesser of $5 million or the unused exemption of the latest spouse to die. So, for instance, if Mary remarries and her new husband leaves her $1 million of unused exemption, Mary's exemption would be capped at $6 million.

The big sticking point, however, is that these favorable tax rules are guaranteed to remain in effect only through 2012. Flexibility could be built into an estate plan for potential estate tax law changes including a potential decrease in the exemption amount, but families with substantial assets should stay vigilant in creating and revising their estate plans. ●

4 Retirement Plan Choices

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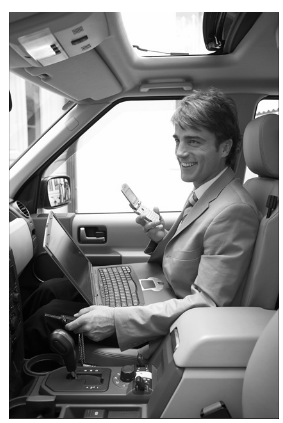
whether it's set up as a defined-contribution or a defined-benefit plan. For 2011, the maximum deductible amount for a defined-contribution Keogh is the lesser of 20% of earned income or $49,000 ($54,500 if you're at least 50 years old).

If you have a defined-benefit Keogh, your annual contributions will be computed actuarially to deliver a specified amount of retirement income. The plan may provide an annual retirement benefit equal to 100% of the average income earned during your three highest-paid years, or $195,000, whichever is less. Rules on RMDs also apply to Keogh plans.

4. Solo 401(k) plans. This staple of retirement planning for the employees of large companies used to be pretty much off limits to the self-employed, who were deterred by prohibitively high administrative costs. But now it's feasible to operate a 401(k) for just one person (or for a sole proprietor with a few employees).



The maximum tax-deductible salary deferral allowed for 2011 is $16,500 ($22,000 if you're at least 50). A major advantage of this plan for the self-employed is that it lets you combine contributions as an employee with matching contributions as an employer. This lets you reach the $49,000 maximum for retirement plans this year ($54,500 for those 50 and over).

Most other rules relating to contributions and distributions from defined-contribution plans also apply to solo 401(k)s. But if you're the only employee, you don't have to worry about tough nondiscrimination rules that normally apply to 401(k)s.

Any one of these retirement plan options might work for your business, but finding the best fit means taking a closer look at the details of each and considering its pros and cons for your enterprise. We can help you explore the options. ●

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