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NEWSLETTER
Mini-401(k) Plans Mean Tax & Investment Benefits to Small Business Owners

Because of the recently increased contribution and deduction limits, the use and benefits of 401(k) plans has greatly expanded making them attractive for the first time ever to a one-person business. These businesses can now contribute and deduct a profit-sharing contribution of 25% of the owner's compensation (or net earnings if self-employed), limited to $45,000 in 2007. Plus, even if contributions by this time have reached $45,000, an owner who is age 50 or older can make a catch-up contribution of up to an additional $5,000.

All of this means the possibility of large contributions for one-person 401(k) plans while maintaining contribution flexibility (although large contributions are allowed, they are not required to be made each year). In fact, given the right circumstances, contributions can be increased by as much as $20,000 over those allowed to be made to a plain profit-sharing plan. Or, if business is down, the owner can simply contribute less that year.

Of course, administration costs of a 401(k) plan are likely to be higher than those of a regular profit-sharing plan. But, as these plans have become more popular, they are being offered at competitive prices. Also, since these plans avoid the complicated nondiscrimination and coverage testing, additional administrative expenses should be justifiable.

One-person 401(k) Plans for Self-employed Individuals.

A mini-401(k) plan works not only for a sole owner/employee of a corporation, but also for self-employed individuals. However, a self-employed individual's earned income is determined after the deduction for half of the self-employment (SE) tax and also a reduction for the self-employed individual's deductible plan contribution. In effect, a sole proprietor's maximum contribution is limited to 20% of self-employment income.

Example: Maximizing Contributions for Single-employee (Self) Company.

Randy, age 50 (by the end of the current year), is self-employed and has no employees. The company is also the only source of Randy's earned income. Randy earns $145,000 (net of the 1/2 SE tax) in the current year and wishes to maximize contributions to a retirement account.

Randy believes that the business will probably continue to be profitable; however, he prefers not to be obligated to a mandatory contribution each year. The mini-401(k) allows Randy to determine each year how much to contribute. Randy does not expect to hire employees and will remain a one-person company.

The following table reflects the maximum amount that could be contributed to a 401(k) plan for Randy in 2007.

25% (20% for self-employed individuals) profit-sharing contribution ($145,000 × 20%)	$ 29,000
Elective 401(k) deferrals	20,000
Contributions subject to annual addition limit	49,000
Less: The amount over $45,000	<4,000>
401(k) catch-up contributions	5,000
Total contributions	$ 50,000

The previous information and example illustrates how a mini-401(k) plan can benefit a single-employee company as a result of recent law changes. Couples who are the only employees of a closely held company may also find that a mini-401(k) plan makes sense for tax and retirement planning. In addition, small businesses employing only family members may reap significant benefits from establishing a mini-401(k) plan. Please call GO! at 212.931.8000 if you have questions regarding mini-401(k) plans or any other type of retirement plan.