

# Use comparability method to save for retirement

**A**s a business owner you're continuously looking for new, innovative ways to save for retirement and compensate employees.

One approach is profit-sharing plans using the new comparability method. This method enables business owners to increase the amount they can save for retirement — as well as reward loyal employees — all within a tax-advantaged qualified plan.

If you are older than most of your employees you will likely be able to contribute more pretax dollars for your own retirement using this method. In addition, you control how much you contribute each year to the profit-sharing plan. If the company is having a lean year, skip or reduce the contribution. If you are having a great year, contribute enough to ensure that you are making the maximum contribution for a qualified defined-contribution retirement plan — \$45,000 in 2007 or \$50,000 if you are age 50 or older.

New comparability guidelines allow you to define groups or classes of employees. Each receives a different percentage of compensation as an employer contribution. For a small, closely held business, defining the owner and the employees as two groups may make the most sense.

Here's an example:

Susan, 45, owns a technology consulting company. She has five employees, ages 25, 27, 29, 35 and 38. Susan's salary is \$225,000, and her employees' salaries range from \$40,000 to \$90,000. With comparability the amount of profit sharing allocated to Susan — the only member of the owner group — could be up to 20 percent of her salary, or \$45,000. The members of the employee group could receive a much lower 5 percent of their respective salaries — \$2,000 to \$4,500.

If coupled with a 401(k) plan, the total of Susan's salary deferrals, employer match and profit sharing could not exceed \$45,000.

A vesting schedule can be applied to the profit-sharing portion. For example, profit sharing in a plan with a four-year vesting schedule would vest 25 percent each year. An employee who leaves the company after two years would receive 50 percent of his or her profit-sharing account. Only after four years of employment would the employee own 100 percent of their profit-sharing account.

The plan is not subject to nondiscrimination testing if it's part of a safe harbor 401(k) plan. When using a safe harbor 401(k)

plan, the employer provides a match or a separate profit-sharing contribution that immediately is vested with the employee. The advantage of the safe harbor 401(k) is that no discrimination testing is necessary. If the plan is not a safe harbor plan, nondiscrimination testing must be done each year, which could result in the owner having to take refunds of employee deferrals, employer match or both.

Ensuring that a qualified plan is regulatory compliant requires the services of a third-party administrator, such as Digital Retirement Solutions, or DRS, in Longmont.

DRS provides plan design, cross-testing and reporting for a number of national large and small businesses. According to Jennifer Corbaley, director of business development at DRS, most business owners find that implementing the plan is quite easy and straightforward.

"We do all the calculations and are very sensitive to the needs of small business owners, many of whom may be filling the role of human resources and benefits administrator for their employees," Corbaley said.

This process includes reviewing the business' qualified retirement plan. If there isn't a plan in place, select a financial adviser to review various retirement plan options, including the SIMPLE IRA, Simplified Employee Pension, or SEP, profit sharing and 401(k) plans.

For business owners with employees who wish to implement a qualified 401(k) plan, a financial adviser could partner with a specialist to develop a plan that meets their specific retirement planning needs. A financial adviser would be responsible for selecting the mutual fund options available for investments and would offer assistance to plan participants in making their investment decisions.

The comparability model can provide more efficient and flexible profit-sharing plans for business owners and employees. While the steps outlined provide a starting point, there are still a number of issues that you need to consider.

Business owners should consult with a financial adviser to ensure this approach is the best fit for their company's retirement planning needs.

*Rita Johnson is a financial adviser at the Millstone Evans Group of Raymond James & Associates in Boulder. She can be reached at 303-402-6907 or e-mail [rita.johnson@raymondjames.com](mailto:rita.johnson@raymondjames.com).*



#### **GUEST OPINION**

*Rita Johnson*