

Simplified Employee Pension (SEP) Plans...An Overview

Description:

A SEP consists of employer-funded individual retirement accounts (IRAs) provided for each participating employee. The employer makes contributions to these "SEP-IRAs" on a discretionary basis. The plan has fewer IRS reporting and disclosure requirements and tends to be easier to administer than other types of qualified retirement plans.

SEP Contributions:

Each eligible employee must have his or her own IRA, into which the employer can make contributions up to specified limits. While the employer is not obligated to make a SEP contribution each year, employer contributions to a SEP cannot discriminate in favor of highly compensated employees. Contributions to a SEP are deductible by the employer and excluded from the employee's current income. In effect, a SEP consists of an "employer-provided IRA" for each participating employee that has higher contribution limits than traditional IRAs that individuals establish for themselves.

Advantages:

SEPs have minimal administrative and reporting requirements.

The employer has flexibility as to whether to contribute to the SEP each year and has until its tax-filing deadline to make SEP contributions.

The employee directs how his/her IRA is invested and assumes the risk of investment performance.

Disadvantages:

Virtually all employees must be covered by a SEP.

Since SEP contributions are made to an IRA owned by the employee, full vesting is immediate.

SEPs tend to be more advantageous for younger employees with more time until retirement.