

# Tax Free Individual 401(k) Plans Strategies (The super charged retirement BRIEFS plan for small business)

Written by Dave Owens,  
CPA, CES  
owens@1031-ira.com  
239-333-1031

April 2011

For Other Informative Briefs go to [www.1031-ira.com](http://www.1031-ira.com)

## DO THE MATH: THE SEP IRA VS. THE INDY K

The SEP IRA is the typical choice for a self employed person when choosing a retirement plan. Is it the best choice?

Joe Realtor, age 49, has self-employment net income of \$100,000. With a SEP IRA the contribution would be 20% of the self employment income after the one deduction for FICA taxes. The calculation would be  $\$92,935 \times 20\% = \$18,587$ .

Now, if Joe sets up a Indy K plan his total contribution could be \$35,087. The contribution consists of two components, the employee and employer contribution. The employee contribution is the max of \$16,500. The employer contribution is  $\$92,935 \times 20\% = \$18,587$ . Combined contribution is  $\$16,500 + 18,587 = \$35,087$ . Indy K wins \$35,087 to \$18,587.

If Joe had incorporated his business, the SEP contribution would be \$25,000 and the Indy K contribution would be \$41,5000. The Indy K is still a better option.

If Joe was over 50 years old, his Indy K employee contribution could be increased by \$5,500. The SEP does not have a catch up contribution.

## PLANNING TIP

One other nice feature of the Individual (k) is that you can also contribute to a nondeductible IRA for the same tax year. This will give an additional \$5,000 to tuck away in a tax deferred account. You cannot do this with a SEP IRA. A nondeductible IRA does not penalize you, the nondeductible contributions are not double taxed when withdrawn from the account.

## ARE YOU A SAVVY BUSINESS PERSON? THE INDY K MAY BE THE RIGHT RETIREMENT PLAN FOR YOU !

If you are looking to improve your retirement plan and you are a profitable small business, an Individual K Plan might be your best bet to start saving and accumulate wealth. These plans are also called Indy Ks or Solo K plans. The Indy K has some unique benefits that Traditional and SEP IRAs cannot offer.

### The Indy K benefits include:

- Highest Contribution Limits in 2011
  - ⇒ \$16,500 for employee
  - ⇒ Employees over age 50 catch up contribution of \$5,500
  - ⇒ 25% of compensation for Employer Match (Profit Sharing Contribution)
  - ⇒ Max contributions of \$49,000 or \$54,500 if over age 50
- Roth Contribution Provision (See Below)
- Loan Provision up to a max of \$50,000 or 50% of the plan assets
- Section 401 is not subject to Unrelated Business Income Tax is leveraged assets
- Tax returns are only required if plan assets exceed \$250,000.
- Can be used by an incorporated or unincorporated business
- Current IRAs can be rolled into the Indy(k) if setting up a new plan

### Individual K Plan Restrictions:

- This Plan is not eligible for business with common law employees. The only participants can be the employer and their

spouse. General partners on a form 1065 are also eligible. There is an exception: the employer can have employees if they work less than 1000 hours per year, or are under the age of 21.

- 401(k) Plans require participants to start withdrawals at age 70 1/2 similar to a required minimum distribution

Finding the right retirement plan for a small business can difficult. An Individual K Plan can be very advantageous for a self employed professional or consultant. The plan lends itself to maximizing contributions for profitable small businesses. It is a great plan for someone needing to accumulate wealth quickly.

### Important Dates for Individual K Plans

- Deadline for establishing an Individual (k) Plan is the last day of the tax year. For a calendar year company, the date is December 31st.
- Deadline for employee contributions depends on if the business is incorporated or not. If the business is not incorporated, the employee contribution is required the same date as the individual's tax return including extensions. If the business is incorporated, typically the employee contribution would be due by January 31st after the plan year, unless a written plan is in place.
- The deadline for funding the profit sharing portion of your Individual (k) plan is your business tax return due date, including extensions.

## ROTH 401(K) FEATURE

If there is one opportunity all long term investors should know, it is the how a Roth feature works in all retirement accounts. Started back in 1997, a Roth feature in a retirement plan allows all distributions on earnings to be 100 % tax free. The trade-off is that the contributions to the plan are not tax deductible. The theory is this, if you contribute to you 401(k) with after-tax dollars, one benefit is the investments grow tax free. The main benefit is the tax free withdrawal of income after age 59 1/2. Some other rules regarding Roth 401(k) include: once such money is invested in a Roth 401(k), it cannot be moved to a regular 401(k). After separation of service, the Roth 401(k) can be rolled to a Roth IRA. Unlike Roth IRAs, with a Roth 401(k), you must begin distributions upon reaching age 70 1/2. Please note it is at the employer's discretion to add the Roth 401(k) feature to the company retirement plan. It is not required. For 2011, the Roth 401(k) contribution limit is \$16,500.

Being rich is having money,  
being wealthy is having time.  
- Margaret Bonnano

Dave Owens, CPA, CES

# Tax Free Strategies – Opportunities for the Savvy Investor

For Other Informative Briefs go to [www.1031-ira.com](http://www.1031-ira.com)

## Self-Directed Retirement Accounts

A self-directed IRA allows you to invest in both “traditional” investments such as stocks, bonds, and mutual funds, as well as “non-traditional” investments, like real estate, mortgages/deeds of trust, private placements, tax liens, and other private placements and limited partnerships. A self-directed IRA enables you to use your investment knowledge and expertise to manage your own investments. It is a common misconception that you can only hold CD’s, stocks, bonds, and mutual funds in your IRA. This is simply not true. A self-directed IRA quite simply is an IRA account that allows you to directly manage and choose which investments to purchase.

There are so many options to consider with a self-directed IRA. Listed below are the most popular investments

- Real Estates
  - ⇒Raw land
  - ⇒Rentals (Single Family/Duplex/Triplex)
  - ⇒Foreclosures
  - ⇒Short Sales
  - ⇒Condominiums/Commercial
- Notes/Mortgages
- Private Stocks
- Gold and other precious metals
- Private LLCs

- Structured Settlements
- Tax Liens/Certificates
- CDs/Stocks & Bonds
- Commodities/Futures/Forex
- & More

Why invest with your IRA dollars—The main benefit of IRA investing vs after-tax investing is the opportunity for tax free gains inside your account. By not having to pay the taxes on a sale of assets, you can keep more money for yourself to grow your nest egg and build wealth

### *How to set up a Self-Directed IRA?*

*The first step to get started in self-direction is finding the right IRA Administrator. Entrust is one of the top IRA Administrators in the United States. Entrust focuses on helping IRA investors take control and purchase the assets they want. Entrust can be reached on the web at [www.1031-ira.com](http://www.1031-ira.com).*

Once you have identified your administrator, you will need to open an account and transfer funds from an existing IRA or make a contribution. Now that the account is set up, you will direct your administrator on what type of non-traditional asset you would like to purchase. ***Self Direction is easy, so why not take control today?***

Have a great day!

## REAL ESTATE IRAS

If you've got an urge to sock away something in your IRA besides stocks, bonds and mutual funds, you may want to consider real estate. Raw land, houses, condos, commercial properties and even mortgage notes -- you can use an IRA to broaden your portfolio. A real estate IRA can be a great investment and offer a tremendous opportunity to investors who want to control and grow their IRA. Now may be the time to take advantage of the record low prices in the real estate market and use your IRA to get started investing today.

## FREE eBook ON REAL ESTATE IRAs

If you are looking to get started in Real Estate IRAs, look no further than the eBook *Understanding Real Estate IRAs* written by Dave Owens CPA. The free download of this book can be found at [www.daveowens.com](http://www.daveowens.com). The book is a hands-on guide to the ins and out of real estate IRA investing.

## 1031 EXCHANGES—WHAT IS A "QUALIFIED INTERMEDIARY?"

In a 1031 exchange, an investor must do more than sell real estate and reinvest the proceeds. To qualify for the favorable tax treatment, the investor can't touch the proceeds from the sale. This is where a "qualified intermediary" or man-in-the-middle comes in. The investor hires an intermediary to handle the money in the 1031 exchange account until the investor is ready to close on a new property, which consummates the 1031 exchange. The QI's role also includes facilitating the exchange using an exchange agreement, which means the QI becomes a party to the transaction. Based on the above description of the "qualified intermediary's" role, you can appreciate why it is important to choose an intermediary carefully. Choose an experienced Qualified Intermediary.

- How many years has your Qualified Intermediary been in business?
- How many exchanges have they performed
- Is the Qualified Intermediary Insured?
- Where are the proceeds kept during the holding period?

***1031 Tax Free Strategies has been performing 1031 Exchanges since 1997. Trust an experienced Qualified Intermediary to help ensure your exchange is handled with the highest degree of professionalism. For more info go to [www.1031company.com](http://www.1031company.com) or call 239-333-1031***