TAX CREDIT FOR SMALL PLAN STARTUP COSTS

(DEFINED CONTRIBUTION PLANS)

PLAN YEARS BEGINNING JANUARY 1, 2023

Small businesses now have a great opportunity to receive a Tax Credit when they establish a new SEP-IRA, SIMPLE-IRA, or 401(k) Profit Sharing Plan

WHICH EMPLOYERS ARE ELIGIBLE TO CLAIM THE TAX CREDIT?

- Employers with 100 or fewer employees who received at least $5,000 of compensation in the prior year.
- Employers with at least one non-highly compensated (NHCE) plan participant.
- Employers who have not contributed to another retirement plan covering substantially the same employees during the previous three tax years.

CALCULATION OF THE TAX CREDIT AMOUNT:

For each of the first three years a plan is established, the tax credit is 100% of actual startup costs with the following limitations:

Maximum tax credit per year will be

The greater of

$500

OR

The lesser of:

i. **$250** x the number of NHCEs eligible for the Plan, or

ii. **$5,000**

Example:	5 NonHCEs	5 x $250.00 = $1,250
	10 NonHCEs	10 x $250.00 = $2,500
	15 NonHCEs	15 x $250.00 = $3,750
	20 NonHCEs	20 x $250.00 = $5,000

The maximum tax credit is $5,000 per year for three years.

WHAT ITEMS ARE CONSIDERED QUALIFIED STARTUP COSTS?

Employer may claim the credit for ordinary and necessary costs related to:

- the establishment and administration of the Plan; and
- the retirement-related education of employees about the Plan.

DEDUCTION OR TAX CREDIT – NOT BOTH

The eligible startup costs are generally deductible as ordinary business expenses. However, the employer can decide to claim the tax credit rather than deduct the expenses. An employer cannot deduct the expenses and get a tax credit for the same expenses.

TAX CREDIT FOR EMPLOYER CONTRIBUTIONS

(DEFINED CONTRIBUTION PLANS)

STARTING JANUARY 1, 2023

Beginning with taxable years after December 31, 2022, employers may be allowed to claim a tax credit for employer contributions made during the initial five years of a defined contribution plan.

ELIGIBLE EMPLOYERS WHO QUALIFY FOR THE TAX CREDIT

- Employers with 100 or fewer employees who received compensation of $5,000 or more in the prior year.
- Employers with at least one non-highly compensated (NHCE) plan participant.
- Employer cannot have contributed to another retirement plan covering substantially the same employees during the previous three tax years.

CALCULATION OF THE TAX CREDIT FOR UP TO 50 EMPLOYEES

Year 1	100% of actual employer contributions, up to $1,000 per employee
Year 2	100% of actual employer contributions, up to $1,000 per employee
Year 3	75% of actual employer contributions, up to $1,000 per employee
Year 4	50% of actual employer contributions, up to $1,000 per employee
Year 5	25% of actual employer contributions, up to $1,000 per employee

Exclusions: Disregard any employee with FICA wages greater than $100,000 (indexed) in the year the tax credit is calculated.

Employer contributions include nonelective, matching, and QNECs/QMACs.

PHASE-OUT REDUCTION FOR EMPLOYEES 51 – 100

The Tax Credit amount shall be reduced if there were more than 50 employees in the **preceding tax year:**

Tax Credit amount is reduced by 2% for any employee over 50 in the prior year.

Example: Employer with 60 employees in prior tax year – there would be 10 extra employees
Tax Credit Amount is determined to be $30,000 based on all employees in the current year
Reduction Rate is 20% (2% x 10 employees)

Phase-out Adjustment is then calculated as follows:
Reduction Amount is $6,000 ($30,000 x 20%)
Tax Credit Amount will be adjusted to $24,000 ($30,000-$6,000)

DEDUCTION OR TAX CREDIT – NOT BOTH

Employer contributions are generally deductible as ordinary business expenses. However, the employer can decide to claim the tax credit and then deduct contributions made that exceed the tax credit amount.