Innovative Retirement Plans
for Small Businesses

IRAs | Qualified Plans | Life Insurance

Retirement Planning Guide

2023 EDITION

Lafayette Life Insurance Company

A member of Western & Southern Financial Group

Retirement Services

DESIGN | ADMINISTRATION | FUNDING

LL-3546 (01/23)

Retirement Planning Guide | 2023 EDITION

Plan Positioning Options

Retirement Plan Option	Small Businesses All Entities 100 Employees or Less	Medium to Large Corporations	Individuals	Lafayette Life Retirement Services
EMPLOYER-SPONSORED PLANS				
SEP IRA	✓			✓
SIMPLE IRA/401(k) 100 Employees or Less	✓			
Defined Benefit	✓	✓		✓
412(e)(3)	✓	✓		✓
Cash Balance	✓	✓		✓
Profit-Sharing	✓	✓		✓
Money-Purchase	✓	✓		✓
Traditional 401(k)	✓	✓		✓
Safe Harbor 401(k)	✓	✓		✓
INDIVIDUAL OPTIONS				
Traditional IRA			✓	✓
Roth IRA			✓	
Nonqualified Deferred Annuity			✓	✓
Nonqualified Immediate Annuity			✓	✓

Traditional IRA

IRA: Individual Retirement Account

A tax-favored savings plan that encourages accumulation of savings for retirement

Contribution Limits

- Annual contribution limit for individuals is the lesser of $6,500 or 100% of compensation; the $6,500 limit includes contributions for both a traditional IRA and Roth IRA combined.
- Married couple's maximum annual contribution is lesser of $13,000 or 100% of compensation; each spouse must maintain his or her own separate IRA, and the $6,500 limit applies to each spouse separately.
- Catch-up provision: Workers age 50 (by the end of the calendar year) or older are permitted to make an additional $1,000 contribution, which makes the annual contribution limit $7,500 for workers who attain age 50 or older on or before Dec. 31, 2023.

IRA Eligibility and Deductibility

- Any U.S. taxpayer who earns compensation can make a contribution to a traditional IRA.
- If neither the taxpayer nor the taxpayer's spouse is an active participant in an employer sponsored retirement plan, their traditional IRA contributions are deductible.
- If an individual is not an active participant in a retirement plan but the individual's spouse is a plan participant, then the non-active participant's IRA contributions are deductible if the couple's income is below a certain limit (i.e., $218,000 or less for full deduction; more than $218,000 but less than $228,000 for partial deduction, indexed for 2023).
- If an individual is an active participant in a retirement plan their IRA contributions are deductible, provided the taxpayer's adjusted gross income (AGI) falls below a certain limit.

2023 Indexed AGI Limits for Deductible IRA Contributions

Filing Status	Full IRA Deduction	Reduced IRA Deduction	No IRA Deduction
Married, filing separately	None	Less than $10,000	$10,000 or more
Individual	$73,000 or less	More than $73,000 to $83,000	$83,000 or more
Married, filing jointly	$116,000 or less	More than $116,000 to $136,000	$136,000 or more

Traditional IRA (continued)

Distributions from Traditional IRAs

- Participants may take a withdrawal from the IRA at any time; however, the withdrawal will be subject to a 10% excise (penalty) tax, in addition to ordinary income taxes, unless the distribution qualifies under one of these exceptions:
  - Age 59½ or older
  - Substantially equal periodic payments over life or life expectancy
  - Death or disability of participant
  - Medical expenses in excess of 7.5% of adjusted gross income
  - Qualified higher education expenses (i.e., tuition, fees, books, supplies, etc.)
  - First home purchase ($10,000 lifetime limit)
- Required minimum distribution (as defined by the IRS) must begin no later than when IRA owner attains age 72.

Target Market

- Individuals who are not currently participating in or contributing to an employer-sponsored retirement plan.
- Individuals interested in a rollover vehicle for retirement plans, such as 401(k), 457(b), 403(b), SEP IRA and SIMPLE.

Roth IRA

Roth IRA

A nondeductible IRA with the potential of earnings being distributed income tax free

Differences between Roth IRAs and Traditional IRAs

- Roth IRA contributions are made on an after-tax basis; contributions to traditional IRAs may be tax deductible, depending on whether the individual participates in a retirement plan and their AGI. Contributions to Roth IRAs are not deductible.
- Roth IRA earnings may qualify for tax free distribution; traditional IRA earnings do not qualify for tax free distribution.
- Withdrawals from Roth IRAs are distributed "investment in the contract," or basis, first.
- Pre-death required minimum distribution rules do not apply to Roth IRAs but do apply to traditional IRAs.

Contribution Limits

- Annual contribution limit for individuals is the lesser of $6,500 or 100% of compensation; this $6,500 limit applies to combined contributions to both a traditional IRA and Roth IRA. An individual of any age who earns compensation may establish or contribute to a Roth IRA in the year compensation is earned.

  Caveat:
  - Full contribution is permitted for single taxpayers with modified adjusted gross income (MAGI) up to $138,000.
  - Contributions are phased out for single taxpayers with MAGI between $138,000 to $153,000.
- A married couple's maximum annual individual contribution is the lesser of $6,500 or 100% of compensation; each spouse must maintain his or her separate Roth IRA. The $6,500 limit applies separately to each spouse.

  Caveat:
  - Full contribution is permitted for married joint filers with MAGI up to $218,000.
  - Contributions are phased out for married joint filers with MAGI between $218,000 to $228,000.
  - Contributions are phased out for a married filer who files separately between $0 to $10,000 MAGI.
  - Contributions are phased out for single, head of household filers between $138,000 to $153,000.
- Catch-up provision: Workers age 50 (by the end of the calendar year) or older are permitted to make an additional $1,000 contribution for 2023, for a total 2023 contribution of $7,500.

Roth IRA (continued)

Two Requirements for Roth IRA Earnings to be Distributed Tax Free

- Distribution must be made after the five-year holding period has been satisfied.
- Distributions must be made under one of four conditions:
  - Owner is at least 59½ years old.
  - Distribution is paid to a beneficiary at death of owner and the five-year holding period is satisfied.
  - Owner is disabled.
  - Withdrawal is made to pay qualified first-time homebuyer expenses ($10,000 lifetime limit).

Penalty-Free Withdrawals

- Owner can withdraw money prior to age 59½ from a Roth IRA (or traditional IRA) and avoid the 10% excise (penalty) tax on the taxable portion of the distribution (if any), for any of the following reasons:
  - Death.
  - Disability.
  - Substantially equal periodic payments over life or life expectancy.
  - Medical expenses in excess of 7.5% of adjusted gross income.
  - New home purchase ($10,000 lifetime limit).
  - Qualified higher education expenses (i.e., tuition, fees, books, supplies).

Conversions from Traditional IRA to Roth IRA

Money can be converted from a traditional IRA to a Roth IRA regardless of the owner's age, income level or tax filing status. The amount converted is taxed to the owner in the year of the Roth conversion.

Target Market

The Roth IRA is most tax efficient when the owner will be in a higher tax bracket at retirement than at the time of the Roth IRA contribution or conversion:

- A tax-free source of income allows the owner greater flexibility in liquidating other taxable assets at retirement.
- There is no requirement to take distributions during a Roth IRA owner's lifetime.
- A Roth IRA may be an appropriate choice if the individual expects to defer the start of distributions past the date they attain age 72, or does not expect to take Roth IRA distributions during their lifetime.

SEP IRA

SEP: Simplified Employee Pension

Small employer retirement plan using an IRA as the funding/investment vehicle

Employer Contribution Limits

- Employer contribution limit is the lesser of 25% of employee's salary ($330,000 salary cap as indexed for 2023) or $66,000 (this amount may be less for highly compensated employees).
- The employer must contribute an equal percentage for the benefit of all eligible employees with immediate vesting; for example, if a business owner contributes 8% to his or her account, the employer must contribute 8% for all eligible employees, if using IRS Form 5305.
- Employer contributions only; employee salary deferrals are not permitted (exception: SAR-SEP plan); SAR-SEP plans, established prior to Jan. 1, 1997, permit employee salary deferrals (see page 9).
- Employer contributions, which are determined on a year-to-year basis, are typically discretionary.

Employee Eligibility Requirement

- Participant must have been employed by the company during at least three of the last five preceding years.
- Employee must typically be age 21 or older (however, employer can set plan eligibility age at 18) and have received at least $750 in compensation (as indexed for 2023).

Key Points

- Loans from SEP IRAs are not permitted.
- Distributions are taxed as ordinary income, the same as IRA distributions.
- Less flexible than a profit sharing plan or 401(k) plan.

Target Market

- Small employers, sole proprietors or small nonprofit organizations with a limited benefit budget looking to establish their first retirement plan, which is easy to administer.
- Additional factors favoring a SEP IRA: no filing requirements, limited fiduciary liability and more cost-effective administration, as compared to a 401(k) or other profit-sharing retirement plan.

SIMPLE IRA

SIMPLE: Savings Incentive Match Plan for Employees

Small employer retirement plan using an IRA as the funding vehicle

Contribution Limits

- Employer contribution limit (employer must select from these two options):
  - 100% match provided on the first 3% of employee's salary deferral (participating employee).

    Example: If an employee defers 5% of salary into a SIMPLE IRA, the employer must contribute 3% in employee's account. If employee defers 1% of salary, employer must contribute 1%.
  - 2% non-elective contribution provided for all eligible employees (regardless of participation).
    - If employer elects this option, the maximum employer contribution is $6,600 ($330,000 cap x 2%).
- Employee deferral limit: $15,500 per plan year (indexed for 2023); up to 100% of compensation.
  - Employees age 50 (by the end of the calendar year) or older are permitted an additional $3,500 catch-up contribution for 2023, if the plan permits, for a total elective deferral of $19,000.

Plan Eligibility Requirements

- Any type of business with 100 or fewer employees may establish a SIMPLE IRA; however, no other qualified plan, 403(b), SEP IRA or 457 plan can be maintained.
- Employer must notify participants of 60-day election period prior to the calendar year-end to elect salary deferral or modify a prior election; the deadline is therefore Nov. 2.
- Employer must provide employee with a Summary Plan Description and account statements within 30 days of the end of a calendar year (contributions must be made between Jan. 1 and Dec. 31).
- Employer must cover any employee who earned $5,000 in any two previous years and is expected to earn $5,000 during current year (exception: employees subject to collective bargaining).

SIMPLE IRA (continued)

Key Points

- SIMPLE IRAs replaced SAR-SEP IRA plans on Jan. 1, 1997.
- Withdrawals can't be restricted; however, withdrawals within the first two years of the employee's initial contribution are subject to a 25% penalty tax in addition to income tax.
- All contributions (employer and employee) are 100% vested immediately.
- Participant loans are not permitted.
- No discrimination testing, annual reporting or administration cost is required of the employer.
- No discrimination testing is required by the employer, meaning highly compensated employees can defer up to $15,500 annually, regardless of the amount lower paid employees defer.

Penalty Tax

- Distributions prior to age 59½ will be subject to a 10% early withdrawal penalty unless such distribution qualifies for one of the following exceptions:
  - Death.
  - Disability.
  - Substantially equal periodic payments over life or life expectancy of SIMPLE IRA owner.
  - Medical expenses in excess of 7.5% of adjusted gross income.
  - Distributions to a nonparticipant pursuant to a qualified domestic relations order.

Target Market

- Small nonprofit organizations and small employers with limited benefits budgets looking for a retirement plan that is inexpensive and easy to administer may find a SIMPLE IRA to be a good fit.
- Employers with 401(k) plans in force may not care to switch to a SIMPLE IRA plan because 401(k)s are more flexible and allow the direction of contributions to a targeted group of employees.

SIMPLE 401(k)

SIMPLE 401(k): Savings Incentive Match Plan for Employees

Small employer retirement plan using a simplified 401(k) as the funding vehicle

Contribution Limits

- Employer contribution requirement (employer must select from these two options):
  - 100% match provided on the first 3% of the employee's salary deferral (participating employee).

    Example: If an employee defers 5% of salary into a SIMPLE 401(k), the employer must contribute 3% in employee's account. If employee defers 1% of salary, employer must contribute 1%.
    - If employer elects this option, the maximum employer contribution is $9,900 per participant ($330,000 cap x 3% in 2023).
  - 2% non-elective contribution provided for all eligible employees (regardless of participation).
    - If employer elects this option, the maximum employer contribution is $6,600 per participant ($330,000 cap x 2%).
- Employee deferral limit: $15,500 per plan year (indexed for 2023); up to 100% of compensation.
  - Employees age 50 (by the end of the calendar year) or older are permitted an additional $3,500 catch-up contribution for 2023, for a total contribution limit of $19,000.

Plan Eligibility Requirements

- Any nongovernmental business with 100 or fewer employees may establish a SIMPLE 401(k); however, no other qualified plan, 403(b) or SEP IRA plan can be maintained.
- Employer must notify participants of 60-day election period prior to the calendar year-end to elect salary deferral or modify a prior election; the deadline is therefore Nov. 2.
- Employee withdrawals cannot be restricted but are subject to income tax and a possible 10% penalty tax.
- Employees are eligible to contribute if they've earned $5,000 and are 21 years of age or have 1,000 service hours in a prior year (employer may exclude nonresident aliens and certain union employees).
- The plan must be maintained on a calendar-year basis (i.e., contributions are made from Jan. 1 to Dec. 31).

SIMPLE 401(k) (continued)

Key Points

- All contributions (employer and employee) are immediately 100% vested.
- Participant loans are permitted (if allowed by the plan document).
- No discrimination testing or top-heavy[1] testing is required by the employer.
- Employers with SIMPLE 401(k) plans are subject to administrative expenses for plan document filing and amendments, Form 5500 Schedule A IRS filing and IRC Sec. 415 limit testing.

Penalty Tax

- Distributions prior to age 59½ will be subject to a 10% early withdrawal penalty unless such distribution qualifies for one of the following exceptions:
  - Death.
  - Disability.
  - Substantially equal periodic payments over life or life expectancy of the participant.
  - Medical expenses in excess of 7.5% of adjusted gross income.
  - Separation from service after age 55 (one-time exception).
  - Distributions to a nonparticipant pursuant to a qualified domestic relations order (QDRO).

Target Market

- SIMPLE 401(k) plans are more attractive than a SIMPLE IRA plan for businesses interested in loan provisions, more restrictive hours requirements for eligibility, exclusion of employees under age 21 or bankruptcy protection under the Employee Retirement Income Security Act (ERISA).

1 A plan is considered to be top heavy if the employer's contributions to key employee accounts are greater than 60% of the employer contributions to non-key employee accounts.

SIMPLE IRA and SIMPLE 401(k): Comparison

	SIMPLE IRA	SIMPLE 401(k)
Employee Eligibility Requirements	Any employee earning $5,000 or more in any two prior years and expected to earn $5,000 in the current year.	Any employee earning $5,000 and the later of 21 years of age or 1,000 service hours in a prior year (may be less pursuant to plan terms).
Employee Deferral Limit	$15,500 per plan year, up to 100% of compensation.	$15,500 per plan year, up to 100% of compensation.
Employer Contribution Limit	If the employer elects the 3% deferral option, up to $15,500 annually; if the employer elects the 2% deferral option, up to $6,600 annually ($330,000 x .02). Limits are per participant.	If the employer elects the 3% deferral option, up to $9,900 annually ($330,000 x .03); if the employer elects the 2% deferral option, up to $6,600 annually ($330,000 x .02). Limits are per participant.
Participant Loans	Not permitted	Permitted if allowed by plan document
Rollovers	Permitted to IRA without penalty only after two years—may roll into another SIMPLE IRA prior to two years.	Permitted to IRA or qualified plan immediately.
Excise Tax	Withdrawals during the first two years subject to a 25% excise tax; 10% thereafter until employee attains age 59½.	Withdrawals subject to 10% penalty tax on distributions prior to age 59½.
Competitive Advantage	Minimal administration expenses, and no 5500 filings or 415 limit testing required.	Loans permitted; may have more restrictive eligibility requirements; exclusion of employees under 21; and bankruptcy protection under ERISA.

Defined Benefit Pension Plan

Employer Contribution Limits

- Annual benefits are limited to the lesser of $265,000 or 100% of the employee's highest three years' (consecutive) compensation (indexed for 2023).
- Annual compensation taken into account for benefit calculations is $330,000 (indexed for 2023).
- Contribution amount is based on actuarial assumptions and computations; consequently, an actuary must determine the plan deductible contribution limit.

Defined Benefit Pension Plan

A retirement plan in which contributions are based on what is needed to provide a determinable future benefit to the plan participants

Key Points

- Allows an employer to create substantial retirement benefits for employees.
- Can be paired with a defined contribution plan to provide additional benefits.

412(e)(3) Plan

412(e)(3) Plan Opportunities

- Exempt from minimum funding requirements because plan is fully funded.
- Tax deductible contributions are not subject to minimum funding rules which results in contributions that may be larger than contributions to a traditional defined benefit plan.

412(e)(3) Plan

A defined benefit plan funded exclusively with annuities or a combination of annuities and life insurance to create a guaranteed retirement income benefit

How it Works

The plan trustee purchases annuities or a combination of annuities and life insurance for each participant in the plan. Premium payments are made to the insurance contracts each year for purposes of funding the future retirement benefit for each participant.

- The plan must be level funded and must begin when the participants are eligible and must end no later than the normal retirement date. No loans are allowed.

Target Market

- Used by small businesses (often 10 or fewer employees) that are stable, profitable and have significant and consistent cash flow.

Cash Balance Plan

Cash Balance Plan

A hybrid defined benefit plan that combines features of defined contribution and defined benefit plans

Employer Contribution Limits

- Annual compensation taken into account for benefit calculations is $330,000 (indexed for 2023).
- Formula may be based on either a lump sum or an accrued benefit.
- Contribution amount is based on actuarial assumptions and computations; consequently, an actuary must determine the plan deductible contribution limit.

Key Points

- Like a defined benefit plan, there is a specified benefit at retirement.
- Like a defined contribution plan, each participant has an account balance although it is hypothetical.
- The employer must contribute an amount determined by an actuary.
- Unlike defined benefit plans, cash balance plans typically offer a lump sum distribution option at retirement, termination of employment, death and disability.
- Cash balance plan may be combined with a 401(k) profit sharing plan to enhance the overall plan design.

Advantages

- The account balance approach may have more meaning for younger employees further away from retirement age.
- Provides portability not provided by a traditional defined benefit plan.
- Tax deduction for the contribution can be significantly higher than a defined contribution plan.

Profit Sharing Plan

401(a) Plan

A qualified plan set up as either a profit sharing plan or money purchase plan

Employer Contribution Limits

- Individual employee limit is the lesser of $66,000 or 100% of employee's compensation (indexed for 2023).
  - Employer contributions are discretionary from year to year. However substantial recurring contributions must be made.
  - The employer deductible limit is up to 25% of total considered compensation. Compensation is limited to $330,000 per participant (indexed for 2023).

Employee Contribution Limit

- Non discriminatory amount of after-tax contributions provided allowed by plan document.
  - Employee contributions are 100% vested at all times.

Profit Sharing Allocation Formulas

- Non Integrated.
- Integrated with Social Security.
- Cross Tested.
  - New Comparability.
  - Age Weighted.

Money Purchase Plan

Employer Contribution Limits

- The employer deduction limit is up to 25% of considered compensation. Compensation is limited to $330,000 per participant (indexed for 2023).
  - Individual employee limit is the lesser of $66,000 or 100% of employee's salary (indexed for 2023).
  - Employer contributions are mandatory and are typically based on a percentage of the employee's compensation.
  - Employee after tax contributions may be permitted.

Key Points

- Profit sharing plan is considered to be the most flexible plan design due to ability to change contribution amount from year to year.
- Money purchase plan may be less desirable due to mandatory annual employer contributions.

Target Market

- Employers who are seeking to attract and retain employees.
- Employers who desire to provide a retirement benefit without the complexity of a defined benefit plan.

Traditional 401(k) Plan

401(k) Plan

A qualified profit sharing plan with a salary deferral feature

Employer Contribution Limits

- Employer deduction limit is 25% of considered compensation. Employee salary deferral contributions are considered employer contributions.
- Individual employee limit is the lesser of $66,000 or 100% of salary (indexed for 2023).
  - Individual limit includes salary deferral amounts contributed by participant.
  - Employer contributions may be attributable to either an employer discretionary contribution or a match contribution (based on employee's deferral amount) or both.

Employee Deferral Limit

- $22,500 per plan year (indexed for 2023) up to 100% of compensation.
  - Employee deferrals are 100% vested immediately.
  - Employees age 50 or older are permitted to make a catch-up contribution up to $7,500 (indexed for 2023) for a total deferral limit of $30,000.

Key Points

- Participant loans may be allowed.
- Upon separation of service a participant's vested account balance may be rolled into an IRA or another qualified plan, provided the receiving qualified plan allows for the acceptance of rollovers.
- Withdrawals from 401(k) plans are restricted. The plan document will define the withdrawal features of the plan.
- Distributions occur from a triggering event. These include termination of employment, death, disability and retirement. The plan document will define the distribution features along with the timing of when the distribution will occur.

IRS Required Testing

- **Actual Deferral Percentage Test (ADP):** A nondiscrimination test required for plans that allow for employee deferrals. The deferral percentage that the highly compensated employees can make is directly related to that of the non highly compensated employees.
  - The simple rules are if the ADP for the non highly compensated employees is less than 2%, the ADP for the highly compensated employees is up to two times.
  - If the ADP for the non highly compensated employees is between 2% and 8%, the ADP for the highly compensated employees can be 2 percentage points higher.
  - If the ADP for the non highly compensated employees is more than 8%, the ADP for the highly compensated employees can be up to 1.25 times higher.

Traditional 401(k) (continued)

- **Actual Contribution Percentage Test (ACP)**: A nondiscrimination test for plans that provide a matching contribution. A plan satisfies the ACP test for a plan year if:
  - The ACP for the eligible highly compensated employees for the plan year is not more than the ACP for the non highly compensated employees multiplied by 1.25; or
  - The excess of the ACP for the highly compensated employees for the year over the ACP for the non highly compensated employees for the year is not more than two percentage points, and the ACP for the highly compensated employees is not more than the ACP for the non highly compensated employees multiplied by two.

Target Market

- Provides an opportunity to engage employees in their own retirement planning.
- A method for the retention and attraction of employees.

Safe Harbor 401(k) Plan

Safe Harbor 401(k) Plan

A 401(k) plan that does not require the ADP test or the ACP test, provided the safe harbor requirements are met.

Safe Harbor Formula

- One of two methods must be followed:
  - Employer matching contribution of 100% of the first 3% of participant deferrals and 50% of the next 2% of deferrals; or
  - 3% non-elective employer contribution.

Target Market

- Businesses that expect or are experiencing low participation by the employees in their current 401(k) plan.
- Businesses that are looking to eliminate the Actual Deferral Percentage (ADP) testing and/or the Actual Contribution Percentage (ACP) testing required by their current 401(k) plan.

Designated Roth 401(k) Accounts

401(k) designated Roth contributions are after-tax salary contributions that can be accepted by 401(k) plans allowing such contributions.

- If a 401(k) plan adopts a designated Roth account feature, employees can designate some or all of their elective contributions as designated Roth contributions, which are included in gross income, rather than having them classified as traditional, pre-tax elective contributions.
- Designated Roth contributions must be kept separate from previous and current 401(k) pretax elective contributions; a separate, designated Roth account must be established for each participant making designated Roth contributions.
- Once a payment is designated as a Roth contribution, it cannot later be changed to a pretax elective contribution.

The *American Taxpayer Relief Act of 2012* (ATRA) expanded in-plan Roth conversion rules to 2016 and beyond. Participants in 401(k), 403(b) and 457 retirement plans offering a designated Roth account can convert any non-Roth account to a Roth account within the plan, regardless of whether it is otherwise distributable from the retirement plan at the time of conversion. The new rule does not allow transfers out of the plan to a Roth IRA. As under prior law, converted amounts are subject to tax as ordinary income and not subject to mandatory withholding or 10% early withdrawal penalty.

- **Employee Contribution:** An employee can make contributions to both a designated Roth 401(k) account and to a pre-tax 401(k) account in the same year and in any proportion. However, the combined amount contributed in any one year is limited by the 402(g) limit—$22,500 for 2023 (plus an additional $7,500 in catch-up contributions if age 50 or older) for a total contribution limit of $30,000.
- **Employer Contribution:** Only an employee's designated Roth contributions can be made to designated Roth 401(k) accounts.
- **Penalty-free Withdrawals:** Earnings will be included in gross income unless the participant has maintained a Roth 401(k) account for five years and is either disabled or over age 59½.

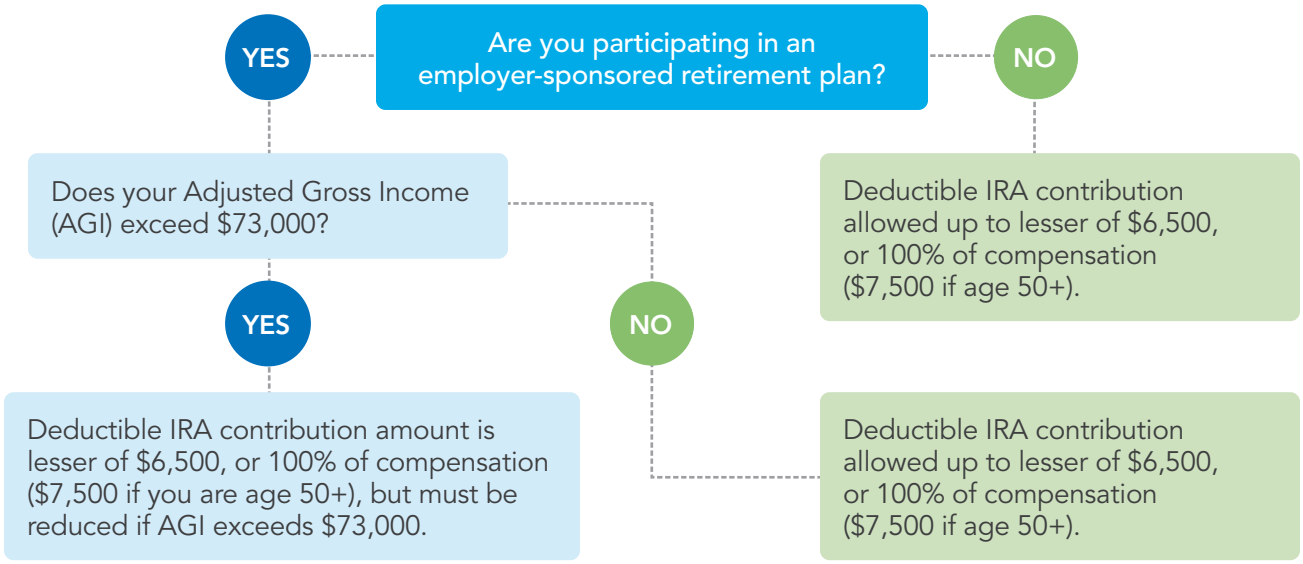
401(k) Mirror Nonqualified Deferred Compensation Plan

A nonqualified plan, sometimes used in conjunction with a 401(k) plan, may include a corporate-owned life insurance policy as part of this plan, which allows highly compensated employees to reduce their taxable wage base by contributing pre-tax dollars. It is not restricted by qualified plan rules. The employer cannot take a deduction for the amount deferred into the plan at the time of deferral. The employer's deduction is taken when the benefit is paid to the employee.

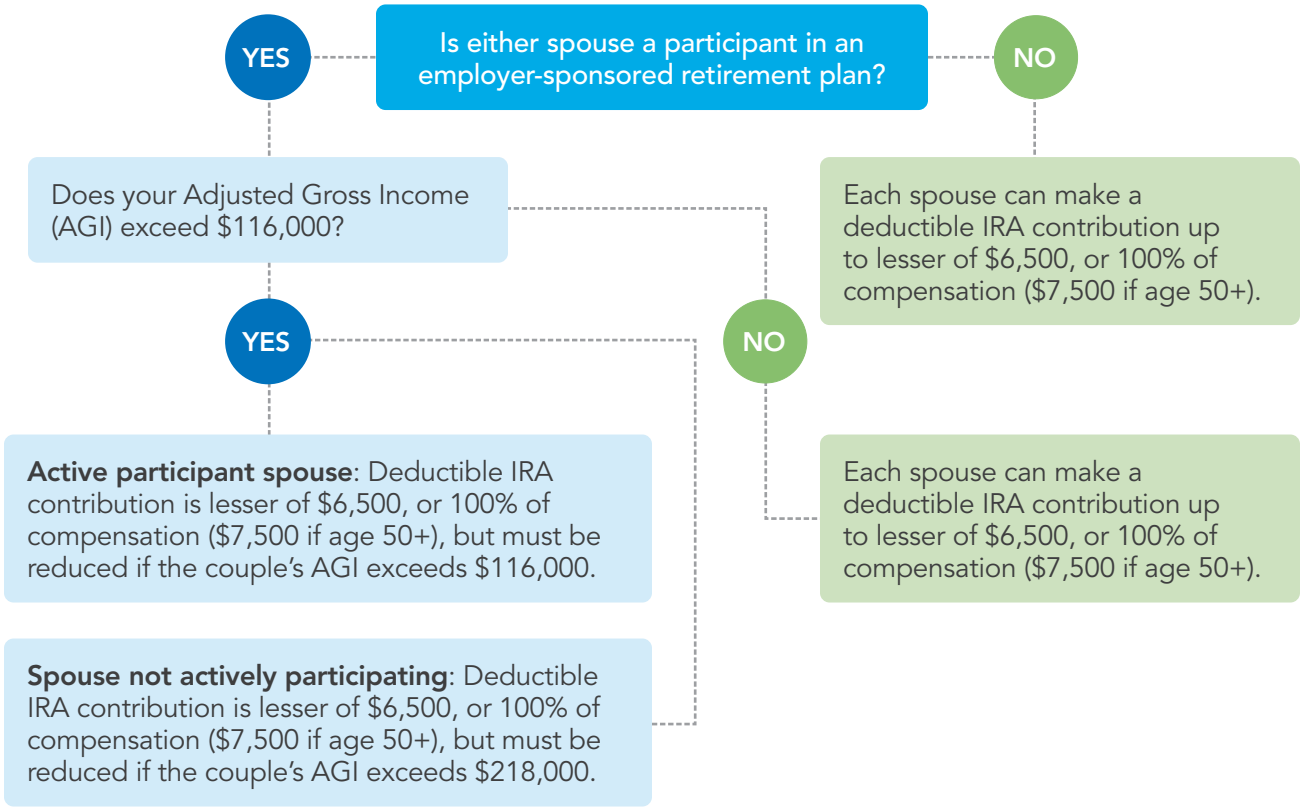
- Primary goal is to attract, retain, reward and retire key employees by providing an additional deferral option above amounts allowed with a traditional 401(k) plan.
- A rabbi trust is sometimes used to segregate the assets in the event of a change in company management.

2023 Traditional IRA Contributions

Single Taxpayer

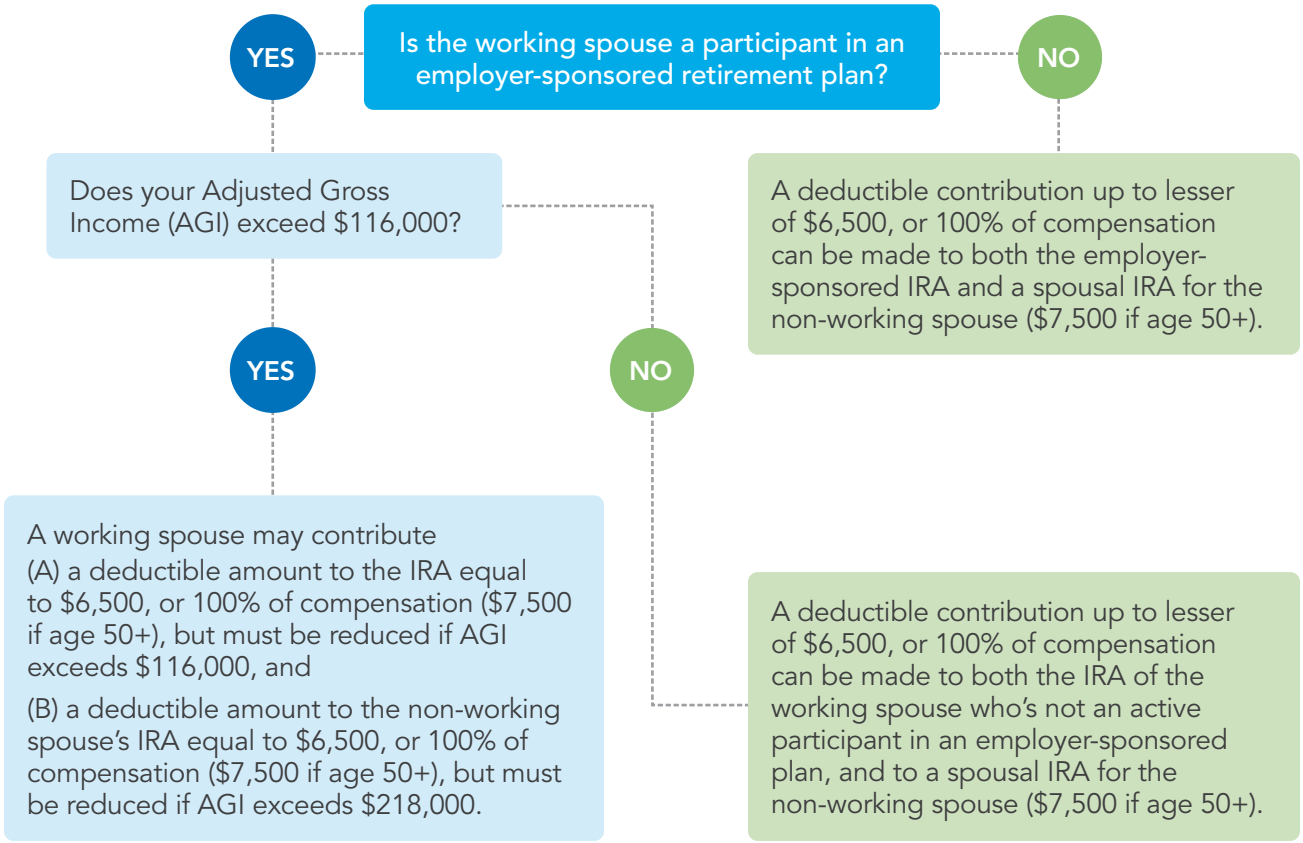


Married Couple Filing Jointly — Both Employed



2023 Traditional IRA Contributions (continued)

Married Couple Filing Jointly — Only One Employed



2023 Roth IRA Contributions

Single Taxpayer

Is your Modified Adjusted Gross Income (MAGI) more than $138,000?

YES

Nondeductible Roth IRA contribution amount is lesser of $6,500, or 100% of compensation ($7,500 if age 50+), but must be reduced if the MAGI exceeds $138,000, and further reduced dollar-for-dollar for traditional IRA contributions.

NO

You may make a Roth IRA contribution up to lesser of $6,500 ($7,500 if 50+) or 100% of compensation, reduced dollar-for-dollar for traditional IRA contributions.

Married Couple Filing Jointly — Both Employed

Does your MAGI exceed $218,000?

YES

Nondeductible Roth IRA contribution amount is lesser of $6,500, or 100% of compensation ($7,500 if age 50+), but must be reduced if the couple's MAGI exceeds $218,000, reduced dollar-for-dollar for traditional IRA contributions.

NO

Each spouse can make a Roth IRA contribution up to lesser of $6,500 ($7,500 if age 50+) or 100% of compensation, reduced dollar-for-dollar for traditional IRA contributions.

Married Couple Filing Jointly — Only One Employed

Does your MAGI exceed $218,000?

YES

Nondeductible Roth IRA contribution amount equal to $6,500, or 100% of compensation ($7,500 if age 50+), but must be reduced if the couple's MAGI exceeds $218,000, to both a Roth IRA and spousal Roth IRA for the non-working spouse, reduced dollar-for-dollar for traditional IRA contributions.

NO

A working spouse may contribute lesser of $6,500 ($7,500 if age 50+) or 100% of compensation to both their Roth IRA and spousal Roth IRA for the non-working spouse, reduced dollar-for-dollar for traditional IRA contributions.

Insurance-Based Retirement Program

Goal: To supplement retirement income and provide life insurance protection in the event of an employee's premature death.

How it Works

- The individual or employer pays the premium to fund a life insurance policy owned by the employee.
- Employee names their desired policy beneficiary or beneficiaries.
- At retirement, the policy owner may take partial surrenders (up to the amount of total premiums paid) and loans from the policy on a tax-advantaged basis (if set up properly) to supplement retirement income.
- These statements assume the life insurance contract remains in force and qualifies as life insurance under section 7702 of the Internal Revenue Code, and is not a Modified Endowment Contract (MEC) under section 7702A. Loans and partial surrenders from a MEC are generally taxable and, if taken before age 59½, may be subject to a 10% penalty tax. Loans and partial surrenders reduce the amount of any death benefits payable.
- At the insured's death, policy beneficiaries receive death benefit proceeds generally income tax free.

Features

- The withdrawal method (i.e., first-in, first-out) depletes the principal in the policy (tax-free) first, followed by policy loans.

  Caveat: In order for the life insurance policy to retain its tax advantages, it must remain in force and not be classified as a MEC. If the policy lapses, the gain/earnings are taxed as ordinary income.[1]
- Partial surrenders are distributed on a first-in, first-out basis (after-tax premiums first, as long as policy remains a non-MEC).
- Beneficiaries are provided replacement income in the event of an employee's premature death.
- Beneficiaries receive death benefit proceeds income tax free (IRC section 101(a)).
- No additional fees, administration or discrimination testing is required.
- Liberal funding levels (relative to a qualified plan).
- Cash value grows tax deferred, providing greater growth potential.
- Cash value in the policy may be available for emergencies or financial planning needs (e.g., college funding, mortgage acceleration).

Target Markets

Insurance-based retirement programs can be ideal for sole proprietors, small business owners or high-net-worth individuals who have maximized other retirement plan contributions and would like to supplement their retirement income in a tax-advantaged manner.

1 This assumes contract remains in force, qualifies as life insurance under section 7702 of the Internal Revenue Code, and is not a modified endowment contract (MEC) under section 7702A. Loans and partial surrenders from a MEC are generally taxable and, if taken before age 59½, may be subject to a 10% penalty tax. Loans and partial surrenders will reduce any death benefits payable.

Executive Bonus Plan—IRC Section 162

Goal: To retain and reward key employees by making a taxable contribution into a life insurance policy owned by the insured employee. The employer premium contribution is tax deductible by the employer as compensation and is a taxable bonus to the employee.

Estate Planning: If the employee wants to exclude the policy from his or her gross taxable estate upon death, the initial applicant and owner of the policy should be a third party (e.g., spouse or trustee), and the employee should not retain any incidents of ownership in the policy.

Benefits to Employer

- Employer rewards and retains key employees, while supplementing their retirement.
- Selective participation is allowed without violating ERISA/IRS nondiscrimination rules.
- Premiums paid by the employer may provide an immediate employer tax deduction.
- Administration cost is minimal due to the simplicity of setup and implementation.
- Amounts of coverage on various employees/executives can differ.
- Plans can be established or terminated without IRS notice, approval or restriction.

Benefits to Executives

- Supplemental retirement assets can be accumulated.
- Beneficiaries receive generally income-tax-free death benefit proceeds (IRC section 101(a)).
- Key employee/executive controls and owns the life insurance policy.
- Cash value grows income tax deferred.

Key Points

- Employer cannot be the owner or a beneficiary of the insurance policy.
- The premium paid by the employer is considered additional compensation to the employee and will be taxed as ordinary income to the employee.
- The premium paid by the employer must be considered "reasonable compensation" when added to all other compensation for the employer to receive an income tax deduction.
- If the goal is to retain key personnel for a period of time, a written agreement between the employer and employee, such as a Restricted Employee Benefit Agreement (REBA), may help.

Target Markets

- C Corporations
- S Corporations (S Corporations may want to consider this as an alternative to a split-dollar plan)
- Partnerships (for employees only)
- Limited Liability Companies (for employees only)
- Sole proprietorships (for employees only)

Split-Dollar Plan

Goal: To retain and reward key employees by splitting the cost of a life insurance policy between employer and employee while accumulating cash value on a tax-deferred basis.

Benefits to Employer

- Discrimination in favor of owners and key employees is permitted.
- The employer's share of premiums is secured/protected within the policy.
- The plan is exempt from ERISA vesting, funding and participation rules.

Policy Ownership

- **Endorsement method:** The employer owns the policy and the cash value; the employee's interest is recorded as a policy endorsement.
  - A written endorsement is typically filed with the insurance company issuing the policy.
  - Employer is required to provide a plan summary to all participants.
  - Under current regulations, the endorsement method is taxed under the traditional split-dollar agreement economic benefit rules described below:
    - Employer pays the premiums required.
    - Employee is taxed on the economic benefit of life insurance coverage to the extent that the employer pays the premium and is not repaid by the employee.
    - The economic benefit includes the value of current life insurance protection (Table 2001 values or actual term insurance rates).
- **Loan regime method:** The employee owns the policy and the cash value; the employer's interest is secured by a collateral assignment of the contract.
  - Funds provided by the employer under the loan regime method will be treated as a series of loans; the employee will be taxed on any interest not paid or capitalized into loan principal.
  - If the employee is not obligated to repay the loan, the funds will be treated as current compensation to the employee.

Target Markets

- Vehicle for a C Corporation or a closely held business desiring to provide additional life insurance or supplemental retirement resources for a limited and select group of key employees.
- Lower corporate tax rates favor split-dollar strategy—lower-rate entity uses nondeductible premium dollars and higher-rate individuals minimize tax exposure by only recognizing economic benefit or loan interest (rather than recognizing entire premium).

Deferred Compensation Plan— Supplemental Executive Retirement Plan (SERP)

Goal: To retain and reward talented/valuable key employees by providing an additional incentive (i.e., deferred compensation) to them and their families for remaining employed with the company.

How it Works

- A corporation purchases a life insurance policy to help fulfill its contractual agreement with certain key employees. The policy cash value and death benefit may be used to offset the employer's financial contributions.
- A deferred compensation agreement is typically designed to guarantee key employees a prearranged payout at retirement (or to their survivors if the employee dies prior to retirement), if they remain employed by and fulfill their contractual obligations to the employer.
- A corporation (employer) owns the policy and uses it to informally fund deferred compensation benefits.
- A corporation (employer) is required by contract to provide future benefits to key employees (or the employees' survivors) if they meet their contractual obligation to the employer.
- If key employees do not fulfill their commitment, they forfeit the deferred compensation to employer.
- Employer-owned policies on the life of an employee with the death benefit payable to the employer must meet the notice and consent rules of IRC Sec. 101(j).

Target Markets

- Used by C Corporations to compensate executives while retaining maximum control over the policy.
- Cost recovery by the corporation for its life insurance expense may be part of a plan design. A tax deduction is available when benefits are paid out to key employees.
- Popular with closely held businesses interested in providing a substantial benefit to owners and key personnel without including all employees.

Notes

The Lafayette Life Insurance Company

With more than 115 years of service to policyholders, The Lafayette Life Insurance Company is a financially strong provider of individual life insurance, annuities, and retirement and pension products and services.

Lafayette Life is a member of Western & Southern Financial Group, Inc., a family of financial services companies whose heritage dates back to 1888. With the strength of our organization and our ongoing commitment to servicing you, your business and your family, The Lafayette Life Insurance Company is a company you can depend on. Find out more about our financial strength and distinguished history at www.LafayetteLife.com.

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