Selecting the Best Retirement Plan for Your Practice

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An independent physician practice that does not have access to a hospital?s retirement plans has several retirement plan options to consider. Doctors who are employed by hospitals will usually be able to participate in the hospital?s retirement plan that is either an Internal Revenue Code (IRC) section 403(b) plan (if a nonprofit or governmental entity) or an IRC section 401(k) plan that allows employees to make pre-tax or Roth contributions. These plans will generally have some type of employer contribution either through a matching contribution or an employer contribution. Independent physician practices should also consider implementing a retirement plan for their owners and employees to help maximize retirement savings and lower taxable income. Below is an outline of plans that may be provided.

SIMPLE IRA

A small practice with under 100 employees may consider setting up a SIMPLE IRA. These plans are very simple to set up and involve little administrative oversight.

The SIMPLE IRA allows the employer to contribute to IRAs set up for employees and selected by the employer. Employees may contribute up to $12,500 to the IRA in 2018. The employer must contribute to all employees at least a 2% nonelective contribution or a 3% matching contribution. There is no nondiscrimination testing required, meaning that highly compensated employees would not be limited in their ability to defer pre-tax contributions as may occur with IRC section 401(k) plans.

Eligibility may be limited to employees with two years of service, with a year of service granted to an employee with $5,000 in earnings. There are no annual filings required. The downside to this plan is that the contribution limit is lower than a 401(k) plan, and an employer contribution must be made to all employees.

401(k) Plan

Perhaps the most well-known retirement plan is the 401(k) plan. Employees may defer up to $18,500 in 2018 plus $6,000 in catch-up contributions for employees who will be age 50 or older in 2018. The plan may be set up to allow employees to defer on a pre-tax basis or an after-tax basis known as Roth contributions.

An employer may choose to give an employer contribution either as a match or an employer profit-sharing contribution, but such contribution is not required. There is flexibility in the amount of the contribution, as it may change by year. Different groups of employees may receive varying employer contributions, though this design must pass nondiscrimination testing for treatment of non-highly compensated employees.

An owner of the practice group may contribute up to $55,000 a year for 2018 to his or her account as deferrals and the profit-sharing contribution. The contribution is tax-deductible to the owners of the practice as the employer.

Service for eligibility is based on hours rather than wages, and an employer may require that the employee complete 1,000 hours of service and be employed on the last day of the plan year to receive an employer contribution.

401(k) plans require more administrative oversight and expense than SIMPLE IRAs. Nondiscrimination testing and annual filings with the Department of Labor (?DOL?) are required. High wage earners and owners may also be limited in their deferrals if non-highly compensated employees are not deferring enough. There are ways to avoid this problem, including adopting a safe harbor contribution or adding automatic enrollment. There is also greater fiduciary liability for those overseeing a 401(k) plan, as they are responsible for selecting and maintaining investment options for the plan.

Defined Benefit Plans

In recent years these plans have decreased in popularity due to strict funding requirements and expensive administration, but they provide for a high level of retirement savings and a guaranteed benefit. Under a defined benefit plan, the benefit is determined as a monthly amount payable at retirement age. The maximum annual benefit for an individual for 2018 is $220,000.

An employer must make an annual contribution to the plan. The limit on these contributions is higher than the $55,000 limit for 401(k) plans, allowing practice owners to save more for retirement. The owners of the practice will receive a tax deduction for the employer contributions to the plan. Employees are not able to direct their investments, and the funds are placed in a group trust to be managed by the employer.

These plans are expensive to maintain as the employer must hire an actuary to calculate the required funding amount for benefits and pay annual insurance premiums to the Pension Benefit Guaranty Corporation. An annual filing with the DOL is required. This plan may be offered along with a 401(k) plan.

Cash Balance Plan

These hybrid plans are growing more popular with professional groups, including physician groups, because they allow for a large contribution amount. The plan is a defined benefit plan but has individual accounts like a 401(k) plan described above. Similar to a defined benefit plan, participants are promised a certain amount at retirement age, which is stated as an account balance, but participants may not direct the investment of their accounts. The annual retirement benefit may be set as a flat dollar amount or a percentage of pay.

The employer makes an annual contribution. As with the defined benefit plan, the annual contributions can be substantially more than the $55,000 limit applicable to a 401(k) plan. The owners of a practice may work with an actuary to determine the annual contributions needed over an owner?s working years to hit the maximum yearly benefit of $220,000 payable at normal retirement age over the participant?s life. This will generally benefit employees who are closer to retirement, as they may make larger contributions over a condensed period. As with the plans discussed above, the owners may receive a tax deduction for the contributions to the plan.

The plan grows each year by being credited with interest credits. The interest rate must be a market rate of return, such as the 30-year Treasury bond rate or the rate of return on the assets of the plan. There are no employee contributions.

Conclusion

There are a variety of options available to independent professional practices to assist their owners and employees in preparing for retirement. If you have any questions regarding this article or establishing a plan, contact Ellie Clendenin at eclendenin@williamsmullen.com or (804) 420-6469.

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