Tax credits for retirement plan startup and automatic enrollment costs

Wealth Management

Are you considering setting up a retirement plan or adding automatic enrollment to an existing plan, but are hesitant to do so because of costs and annual administration expenses? If so, you need to know that you may be eligible to claim a tax credit for part of the ordinary and necessary costs of starting and maintaining an employer sponsored plan (including SEPs, SIMPLEs, profit-sharing and 401(k) plans).

The Setting Every Community Up for Retirement Enhancement (SECURE) Act of 2019 and the SECURE 2.0 Act of 2022 provide valuable types of retirement plan tax credits for small business owners:

SECURE 2.0 Act increased the small employer pension plan startup credit

Effective for plan years beginning after December 31, 2022, the nonrefundable tax credit is an amount equal to 100% of the qualified startup costs for the year for employers with up to 50 employees. The credit amount is the greater of $500, or the lesser of $250 for each non-Highly Compensated Employee (NHCE) who are eligible to participate in the plan, or $5,000. This credit is available for up to three years. Except in the case of defined benefit plans, an additional credit is provided. The amount of the additional credit generally will be a percentage of the amount contributed by the employer on behalf of employees, up to a per-employee cap of $1,000. This full additional credit is limited to employers with 50 or fewer employees and phased out for employers with between 51 and 100 employees.

Applicable percentage	Year
100%	1st, 2nd
75%	3rd
50%	4th
25%	5th

There is no credit available after the 5th year.

- SECURE 2.0 Act allows for the small employer pension plan startup credit to be available for three years for employers joining a Multiple Employer Plan (including a Pooled Employer Plan), regardless of how long the MEP has been in existence. This is effective retroactively for taxable years beginning after December 31, 2019.

Small employer automatic enrollment credit

This credit is $500 per year for up to three years beginning with the first taxable year for which the employer includes an Eligible Automatic Contribution Agreement (EACA) in an existing or new qualified plan.

An employer with a plan that includes only an Automatic Contribution Arrangement (ACA) does not qualify for the credit; the plan must be amended from an ACA to an EACA to take advantage of the credit. The credit also applies to a Qualified Automatic Contribution Arrangement (QACA) that meets the EACA requirements.

To be eligible, an employer:

- Must sponsor a plan which has at least one employee eligible to participate who is not considered a highly-compensated employee (an individual who is at least a 5% owner or anyone who earned more than $150,000 in 2023).

- Must have had no more than 100 employees during the preceding year who received at least $5,000 of compensation.
- Must not have maintained a plan where substantially the same employees benefitted during the three tax years immediately before the first year for which the credit is claimed.

Your company retirement plan

These credits are a great benefit to getting your company retirement plan started. At RBC Wealth Management, we recognize the importance of selecting and designing an appropriate retirement plan for you and your employees. If you have any questions on this or other retirement-related topics, please contact your RBC Wealth Management financial advisor.