



Power Your Savings Plan

BY AMIT AGRAWAL

Illustration by Gilberto Saucedo

We are all aware of the importance of saving for tomorrow. It's probably even one of our perennial New Year's resolutions. For solo and small law firms, it's especially important to have a savings strategy because all your time can easily be spent working in the practice of law. But it can pay big dividends to spend some time working on your law practice to help you stay competitive and to increase your long-term financial stability.

When I say "working on your law practice," I'm talking about using your firm as a vehicle to save for tomorrow. You can do this through a pension plan, a salary-deferral plan, or both. For the purposes of this article, we'll limit our discussion to various types of salary-deferral plans.

There are several advantages to setting up your retirement plan through your firm. Here are some of the benefits of using your law firm as the engine that powers your savings.

Benefits of Having a Firm-Based Plan

First, an obvious benefit of running a retirement plan through your business is that it's a convenient way to save for tomorrow while you take care of today's pressing matters. Most solo and small firms are constantly preoccupied with urgent fires to put out. A retirement plan maintained

through the business itself is more likely to get the periodic attention it deserves.

Second, there are financial incentives to setting up a retirement plan through your firm. You may be able to take advantage of a tax credit that's available to small companies that covers some of the costs of creating and maintaining a retirement plan. Specifically, the credit applies to 50 percent of the first \$1,000 in administrative and start-up expenses over the initial three years of the plan's establishment. You can also make contributions to the plan for yourself and your employees that are tax-deductible to the firm.

Third, you help your employees save for the future. You may be providing your employees with their only avenue for making pre-tax and possibly post-tax contributions to a retirement fund. You will also be helping them (and yourself, of course) enjoy tax-deferred compound-

ing of any investment earnings inside their respective retirement plan accounts.

Having a retirement plan will make your firm more attractive to potential hires and make employees more likely to stick around. The smaller the firm, the greater the potential impact of employee turnover, so the more you can do to retain key personnel, the better. A work-based retirement plan is crucial because it's one of the most sought-after benefits today. But not every firm has one, so it also positions you competitively in the landscape of legal employers and gives you an edge when it comes to recruiting the very best talent.

Types of Firm-Based Plans

The following are some of the major types of salary-deferral plans that are available to small firms. It's important to select the appropriate plan, whether you're

establishing one for the first time or evaluating the one you already have in place.

SEP IRA

A Simplified Employee Pension Individual Retirement Arrangement, or SEP IRA, is a good choice for firms that have significantly variable profits from year to year because contributions to a SEP plan are discretionary. Some key attributes of a SEP plan are that the firm can contribute up to 25 percent of an employee's eligible compensation for a maximum of \$49,000 per individual in 2010; the firm's contributions are discretionary and may vary from year to year; and only the firm can contribute to the plan.

It is possible to structure an SEP so that only long-term employees are eligible for contributions. Generally speaking, the same formula must be used to compute the contribution amount for all eligible employees, from owners of the firm down to part-time workers.

SIMPLE IRA

Some key attributes of Savings Incentive Match Plan for Employees, or SIMPLE IRAs, are that the firm's contribution amounts are significantly limited compared to the contribution amounts for a SEP plan; employees can save through payroll deductions, up to \$11,500 for 2010 (or \$14,000 for employees ages 50 and over); and the firm's annual contributions are mandatory, unless employee-notification requirements are met.

Unlike a SEP, the SIMPLE plan encourages employees to save for retirement through payroll deductions that reduce their personal federal taxable wages. Like the SEP, part-time employees cannot be excluded from the plan based solely on their status as part-time. Because of the limitations on the firm's contribution amounts, partners may not be able to sock away as much per year with a SIMPLE as they would with a SEP.

401(k)

Named for the section of the Internal Revenue Code that created them, 401(k)s are perhaps the most well-known type of employer-based retirement plan. Some key attributes are that the firm's employees can save through payroll deductions — up to \$16,500 for 2010 (or \$22,000 for employees ages 50 and over); the firm can contribute up to 25 percent of an eligible

employee's total compensation — total firm and employee contributions cannot exceed \$49,000 for 2010 (\$54,500 over age 50) for any one employee; and the firm's annual contributions can be either mandatory or discretionary, depending on how the plan is structured.

In general, 401(k)s have administrative requirements such as IRS filings and fidelity bonds that may make them costlier and less time-effective when compared to the other plans mentioned above. However, in the case of solo firm, the owner-only 401(k), or "Solo" 401(k) plan, as it's sometimes called, can keep administrative costs relatively low while providing increased retirement savings. As the name implies, these plans are only available to firms that employ just the owner (or owner and spouse).

One other option in the 401(k) realm is to add a Roth feature to an existing plan. A work-based Roth 401(k) functions similarly to a personal Roth IRA, but it doesn't have income eligibility requirements. Thus, someone who can't contribute to a Roth IRA because they earn too much may really benefit from

having a Roth 401(k) plan through work. It is surprising how frequently even large companies fail to offer the Roth feature inside their 401(k) plans, so this presents a valuable opportunity for a law firm to distinguish itself in the retirement-planning arena.

Conclusion

It's a good idea to get started with a basic retirement plan that suits your current needs and then add features to it as your law practice grows. The earlier you begin, the longer you'll have for your savings to grow.



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