



## The IRS May Be Watching

How the IRS will view your salary can be an important factor in determining how much you pay yourself. For example, owners of C corporations may face an “unreasonable compensation” audit if the IRS interprets an owner’s large salary as a disguised dividend. Because dividends – unlike salaries – are not deductible, an unfavorable determination could result in an overdue tax notice, back-interest charges and penalties for the business.

On the other hand, if you own an S corporation, you could face an audit for paying yourself too little – especially if the business is profitable and doing well. Why? The IRS may determine that you’re trying to avoid FICA and Medicare taxes by keeping your salary unreasonably low.

Talk with your CPA about what the IRS would consider “reasonable compensation.” If what you receive is out of line with what owners of comparable businesses are making, you could be setting yourself up for a visit from the IRS. If things don’t go your way, the costs could be substantial.

## Keep an Eye on Retirement

The amount you can save for retirement in a qualified plan is calculated based on eligible compensation. Therefore, when determining your compensation, keep in mind that what you pay yourself affects how much you can save for retirement: Generally, the more you earn, the more you may be able to save. The following chart shows how your business structure may affect your retirement plan contributions.

## Take Your Compensation Seriously

The compensation you receive from your business should not be taken lightly. We’ve touched on just a few issues here – there are many others. Do your research – plenty of books and articles are available to help you get started. In addition, talk with your business advisors, especially your CPA and attorney. Your goal should be to arrive at a compensation plan that’s good for your business and will satisfy your family’s needs, your employees and the IRS.

Business Structure	Eligible Owner Compensation for Retirement Plan Contributions
<b>Sole Proprietorship</b>	Net Schedule C income minus 50% of the self-employment tax minus the employer’s contribution to the retirement plan* for the self-employed person.
<b>Partnership</b>	Net K-1 income minus 50% of the self-employment tax minus the employer’s contribution to the partners.
<b>S Corporation</b>	W-2 income only. The “pass through” cannot be used to calculate retirement plan contributions.
<b>Corporation</b>	W-2 income only.
<b>Limited Liability Corporation</b>	Depends on how the business is taxed: <ul style="list-style-type: none"><li>• If taxed as a partnership, see either Sole Proprietorship or Partnership, depending on the number of business owners.</li><li>• If taxed as a corporation, see S Corporation.</li></ul>

\* This calculation does not apply to SIMPLE IRAs. Compensation for SIMPLE IRAs is defined as Net Schedule C income.

# A Successful Retirement Plan: The Sum of Its Parts

With a well-tuned car, you don’t have to worry about what’s happening under the hood while you’re cruising down the road. Similarly, a retirement plan is really the sum of its parts, and when it’s all working, it’s easy to forget about everything that must come together.

If you’re considering establishing a plan or have a plan that’s not living up to expectations, you need to know

about the key elements that go into putting together a plan that works. You need to understand your alternatives for selecting:

- A plan type that meets your business’s unique needs
- A plan administrator to handle the day-to-day record keeping and administration

- An investment structure that offers participants a variety of alternatives
- A trustee to handle plan assets
- Ongoing service and support for your participants and you, as plan sponsor

### Selecting a Plan

At one time, business owners had few choices when selecting a type of plan. However, today there's a wide variety from which to choose: defined benefit, SIMPLE IRA, SEP IRA, profit sharing, 401(k) – to name a few. For information on the different plans available, ask your financial consultant for our "Retirement Plan Summary" report.

Selecting the right plan requires understanding the different plans' attributes as well as knowing your business and personal financial needs and those of your employees.

If your business already has a plan, you may need to perform a plan review to determine whether it still meets your needs or whether it's time for a change. By first setting goals for your plan, you can take steps to help ensure your plan is on track toward your objectives.

Your financial consultant can help you develop an overall picture of your situation by helping you complete our "Retirement Plan Questionnaire."

### Choosing a Plan Administrator

Plan administration is a key component of most retirement plans. Behind every smooth-running plan is a high-quality third-party administrator.

The plan administrator is responsible for accurate, timely record keeping, including:

- Employee eligibility tracking
- Compliance testing and required reporting
- Allocation of plan contributions and vesting of participant accounts
- Participant statement preparation
- Participant distributions and plan loans

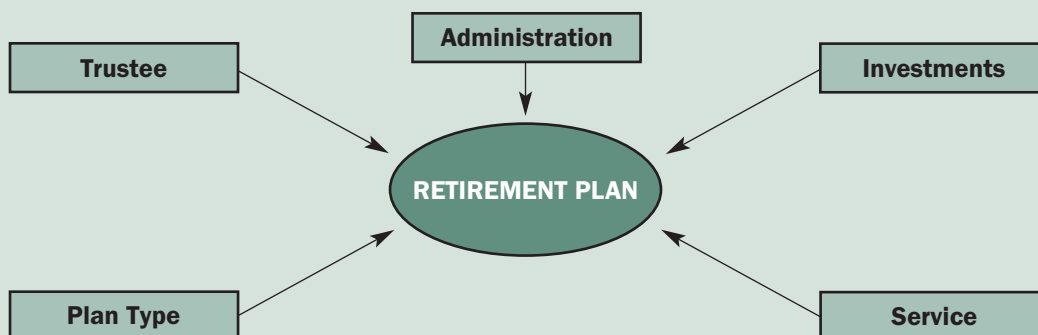
Third party administrators tend to specialize in meeting the needs of certain types of businesses. Your number of participants, the size of their accounts and the level of technology needed may help determine which administrator is best for you.

### Selecting Your Investment Provider

Because participants depend on your plan's investments to help them reach their retirement goals, selecting the right investment provider may be the most important decision you make when designing your plan. When choosing an investment provider, remember that your type of plan and who is responsible for making investment decisions affect what the plan's investments should be. If participants are responsible for directing their investments, finding a provider that offers a broad array of investment choices to meet a variety of needs is vital. These choices may include:

**Individual securities.** You may want to find a provider who will let your participants hold individual stocks, bonds, certificates of deposit, money market fund investments and other securities in one convenient account.

These key elements must work together to create a successful retirement plan.



**Mutual funds.** Because they offer ease of diversification, mutual funds are one of the most popular retirement plan investments. Look for a provider that offers a variety of fund families and the guidance you need to choose the funds that best match your objectives and your participants' needs. Mutual fund investing involves risk. Your principal and investment return in a mutual fund will fluctuate in value. Your investment, when redeemed, may be worth more or less than the original cost.

**Private money management.** Plan participants may want to turn to private money managers to make their investment buy and sell decisions. A good provider should help you narrow the list of managers so you can select those that help meet your participants' objectives. Some providers, such as A.G. Edwards & Sons, Inc., also offer their own in-house money managers.

### Naming a Plan Trustee

Every qualified retirement plan must have a trustee who is responsible for the plan's assets. Your plan's trustee – whether it's you, as plan sponsor, or a corporate trustee – will have a number of responsibilities, including:

- Reviewing plan assets to ensure they are in all participants' best interest
- Managing plan investments prudently by maintaining proper diversification
- Establishing investment goals and objectives for the plan to meet and continually reviewing investments to ensure they adhere to your guidelines

### Ongoing Service for the Long Haul

In selecting a firm to work with on your retirement plan, you need to find one that will help pull together

#### How A.G. Edwards & Sons, Inc. Can Help

Your A.G. Edwards & Sons, Inc. financial consultant, working with the retirement plan experts in our Home Office, can help with all the issues discussed in this article, including:

- Determining the right type of plan for your business
- Finding an appropriate administrator
- Providing a broad range of investment alternatives
- Offering trustee services, including *PenTrust* employee benefit services – our discretionary fiduciary services for managing plan assets, through A.G. Edwards Trust Company FSB<sup>†</sup>
- Providing ongoing service for you, your business and plan participants

For more information, ask your financial consultant for a copy of the “Our Approach to Business Retirement Plans” brochure.

all the key components that lead to a successful plan. You also need a firm that will work with you over the long term by providing a variety of valuable services, such as:

- Conducting enrollment meetings with employees to explain how your plan works and the benefits of participation
- Meeting with you regularly to review investment performance and explain account statements
- Conducting seminars or confidential one-on-one meetings to address plan distribution issues

To determine whether a firm is right for your business, ask for a no-cost proposal from that firm.

<sup>†</sup> An affiliate of A.G. Edwards and Sons, Inc.



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