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Self-Employed Retirement Account Comparison Guide (SEP IRA vs Solo 401k vs SIMPLE)

Self-employed people have access to the most generous retirement contribution limits in the tax code, but most leave tens of thousands of dollars on the table every year by defaulting to a SEP IRA without comparing it to a Solo 401(k). The right account depends on your net self-employment income, whether you have employees, your entity structure, whether you want a Roth option, and whether you might ever need a loan. This guide walks through both accounts from the contribution formula up, shows the exact crossover point where the Solo 401(k) starts winning, covers spouse contributions, and maps out S corp optimization, so you can make the calculation for your specific situation.

1. Foundation

The SEP IRA and Solo 401(k) serve the same goal — deferring as much self-employment income from taxes as possible — but they reach different maximums through different formulas. The SEP IRA allows only employer contributions, calculated at 25% of net self-employment income after adjustments (or, for sole proprietors and single-member LLCs taxed as sole props, approximately 20% of net profit after the self-employment tax deduction). The 2025 annual contribution limit is \$70,000. The math: if your net Schedule C income is \$200,000, the deductible contribution is roughly $\$200,000 \times 0.9235$ (removing the SE tax deduction) $\times 0.25 =$ about \$46,175. The SEP IRA's advantage is simplicity — you can open one with Fidelity, Vanguard, or Schwab in under 30 minutes, there is no annual filing requirement, and you can contribute up until the tax deadline including extensions (October 15 for individuals who file a Form 4868). The disadvantage is that if you ever hire even one employee who meets the age and service requirements,

you must contribute the same percentage to their SEP IRA that you contribute to your own.

The Solo 401(k) has two contribution layers that make it dramatically more powerful at lower and moderate income levels. The first layer is the employee deferral: in 2025, you can contribute up to \$23,500 as the employee, or \$31,000 if you are 50 or older (using the \$7,500 catch-up). The second layer is the employer profit-sharing contribution of up to 25% of W-2 compensation (if you are an S corp) or approximately 20% of net self-employment income (if you are a sole prop or single-member LLC). Together, the two layers can reach \$70,000 in 2025 (or \$77,500 with catch-up). The Roth option — available in many Solo 401(k) plans — allows the employee deferral portion to go into a Roth sub-account, meaning no deduction now but tax-free growth and withdrawals forever. The loan provision allows borrowing up to 50% of vested balance or \$50,000, whichever is less. Disadvantages: Solo 401(k) is only for businesses with no full-time employees other than the owner and spouse; a Form 5500-EZ is required once plan assets exceed \$250,000; and setup must be completed by December 31 of the year you want contributions to apply (unlike the SEP IRA's April or October deadline).

The crossover point where the Solo 401(k) stops outperforming the SEP IRA is approximately \$233,000 in net self-employment income for a sole proprietor under age 50 in 2025. Below that income level, the employee deferral makes the Solo 401(k) the clear winner. At \$80,000 net SE income, the SEP IRA allows roughly \$14,800 in contributions; the Solo 401(k) allows the same \$14,800 in employer profit-sharing plus the full \$23,500 employee deferral, for a total of \$38,300. That \$23,500 difference compounds to a staggering amount over 20 years. At \$130,000 net SE income, the SEP IRA allows approximately \$23,900; the Solo 401(k) allows \$23,900 plus the \$23,500 deferral, totaling \$47,400. The difference narrows as income rises. Above \$233,000, both plans approach the \$70,000 cap and the SEP IRA's simpler administration becomes a legitimate tie-breaker. For S corp owners, the calculation uses W-2 salary as the base rather than net SE income, which introduces another optimization variable: the right W-2 salary minimizes payroll taxes while maximizing Solo 401(k) contributions.

2. Step-by-Step System

1

Calculate your net self-employment income

Start with your Schedule C net profit (gross revenue minus business expenses). From that number, subtract the deductible portion of self-employment tax, which is 50% of SE tax. SE tax is 15.3% on the first \$176,100 of net earnings in 2025 and 2.9% on earnings above that. Example: if Schedule C net profit is \$120,000, SE tax is approximately $\$120,000 \times 0.9235 \times 0.153 = \$16,943$. Half of that is \$8,471. So net SE income for plan contribution purposes = $\$120,000 - \$8,471 = \$111,529$. For an S corp owner who pays themselves a reasonable W-2 salary, the SE tax calculation works differently — W-2 wages are subject to payroll tax, and the corporation's distributions are not. The Solo 401(k) employer profit-sharing contribution for an S corp owner is 25% of W-2 wages (not total distributions). This is why S corp owners should model their optimal W-2 salary as the balance point between payroll tax cost and retirement account contribution capacity.

2

Calculate your maximum SEP IRA contribution

For a sole proprietor or single-member LLC: SEP contribution = net SE income (after SE tax deduction) \times 25%. But because the net SE income is itself reduced by the SEP contribution (circular reference), the effective rate on net profit before the SEP contribution is approximately 20%. The IRS provides Worksheet 2 in Publication 560 for the exact iterative calculation. Quick formula: SEP max \approx (net Schedule C profit – SE tax deduction) \times 0.2. At \$80,000 net profit: SE tax deduction \approx \$5,651; SEP max \approx $(\$80,000 - \$5,651) \times 0.20 = \$14,870$. At \$150,000 net profit: SE tax deduction \approx \$10,597; SEP max \approx $(\$150,000 - \$10,597) \times 0.20 = \$27,881$. At \$280,000 net profit: SE tax deduction \approx \$17,476 (SE tax caps); SEP max \approx $(\$280,000 - \$17,476) \times 0.20 = \$52,505$. Above roughly \$350,000 in net profit, SEP contributions hit the \$70,000 annual cap. The SEP IRA deadline for contributions is your tax filing deadline including extensions — October 15 for most self-employed individuals who file Form 4868.

3

Calculate your maximum Solo 401(k) contribution

Sum two layers. Layer 1 — Employee elective deferral: up to \$23,500 in 2025 (or \$31,000 if age 50+). This comes entirely from earned income; it is not calculated as a percentage. You simply defer up to the limit. Roth sub-account option: you can designate all or part of the elective deferral as Roth (after-tax), allowing tax-free growth and withdrawals. Layer 2 — Employer profit-sharing: same formula as SEP IRA ($\approx 20\%$ of net SE income for sole props, 25% of W-2 for S corps). Total cap is \$70,000 (or \$77,500 with catch-up). Example at \$80,000 net profit: employee deferral = \$23,500 + employer profit-sharing \approx \$14,870 = total \$38,370. The employee deferral is the reason the Solo 401(k) wins at lower income levels. Important: the Solo 401(k) plan document must be established (signed) by December 31 of the year for which you want to make contributions. You can contribute until your tax filing deadline, but the plan must exist before year-end. Open at Fidelity (no plan documents fees, self-directed), Vanguard, Schwab (both good options with index funds), or a self-directed custodian if you want alternative investments.

4

Run the crossover analysis at your income level

Build a three-column table: income, SEP IRA max, Solo 401(k) max. Calculate at \$50,000, \$80,000, \$100,000, \$150,000, \$200,000, \$250,000, and \$300,000 net self-employment income. At \$50,000 net profit: SEP \approx \$9,300; Solo 401(k) \approx \$9,300 + \$23,500 = \$32,800. Difference: \$23,500. At \$100,000: SEP \approx \$18,588; Solo 401(k) \approx \$18,588 + \$23,500 = \$42,088. Difference: \$23,500. At \$200,000: SEP \approx \$38,487; Solo 401(k) \approx \$38,487 + \$23,500 = \$61,987. Difference: \$23,500. The difference remains approximately \$23,500 at every income level below the crossover — it is constant because it equals the fixed employee deferral. The crossover occurs when the SEP IRA employer-only contribution reaches \$70,000, which requires net SE income of roughly \$350,000. Below \$350,000 in net SE income, the Solo 401(k) almost always allows larger total contributions. The tradeoff: more paperwork, December 31 plan establishment deadline, Form 5500-EZ when assets exceed \$250,000, and no W-2 employees allowed (other than a spouse).

5

Add a spouse and understand contribution deadlines

If your spouse works in the business and receives W-2 wages or a share of self-employment income, they can participate in the Solo 401(k) with their own employee deferral and employer contribution. This potentially doubles the household contribution. Example: owner earns \$150,000 net SE income, contributes \$18,588 (employer) + \$23,500 (employee) = \$42,088. Spouse earns \$60,000 W-2 from the business, contributes up to \$15,000 (employer: 25% of \$60,000) + \$23,500 (employee) = \$38,500. Combined household Solo 401(k) contributions: \$80,588. For a SEP IRA with two participants, both would receive the same percentage of compensation — so at 20%, owner contributes \$30,000 and spouse contributes \$12,000 for a total of \$42,000. The Solo 401(k) doubles household contributions in this scenario. Deadline summary: SEP IRA — any time until tax filing deadline including extensions; Solo 401(k) plan must be established by December 31, but contributions can be made until tax filing deadline. For 2025 tax year, plan establishment deadline is December 31, 2025; contribution deadline is April 15, 2026, or October 15, 2026, with extension.

6

Choose based on entity structure and long-term plan

Sole proprietors and single-member LLCs taxed as sole props: use the Solo 401(k) below \$230,000 in net income, and consider Roth designations during lower-income startup years. S corp owners have a separate optimization layer: the right W-2 salary is often between \$40,000 and \$80,000 for moderate-income S corps, balancing payroll tax (which costs ~15.3% on wages) against the Solo 401(k) employer contribution capacity (25% of W-2). Example: S corp with \$200,000 profit, \$60,000 W-2 salary. Payroll tax on \$60,000 \approx \$9,180. Solo 401(k): employee deferral \$23,500 + employer 25% of \$60,000 = \$15,000; total \$38,500. Tax savings at 32% marginal rate: $\$38,500 \times 0.32 = \$12,320$. Net benefit: $\$12,320 - \$9,180$ (incremental payroll tax vs. taking \$60K as distribution) = depends on your full calculation, but typically the combination wins. If you have even one full-time W-2 employee besides a spouse, the Solo 401(k) is disqualified. Switch to a SEP IRA, a SIMPLE IRA, or a traditional 401(k) with a third-party administrator. Run the SIMPLE IRA numbers if you have employees: employer matches up to 3% of compensation or a 2% non-elective contribution, with simpler administration than a traditional 401(k).

3. Key Worksheets & Checklists

Use these worksheets with your actual Schedule C figures or W-2 wage plan. The comparison table makes the decision visible in 10 minutes. The deadlines checklist prevents the most expensive mistake — missing the December 31 Solo 401(k) establishment window and defaulting to a SEP IRA because you ran out of time.

SEP IRA vs Solo 401(k) Side-by-Side

| | |
|------------------------------------|---|
| 2025 annual limit | \$70,000 (same for both) |
| Contribution type | SEP: employer only (\approx 20% of net SE income). Solo 401k: employee deferral up to \$23,500 + employer profit-sharing up to 25% of W-2 or \approx 20% of net SE income. |
| Roth option | SEP: No. Solo 401k: Yes — employee deferral portion can be Roth. |
| Loan provision | SEP: No. Solo 401k: Yes — up to 50% of vested balance or \$50,000, whichever is less. |
| Employees allowed | SEP: Yes, but you must contribute same percentage for all eligible employees. Solo 401k: No full-time employees other than spouse. |
| Plan establishment deadline | SEP: Tax filing deadline (April or October). Solo 401k: December 31 of plan year. |
| Contribution deadline | Both: Tax filing deadline including extensions (October 15 for individuals). |
| Annual filing requirement | SEP: None. Solo 401k: Form 5500-EZ when assets exceed \$250,000. |
| Administration complexity | SEP: Very simple — no plan documents required beyond the IRS model. Solo 401k: Moderate — requires plan document, contribution tracking, Form 5500-EZ at \$250K+. |
| Best for | SEP: High-income self-employed (\$230K+ net SE income), those who want simplicity, or those who hire employees. Solo 401k: Most self-employed under \$230K |

net income who want maximum tax shelter and possibly Roth or loan features.

Contribution Calculator Worksheet

| | |
|--|--|
| Gross Schedule C revenue | Total self-employment income before any expenses. |
| Business expenses | All deductible expenses from Schedule C: supplies, software, home office, vehicle, health insurance (if not separately deducted), professional services. |
| Net Schedule C profit | Gross revenue minus business expenses. |
| SE tax (15.3% on first \$176,100; 2.9% above) | Net profit \times 0.9235 \times 0.153 (for income under SE tax wage base). |
| SE tax deduction (50% of SE tax) | SE tax \div 2. This reduces your adjusted gross income and your plan contribution base. |
| Net SE income for plan purposes | Net profit minus SE tax deduction. |
| SEP IRA maximum | Net SE income for plan purposes \times 0.20 (capped at \$70,000). |
| Solo 401(k) employer max | Same as SEP IRA maximum above. |
| Solo 401(k) employee deferral | Up to \$23,500 (or \$31,000 if age 50+), not to exceed net SE income for plan purposes. |
| Solo 401(k) total max | Employer max + employee deferral, capped at \$70,000 (or \$77,500 with catch-up). |

Decision and Deadline Checklist

- Calculate net SE income (or W-2 salary if S corp) before deciding which account maximizes contributions at your actual income level.
- If income is below \$230,000 net SE income and you have no non-spouse full-time employees: Solo 401(k) almost certainly allows larger contributions — open one before December 31.
- If income exceeds \$230,000 and simplicity matters: SEP IRA is defensible, but model whether a Solo 401(k) + Roth option adds value.
- Mark December 31 in your calendar as the Solo 401(k) plan establishment deadline. Set the reminder for October 1 so you have time to choose a provider and sign documents.
- If married and spouse works in the business: model spousal contributions to both plan types; the Solo 401(k) often doubles household deductions.
- If you are an S corp: model optimal W-2 salary at several levels (\$40K, \$60K, \$80K) to find the balance between payroll tax cost and Solo 401(k) employer contribution capacity.
- Once plan assets exceed \$250,000: file Form 5500-EZ by July 31 each year for the Solo 401(k).
- Rollover old 401(k) or traditional IRA balances into the Solo 401(k) to consolidate, improve investment options, and simplify RMD planning.

4. Common Mistakes

Defaulting to a SEP IRA because it is simpler without running the numbers

At \$80,000 net self-employment income, the Solo 401(k) allows roughly \$23,500 more in contributions than the SEP IRA in 2025 — because of the employee deferral layer. At a 24% federal marginal rate plus state taxes, that difference is worth \$5,600 to \$9,000 in immediate tax savings, and the additional invested amount compounds over decades. Running the comparison takes 20 minutes. Not running it is a recurring annual cost.

Missing the December 31 Solo 401(k) plan establishment deadline

The IRS requires the Solo 401(k) plan document to be signed and established by December 31 of the year for which you want to make contributions. Missing this by one day — even with the intention to open one — disqualifies the entire tax year. The SEP IRA's April or October deadline is much more forgiving. If it is late November and you have not established a Solo 401(k) yet, call a provider this week, not next month.

Hiring a non-spouse employee without removing the Solo 401(k)

The Solo 401(k) is only available to owner-only businesses (plus a spouse). If you hire a full-time employee who has worked 1,000 hours or more in a year and meets other eligibility criteria, you must either offer them plan participation or terminate the Solo 401(k) and switch to a SEP IRA or traditional 401(k). Failing to do this creates a disqualified plan — with retroactive taxes and penalties. Review eligibility rules before your second hire.

Using the wrong percentage formula for sole props vs S corps

The employer profit-sharing rate for a sole proprietor is approximately 20% of net SE income (after the SE tax deduction), not 25%. The 25% rate applies to W-2 wages in an S corp context. Using 25% for a sole prop overstates the contribution and creates an excess contribution — which carries a 10% excise tax per year it remains. Use IRS Publication 560 Worksheet 2 or a tax professional to verify the exact contribution before filing.

5. Next Steps

Pull your last Schedule C (or ask your accountant for net SE income after SE tax deduction) and fill in the contribution calculator worksheet above. If your net SE income is below \$230,000 and you do not have the Solo 401(k) yet, decide on a provider (Fidelity's self-directed Solo 401(k) is free to open and has no annual fees). If you are an S corp, ask your accountant to model three W-2 salary scenarios and calculate the combined payroll tax cost versus the incremental retirement account deduction at each level. For the Roth question: if your income is lower this year than it will be in five years, Roth deferral inside the Solo 401(k) is often the highest-value move available. Use the IRS COLA page each October to check updated contribution limits for the coming year, since limits typically adjust annually for inflation. For further reading, IRS Publication 560 (Retirement Plans for Small Business) covers both plan types in detail. The deadline calendar is simple: December 31 for plan establishment, and your tax filing deadline (with extensions) for contributions.

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