CASH BALANCE PLANS 2018

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HISTORY AND BASIC STRUCTURE OF A CASH BALANCE PLAN

- Started in 1985, approved prospectively by IRS in Pension Protection Act of 2006 (PPA), final regulations passed in October of 2014.

- A hypothetical account balance is established for each participant, as follows:

  Beginning Balance
  + Contribution Credits (usually defined as a percent of pay)
  + Interest Credits (defined in plan document, guaranteed interest)
  = Ending Balance

- Employer funded, pooled assets, trustee/advisor directed investments, required annual contributions.

- Payable as a lump sum at retirement or termination (annuities also available).

ADVANTAGES OF A CASH BALANCE PLAN

- Large tax deductions
- For the company, money contributed to the plan is tax deductible now.
- For participants, taxation on benefits is deferred until received as income.
- Accelerated retirement savings for Owners and Key employees
- Can vary contribution by owner
- Easy to understand, straight forward hypothetical account balance
- Employer's liability is easily defined

HOW CASH BALANCE PLANS CAN GROW AND STABILIZE YOUR BUSINESS

- Addition of new clients from new pool of prospects.
- Client retention increases (your competition may offer this).
- Enables you to have a greater menu of services and expertise.
- Helps differentiate yourself. Expands your referral network.
- Assets in Cash Balance plans can grow quickly. Not uncommon for annual required contributions to be greater than $200,000 per owner.
- Can provide large benefits for select employees (approximately $2.6m to $2.9m for each owner at retirement).

WHO IS AN IDEAL CANDIDATE FOR A CASH BALANCE PLAN?

- Businesses demonstrating consistent cash flow and profits
- Professional practices such as Doctors, Dentists, Attorneys
- Family Businesses
- Sole proprietorships (owners with younger employees, or any age if no employees)
- Partnerships with varying goals and needs among the partners
- Owners who desire to contribute more than $55,000 per year
- Companies already making a profit sharing contribution to their staff

HOW ARE INVESTMENTS HANDLED?

- Plan assets are pooled and invested by the trustees usually with an investment manager.
- Investment return does not affect the amount that is credited to participants' accounts.
- If the plan's investment earnings exceed the crediting rate, the excess will be used to reduce future employer contributions.
- Conversely, if the plan's investment earnings are less than the crediting rate, then future employer contributions will be increased.
- This make-up is typically spread over seven years.
- A wide range of investment vehicles can be used by the plan sponsor to achieve the interest crediting rate, which is usually set at 4% or 5%.

MAXIMUM CONTRIBUTIONS

Age	DC Plan 401k/Profit Sharing	DB Plan Cash Balance	DB + DC Plans*
65	$61,000	$259,500	$300,500
60	$61,000	$253,000	$294,000
55	$61,000	$196,700	$237,700
50	$61,000	$152,000	$193,000
45	$55,000	$117,800	$152,800
40	$55,000	$ 91,400	$126,400
35	$55,000	$ 71,000	$106,000

* Plans not covered by the PBGC (professional service employers with 25 or fewer employees – i.e. doctors, dentists, attorneys, etc). Maximum overall deduction limit is full DB plan contribution, plus DC plan contribution up to 6% of total pay (if DC plan contribution is greater than 6% of total pay, total of DB plan and DC plan contributions is limited to 31% of total pay).

EXAMPLE

Name	Age	Annual Salary	401(k)	Profit Sharing	Cash Balance	Total Contributions
				(6% of pay)	(40% of pay)	
Owner	60	$275,000	$24,500	$16,500	$110,000	$151,000
Spouse	55	50,000	24,500	3,000	20,000	47,500
Subtotal		**$325,000**	**$49,000**	**$19,500**	**$130,000**	**$198,500**
				(6% of pay)	(2% of pay)	
Employee 1	40	$50,000	$0	$3,000	$1,000	$4,000
Employee 2	35	40,000	0	2,400	800	3,200
Employee 3	30	30,000	0	1,800	600	2,400
Subtotal		**$120,000**	**$0**	**$7,200**	**$2,400**	**$9,600**
Total		**$445,000**	**$49,000**	**$26,700**	**$132,400**	**$208,100**

Percent of total contributions to owner and spouse (includes 401k) …… 95.4%

Q & A

→ How does a Cash Balance Plan work?

Answer: Each participant has an account which grows annually in two ways: first, a contribution and second, an interest credit, which is guaranteed rather than dependent on the plan's investment performance.

→ Can Cash Balance plans be offered in addition to 401(k) Profit Sharing plans or other plans?

Answer: Yes, the employer can offer a combination of qualified retirement plans in order to produce a larger contribution.

→ What are the distribution options upon retirement or if leaving the employer?

Answer: Any vested account in a Cash Balance Plan can be paid as a lump-sum distribution or annuity. Lump sums are usually rolled over to an IRA.

→ Must everyone participate equally in the Cash Balance plan?

Answer: No. Each participant can have a different amount contributed for them.

Q & A (continued)

→ Can Cash Balance contributions change?

Answer: Yes, but with restrictions. Cash Balance plans can be amended periodically to permit different contribution levels. Any changes must be made before any employee works 1,000 hours during a plan year. In addition, a plan can also be frozen or terminated.

→ Is the plan subject to IRS nondiscrimination testing?

Answer: Yes, like any other qualified plan, a Cash Balance Plan is subject to nondiscrimination testing. Employers can anticipate contributions in the range of 5% to 7.5% of pay for staff. The exact percentage required for employees depends on the results of nondiscrimination testing.

→ How do design and administrative costs compare with 401(k) Profit Sharing plans?

Answer: They are higher than a 401(k) plan because the plan is maintained by an actuary who needs to certify each year that the plan is in compliance with the Internal Revenue Code.

DISCLAIMER

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