

# Cash Balance Plans

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## 2024



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# How a Cash Balance Plan Works

Each participant has a hypothetical account balance which grows annually in two ways: first, a principal credit, which is a contribution usually defined as a percentage of pay, and second, an interest credit, which can be guaranteed rather than dependent on the plan's investment performance.

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



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.**





## Ideal Candidates 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 DC plan permits.
- ▶ 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 typically affect the amount that is credited to participants' hypothetical account balances.
- ▶ 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 (typically spread over up to fifteen 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

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Age	DC Plan 401k / Profit Sharing	DB Plan Cash Balance	DB + DC Plans*
65	\$76,500	\$329,900	\$381,100
60	\$76,500	\$318,400	\$369,600
55	\$76,500	\$248,200	\$299,400
50	\$76,500	\$193,500	\$244,700
45	\$69,000	\$150,900	\$194,600
40	\$69,000	\$117,700	\$161,400
35	\$69,000	\$ 91,900	\$135,600

- When a plan is not covered by the PBGC (such as professional service employers with 25 or fewer employees – i.e. doctors, dentists, attorneys, etc.) then there is a combined plan deduction limit which reduces the DC plan contributions permitted beyond the 401(k) salary deferral amounts. Generally, this limit is 6% of compensation, unless both plans' contributions total less than 31%. Therefore, the combined total may be less.

# EXAMPLE

Name	Age	Annual Salary	401(k)	Profit Sharing (6% of pay)	Cash Balance (40% of pay)	Total Contributions
Owner	60	\$345,000	\$30,500	\$20,700	\$138,000	\$189,200
Spouse	55	50,000	30,500	3,000	20,000	53,500
<b>Subtotal</b>		<b>\$395,000</b>	<b>\$61,000</b>	<b>\$23,700</b>	<b>\$158,000</b>	<b>\$242,700</b>
				(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
<b>Subtotal</b>		<b>\$120,000</b>	<b>\$0</b>	<b>\$7,200</b>	<b>\$2,400</b>	<b>\$9,600</b>
<b>Total</b>		<b>\$515,000</b>	<b>\$61,000</b>	<b>\$30,900</b>	<b>\$160,400</b>	<b>\$252,300</b>
Percent of total contributions to owner and spouse (includes 401k):						96.2%



# Q & A

**Can Cash Balance plans be offered in addition to 401(k) Profit Sharing 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 contribution level.

**Can Cash Balance contributions change?**

• **Answer:** Yes, but with restrictions. In addition, a plan can 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 annual nondiscrimination testing.

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

• **Answer:** They are higher because the plan is maintained by an actuary who certifies each year that the plan follows the Internal Revenue Code.

# Disclaimer

This information is of a general and informational nature and IS NOT INTENDED TO CONSTITUTE LEGAL OR TAX ADVICE. Rather, it is provided to inform you of current information about legislative, regulatory changes, and other information of interest.

The information is based on current interpretations of the law and is not guaranteed. Neither the company nor its representatives give legal or tax advice. Please consult your attorney or tax advisor for answers to specific questions.



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