



# Cash Balance Plan

- ◆ **Increased Tax Deduction**
- ◆ **More Predictable Results**
- ◆ **Higher benefit limits for owners and key employees**
- ◆ **Enables owner or partner to fund a plan that generates as much as \$195,000 in annual retirement income.**

**NOT FOR USE WITH THE PUBLIC**

## What are the Benefits of a Cash Balance Plan?

Traditional Defined Benefit Plans have always been appealing to owners of successful small businesses due to their ability to allow contributions that may be far in excess of those available under a Profit Sharing or 401(k) Plan. It is ideal for partners or owners who desire to contribute more than \$49,000 / year to their retirement account. A Cash Balance Plan has some features that appeal to small business owners:

### Maximize Contributions to Owners while Keeping Employee Contribution Costs Low

A Cash Balance arrangement uses special testing procedures to show that anti-discrimination rules are satisfied. This allows a “Tiered” formula to be used with the potential for the owners to be allocated up to the maximum in exchange for a modest contribution to other employees.

### More Equitable Benefit Accruals for Owners

Since accruals to owners participating in a Cash Balance Plan can be defined as a percentage of compensation (or a flat dollar amount), two owners can accrue benefits at the same rate, even if their ages are quite different. This may seem trivial, but it is quite difficult to accomplish with a traditional DB Plan.

- ◆ Higher Tax Deduction
- ◆ Maximize to Owners
- ◆ Same benefit to all owners
- ◆ Benefits easier to understand

### Add a Cash Balance Plan to an Existing 401(k)

A Cash Balance Plan works best when it is combined with a Tiered 401(k) Plan. So, a company that currently sponsors a 401(k) Plan can simply add a new Cash Balance Plan to their existing retirement program, without disrupting employee deferrals.

### Employee Benefits are Easier to Understand

Cash Balance Plan participant statements have a beginning and ending dollar-value balance. This allows participants to have a clear understanding of the current value of their benefit under the plan.

In a traditional Defined Benefit Plan, participants tend to not fully understand a benefit payable at retirement age and do not appreciate what the company is contributing on their behalf.

## Understanding Cash Balance Plans

Cash Balance Plans have been around for a number of years, but there had been a lack of guidance from IRS. The *Pension Protection Act* (“PPA”) passed in August of 2006, included provisions that removed this uncertainty for new Cash Balance Plans.

### A Cash Balance Plan is a type of a Defined Benefit Plan:

- ◆ Fixed contributions are credited to each participant at the end of each year.
- ◆ Employers can designate different benefit amounts for select employees such as owners and executives, subject to nondiscrimination testing.
- ◆ In addition, participants receive interest credits based on the interest rate defined in the plan. The credit is a fixed rate specified in the plan. Increases or decreases in the value of the plan’s investments do not directly affect the benefits promised to the participants. The investment risks and rewards are borne solely by the employer.
- ◆ The plan maintains a hypothetical account balance for each participant. When the participant retires, his benefit is the value of the hypothetical account. This lump sum value can be converted to a monthly pension at retirement.
- ◆ A Cash Balance plan is a Hybrid Plan. It appears to participants as a Defined Contribution Plan but is treated under the Internal Revenue Code as a Defined Benefit Plan. Participant statements look like a Defined Contribution Statement.

Cash Balance Plan  
Is equal to  
  
Pay Credit  
+  
Guaranteed interest credit

### Can a Cash Balance Plan be combined with a 401(k) Profit Sharing Plan?

To produce larger contributions, especially for Principals and Owners, Cash Balance Plans are usually combined with 401(k)/Profit Sharing Plans. The 401(k) and Profit Sharing component can also provide flexibility in the combined plan.

## How are investments in a Cash Balance plan managed?

The investment strategy for Cash Balance plans can differ greatly from a 401(k) plan. The plan liability values fluctuate only minimally with interest rates, so the costs, which typically are based on salary, are more predictable. In a Cash Balance Plan, the *interest crediting rate* (ICR) helps determine the participant's investment return on the cash balance account. The sponsor can seek to minimize plan volatility by structuring a portfolio with a return that matches the ICR as closely as possible.

Participants cannot direct the investments

- ◆ Assets in the plan are not allocated to participants. Participants cannot direct the investments. The pooled fund is invested by the Trustees and Investment Advisers.
- ◆ Since interest credit guarantees cannot exceed market rate of return, assets may be invested conservatively.
- ◆ The plan sponsor has the responsibility to fund the plan so that it meets the benefits promised in the plan.

Plan sponsor has responsibility to fund the plan to meet its benefits promised

- ◆ Over or Under performance may impact the plan's annual funding requirements. The selection of the investment option(s) is critical to achieve returns that may come closest to the plan's targeted rate of return.

### What are the other features of the Cash Balance Plan?

- ◆ When a participant becomes entitled to receive benefits under a cash balance plan, the benefits are defined in terms of an account balance.
- ◆ If a participant receives a lump sum distribution, that distribution generally can be rolled over into an Individual Retirement Account (IRA) or to another employer's plan if that plan accepts rollovers. This makes Cash Balance plans portable, therefore appealing to participants.

## Is a Cash Balance plan right for you?

A Cash Balance plan may not be appropriate for all small businesses and professional practices. For consistently profitable enterprises, however, it may provide great potential benefits. It is ideal for partners or owners who desire to contribute more than \$49,000 / year to their retirement account. Keep in mind the following considerations:

### **Mandatory annual contributions & participation required**

- ◆ Employers control the investment choices and bear the investment risk.
- ◆ Businesses and practices should have historically strong and consistent profit margins.
- ◆ 40% of employees must benefit from the Cash Balance Plan.
- ◆ There are non-discrimination rules in place for Cash Balance plans that may impact mandatory funding requirements.

Working with your Third Party Administrator, your CPA, and your Financial Advisor is key to ensure an accurate illustration and objective that might benefit you and your employees.

## Sample Cash Balance Plan illustration

This medical practice includes four partners, a partner's spouse and some employees. The chart illustrates how a 401(k) Profit Sharing Plan combined with a Cash Balance Plan can result in higher contributions to the partners and the spouse.<sup>1</sup>

|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        | Age                | Salary     | Cash Balance     | 401(K)    | Safe Harbor     | Profit Sharing  | Total Contribution |                             |                   |                                   |                  |                                               |                   |                                         |            |                            |                   |                               |                    |                        |                   |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------|------------|------------------|-----------|-----------------|-----------------|--------------------|-----------------------------|-------------------|-----------------------------------|------------------|-----------------------------------------------|-------------------|-----------------------------------------|------------|----------------------------|-------------------|-------------------------------|--------------------|------------------------|-------------------|
| <b>Group 1:</b> Partner 1                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              | 67                 | \$ 245,000 | \$190,000        | \$ 22,000 | \$ 7,350        | \$ 7,350        | \$ 226,700         |                             |                   |                                   |                  |                                               |                   |                                         |            |                            |                   |                               |                    |                        |                   |
| <b>Group 2:</b> Partner 2                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              | 53                 | \$ 245,000 | \$140,000        | \$ 22,000 | \$ 7,350        | \$ 7,350        | \$ 176,700         |                             |                   |                                   |                  |                                               |                   |                                         |            |                            |                   |                               |                    |                        |                   |
| <b>Group 3:</b> Partner 3                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              | 48                 | \$ 245,000 | \$ -             | \$ 16,500 | \$ 7,350        | \$ 7,350        | \$ 31,200          |                             |                   |                                   |                  |                                               |                   |                                         |            |                            |                   |                               |                    |                        |                   |
| <b>Group 4:</b> Partner 4                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              | 39                 | \$ 245,000 | \$ -             | \$ -      | \$ 7,350        | \$ 7,350        | \$ 14,700          |                             |                   |                                   |                  |                                               |                   |                                         |            |                            |                   |                               |                    |                        |                   |
| <b>Group 5:</b> Spouse of Partner 2                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    | 52                 | \$ 154,000 | \$ 75,000        | \$ 22,000 | \$ 4,620        | \$ 4,620        | \$ 106,240         |                             |                   |                                   |                  |                                               |                   |                                         |            |                            |                   |                               |                    |                        |                   |
| <b>Group 6:</b> 17 Employees                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           |                    | \$ 616,690 | \$ 12,334        | may vary  | \$18,501        | \$30,834        | \$ 61,669          |                             |                   |                                   |                  |                                               |                   |                                         |            |                            |                   |                               |                    |                        |                   |
| <b>TOTAL</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           |                    |            | <b>\$417,334</b> |           | <b>\$52,521</b> | <b>\$64,854</b> | <b>\$ 617,209</b>  |                             |                   |                                   |                  |                                               |                   |                                         |            |                            |                   |                               |                    |                        |                   |
| <table> <tr> <td><b>Total benefit Amount</b></td> <td><b>\$ 617,209</b></td> </tr> <tr> <td><b>Total benefit to employees</b></td> <td><b>\$ 61,669</b></td> </tr> <tr> <td><b>Total benefit to partners &amp; spouse</b></td> <td><b>\$ 555,540</b></td> </tr> <tr> <td><b>Percent to partners &amp; spouse</b></td> <td><b>90%</b></td> </tr> <tr> <td><b>Tax Savings (@ 45%)</b></td> <td><b>277,744.05</b></td> </tr> <tr> <td><b>Less Cost of Employees</b></td> <td><b>\$ (61,669)</b></td> </tr> <tr> <td><b>Net Tax Savings</b></td> <td><b>216,075.05</b></td> </tr> </table> |                    |            |                  |           |                 |                 |                    | <b>Total benefit Amount</b> | <b>\$ 617,209</b> | <b>Total benefit to employees</b> | <b>\$ 61,669</b> | <b>Total benefit to partners &amp; spouse</b> | <b>\$ 555,540</b> | <b>Percent to partners &amp; spouse</b> | <b>90%</b> | <b>Tax Savings (@ 45%)</b> | <b>277,744.05</b> | <b>Less Cost of Employees</b> | <b>\$ (61,669)</b> | <b>Net Tax Savings</b> | <b>216,075.05</b> |
| <b>Total benefit Amount</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                            | <b>\$ 617,209</b>  |            |                  |           |                 |                 |                    |                             |                   |                                   |                  |                                               |                   |                                         |            |                            |                   |                               |                    |                        |                   |
| <b>Total benefit to employees</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      | <b>\$ 61,669</b>   |            |                  |           |                 |                 |                    |                             |                   |                                   |                  |                                               |                   |                                         |            |                            |                   |                               |                    |                        |                   |
| <b>Total benefit to partners &amp; spouse</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          | <b>\$ 555,540</b>  |            |                  |           |                 |                 |                    |                             |                   |                                   |                  |                                               |                   |                                         |            |                            |                   |                               |                    |                        |                   |
| <b>Percent to partners &amp; spouse</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                | <b>90%</b>         |            |                  |           |                 |                 |                    |                             |                   |                                   |                  |                                               |                   |                                         |            |                            |                   |                               |                    |                        |                   |
| <b>Tax Savings (@ 45%)</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                             | <b>277,744.05</b>  |            |                  |           |                 |                 |                    |                             |                   |                                   |                  |                                               |                   |                                         |            |                            |                   |                               |                    |                        |                   |
| <b>Less Cost of Employees</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          | <b>\$ (61,669)</b> |            |                  |           |                 |                 |                    |                             |                   |                                   |                  |                                               |                   |                                         |            |                            |                   |                               |                    |                        |                   |
| <b>Net Tax Savings</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                 | <b>216,075.05</b>  |            |                  |           |                 |                 |                    |                             |                   |                                   |                  |                                               |                   |                                         |            |                            |                   |                               |                    |                        |                   |

<sup>1</sup>This hypothetical illustration represents a sample plan design using various actuarial assumptions and plan provisions, and is intended for illustrative purposes only. Consult with your TPA for a customized illustration based on your specific plan design(s) and/or employee demographics.



**Golden K Plans, Inc.** is a Third Party Administration firm specializing in the cutting-edge design, consultation and administration of all services necessary for the operation of qualified tax deferral plans.

We provide independent professional assistance to you, your accountant, attorney and investment advisor. One of the strongest areas of our services is that of "tailored" plans. We know that one size does not fit all, not in clothes, not in plans. We analyze the growth patterns, cash flow requirements, and tax situation of your business to develop a benefit package tailored to your unique needs.

The services we provide for our clients range from simple to very complex. Many of our clients want and appreciate simple plans that are cost efficient without sacrificing careful design, timely reports, and participant materials which are attractive and easy to understand.

We are particularly gratified that much of our business comes as referrals from existing clients, accountants, attorneys, and other professional advisors.

To request a proposal  
or to learn more about  
**The Cash Balance Plan**

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Cash Balance plan designs are complex and require the assistance of a Third Party Administrator. Additionally, Cash Balance plans require annual employer funding and they may not be suitable for some businesses. Certain restrictions and limitations will apply based on plan design and retirement plan rules, among other factors, which may affect tax deductions, funding levels and distribution of plan benefits.

This information cannot be used or relied upon for the purpose of avoiding IRS penalties. These materials are not intended to provide tax, accounting or legal advice. As with all matters of a tax or legal nature, you should consult your own tax or legal counsel for advice.