

# Cash balance plans



Wealth  
Management

Cash balance plans are one of the most popular, yet least known, options for a business owner to make large annual tax-advantaged contributions to their and their employee's retirement plans. The market has grown 15 times in the last 20 years. Cash balance plans account for nearly half of all defined benefit plans.\*

A cash balance plan is a type of IRS-qualified retirement plan known as a "hybrid" plan. In a cash balance plan, each participant has an account that grows annually in two ways: first, with an employer contribution and second, with an interest credit, which is specified in the plan document rather than dependent on the plan's investment performance as in a 401(k) profit sharing plan.

Annual contributions benefit owners and highly compensated employees the most, with a modest contribution to the non-highly compensated staff. The contributions for cash balance plans are calculated based on the employees' ages, compensation and employee classes. The employer decides the percent of contribution for each employee. Since this type of cash balance plan heavily favors the owners or key employees, it is almost always set up in combination with a 401(k) plan so that together they satisfy nondiscrimination requirements.

Cash balance plans work especially well where owners or key employees and some of the other employees are more advanced in age. They work best for a business with at least eight employees. The following is only one example of how a cash balance and 401(k) plan combination can benefit your company.

## Benefits for cash balance plans

1. Cash balance plans are a hybrid of the traditional defined benefit and defined contribution plans. The participant can see a hypothetical balance, the money is creditor protected and they can take the money with them when they retire.
2. Flexible investment options, from fixed rate crediting to actual rate of return.

## Ideal client profile

- Small business owner with a less than 10 to 1 ratio of employees to owners.
- Owner-only businesses
- Professional groups like lawyers, doctors, dentists, accountants, engineers and architects
- Family and closely held businesses
- Companies that have reached their max 401(k)/profit sharing funding limits, but are still looking for additional tax savings

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## Summary of contributions

Name	Age	Annual salary	401(k)	Profit sharing	Cash balance	Total contribution	Tax savings
2 owners							
Owner	68	\$330,000	\$30,000	\$43,500	\$365,426	\$438,926	\$197,517
Spouse	58	\$65,000	\$30,000	\$3,900	\$90,035	\$123,935	\$55,771
<b>Subtotals</b>		<b>\$395,000</b>	<b>\$60,000</b>	<b>\$47,400</b>	<b>\$455,461</b>	<b>\$562,861</b>	<b>\$253,287</b>
4 staff				7.5% of pay			
Employee 1	40	\$51,000		\$3,825	\$700	\$4,525	
Employee 2	33	\$41,000		\$3,075	\$700	\$3,775	
Employee 3	26	\$34,000		\$2,550	\$700	\$3,250	
Employee 4	43	\$21,000		\$1,575	\$700	\$2,275	
<b>Subtotals</b>		<b>\$147,000</b>	<b>\$0</b>	<b>\$11,025</b>	<b>\$2,800</b>	<b>\$13,825</b>	<b>\$6,221</b>
<b>Grand totals</b>		<b>\$542,000</b>	<b>\$60,000</b>	<b>\$58,425</b>	<b>\$458,261</b>	<b>\$576,686</b>	<b>\$259,509</b>
<b>Percent of contribution to owners</b>						<b>97.6%</b>	

## Summary of tax savings

Name	Age	Annual salary	401(k)	Profit sharing	Cash balance	Total contribution	Tax savings
2 owners							
Owner	62	\$330,000	\$30,000	\$19,800	\$341,904	\$391,704	\$176,267
Spouse	59	\$50,000	\$30,000	\$3,000	\$68,123	\$101,123	\$45,505
<b>Totals</b>		<b>\$380,000</b>	<b>\$60,000</b>	<b>\$22,800</b>	<b>\$410,027</b>	<b>\$492,827</b>	<b>\$221,772</b>