

The Cash Balance and 401(k) Plan Combination



Suitability Profile

- Profits far exceed salaries & expenses, consistently, for the foreseeable future
- Each owner able to take W2 salary of \$250,000+ annually
- Each owner's S-Corp distribution is \$250,000+ annually
- Owners need more than 401(k) alone plan can provide (\$73,500 each)
- Owners want to control the cost of benefits to non-owners
- Owners are having the Pension Discussion:age 50 or more.
 - We need an expense to offset earnings by about \$D annually for the next Y years...
 - Example:
D = \$350,000
Y = 10 years Or, \$350,000/yr. for 10 years
- Owner-only businesses
- Businesses with up to 15-20 employees
- Ideal census demographics
 - 2-3 employees for each owner
 - Owners 7-10 years older than employees on average

Disadvantages

The biggest disadvantage of the Cash Balance & 401(k) Plan Combination is the added cost of a second plan. However, there is some economy of scale, and the cash balance plan administration workload is much less than the 401(k) plan's workload. As a standalone plan, cash balance administrative fees are like a 401(k) plan \$3,000-\$7,000 per year depending on plan size and complexity. Asset-based fees will range between .5% and 2% of plan assets.

Advantages

Alluded to previously, the biggest advantage of the Cash Balance & 401(k) Plan combination is that it can generate the largest potential qualified plan allocations for owners, often exceeding \$150,000 per year. There is great ability to control the benefit-cost of non-owner allocations relative to owner allocations. Employers often appreciate the ancillary advantage of sheltering large asset pools from the claims of its creditors.

Cash Balance & 401(k) Combination Plan Allocations

The Cash Balance & 401(k) Plan combination relies on successfully passing a series of regulatory non-discrimination requirements. These arrangements work best for firms with owners 10 years older on average than non-owners. Owner benefits are typically minimized in the 401(k) Plan and maximized in the Cash Balance Plan. Non-owners typically benefit most in the 401(k) Plan.

2024 401(k) Limits

Employee Maximum	\$66,000
Employee 401(k)	\$22,500
Employee Catch-Up	\$7,500

Allocations

Profit Sharing 401(k) Plan Limits

The 401(k) plan allows both employer and employee contributions. The maximum annual contribution limit for an **employer** in any year is 25% of eligible payroll. The maximum annual contribution by an **employee** is 100% of pay up to a specific dollar amount that is indexed every year. Employees aged 50 or more years are allowed an additional catch-up contribution. The maximum amount of employer and employee contributions that can be allocated to any one individual is again, 100% of compensation up to a specific dollar amount that is indexed every year.

Cash Balance Plan Limits

The annual contribution is calculated by the plan's actuary is generally fully *tax-deductible*, i.e. offsets taxable earnings *dollar-for-dollar*.

Annual cash balance pension contributions are generally much larger than the Profit Sharing and 401(k) limits above. As a function of good plan design — especially for the first year — it's not always a good idea to allocate more to an owner that can be distributed as a lump sum under the limits. This year one maximum cash balance allocation by age is significant.

2024 Cash Balance Limits	
Age	Maximum Allocation
50	\$199,666
55	\$254,830
60	\$325,235
65	\$335,762

Cash Balance & 401(k) Combination Plan Case Study

To illustrate how the Cash Balance & 401(k) arrangement works, we examine a sample employer with the following characteristics:

- Established business
- S-Corporation
 - Two owners
 - Ages 55 and 50
 - Each owns 50%
 - Each owner able to take \$250,000+ in salary
 - Substantial earnings distributions to each owner in addition to salary
 - Owner compensation is consistent, predictable
- Five non-owners
- Business earnings are consistent, predictable
- Pension Discussion:
 - Owners need to offset earnings by about \$350,000

The Cash Balance and 401(k) Combination Plan										
Position	Age	W2 Pay	ER 3% Safe Harbor	EE 401(k)	EE Catch-Up	ER PS %	ER PS \$	ER CB %	ER CB \$	Total
Owner A	55	\$200,000	\$0	\$22,500	\$7,500	3.0%	\$6,000	60.0%	\$120,000	\$156,000
Owner B	50	\$200,000	\$0	\$22,500	\$7,500	3.0%	\$6,000	60.0%	\$120,000	\$156,000
Staff 1	50	\$65,000	\$1,950	\$0	\$0	3.0%	\$1,950	2.0%	\$1,300	\$5,200
Staff 2	55	\$40,000	\$1,200	\$0	\$0	3.0%	\$1,200	2.0%	\$800	\$3,200
Staff 3	35	\$30,000	\$900	\$0	\$0	3.0%	\$900	2.0%	\$600	\$2,400
Staff 4	30	\$25,000	\$750	\$0	\$0	3.0%	\$750	2.0%	\$500	\$2,000
Staff 5	25	\$20,000	\$600	\$0	\$0	3.0%	\$600	2.0%	\$400	\$1,600
									Owners	\$312,000
									Non-Owners	\$14,400
									Total	\$326,400
									% to Owners	96%

For illustrative purposes only.

ER 3% Safe Harbor = Employer's Safe Harbor contribution equals 3% of pay.

EE 401(k) = Employee's voluntary salary deferral contribution.

EE Catch-Up = Employee's voluntary salary deferral contribution if age 50+.

ER PS % = Employer's discretionary profit-sharing contribution expressed as a percent of pay.

ER PS \$ = Employer's discretionary profit-sharing contribution expressed as a dollar amount.

ER CB % = Employer's Cash Balance participant allocation expressed as a percent of pay.

ER CB \$ = Employer's Cash Balance participant allocation expressed as a dollar amount.

This chart shows employee census and compensation. In the 401(k) Plan, non-owners receive a total of 6% of pay in safe harbor and profit-sharing contributions ("ER 3% SH", "ER PS %", "ER PS \$"). The owners only receive a 3% of pay profit sharing allocation but are allowed to maximize their own salary deferrals ("EE 401(k)").

In the Cash Balance Plan, the non-owners receive a 2% of pay allocation ("ER CB%", "ER CB\$"). The total benefit to non-owners from both plans is 8%, a very competitive benefit indeed! The owners receive a 60% of pay allocation; and overall, 95% of the plan contributions attribute to the owners. Even though total Cash Balance Plan allocations are lower than the annual funding goal, the employer can fund the plan with an annual contribution that is slightly higher, bringing total annual contributions to the desired goal.

Cash Balance & 401(k) Combination Plan Case Study

How high is up?

Suppose the employer is even more profitable, and that the owners can pay themselves even larger salaries. The maximum earned income that can be recognized for plan purposes is indexed every year. Assuming the maximum allowed salary for each owner, the Cash Balance and 401(k) Combination achieves the largest potential qualified plan allocations for them. And, perhaps most compellingly, well over **90%** of the total contribution attributes to the owners.

The Cash Balance and 401(k) Combination Plan										
Position	Age	W2 Pay	ER 3% Safe Harbor	EE 401(k)	EE Catch-Up	ER PS %	ER PS \$	ER CB %	ER CB \$	Total
Owner A	55	\$330,000	\$0	\$22,500	\$7,500	3.0%	\$9,900	60.0%	\$198,000	\$237,900
Owner B	50	\$330,000	\$0	\$22,500	\$7,500	3.0%	\$9,900	60.0%	\$198,000	\$237,900
Staff 1	50	\$65,000	\$1,950	\$0	\$0	3.0%	\$1,950	2.0%	\$1,300	\$5,200
Staff 2	55	\$40,000	\$1,200	\$0	\$0	3.0%	\$1,200	2.0%	\$800	\$3,200
Staff 3	35	\$30,000	\$900	\$0	\$0	3.0%	\$900	2.0%	\$600	\$2,400
Staff 4	30	\$25,000	\$750	\$0	\$0	3.0%	\$750	2.0%	\$500	\$2,000
Staff 5	25	\$20,000	\$600	\$0	\$0	3.0%	\$600	2.0%	\$400	\$1,600

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ER CB %= Employer's Cash Balance participant allocation expressed as a percent of pay.

ER CB \$= Employer's Cash Balance participant allocation expressed as a dollar amount.

Owners	\$475,800
Non-Owners	\$14,400
Total	\$490,200
% to Owners	97%

If you're considering or need help with a qualified retirement plan, Manning & Napier has professionals on staff with decades of experience evaluating and implementing a wide range of plan designs. Contact your Manning & Napier representative today to learn more.