CASH BALANCE PLANS

Reduce Taxes with Cash Balance Plans

Understanding the Basics

Many business owners and partners of firms are looking for larger tax deductions and accelerated retirement savings. Cash balance plans may be the perfect solution for them. Below are the most common questions FuturePlan receives.

What is a cash balance plan?

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 a hypothetical account (separate from any defined contribution account) that represents each participant's accrued retirement benefit. The account 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.

How does a cash balance plan work?

The annual interest credit is specified in the plan document and is not directly dependent on the plan's investment performance as in a 401(k) profit sharing plan. The interest credit is usually a fixed rate of return of 4%. When participants terminate employment, they are eligible to receive the vested portion of their account balance as a lump-sum benefit.

How much can be contributed for me in a cash balance plan?

The employer contribution is determined by a formula specified in the plan document. It can be a percentage of pay or a flat dollar amount. **Below are the limits for 2025 by age group.**

2025 MAXIMUM CONTRIBUTION LIMITS

401(k), 401(k) with Profit Sharing and Cash Balance Plans					
Age	401(k) only	401(k) with Profit Sharing	Cash Balance	Total	Tax Savings*
66-70	$31,000	$77,500	$383,000	$460,500	$207,200
60-65	$31,000	$77,500	$342,000	$419,500	$188,700
55-59	$31,000	$77,500	$280,000	$357,500	$160,800
50-54	$31,000	$77,500	$218,000	$295,500	$132,900
45-49	$23,500	$70,000	$170,000	$240,000	$108,000
40-44	$23,500	$70,000	$132,000	$202,000	$90,900
35-39	$23,500	$70,000	$103,000	$173,000	$77,800
30-34	$23,500	$70,000	$81,000	$151,000	$67,900

***Important:** If you want to obtain your own, or your client's personalized scenario, please provide FuturePlan with a full, up-to-date owner and employee census in order to receive a customized plan design illustration. FuturePlan by Ascensus does not provide tax, legal, or accounting advice. This material has been prepared for informational and illustrative purposes only, and is not intended to provide, and should not be relied on for, tax, legal, or accounting advice. You or your client should consult your/their own tax, legal, and accounting advisors before engaging in any transaction. **FuturePlan by Ascensus provides plan design, administration, and compliance services. It is not a broker-dealer or an investment advisor and does not provide tax, legal, or accounting services. (SEE PAGE 4 FOR ADDITIONAL DISCLOSURES.)**

How are plan investments handled?

Plan assets are pooled and invested by the trustee or investment manager. If the plan's investment earnings exceed the rate specified in the plan document, the excess will be used to reduce future employer contributions. This will not affect the amount that is credited to the participants' accounts. Conversely, if the plan's investment earnings are less than the rate specified in the plan document, then future employer contributions will be increased.

The plan's minimum funding is typically spread out over 15 years, but can be made up sooner. A wide range of investment vehicles can be used by the plan sponsor to target the interest crediting rate that's specified in the plan document with the target rate usually specified in the investment policy for the cash balance plan as agreed upon with the plan's investment/financial advisor.

Can cash balance plans be offered in addition to 401(k) profit sharing plans or other plans?

Yes, the employer can offer a combination of qualified retirement plans in order to produce a larger contribution. In fact, in most cases, a 401(k) profit sharing plan in conjunction with a cash balance plan is necessary to produce the desired amount of owner and employee contributions.

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

Assuming the plan document permits lump-sum distributions, any vested account in a cash balance plan can be paid as a lump-sum distribution or annuity. An eligible rollover distribution paid as a lump-sum can be rolled over to an IRA or another qualified retirement plan. Not all lump-sum distributions are eligible for rollover (such as an RMD).

Can cash balance contributions change?

Yes, but with restrictions. Cash balance plans can be amended periodically to permit different contribution levels. Usually, any reductions must be made before any employee works 1,000 hours during a plan year. In addition, a plan can also be frozen or terminated. Certain 15- to 45-day notices are required to participants when benefits are reduced.

Must everyone participate equally in the cash balance plan?

No. Each participant can have a different amount contributed for them within a range of minimum meaningful benefits and IRS maximum benefits as outlined on page one in the contribution summary for how much can be contributed to a cash balance plan.

What about tax deductions and allocation of plan contributions for partnerships?

- Contributions made on behalf of non-partner employees are taken as a tax deduction on the partnership or corporate tax return.
- Contributions made on behalf of partners/owners are taken as a tax deduction on personal or corporate tax returns.

However, to be sure that the amount deducted for tax purposes by a partner (as shown on Schedule K-1) is the same as the amount contributed on behalf of the partner, the partnership's agreement must permit allocation method.

NOTE: Most partnerships that adopt cash balance plans do not want the partners' contributions allocated like most other firm expenses, in proportion to ownership. The partnership agreement or internal policy should assure each partner is allocated an appropriate share of the plan's cost.

Is the plan subject to IRS nondiscrimination testing?

Yes, like any other qualified retirement plan, a cash balance plan is subject to IRS nondiscrimination testing. Employers can anticipate contributions in the range of 5% to 7.5% of pay for staff if the owners or partners receive the maximum cash balance contribution. The exact percentage required for employees depends on the number of employees included in the plan and the results of nondiscrimination testing and may be more than 7.5% of pay.

How does the cost to set up and maintain a cash balance plan compare with the cost of a 401(k) profit sharing plan?

Although it may appear that cash balance plans are more expensive to set up and maintain than 401(k) profit sharing plans, cash balance plans are typically more cost-effective as measured by their expense as a percentage of annual contributions.

The legal contribution limits imposed on 401(k) profit sharing plans combined with fees to cover the high cost of plan administration, make 401(k) plans a more costly way to deliver retirement savings. Cash balance plans ultimately help employers and participants save more with significantly higher tax-deferred contribution limits and major tax deductions.

EXPERIENCE MATTERS

FuturePlan's Cash Balance Center of Excellence has been successfully designing and administrating cash balance plans for 36 years. As one of the country's leading cash balance plan administrators, we bring deep expertise and a multitude of options to the plan design table.

4,500+ cash balance plans serviced

470 credentialed retirement plan professionals

36 years of cash balance plan expertise**

60 on-staff actuaries

For additional information about cash balance plans, visit FuturePlan.com or call 866-929-2525.

*(Plan Limits) $23,500 for 401(k) plan; $7,500 catch-up (age 50 or older); $46,500 profit sharing. Amounts shown in the chart do not include the additional catch-up contributions for participants aged 60-63. This hypothetical chart assumes a 45% tax bracket of combined federal and state taxes and taxes are deferred. The following assumptions also apply:

- Maximum annual contribution amounts for the cash balance/defined benefit plan are calculated using 4% interest rates and assuming no pre-retirement mortality and using the latest available applicable mortality tables.
- The maximum cash balance amounts assume a 3-year average compensation of at least $280,000 (the maximum annuity limit for 2025), and prior years of service.
- The amounts needed to fund the cash balance/defined benefit plan may be reduced by a participant's prior highest 3-year salary history if it is less than the IRS maximum annuity limit (as shown above) or below the IRS maximum compensation limits under 401(a)(17) (e.g., $350,000 for 2025, $345,000 for 2024, etc.) and other deduction limits may apply.
- The amounts needed to fund in the cash balance/defined benefit plan will also be reduced if a participant participated in any prior cash balance/defined benefit plan of the employer or a related employer.
- Further, amounts shown may be reduced if the cash balance/defined benefit plan is not covered by the Pension Benefit Guaranty Corporation (PBGC), which may limit the amount available to fund in any paired 401(k) profit sharing plan of the employer. (Plans typically not covered by the PBGC are professional service businesses with fewer than 26 active participants.)
- It is also important to note that amounts shown are estimates and will vary depending on an employer's demographics of owners and employees along with a myriad of other factors and considerations.

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**As of 2025.

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