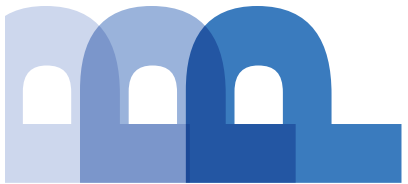
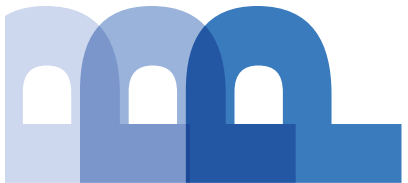
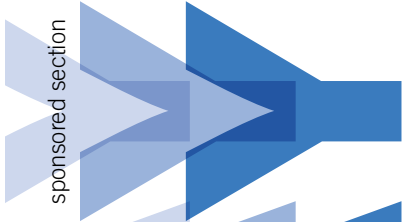




sponsored section



Cash balance emerges as a viable solution for many business owners

In a very short time, cash balance start-ups are becoming increasingly evident in the small- to mid-size corporate marketplace. The interest is driven by multiple factors: Joe Frustaglio, Vice President of Sales for Nationwide Financial’s private-sector retirement plans, calls the phenomenon a “triple play.” “We see it as a triple play, really, to use a baseball analogy—not only because it can be a win-win for all parties, but also because it’s an effective way for small-business owners to increase personal and employee retirement contributions, retain employees, and receive tax deductions.”



PLANSPONSOR talked to a panel of cash balance professionals on this emerging trend. Dan Kravitz is President of Louis Kravitz and Associates, Inc, a 70-person retirement plan administration and consulting firm based in Southern California; Laurence Balter is President of the Wailea Capital Group, an investment professional based in Wailea, Hawaii, and a Registered Representative with and securities offered through Linsco/Private Ledger, Member NASD/SIPC; Ron Renard is Director of Accounting at the law firm of Barger & Wolen, a 135-person law firm based in Los Angeles, which has added a cash balance plan; and Karen Eisenbach and Joe Frustaglio, both vice presidents in Nationwide's private-sector retirement plans group.

PS: Only a few short years ago, the interest in cash balance plans seemed stalled. What has changed so quickly?

Eisenbach: Many small-business owners defer putting money aside for retirement to help grow and support their businesses. As their businesses become more profitable and retirement draws nearer, many realize that they need to step up their retirement contributions. Cash balance plans enable small-business owners to invest more than their 401(k)s permit, ultimately helping them meet their retirement income needs.

Kravitz: Another driver is the tax-efficient retirement savings—it has become clear what a successful vehicle cash balance plans can be for business owners and partners, particularly for small professional services firms. Originally, they were used by large companies looking to convert their defined benefit [DB] plans into cash balance plans. This new interest is driven largely by smaller companies with existing 401(k) plans that are looking to save more money.

PS: How did the passage of the Pension Protection Act, PPA, change the status of cash balance plans?

Kravitz: It was obviously a very positive development. It represented a new beginning for cash balance plans as it statutorily recognized them, and eliminated the issue of age discrimination for new plans. It gave cash balance plans a new beginning.

Eisenbach: As Dan mentioned, the PPA provided clarity around cash balance plans. In addition to providing regulations around age discrimination, it eliminated the whipsaw calculation and established guidelines on conversions.

PS: Cash balance plans help business owners save more, but they're also a big plus in terms of retirement contributions for employees, right?

Kravitz: Absolutely, this is a classic win-win situation. A well-designed cash balance plan can be an effective savings vehicle for business owners and can increase retirement contributions for all employees. Data from the Profit Sharing/401(k) Council of America shows that the average contribution in a profit-sharing plan is 4% of compensation, but that can rise to 6% or higher when the employer sponsors a cash balance plan.

Frustaglio: The simplicity of the cash balance plan is a great benefit for the employee. Unlike a traditional defined contribution [DC] plan, the employees don't make contributions and they aren't required to make any investment decisions. The flexibility and portability of the plan is also appealing. Cash balance plans allow the employees to take their account balance in a lump sum and roll it into an IRA when they separate from service or retire. Employees also have the ability to annuitize. It's a very participant friendly option.

PS: The litigation we had in the space hasn't dampened this enthusiasm?

Kravitz: No, this is a very different phenomenon from the large-market DB-to-cash-balance conversions. We're creating brand-new cash balance plans—in situations where there was never a defined benefit plan—to increase retirement assets.

PS: Is there a profile for the type of company where a start-up cash balance plan makes the most sense?

Balter: From an investment professional's standpoint, you're looking for a business with consistent cash flows and profits, as it can make the required minimum contributions year after year. Another sign a company is a good candidate



From left: Kravitz, Balter, Renard, Eisenbach, and Frustaglio

“Cash balance plans combine the higher contribution limits of a DB plan with the flexibility and portability of a 401(k).”

is if the owners/partners are more than 40 years of age and need to catch up on their retirement savings and investments.

Kravitz: These plans make particular sense for professional services organizations like medical groups and law firms—in California, where my firm is located, at least half of these cash balance start-ups are, in fact, law firms. They were the pioneers, but any profitable professional services corporation is a good candidate, and so are the right types of manufacturing firms. If you are making profits, and have the disposable income, and are looking to invest additional money for retirement and receive tax deductions, these plans may make perfect sense.

PS: Ron, Barger & Wolen recently added a cash balance plan. Can you take us through that decision?

Renard: We had a 401(k) plan, but that was it. Our financial partner really went through this issue carefully with Dan, and it became very clear that the cash balance plan offered us several benefits. Our partners were highly interested in finding tax-advantaged vehicles in which they could invest and, at the same time, benefit the rank-and-file employees through increased profit-sharing decisions. Once the partners understood what the cash balance plan entailed, it was an easy decision. Certainly, one of the aspects of cash balance that appealed to us was our familiarity with our 401(k) plan and, thus, our familiarity with the DC-like aspects of cash balance. We also liked the fact that the firm could contribute at a level for partners that is suited for their financial circumstances, and that was certainly something that the newer and younger partners appreciated.

Balter: The thing that I try to get across to my clients is that these cash balance plans combine the higher contribution limits of a DB plan with the flexibility and portability of a 401(k). On top of that, the tax savings can help offset the funding and administration costs. There are very successful business owners who have nothing but their business itself to show for a lifetime of taking risk and working hard, and here we have a qualified plan that can allow an owner to save up to \$2.5 million by the age of 65. It's no surprise that we're seeing interest.

Kravitz: That speaks to the flexibility of the newest generation of cash balance plans—you can tailor contributions for different groups when you're creating the plan document. Their flexibility and familiarity is why they are becoming so popular.

PS: You've talked about the savings these plans

can generate. How has that played out, in a real-world example, at Barger & Wolen?

Renard: We've had our plan in existence now for about five years and, while the number of partners has varied over time, we now have about 34, and over that time we have amassed about \$8 million in the plan.

PS: Complex plans often come with surprises that happen down the road. Has anything about the cash balance plan at Barger & Wolen not gone as expected?

Renard: There have been no surprises—it has worked exactly as it was designed.

PS: How do you introduce a prospect to the idea of a cash balance plan?

Balter: The process should start with a business owner, and preferably a business that already has a 401(k) plan in place, and the appeal is always how much more that individual can invest. When you've demonstrated that, you begin the process of creating the plan architecture, and setting up the contribution levels, which will be a function of cash flow and of individual appetites for investing.

PS: It sounds like you really need an educated investment professional in this process?

Kravitz: Very much so—it is very important to have somebody like Laurence who can understand quickly whether a business merits a cash balance plan. There are a lot of choices to be made before you take your plan document to the IRS to get a favorable determination, so this is not a decision to be made lightly.

Balter: This is really an area where you have to earn your client's trust. The best way to do that is to build up real knowledge in the cash balance space, so you know whether it makes sense for a particular client and, if so, how best to execute the plan.

Frustaglio: If there were ever a role—and an opportunity—for the trusted investment professional to add value, this is it. It's one thing to design and implement a state-of-the-art 401(k) plan, but quite another to do the same thing with a cash balance plan.

PS: How do you typically structure the investment component of these plans?

Balter: The investment risk in these plans lies with the plan sponsor and, so, the natural tendency is to rely on conservative investments. My preference is to work with a group like Nationwide and use a variety of different instruments that will provide the desired risk-adjusted return. However, you want to be conservative in these

plans—you want to take as much investment risk out of the equation as you can.

Kravitz: What I see are equity exposures that max out at about 20% to 30%, but you also are beginning to see asset-allocated funds being used similar to those in 401(k) plans, although they are at the conservative end of the spectrum. As far as the individual participants are concerned, they should look at these plans as the risk-averse elements of their portfolios—if they want to take risk, they should take it in their 401(k) plans or other investments.

Renard: Certainly, we looked at the investment side of this very conservatively at Barger & Wolen: We are very heavily invested in bonds. We've diversified somewhat into CDs, however, and we are looking at other vehicles that may produce slightly better returns as well.

Eisenbach: What we've made available at Nationwide to support these plans is what we call our Retirement Innovator program, which offers a number of investment choices and service options, just as we do with 401(k) plans.

Kravitz: There is also some regulatory change pending in the form of final guidance on what is called the market rate of return—that will supersede the 30-year Treasury rate, which is now hovering around 5.25%. Depending on what is decided, it might give us some more flexibility when it comes to appropriate investment alternatives for these plans.

PS: [How does Nationwide regard these cash balance start-ups in terms of adding value to companies?](#)

Frustaglio: It is clear to us, as it should be now to everyone, that we're all living longer, and putting away enough money for retirement is more challenging than ever before. We're tremendously excited to support these plans, and make our small-business clients aware of how they can help them meet their retirement goals and help them grow their businesses by enhancing their employee-benefits package.

Kravitz: There is no question that these cash balance plans work best in tandem with a well-designed 401(k) plan—then, you have a very powerful retirement program that creates huge benefits for its participants. We are at the very beginning of what I think may well take certain small companies by storm—and, after all, the defined contribution plan was always meant to be a supplemental retirement plan, not the single source of retirement income that it has become. Its limits are just too substantial to be that single source, but that problem is dealt with if you add on a cash balance plan.

Frustaglio: Additionally, I would add that cash balance plans—with the help of a good investment professional and administrator—are relatively easy for the plan sponsor to establish and administer.

Kravitz: While there is a significant need for plan sponsors to consult a professional on the plan design, for the most part, these plans are easier to maintain than a 401(k) plan, as there are fewer moving parts. With 401(k) plans, contributions are made every pay period; in a cash balance plan, you're going to touch the plan a couple of times a year.

PS: [What choices do participants face at the back end of a cash balance plan?](#)

Kravitz: Like a 401(k) plan, you can simply roll the assets into an IRA. However, cash balance plans must give participants the ability to annuitize their assets. Every year, we produce a participant statement that tracks this amount, so everyone knows exactly where he or she stands.

Eisenbach: As more and more Americans face the risk of outliving their retirement assets, we feel that the annuity benefits associated with these plans will become more appealing to plan participants.

PS: [Any closing thoughts?](#)

Kravitz: The 401(k) plan and the cash balance plan do work best when they have a common investment professional and provider. I also would note that having a cash balance plan tends to quickly heighten the interest of the company and its employees in the retirement plan, and often that's not the case when all you have is the 401(k) plan.

Frustaglio: These plans are a great way for small businesses to offer a richer benefits package without the risks associated with a traditional pension product.

[Trust programs and trust services are offered by Nationwide Trust Company, FSB, a division of Nationwide Bank; Nationwide Investment Services Corporation, member FINRA. In Michigan only: Nationwide Investment Svcs. Corporation.](#)

[Investing involves market risk, including possible loss of principal. All guarantees and protections, where available, are subject to the claims-paying ability of the issuing insurance company.](#)

[Federal income tax laws are complex and subject to change. The information in this article 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 adviser for answers to specific questions.](#)

[To learn more about the benefits and risks associated with offering a cash balance plan, please call 1-800-626-3112 and select option 1.](#)

PNM-0832AO



Nationwide®
On Your Side