BPAS

Cash Balance Defined Benefit Plans

May 1, 2024

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BPAS Overview

retirement plan service provider since 1973

5,800 retirement plans 810,000 participants \$110 Billion trust assets	Ownership	Subsidiary of Community Bank System, Inc. (NYSE: CBU) Forbes: one of America's best banks 3,000+ employees and \$16B in assets
	Services	Workplace Retirement Plans Actuarial & Pension Healthcare Consulting IRA VEBA HRA Health & Welfare Plans Fiduciary Collective Investment Funds Fund Administration Institutional Trust
\$1.3 Trillion	Subsidiaries	BPAS Trust Company of Puerto Rico Global Trust Company Hand Benefits & Trust NRS Trust Product Administration





Why Save Pre-Tax?

Projected Value of Saving \$150,000 of Compensation Annually (5% annual investment returns)



- Pay income tax in same year compensation is earned, then save in after-tax vehicle
- Save pre-tax in a qualified plan, then pay tax at end of accumulation period
- Save pre-tax in qualified plan, leave accumulated value in tact
- Required/disciplined savings ensures that assets are set aside for retirement (i.e., not spent)
- Qualified retirement plans are protected from creditors





Save More than \$66,000 a Year







Retirement Program Components





Why Cash Balance Plans?

Cash Balance Plans are the most rapidly growing segment of retirement plans for 2 reasons:

Wealth Accumulation for Retirement

- Many small business owners have focused on building their business and not their retirement nest egg
- The \$66,000/\$73,500 contribution maximums in a 401(k) plan are not enough for those who started saving late
- Is selling business to fund retirement realistic?

Taxes

- Larger tax deferrals
- Potential for permanent tax savings (State specific)



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Similarities & Differences

DC Plan Similarities

- Hypothetical account for each participant
- Accounts grow annually based on contributions and interest credits
- Vesting schedule
- Account balance portable upon termination

Pension-Specific Differences

- Actuarial Calculations
- Benefit based on defined benefit formula
- Annuity benefit option
- EE benefits not affected by investment return
- Benefits may be guaranteed by (PBGC)





The Power of Cash Balance Plans

Maximum Service Credits for 2023

Age 62 NF	RA							
Maximum				Maximum			Maximum	
<u>Age</u>	Age <u>CB Credit</u> Age		<u>Age</u>	Age <u>CB Credit</u>		<u>Age</u>	<u>CB Credit</u>	
30	\$	70,000	42	\$	126,000	54	\$	229,000
31	\$	73,000	43	\$	133,000	55	\$	241,000
32	\$	77,000	44	\$	140,000	56	\$	253,000
33	\$	81,000	45	\$	147,000	57	\$	266,000
34	\$	85,000	46	\$	154,000	58	\$	280,000
35	\$	89,000	47	\$	162,000	59	\$	294,000
36	\$	94,000	48	\$	170,000	60	\$	309,000
37	\$	99,000	49	\$	179,000	61	\$	325,000
38	\$	104,000	50	\$	188,000	62	\$	342,000
39	\$	109,000	51	\$	198,000	63	\$	335,000
40	\$	114,000	52	\$	208,000	64	\$	328,000
41	\$	120,000	53	\$	218,000	65	\$	321,000
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Maximum Lump Sum \$ 3,419,043





Higher Contributions

Cash Balance Plan contributions are higher because:



It's a defined benefit (DB) pension plan



Statutory maximum is annual benefit at retirement (\$265,000 payable no earlier than age 62)

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Pre fit – max the maximum permitted accumulation is nearly \$3.42M

Maximum allowable contributions are those necessary to fund this maximum age 62 accumulation over a period of not less than 10 years





Higher Contributions <u>Higher Tax Deferrals</u>



A high wage earner in NYS with \$200,000 in tax-deferred savings will lower taxes by:

\$74,000 in Federal taxes deferred (top rate of 37%) \$13,700 in NYS taxes deferred (top rate of 6.85% - excludes "millionaire" tax)

\$1,800 in Obamacare Medicare taxes saved (0.9%)





Potential <u>Medicare Tax Savings</u>

Contributions made to a plan instead of paid as W-2 taxable compensation (e.g., owners in C-Corp "bonused out" at year-end)

Total tax reduction = \$95,300 – almost half!





deferrals
\$7,600 in permanent tax savings

• \$87,700 in tax

Retiring to a state without income tax turns state tax deferrals into permanent tax savings





What About the Existing Plan?

Cash Balance contributions are often *in addition to* maximum DC plan contributions

A 55-year-old could potentially get:

- Complicated tax deduction rules apply to small professional service employers (<25) and Owner-Only plans
- CB contribution of \$241,000
- plus the \$66,000 DC maximum
- *plus* \$7,500 in 401(k) catch-up contribution
- Total = \$314,500 *annually*





Plan Design Summary

EXAMPLE

Participant	Estimated Eligible Comp	401(k) Deferral	3% Safe Harbor	Profit Sharing	Cash Balance	Total Retirement	Current Design	Difference
Owner Age 55	330,000	30,000	-	43,500	241,000	314,500	73,500	241,000
NHCE Age 40	50,000	-	1,500	2,125	1,125	4,750	2,500	2,250
NHCE Age 30	35,000	-	1,050	1,488	788	3,325	1,750	1,575
NHCE Age 25	25,000	-	750	1,063	563	2,375	1,250	1,125
Grand Totals	440,000	30,000	3,300	48,175	243,475	324,950	79,000	245,950
		Own	er Percentage	of Owner Inv	ested Cost =	97%	93%	98%

Design Notes:

- Assumed current design to be safe harbor 401(k) with cross-tested profit sharing and 5% total contribution for employees.

- Owners will typically receive over 90% of total contribution dollars invested and often receive nearly all of the additional contribution dollars invested.

- If Owners will contribute 4.5% to 5% for employees to save \$66,000 to \$73,500 for themselves, why would they not contribute another 4.5% to 5% for employees to individually save an additional \$100K, \$150K, \$200K or more for themselves?

* If small professional services (doctor, lawyer, etc.) then combined plan deduction limit could prevent Owner from getting maximum profit sharing, which would be reduced to \$18,425 in the above example such that total Employer contributions to the DC plan are 6% of eligible payroll. Owner still gets approximately 97% of the total and 98% of the incremental difference.

Assumptions & Notes:

Cash balance interest crediting rate assumed 4% fixed

Actuarial conversion of cash balance using IRS mortality and 5%

Normal Retirement/Testing Age of 62





What's the Catch?



Qualified retirement plan

= complex IRS rules

- Coverage & nondiscrimination
- Maximum benefits
- Minimum eligibility, participation, and vesting



DOL (ERISA)

Reporting/Disclosure
 requirements



PBGC coverage & premiums, unless exempt

- (professional services < 25 plan participants and owner only)
- 2023 flat rate = \$96/ participant (plus variable rate premium if plan is under funded)

Point: need expert/specialist to administer





Cash Balance Plan Candidates











Owners that are relatively older than employees Owners with compensation at or near \$330,000 after funding.

Business cash flow is sufficient to fund the program for at least 3-5 years Owners are able to contribute 7.5% to 10% of pay for employees annually on a non-matching basis Owners max out the DC plan at \$66,000



CASH BALANCE PLAN

Investing Holistically

The Spectrum of Vehicles

			-		
	Totality of Vehicles	Cash Balance Plan	401(k) Plan	IRA	Outside of Tax Qualified Plans
Accumulations		Cap on Lump Sum	No Maximum Lump Sum	No Maximum Lump Sum	No Maximum Accumulation
Investment Options		Pooled Investments	Individual Direction Limited by Plan Options	Individual Direction with Some Statutory Restrictions	Individual Direction
Taxability		Distributio	Potential for Favorable Capital Gains Tax Treatment		
Common Investment Approach		·	Conservative	Aggressive	
Risk Seeking Assets	40-80%	20-50%	Depends on	Depends on Appetite for Risk	60-100%
Fixed Income	20-60%	50-80%	Appetite for Risk		0-40%





BPAS Expertise



Given the complexities of a combined CB/401(k), it is advantageous to have the same provider service both plans

BPAS Delivers

- BPAS Actuarial & Pension Services (APS): Provides expert Cash Balance services and coordinates interaction between plans
- **BPAS Workplace Retirement Plans (WRP):** Provides expert, flexible Defined Contribution services

One company. One call.





Let's Connect



Jason Disco

Senior Vice President, Pension Sales & Consulting BPAS Actuarial & Pension Services



Referring a Lead?

- Provide census information in Excel
- Provide information on corporate structure (e.g., C-Corp, S-Corp, Partnership, etc.), existing plan, if any, prospective client objectives, and any other relevant information



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Q&A Open Discussion

14