

How To Know if a “Cross-Tested” Retirement Plan is Right for Your Business

If you are a small business owner who is older and more highly compensated than your employees, you can maximize your share of company retirement plan contributions. Thanks to current laws, you can set up a Profit Sharing retirement plan that allows discretionary company contributions. The benefit to you: in leaner years you are not required to fund your retirement plan.

The Benefits of a New Comparability or Cross-Tested Plan

New comparability plans usually favor older, more highly compensated employees including the business owners. Contributions are allocated based on formulas that calculate benefits at retirement. (Don't worry, we do all the math!)

With a new comparability plan, employees get divided into groups based on plan sponsor funding objectives. Thanks to cross-testing, plans sponsors can provide different benefits to different groups. Typically, one group includes owner employees, who receive a larger benefit, and the other group includes non-owner employees, who receive a smaller benefit. While the benefit accrual rates differ, the design of these plans pass IRS general non-discrimination rules.

A typical “cross-tested” plan design incorporates a 401(k) feature and a 3% non-elective Safe Harbor contribution to maximize the owner and/or key employees' contributions.

The Benefits of an Age-Weighted Plan

Age-weighted retirement plans benefit older, more highly compensated employees. That is because your contributions are converted to equivalent benefits at retirement. Generally, older employees have less time to save for retirement but receive higher compensation than younger workers. But with an age-weighted plan, they can make larger contributions.

The Benefits of an Integrated Plan

Plans that are “integrated” with Social Security allow for higher contributions on wages above the Social Security wage base. These plans are generally best for young business owners who have high wages.



The Expertise you need. The Attention you deserve. The Creativity you want.

805 Broadway, Suite 600
Vancouver, Washington 98660
360.694.8409 | 360.696.2113 fax
www.pensionplanspecialists.com

Example: If you take a look at the following chart, you will see that each plan design scenario shows the same total owner contribution. By using alternative plan designs, the plan sponsor maintains the owner's contribution and reduces the cost to fund the plan by \$18,000.

Hypothetical Profit Sharing Design Scenarios						
Participant	Age	Eligible Compensation	Pro Rata Allocation %	Integrated Allocation %	Age-Weighted Allocation %	New Comparability Allocation %
Owner	55	\$250,000	\$50,000 (20%)	\$50,000 (20%)	\$50,000 (20%)	\$50,000 (20%)
EE 1	20	\$30,000	\$6,000 (20%)	\$5,023 (16.74%)	\$900 (3%)	\$1,500 (5%)
EE 2	55	\$30,000	\$6,000 (20%)	\$5,023 (16.74%)	\$6,000 (20%)	\$1,500 (5%)
EE 3	40	\$30,000	\$6,000 (20%)	\$5,023 (16.74%)	\$1,765 (5.88%)	\$1,500 (5%)
EE 4	30	\$30,000	\$6,000 (20%)	\$5,023 (16.74%)	\$900 (3%)	\$1,500 (5%)
TOTAL		\$340,000	\$74,000	\$70,093	\$59,565	\$56,000
% to Owner			67.57%	71.33%	85.37%	89.29%

Note: Cross-tested plans are sensitive to demographic changes. For Illustrative Purposes Only: Changes in the information will directly impact the results provided.

This information is written in connection with the promotion or marketing of the matter(s) addressed in this material. The information cannot be used or relied upon for the purpose of avoiding IRS penalties. These materials are not intended to provide tax, accounting or legal advice. As with all matters of a tax or legal nature, you should consult your own tax or legal counsel for advice.