



New Comparability 401(k) Plans

Is this the right plan design for your company sponsored plan?

The contributions in a retirement plan cannot discriminate in favor of owners and highly paid employees. How then can a new comparability plan enable companies to contribute the maximum allowed under law to the owner's account without doing the same for staff?

New comparability plans rely on "cross-testing" where benefit accrual rates rather than contribution amounts are used to prove nondiscrimination. The accrual rate is determined by taking the profit sharing contribution provided today, increasing it at an assumed interest rate until normal retirement age and then converting it into a monthly benefit. This process is done for each participant, whether 10 years or 40 years from normal retirement, and then all of the accrual rates are compared.

Example: A contribution today of \$2,548 to someone 38 years from retirement may seem unequal when compared to a \$36,500 contribution to someone 10 years from retirement, but if looked at as a benefit provided at normal retirement versus the current amount, the contributions today are more equivalent.

Suppose a \$36,500 contribution is made to a 55 year-old (Michael) with \$275,000 of wages. This will provide a retirement benefit of \$662.29 per month or an accrual rate of 2.89% of current monthly compensation at age 65. Also suppose a \$2,548 contribution is made to a 27 year-old (Tiffany) with \$52,000 of wages. This will provide a retirement benefit at age 65 of \$454.57 per month or an accrual rate of 10.49% of current monthly compensation. Without cross-testing, the comparison would be between the higher paid person (Michael) who received a 13% contribution ($\$36,500 \div \$275,000$) and the lower paid person (Tiffany) who received a 4.9% contribution ($\$2,548 \div \$52,000$), which would fail nondiscrimination testing. With cross-testing, the 27-year old is actually receiving a larger retirement benefit at age 65 as a percentage of current monthly compensation, so non-discrimination passes!

Name	Earnings	Att Age	Deferral		3% Safe Harbor	Profit Sharing		Catch Up	Total Contribution			
			Dollar	%	Dollar	Dollar	%	Dollar	Amount	% of Pay	Employer Cost	% of Total
Michael	275,000	55	18,500	6.7	8,250	28,250	10.27	6,000	61,000	22.2	61,000	84.52
Tiffany	52,000	27	1,040	2.00	1,560	988	1.90	0	3,588	6.90	2,548	3.53
Brad	34,000	48	680	2.00	1,020	646	1.90	0	2,346	6.90	1,666	2.31
Cathy	52,000	47	1,040	2.00	1,560	988	1.90	0	3,588	6.90	2,548	3.53
Doug	22,000	33	440	2.00	660	418	1.90	0	1,518	6.90	1,078	1.49
Ellen	36,000	49	720	2.00	1,080	684	1.90	0	2,484	6.90	1,764	2.44
Fran	32,000	39	640	2.00	960	608	1.90	0	2,208	6.90	1,568	2.17
Totals:	503,000		23,060		15,090	32,582		6,000	76,732		72,172	100.00