POLLARD & Associates
A Strongpoint Partner

A. One North Park Drive, Suite 104
Hunt Valley, MD 21030
T. 410.771.3035 / F. 410.771.3036
pollardpensions.com

Defined Benefit Plan Overview

Advantages

1. A Defined Benefit Plan (DBP) is a type of tax-qualified retirement plan that enables an employer to establish a retirement program that provides the following:
   - Guaranteed benefits
   - Annual contributions in excess of what is available through a Defined Contribution Plan (DCP) – currently $72,000 ($80,000 if the DCP includes a 401(k) feature and the individual is age 50 or older).

2. Maximum Annual Benefit, payable at Normal Retirement Age (NRA) is the lesser of $290,000 or 100% of highest 3-year consecutive average compensation, provided the individual will have a minimum of 10 years of plan participation at NRA. Benefit limit is pro-rated for years of participation less than 10 years. Contributions in excess of $300,000 per year can be generated (depending on age and income level), with a projected lump-sum at NRA of up to $3.7 Million.

3. This maximum benefit is available beginning with a NRA as early as age 62. Benefit payments before age 62 or before completion of 10 years in the plan must be actuarially reduced.

4. Maximum benefit is not reduced by prior accumulation in a DCP maintained by the same or related entity, as it was pre-2002. Therefore, a DBP can be adopted after years of maintaining a DCP without reducing projected DB benefits. Vice versa, after a DBP is fully funded, the employer can revert to a DCP for remaining years of employment.

5. Benefits payable at retirement are not required to be paid as an annuity (subject to spousal consent), but can be designed to allow equivalent lump-sum distributions or rollovers to an IRA.

6. DBPs can also be combined with a DCP depending on the overall retirement plan deduction limits available to the employer. Many employers maintain both a DBP and a 401(k), with the ability to contribute to both.

7. DBPs work very well for a one-person business entity or for entities with employees younger than owners/principals. DBPs can be adopted by both incorporated and unincorporated businesses. Therefore, self-employed individuals, Sub-S corporations and LLCs can maintain DBPs.

8. One-person DBPs are best combined with a one-person 401(k) to maximize deductions and flexibility.

9. Annual contributions must be within the available range of minimum and maximum amounts as calculated by the Plan’s Actuary; therefore contributions can be minimized in lower profitable years and maximized in more profitable years. Level annual contributions are not required as they are in a 412(i) Plan.

Disadvantages

1. Annual contributions are not as flexible as with a Profit Sharing Plan, but instead are tied to the plan's guaranteed benefits, fluctuation in market value of plan assets, and actuarial assumptions used to value benefits. The ability to generate the highest possible tax deductions results in loss of some flexibility.

2. The Plan must meet IRS's minimum annual funding obligations and is subject to an annual actuarial certification, which results in higher set up and ongoing administration costs than a typical DCP.

3. The Employer bears the full risk to guarantee benefits accrued by plan participants. If the plan funding is insufficient to meet plan benefit obligations at termination, the employer may either fully fund the plan or allow major shareholders/owners to waive benefits to funded levels.

4. If the Plan covers non-owner employees, it is subject to the Pension Benefit Guaranty Corporation (annual premiums and restrictions on plan termination) unless the employer is a small professional service corporation with less than 25 employees.

5. Funding maximums and annual deposit requirements are subject to change with legislation and IRS regulations.