

THE SUPER 401K PLAN™

&

THE SUPER 401K PLAN™ WITH THE PRIME OPTION

INTRODUCING THE



TAX RESERVE

**A TAX FREE RETIREMENT INCOME/LIFE INSURANCE BENEFIT
FULLY FUNDED BY TAX DEFERRALS**

**MAXIMUM TAX DEDUCTIBLE CONTRIBUTIONS
& BENEFITS FOR THE BUSINESS OWNER
AT THE
MINIMUM REQUIRED COST FOR OTHER PARTICIPANTS**



ABOUT FOX & LALONDE, LLC

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- ✓ **Fox & Lalonde, LLC**, is an independent, fee based third party administrator (TPA) providing consulting, design and administrative services to plan sponsors and their advisors across the United States.
- ✓ **F&L** does not sell any form of investment or insurance product nor will it render any form of investment advice.
- ✓ **F&L** principals, *John Lalonde* and *Bruce Fox*, each have over 30 years of experience in plan benefit and administrative services. John is a member of the WPI Educational Advisory Board.
- ✓ **F&L** plan designs are custom, actuarially certified and individually submitted as required to the appropriate governmental agencies in order to assure the highest possible owner's benefits at the lowest required cost.
- ✓ **F&L** provides comprehensive legal documentation, trust accounting, recordkeeping, benefit statements, plan reporting and governmental filings.



THE PURPOSE OF THIS PRESENTATION

WHY ARE WE HERE?

- ✓ **TO GIVE** YOU, THE ADVISOR, A COMPETITIVE ADVANTAGE
- ✓ **TO ASSIST** YOUR CLIENT ACCUMULATE AND PRESERVE WEALTH USING THE MAXIMUM FUNDING OPTIONS OF TAX QUALIFIED RETIREMENT PLANS WITH ALL ATTENDANT PLANNING, TAX AND COST EFFICIENCIES
- ✓ **TO FAMILIARIZE** YOU WITH AND/OR REINFORCE YOUR KNOWLEDGE OF THE PLAN DESIGN DYNAMICS THAT MAKE UP THE SUPER 401K PLAN™
- ✓ **TO BUILD** WORKING "PARTNERSHIPS" WITH PROFESSIONAL ADVISORS AND THEIR ORGANIZATIONS WITH A "HANDS-ON" TEAM MENTALITY
- ✓ **TO HELP** ADVISORS DEVELOP A NEW AND DYNAMIC PLANNING DIALOG WITH EXISTING CLIENTS, OTHER PROFESSIONALS AND PROSPECTIVE CLIENTS



GOOD PLAN DESIGN PRINCIPALS

THE GOLDEN RULE:

"GOOD" PLAN DESIGNS ALWAYS SATISFY 3 MAIN PRINCIPALS:

- Meets the client objectives
- Cost effective
- Easy to understand

WHAT IS THE BEST STARTING POINT FOR A "GOOD" DESIGN?

MAXIMIZE OWNER BENEFITS; DEFINE, CLASSIFY AND DISPLAY
OTHER KEY & HCE BENEFITS **AT THE REQUIRED MINIMUM COST**
FOR OTHER NHCE PARTICIPANTS – MODIFY IF NEEDED!



WHAT IS A SUPER 401K PLAN™ AND WHAT IS IT'S AUTHORITY?

- **THE SUPER 401K PLAN™** COMBINES A PENSION, PROFIT SHARING AND 401K PLAN i.e. "COMBO" PLANS
- THE **PENSION PROTECTION ACT OF 2006** (PPA)
 - *CHANGED* IRC §404(a)(7) i.e. 25% OF *COMP LIMIT*
- **IRS NOTICE 2007-28** CLARIFIED *DEDUCTION LIMITS* FOR COMBINED D/B AND D/C PLANS (PROFIT SHARING PLANS)
 - PBGC P/S PLANS ALLOW 25%
 - NON-PBGC PLANS ALLOW 6%

**THE SUPER 401K PLAN™ IS NOT A DB(k); DB(K) PLANS = NO P/S!
DB(k) PLANS WILL BE AVAILABLE IN 2010**



WHAT IS A PBGC PLAN?

- **PENSION BENEFIT GUARANTY CORPORATION (PBGC)**
- PBGC Termination Insurance covers D/B Plans that are not exempt
 - A plan established and maintained by a professional service employer *is exempt* that did not have, at any time since the enactment of ERISA, more than 25 active participants
- [ERISA § 4021(c)(2)] A *professional service employer* is a sole proprietorship, partnership, or corporation that is owned or controlled by professional individuals. A professional service individual includes, but is not limited to, physicians, dentists, chiropractors, osteopaths, optometrists, other licensed practitioners of the healing arts, attorneys at law, public accountants, engineers, architects, draftsmen, actuaries, psychologists, scientists, and performing artists.



THE SUPER 401K PLAN™

FIVE CONTRIBUTION COMPONENTS

1. **THE DEFINED BENEFIT PLAN** CAN BE FUNDED 100% IRC § 412(e)(3), Traditional or *Cash Balance*
2. **The PRIME** 401(h) Option Adds 33.33% to the Maximum Pension Contribution e.g. \$250K ACTUARIAL LIMIT TO \$333K
3. **THE 401(k) PLAN** CAN BE FUNDED 100%
4. **THE PROFIT SHARING** CAN BE FUNDED TO 100%
 - **DB plans covered by PBGC**; P/S plan can be funded up to maximum contribution (25% of eligible compensation)
 - **DB plans not covered by PBGC**; P/S plan can be funded up to 6% of eligible compensation regardless of DB contribution
5. **THE TAX RESERVE**, TAX FREE RETIREMENT INCOME/LIFE INSURANCE BENEFIT FUNDED 100% BY TAX DEFERRALS e.g. \$250K Plan Contribution = \$100K Tax Reserve



IMPORTANT TERMS

- ✓ **CASH BALANCE PENSION PLANS (C/B)**
- **"COMBINATION PLANS" e.g. PENSION C/B, D/B & P/S**
- **KEY EMPLOYEES** e.g. OFFICER @ \$160K; 1% OWNER @ \$150K
- **HIGHLY COMPENSATED EMPLOYEES (HCEs)** e.g.. \$110,000 IN 2009 vs. NHCEs i.e. NON-DISCRIMINATION RULES
- **TOP HEAVY (60% TO KEYS)** 3% TO 5% & **SAFE HARBOR** 3% to 4%
- **PBGC PLANS**
- ✓ **CROSS TESTING**
- ✓ **GATEWAY CONTRIBUTIONS**
- ✓ **"PRIME" BENEFITS**
- ✓ **THE TAX RESERVE**



WHAT IS A CASH BALANCE PLAN?

- A **Cash Balance Plan (C/B)** is a Type of Defined Benefit Pension
 - PPA 2006 Applicable Defined Benefit Plan – §411(a)(13)
“...a defined benefit plan under which the accrued benefit (or any portion thereof) is calculated as the balance of a hypothetical account maintained for the participant or as an accumulated percentage of the participant’s final average compensation.”
- CB Plans have Features of Both D/B Plans and D/C Plans (Hybrid)
- **Contributions to fund Retirement Benefits can exceed the combined 401(k) Profit Sharing Maximum of \$49,000 for 2009 PYEs**
- **Actuarially Determined Benefit = Age Relevant Contribution**
Sample Contributions C/B Only:
 - **Age 42 = \$ 70,000**
 - **Age 52 = \$120,000**
 - **Age 62 = \$215,000**



CASH BALANCE PLAN FUNDAMENTALS

- Participants have ***Hypothetical Accounts*** expressed in \$\$\$\$
- It looks like an old fashioned savings account e.g. \$500 or \$1,000
Deposits plus % Postings
- Accounts are credited with:
 - Employer Annual Contribution Credit e.g. \$1,000
 - Annual Interest Credit e.g. 5% = \$50
- Retirement Value is a Lump Sum, the Cash Balance
For Example, \$1,000/ Year @ 5% over 40 years = \$126,190
- **Benefits** are more *easily understood* by the participant
 - Participant receives an annual statement that shows an account balance
- **Costs** are *Understandable* by the Plan Sponsor



CROSS TESTING & GATEWAY CONTRIBUTIONS

- **CROSS TESTING** one plan with another establishes that the benefits at retirement from both plans are essentially “equal in value” at the plan’s normal retirement age. Cross Testing requires that a number of individual nondiscrimination tests be included in the process.
- **The Key to the Super 401(k) Plan™ Design** using the CB Plan or otherwise is “cross-testing” with the accompanying profit sharing plan.
- **The Super 401(k) Plan™ must satisfy the minimum allocation Gateway.** This requirement is met if each NHCE’s combined normal allocation rate (*i.e.*, the sum of the NHCE’s allocation rate under the DC plan and the NHCE’s equivalent allocation rate under the DB plan) is not less than a minimum percentage, based on the highest HCE rate.
- **If the DB plan is designed to fund for maximum benefits for owners, then this Gateway percentage is usually 7.5% of pay.**



Annual Compliance Testing and Government Reporting

- Monitoring of Qualification requirements (§401).
- Contribution deductibility calculations (§404).
- Minimum Participation and Coverage testing (§410)
- Monitoring of Minimum Vesting Standards (§411).
- Monitor compliance with Definitions and Special Rules (§414)
- **Annual addition of benefits and allocations testing (§415).**
- **Top heavy testing (§416).**
- **ADP/ACP testing (applicable to 401(k) plans).**
- Preparation of DOL/IRS Form 5500 and related schedules.
- Preparation of Summary Annual Report for participants.
- Preparation of appropriate PBGC form (for defined benefit plans only).

The GATEWAY CONTRIBUTION @ 7.5% DOES TRIPLE DUTY

- **Safe Harbor P/S @ 3%**
- **Top Heavy @ 5% (Combo Plans)**
- **The Gateway @ 7.5%**



WHAT IS A SUPER 401K PLAN™ Plus “PRIME” OPTION?

- THE **POST RETIREMENT INDIVIDUAL MEDICAL EXPENSE** BENEFIT
- **PRIME BENEFITS** ARE AUTHORIZED UNDER IRC § 401(h)
 - A 401(h) account is a separate fund, or account, of a pension plan to which plan sponsors may contribute funds to be used **exclusively** for retiree health benefits.
 - 401(h) contributions are limited to 25% of the total pension contribution and are in addition to the cost of retirement benefits; the effective add-on contribution is 33.33%
 - 401(h) benefits are *tax deductible* subject to Final Regs Sec.404(a)(3)(f)(2); fully *tax deferred* and payouts are *tax free* under IRC Sec. 105 or 106.
 - 401(h) tax deductible contributions, as allocated, are subject to the annual addition limit for Key Employees and HCEs (\$49,000 in 2009)
 - 401(h) benefits vest at the NRD for employees who go on pay status; employee/participants leaving prior to NRD forfeit 100% of their benefit
- **IRC § 401(h) FUNDS NOT USED FOR BENEFITS REVERT TO THE COMPANY**



WHAT IS THE TAX RESERVE?

- **The Tax Reserve** is the net A/T tax benefit produced by the tax deductibility of a qualified retirement plan contribution less A/T plan costs. For example: a plan contribution of \$100,000 @ a 40% tax bracket reduces current tax by \$40,000; if the plan has \$10,000 in A/T EE and administrative costs, the Tax Reserve equals \$30,000.
- **The Tax Reserve is 100% Tax Deferrals.**
- **The Tax Reserve** is an asset that needs to be invested. Life Insurance is the preferred repository.
- **The Tax Reserve** resolves the issues of having life insurance in the qualified plan i.e. discrimination; the insured; roll-out; estate planning, etc.
- **The Tax Reserve** utilizes the tax characteristics of life insurance to make it the ideal repository for Tax Reserve contributions:
 - **Tax deferred earnings, tax free withdrawals & loans converted to income**
 - **Tax free income to beneficiaries**
 - **The Life Insurance can fund any business, personal or charitable intent**



CASE STUDY #1: Small Plan

| | COMP | CB | P/S | 401(k) | 401(h) | TOTAL |
|------------|-----------|------------------|-----------------|-----------------|-----------------|------------------|
| Owner | \$245,000 | \$215,000 | \$12,250 | \$22,000 | \$20,250 | \$269,500 |
| Spouse | 50,000 | <u>0*</u> | <u>2,500</u> | <u>22,000</u> | <u>0</u> | <u>24,500</u> |
| S/T | | \$215,000 | \$14,750 | \$44,000 | \$20,250 | \$294,000 |

- Excluded for testing purposes

| | | | | | | |
|-------------|-----------|---------------|---------------|--------------|---------------|---------------|
| HCE | 120,000 | 7,500 | 6,000 | 16,500 | 2,500 | 32,500 |
| EE1 | 30,000 | 2,500 | 2,250 | 0 | 825 | 5,575 |
| EE2 | 25,000 | 500 | 1,875 | 0 | 150 | 2,525 |
| EE3 | 25,000 | 500 | 1,875 | 0 | 150 | 2,525 |
| EE4 | 50,000 | <u>0</u> | <u>3,760</u> | <u>6,000</u> | <u>0</u> | <u>9,760</u> |
| S/T | | 11,000 | 15,760 | 22,500 | 3,625 | 52,855 |
| Totals: | \$545,000 | \$226,000 | \$30,510 | \$66,500 | \$23,875 | \$346,855 |
| % To Owners | | 95.13% | 48.34% | | 84.82% | 84.76% |

Tax Savings to Owners: \$294,000 @ 37.1% = \$109,074

Tax Reserve = \$109,074 minus \$14,451 (A/T Cost of EEs + Administration)

THE TAX RESERVE CASE #1: Small Plan

A TAX FREE RETIREMENT INCOME/LIFE INSURANCE BENEFIT FULLY FUNDED BY TAX DEFERRALS (Actual Proposal Detail)

PLAN EXPENSES

| | |
|--------------------------------|--------------------|
| EE RETIREMENT CONTRIBUTIONS | \$26,760.00 |
| UNALLOCATED PRIME (401H) | <u>3,625.00</u> |
| TOTAL PLAN CONTRIBUTIONS | \$30,385.00 |
| INCOME TAX SUBSIDY (FED & ST)* | <u>(11,728.00)</u> |
| A/T EE CONTRIBUTION COST | \$18,657.00 |

| | |
|-----------------------------------|---------------------|
| SET-UP & ANNUAL ADMIN (4 PLANS) | \$ 6,240.00 |
| INCOME TAX SUBSIDY (FED & ST) | (2,315.00) |
| PAYROLL TAX SUBSIDY (\$280,385)** | <u>(8,131.00)</u> |
| A/T SET-UP & ANNUAL ADMIN | <u>\$(4,206.00)</u> |

| | |
|---------------------------|---------------------|
| A/T EE CONTRIBUTION COST | \$18,657.00 |
| A/T SET-UP & ANNUAL ADMIN | <u>\$(4,206.00)</u> |
| NET A/T PLAN EXPENSES | \$14,451.00 |

* Combined FIT + State Tax @ 37.1%

** Payroll Tax (ER+EE) @ 2.9%

INVESTMENT INTEREST RATE ASSUMPTION
PRE 6.5% POST 6.5%

ACTUARIAL RATE ASSUMED D/B 5.5%

OWNER CASH FLOW ANALYSIS

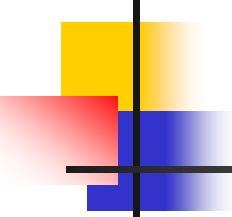
| | |
|-------------------------------|------------------|
| OWNER CASH – BEGINNING of YR. | \$294,000.00 |
| INCOME TAX SUBSIDY @ 37.1% | 109,074.00 |
| \$403,074 @ 6.5% | <u>26,200.00</u> |
| Sub-total Cash Inflows | \$429,274.00 |
| Less: Net A/T Plan Expenses | (14,451.00) |
| OWNER CASH – END of YEAR | \$414,823.00 |
| CASH FLOW RATE OF INCREASE | 41.1% |

OWNER PLAN BENEFITS

| | |
|---------------------------------------|--------------------|
| RETIREMENT @ 6.5% IN 10 YEARS | \$3,934,215 |
| PRIME @ 6.5% IN 10 YEARS | \$ 291,024 |
| <u>TAX RESERVE @ 6.5% IN 10 YEARS</u> | <u>\$1,359,880</u> |
| (\$109,074 - \$14,451 = \$94,623) | |

| | |
|-----------------------------|---------------------|
| TOTAL FV10 ALL BENEFITS | \$5,585,312 |
| AFTER TAX LIFE INCOME/YR | \$348,006.00 |
| TAX FREE PRIME/YR | <u>\$ 26,412.00</u> |
| TOTAL A/T INCOME SUPER 401K | \$374,418.00 |

| | |
|---------------------------------|---------------------|
| A/T LIFE INCOME w/o PLAN | \$279,061.00 |
| BENEFIT INCREASE w PLAN | 34.2% |



CASE STUDY #2: Medium Plan

Case History & Overview

- The total number of employees in this medical group is approximately 600, with about 450 who are older than age 21 and have 1 or more years of service with the plan sponsor
- There is an existing 401(k) with Match; it did not meet testing and partner 401(k) contributions had to be returned
- A \$1 million Annual Contribution; Partner's Share = \$0
- We added a P/S Plan and a C/B for Partners adding a NHCE base to the new plans cover non-discrimination issues; the “old” plan was left intact minus the Physician Partners
- The cash balance plan being a defined benefit plan has to cover a minimum number of eligible employees (IRC 401(a)(26))
- The minimum number of eligible employees that must be covered is the lesser of 40% of eligible employees or 50 employees



CASE STUDY #2: Medium Plan (continued)

| | CB Contrib. | P/S Contrib. |
|--------------------------|----------------------|--------------|
| Shareholder Doctors | | |
| Group1 (9 docs) | \$90,000 | \$ 5,558 |
| Group 2 (2 dos) | \$45,000 | \$ 2,779 |
| Group 3 (2 docs) | \$89,285 | \$ 6,350 |
| Group 4 (1 doc) | \$72,178 | \$20,826 |
| Total: | \$1,151,828 | \$89,106 |
| Other participants (64): | \$32,731 | \$94,789 |
| Shareholder Total: | \$1,240,934 (90.68%) | |

Tax Savings to Owners: \$1,335,723 @ 37.9% = \$506,239

Estimated After-tax Administrative & EE Costs = \$ 46,239

Tax Reserve Estimate = \$460,000/yr



Ideal Candidates for a Super 401k Plan™

Immediate 2009 Tax Benefits

- Owners/professionals seeking a higher contribution/tax deduction than the traditional 401k profit sharing maximum of \$49,000 (\$54,500 with Catch-up).
- Highly profitable companies of all types and sizes.
- Successful family businesses and closely-held businesses.
- CPA and law firms, medical groups and professional firms.
- Older owners who need to squeeze 20 years of retirement saving into 5 to 10 years.
- Owners/partners looking for a way to fund a buy-sell or stock redemption agreement on a tax deductible basis.
- Wealthy owners and professionals with charitable giving intentions stymied by the limitations on tax deductibility.



2009 Estimated Maximum Contributions*

| Age | 401k only | 401k P/S | Super 401k Plan™ |
|-------|-----------|----------|-----------------------|
| 60-65 | \$22,000 | \$54,500 | \$300,000 - \$450,000 |
| 55-59 | \$22,000 | \$54,500 | \$250,000 - \$325,000 |
| 50-54 | \$22,000 | \$54,500 | \$200,000 - \$275,000 |
| 45-49 | \$16,500 | \$46,000 | \$150,000 - \$225,000 |
| 40-44 | \$16,500 | \$46,000 | \$125,000 - \$200,000 |

* Inclusive of spousal benefits where applicable



QUESTIONS & PROPOSALS CONTACT US

THANK YOU FOR SHARING YOUR TIME
WITH US

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