

EGTRRA Retirement Planning Opportunities

Most of these ideas help owner-employees who want to increase their plan contributions and/or skew contribution more toward themselves.

1. **Lower the retirement age in your defined benefit plan to 62.** Prior to EGTRRA, a lowering of the retirement age also lowered the maximum benefit that could be funded, so it was self-defeating. After the 2001 tax changes, the reduction is no longer required, so the reduced retirement age can mean a much larger contribution can be made, tax-deductible, of course.
2. **One-person "maxed-out" defined benefit plans can now add a deferral plan (i.e. 401(k) plan) on top of whatever maximum defined benefit is being used currently.** There has always been a limit on deductions for employees with two plans, and there still is---but the EGTRRA excludes deferral plans from these limitations.
3. **So-called "412(i)" plans (named for a section of the Internal Revenue Code) offer the highest deductible contribution, and an extremely attractive plan design for older employee-owners with few (or no) other employees.** Under this IRC provision, the employer can use the guaranteed rates in insurance and annuity contracts (rather than a higher "market" rate) to figure out what it takes to fund the maximum allowable retirement benefit. As you know, using a lower rate in these calculations, means a higher contribution is necessary to fund the benefit, and this is the amount permitted by law if guaranteed contracts are used. (These insurance and annuity contracts still credit dividends at market rates, but the dividends are applied to reduce future contributions.)

This is great for Baby Boomers who are making high incomes and have realized it's time to start socking away as much as possible into qualified plans. It's also attractive for those who are gunshy of equities, and want to have a safer vehicle for retirement accumulation.

4. **"Simplest Idea" in EGTRRA---convert Money Purchase Pensions ("MPP") into Profit-Sharing Plans!** Until this year's changes, the maximum contribution to a profit-sharing plan was 15% of payroll. On the other hand, you could put 25% of payroll into a money purchase pension. However, the MPP required a fixed commitment with penalties and excise taxes for putting in anything other than the required, inflexible amount each year.

EGTRRA changed the profit-sharing limit to 25%, so now employers can get the 25% maximum without a fixed commitment and without exposure to those penalties and taxes. Profit-Sharing plans permit employer discretion every year and have a couple insurance advantages:

- (1) Participants can purchase life insurance on anyone in whom they have an insurable interest.
- (2) There are no limits on the amount of life insurance purchased if the participant has been in the plan for 5 years or more, or if the money utilized has been in the plan more than 2 years.

5. **Last idea for the New Year: "Safe Harbor" 401(k) plans can lower employer costs (under the right circumstances).** Safe Harbor 401(k) plans will no longer be considered top heavy after 2001, and this means that the minimum 3% contribution for rank-and-file employees is no longer required. Instead, they can offer a matching contribution (100% of the first 3% of pay plus 50% of the next 2%). This is great for those companies whose employees are unlikely to defer much (even with a match). In those cases, the employer will utilize the Safe Harbor matching and be able to sock away a lot without much contribution for employees.