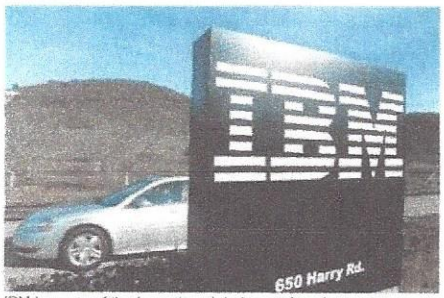
BenefitsPro

Cash balance plans on a tear



IBM has one of the largest cash balance plans in the nation. Photo: AP

Cash balance plans, while still a smaller part of the retirement world, are growing faster than all other account types, including 401(k)s.

There were 9,648 cash balance plans active in 2012 (the most recent year for which complete IRS data is available), up from 7,926 in 2011. This 22 percent increase was significantly higher than the 1 percent growth seen in 401(k)s in the same period.

Cash balance plans, also known as hybrid plans, have been rapidly replacing traditional defined benefit plans. They now make up 25 percent of all defined benefit plans, up from 3 percent in 2001, according to a report from the retirement-plan design firm Kravitz Inc.

The report, the 2014 National Cash Balance Research Report, found that the main engine for this accelerated growth came from small business with fewer than 100 employees. While large firms have been converting their defined benefit plans into cash balance plans as a way to cap their pension liabilities, small firms accounted for 87 percent of cash balance plans.

Also read: Average 401(k) Fidelity balance breaks record

The plans now have assets approaching $1 trillion. Companies contributed $31.2 billion to cash balance plans in 2012, for a total of $858 billion in cash balance assets nationwide.

Driving this growth are a combination of factors including rising taxes and broader options for plan sponsors.

More specifically, the report found that increasing federal, state and local tax rates have pushed many business owners to maximize tax-deferred retirement savings and take advantage of tax deductions for contributions to employee retirement accounts.

These plans also have a hybrid appeal, which combines the high contribution limits of a traditional defined benefit plan "with the flexibility and portability of a 401(k) plan," the report said.

Cash balance plans have also benefited from what the report said is "the boomer generation's lack of retirement preparedness," which is prompting older business owners to accelerate savings and maximize qualified plan contributions.

As recently as five years ago, many financial professionals were unaware of cash balance plans and what they provided. Today, "awareness is dramatically higher and growth has continued to accelerate," the report said.

All of this has promoted new growth that has soared since 2001, with double-digit annual growth and an increase of more than 600 percent in 12 years, the report said.

The states with the largest percentage of cash balance plans are New York and California, which account for 23 percent of all cash balance plans, while the fastest growth is happening in Texas and Florida.

When a cash balance plan is implemented, companies typically more than double contributions to employee retirement savings.

The average employer contribution to staff retirement accounts is 6.3 percent of pay in companies with both cash balance and 401(k) plans, compared with 2.6 percent of pay in firms with 401(k)s alone, according to the report.

Typically, cash balance plans require employers to contribute 5 percent to 8 percent of pay to non-highly compensated employees in order to contribute larger amounts for the owners. "This is often more than double the contribution employees receive at firms without cash balance plans," according to the report.

The largest firms offering these plans include IBM ($54.9 billion), AT&T ($45 billion) and Boeing ($28 billion).

Kravitz has been tracking the annual growth rate and related statistics on cash balance retirement plans since 2008. The company publishes an annual report analyzing comprehensive cash balance data from the most recent IRS Form 5500 filings.