Cash Balance Outlook 2015

September 17, 2015
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Kravitz Inc.
Martha Ophir, Marketing Manager

Goals

1. Give you a clear understanding of the Cash Balance market, present and future
2. Show you how to take advantage of Cash Balance growth
3. Empower you with tools and strategies to grow your business

Agenda

- 2015 Research Report: Highlights & Trends
- What’s Behind Record-setting Growth?
- Cash Balance + Small Business: A Love Story
- Succeeding With Cash Balance Plans
- What’s New: IRS Regulations and More
“Best of Both Worlds”

- Flexibility, Portability, Simplicity
- High Contribution Limits: $2.6 M
- Lifetime Benefit

Cash Balance

401(k)
Profit Sharing

Hybrid
Traditional Defined Benefit

401(k) Profit Sharing

High Contribution Limits: $2.6 M
Lifetime Benefit

Cash Balance

8th Annual Kravitz Research Report

Data analysis using:
- IRS Form 5500 filings, 2001-2013
- DOL - EBSA data
- PSCA Annual Survey

Growth Rate Doubles Projections

Projection based on current growth rates and industry data.
Growth Rate Soars Past 401(k) Plans

Cash Balance: 401(k):

32% 3%

Report Highlights

- The Cash Balance Plan market surged 32% while the 401(k) market increased only 3%
- Cash Balance Plans now make up over 28% of all defined benefit plans, up from 2.9% in 2001
- Small and mid-size businesses continue to drive Cash Balance growth: 89% of plans are in place at firms with fewer than 100 employees
- California and New York still have the most plans, but the fastest growth was in Minnesota and Florida

CB as % of all Defined Benefit Plans
CB Plans by Year Established

- Plans with an effective date prior to 1985 are traditional defined benefit plans that were later converted to Cash Balance. The first IRS-approved Cash Balance plan was established in 1983 by Bank of America.

Company Contribution to Employee Retirement Accounts

<table>
<thead>
<tr>
<th>Plan Type</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>401(k) only*</td>
<td>3%</td>
<td>2.2%</td>
<td>2.2%</td>
<td>2.4%</td>
<td>2.6%</td>
<td>2.8%</td>
</tr>
<tr>
<td>401(k) combined with a Cash Balance plan**</td>
<td>6.2%</td>
<td>5.8%</td>
<td>6%</td>
<td>6.2%</td>
<td>6.3%</td>
<td>6.3%</td>
</tr>
</tbody>
</table>

Company contributions as a percentage of eligible participants' total annual payroll.

Cash Balance Plans by Asset Size

Total assets in all Cash Balance plans nationwide:
- 9928 in 12,731 plans
- Annual contributions for 2013: $35.8 Billion
Cash Balance: Regional Concentration

<table>
<thead>
<tr>
<th>Rank</th>
<th>State</th>
<th>Number of Plans</th>
<th>Percent of Nation's Total</th>
<th>Percent Annual Increase*</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>CA</td>
<td>1,286</td>
<td>10%</td>
<td>36%</td>
</tr>
<tr>
<td>2</td>
<td>NY</td>
<td>1,261</td>
<td>10%</td>
<td>36%</td>
</tr>
<tr>
<td>3</td>
<td>IL</td>
<td>861</td>
<td>7%</td>
<td>29%</td>
</tr>
<tr>
<td>4</td>
<td>OH</td>
<td>854</td>
<td>7%</td>
<td>23%</td>
</tr>
<tr>
<td>5</td>
<td>MN</td>
<td>775</td>
<td>6%</td>
<td>21%</td>
</tr>
<tr>
<td>6</td>
<td>HI</td>
<td>735</td>
<td>6%</td>
<td>27%</td>
</tr>
<tr>
<td>7</td>
<td>FL</td>
<td>599</td>
<td>5%</td>
<td>26%</td>
</tr>
<tr>
<td>8</td>
<td>PA</td>
<td>569</td>
<td>4%</td>
<td>22%</td>
</tr>
<tr>
<td>9</td>
<td>MI</td>
<td>487</td>
<td>4%</td>
<td>20%</td>
</tr>
<tr>
<td>10</td>
<td>MN</td>
<td>426</td>
<td>3%</td>
<td>19%</td>
</tr>
</tbody>
</table>

National Total: 12,271

*Increase is total number of plans between 2012-2013, the most recent year for which complete data is available.

Why Is CB More Popular in Certain States?

- Medical "hubs"
- Higher Taxes
- Population & Age
- CB Champions

Top 7 States that Tax You the Hardest

1. California: 13.4%
2. New York: 8.8%
3. Oregon: 6.8%
4. Texas: 5.9%
5. New Jersey: 5.2%
6. Vermont & D.C.: 5.1%
7. Hawaii: 4.9%

Notes
What’s Driving Cash Balance Growth?

Key to CB Growth: Tax Environment

Understanding Tax Deductions

Above The Line Deductions
Most desirable type of deduction - Reduces AGI
- Qualified Retirement Plan Contributions

Below the Line Deductions
Many limitations - Subject to phaseouts.*
- Charitable Contributions
- State Tax
- Property Taxes
- Mortgage Interest

*subject to phase outs based on income > $250,000/single or > $300,000/married filing jointly
Summary of CB Tax Advantages

Advisor Handout

Client Handout

Retirement Savings Crisis

THE WALL STREET JOURNAL  YOUR MONEY

Retiring Boomers Find 401(k) Plans Fall Short
by J. R. Wilson

The 401(k) generation is beginning to retire, and it isn’t a pretty sight.
The retirement savings plans that many baby boomers thought would see them
through old age are falling short in many cases.
The median household headed by a person aged 60 to 62 with a 401(k)
account has less than one-quarter of what is needed in that account to
maintain its standard of living in retirement, according to data compiled by
the Federal Reserve and analyzed by the Center for Retirement Research at
Boston College for The Wall Street Journal. Even counting Social Security and any

Retirement Savings Crisis

- Longevity challenges: need 25-30 years of retirement income
- Many Boomers under-prepared
- Social Security viability issues, decline of traditional pensions
- Market losses and volatility
- Rising retiree healthcare costs
### Fastest Way to “Catch up”

#### 2015 Contribution Limits

<table>
<thead>
<tr>
<th>Age</th>
<th>Profit Sharing</th>
<th>Cash Balance</th>
<th>TOTAL</th>
<th>Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>50 - 55</td>
<td>$59,000</td>
<td>$242,000</td>
<td>$301,000</td>
<td>$120,000</td>
</tr>
<tr>
<td>55 - 59</td>
<td>$59,000</td>
<td>$195,000</td>
<td>$254,000</td>
<td>$101,000</td>
</tr>
<tr>
<td>50 - 54</td>
<td>$59,000</td>
<td>$140,000</td>
<td>$209,000</td>
<td>$80,000</td>
</tr>
<tr>
<td>45 - 50</td>
<td>$52,000</td>
<td>$114,000</td>
<td>$166,000</td>
<td>$66,000</td>
</tr>
<tr>
<td>40 - 44</td>
<td>$52,000</td>
<td>$87,000</td>
<td>$149,000</td>
<td>$56,000</td>
</tr>
<tr>
<td>35 - 39</td>
<td>$52,000</td>
<td>$66,000</td>
<td>$124,000</td>
<td>$47,000</td>
</tr>
<tr>
<td>30 - 34</td>
<td>$52,000</td>
<td>$51,000</td>
<td>$106,000</td>
<td>$41,600</td>
</tr>
</tbody>
</table>

Cash Balance lifetime limit: $2,600,000

*Assuming 40% tax bracket, taxes are deferred.

### The Rise of Cash Balance Plans

- Forbes
- The Wall Street Journal
- MarketWatch Retirement Plan
- LifeHealthPRO

Cash-balance plans grow

### A Perfect Storm

- Rising Taxes
- Retirement Savings Crisis
- Public Awareness, Media Coverage
- Legislative Changes
Both Sides of the Story

CB growth: driven by small business but also a popular choice for certain large firms and some Fortune 500 companies.

89% Have <100 Employees

<table>
<thead>
<tr>
<th>Participants</th>
<th>Number of Plans</th>
<th>Percent of Nation’s Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Over 10,000</td>
<td>253</td>
<td>2.0%</td>
</tr>
<tr>
<td>1,000 to 10,000</td>
<td>552</td>
<td>4.4%</td>
</tr>
<tr>
<td>100 to 999</td>
<td>549</td>
<td>4.3%</td>
</tr>
<tr>
<td>25 to 99</td>
<td>1,377</td>
<td>10.8%</td>
</tr>
<tr>
<td>10 to 24</td>
<td>2,900</td>
<td>22.8%</td>
</tr>
<tr>
<td>1 to 9</td>
<td>7,090</td>
<td>55.7%</td>
</tr>
<tr>
<td><strong>National Total</strong></td>
<td><strong>12,721</strong></td>
<td></td>
</tr>
</tbody>
</table>

Total participants in Cash Balance plans nationwide: 12.3 million

Why So Appealing to Small Business?

1. Cost efficiency and tax efficiency: ratio of owner/employee contributions works very well for small to mid-size firms
2. Age-weighted contribution limits: ideal for older owners who have sunk most assets into the business and are behind on retirement
3. Asset protection (for lawsuit or bankruptcy)
4. Attracting and retaining key employees (CB plans have greater appeal)
5. Succession planning for family businesses
Large Plans: Top 10 by Asset Size

Top 10 Plans Overall
1. AT&T       $50.79
2. IBM        $49.99
3. Boeing     $29.60
4. United Technologies $22.99
5. Halliburton $21.30
6. AbellioCare $19.68
7. Bank of America $19.49
8. Northrop Grumman $18.33
9. Honeywell International $17.39
10. JPM       $15.40

Top 10 Medical Group Plans
1. Kaiser Permanente $18.68
2. BlueCross BlueShield $18.40
3. Intermountain Healthcare $12.40
4. Shoots Healthcare $12.05
5. North Shore University Hospital $11.48
6. The Children’s Clinic Foundation $10.38
7. Brigham and Women’s Hospital $9.29
8. Memorial Hermann Health $9.20
9. Board of Trustees for Hospital Employees $9.18
10. MedStar Health Inc. $9.08

Top 10 Large Firm Plans
1. JPM       $22.36
2. Goldman Sachs Group $21.60
3. Morgan Lewis & Bockius $21.47
4. Jackson Lewis $18.34
5. Fulbright & Jaworski $15.92
6. Fulbright & Jaworski $15.92
7. Fulbright & Jaworski $15.92
8. Fulbright & Jaworski $15.92
9. Fulbright & Jaworski $15.92
10. O’Melia, Mazzetti & Halsey $15.92

Taking Advantage of CB Growth

You have the basic knowledge...
Now what?
5 tips to get started.

1. Focus on the Right Targets
NOT a mass market product like a 401(k):
Cash Balance is a "niche" product
Who is Ideal?

Business owners with income >$250,000 and consistent profit patterns

Who is Ideal?

Wealthy boomers who need to squeeze 20 years of retirement savings into 10 years

Who is Ideal?

Businesses with a New Comparability plan

Notes
Who is Ideal?

Professional services firms, including medical groups, CPAs, law firms and financial services

Who is Ideal?

Successful family businesses and closely held businesses

Who to avoid:

1. Unpredictable profit patterns
Who to avoid:

1. Unpredictable profit patterns
2. Won't give 5% of pay to employee retirement accounts
3. Multi-partner firms with high internal discord
4. Challenging demographics
2. Understand Plan Combinations

<table>
<thead>
<tr>
<th>Group 1: Owners</th>
<th>Owner 1</th>
<th>Owner 2</th>
<th>Owner 3</th>
<th>Owner 4</th>
</tr>
</thead>
<tbody>
<tr>
<td>Name</td>
<td>60</td>
<td>50</td>
<td>40</td>
<td>35</td>
</tr>
<tr>
<td>Age</td>
<td>$265,000</td>
<td>$265,000</td>
<td>$265,000</td>
<td>$265,000</td>
</tr>
<tr>
<td>Salary</td>
<td>$24,000</td>
<td>$24,000</td>
<td>$18,000</td>
<td>$18,000</td>
</tr>
<tr>
<td>401(k)</td>
<td>$35,000</td>
<td>$35,000</td>
<td>$35,000</td>
<td>$35,000</td>
</tr>
<tr>
<td>Contribution</td>
<td>$109,000</td>
<td>$109,000</td>
<td>$103,000</td>
<td>$103,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Group 2: Staff</th>
<th>Employee 1</th>
<th>Employee 2</th>
<th>Employee 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Name</td>
<td>50</td>
<td>50</td>
<td>65</td>
</tr>
<tr>
<td>Age</td>
<td>$165,000</td>
<td>$125,000</td>
<td>$80,000</td>
</tr>
<tr>
<td>Salary</td>
<td>3% of pay</td>
<td>3% of pay</td>
<td>5% of pay</td>
</tr>
<tr>
<td>401(k)</td>
<td>$4,950</td>
<td>$3,750</td>
<td>$4,000</td>
</tr>
<tr>
<td>Contribution</td>
<td>$4,950</td>
<td>$3,750</td>
<td>$5,000</td>
</tr>
</tbody>
</table>

Subtotals: $1,140,000 $0 $42,500 $18,000 $60,500

Grand Totals: $2,200,000 $84,000 $182,500 $218,000 $484,500

Percent of Contribution to Owners: 88%
3. Reach Out to Tax Advisors & CPAs

Many CPAs are **unaware** of Cash Balance Plans and are thrilled to find a major new deduction/deferral option for clients.

4. Sell the ‘Safe Money’ Story

Market volatility increases the appeal of Cash Balance Plans.

5. Partner with a CB Specialist

- Cash Balance Plans are highly technical and sophisticated
- Lack of experience can lead to failed IRS testing, lower benefits, missed opportunities
- Complex sale, long sales cycle – need a skilled partner
What's Ahead?

5 key factors impacting the CashBalance market in 2015:

- Market absorbing the impact of new 2014 CB regulations
- Growing awareness of the new ICR options and broader investment choices
- Continuing small business confidence
- Election year = no chance of tax reform impacting qualified plans
- Market volatility drives an increase Cash Balance popularity

Guaranteed Retirement Income Issue

- Annuity options and the 'safe money' aspect of Cash Balance plans = increasing popularity
CB Regulations Issued in 2010

Good news for Cash Balance Plan sponsors:
- Greater flexibility and simplicity
- Many more ICR options, including Actual Rate of Return
- Many funding issues minimized
- Increased awareness

2014 Final CB Regulations

- September 2014 - IRS finalizes Cash Balance regulations
- Allows for broader options for choosing Interest Crediting Rate (ICR)
- Key change: allows multiple investment options within a single CB plan

Impact: Shift in ICR Choices

<table>
<thead>
<tr>
<th>Interest Crediting Rate</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed Rate of Return</td>
<td>42.2%</td>
</tr>
<tr>
<td>30-Year Treasury Rate</td>
<td>29%</td>
</tr>
<tr>
<td>30-Year Treasury Rate with a Floor</td>
<td>20%</td>
</tr>
<tr>
<td>Actual Rate of Return</td>
<td>4.4%</td>
</tr>
<tr>
<td>Equity Indexed Rate</td>
<td>0.5%</td>
</tr>
<tr>
<td>Total</td>
<td>100.0%</td>
</tr>
</tbody>
</table>

*Note: chart includes all 550 clients, but 30% of KAVitz large plans (>100 employees) are now using Actual Rate of Return.
Shift in ICR Choices in the Larger Cash Balance Plan Market:

<table>
<thead>
<tr>
<th>Interest Crediting Rate</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>30 Year Treasury Rate</td>
<td>42.9%</td>
</tr>
<tr>
<td>Actual Rate of Return</td>
<td>28.6%</td>
</tr>
<tr>
<td>Fixed Rate of Return</td>
<td>19.0%</td>
</tr>
<tr>
<td>30 Year Treasury Rate with a Floor</td>
<td>9.5%</td>
</tr>
<tr>
<td>100.0%</td>
<td></td>
</tr>
</tbody>
</table>

Interest Crediting Rate Flexibility

- Safe Harbor Rates such as 30 Year Treasury Rate
- Investment Based Rates, a diversified mutual fund
- Fixed Rate up to 6%
- Actual Return of Plan Assets, portfolio must be diversified

How Actual Rate of Return Works

ICR = Actual rate of return on plan assets

Requirement: assets must be "diversified so as to minimize the volatility of returns."

Acceptable: a mix of bonds and equities

Unacceptable: assets exclusively in a sector fund
Understanding Actual Rate of Return

**Advantage**
Minimizes most of the underfunding and overfunding issues

**Disadvantages**
Impact of volatile returns needs to be managed
Preservation of Capital Rule

Preservation of Capital Rule

Participant payout can never be LESS than the sum of employer contributions.

Preservation of Capital Rule

**Example:**
- Employer contributes $1,000 for three years
- Negative return reduces participant account from $3,000 to $2,800

Participant receives the greater of:
(a) Account Balance or
(b) Sum of Employer Contributions

Payout to participant = $3,000
Popularity of Actual Rate of Return

30% of Kravitz large plan clients use Actual Rate of Return

An Unexpected Surprise

Actual Rate of Return With a Twist

Biggest change in the September 2014 Cash Balance Regulations:
IRS now allows for different investment strategies for various groups of participants within one Cash Balance plan.
Three Rules:
1. Diversification
2. Employer securities cannot be > 10%
3. Employer choice, not participant choice

Note: participant direction in Cash Balance plans is still ‘under review’ by the IRS.

Case Study

<table>
<thead>
<tr>
<th>Law Firm</th>
<th>Cash Balance</th>
<th>1. Senior Partners – Very Conservative</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>2. Mid-level Partners – Conservative</td>
</tr>
<tr>
<td></td>
<td></td>
<td>3. Junior Partners – Less Conservative</td>
</tr>
</tbody>
</table>

ICR Law Firm
Helpful Guide: Understanding ICRs

Understanding New ICR Options

Reliance Trust Cash Balance Collectives Series

New investment strategies for Cash Balance plans: 3 collectives targeting different points on the risk spectrum.

- 15% Ultra-conservative
- 25% Conservative
- 35% Moderate

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Cash Balance 2015 Predictions

1. Continued strong CB growth driven by tax climate, economy and awareness
2. Actual Rate of Return becomes even more popular
3. Large firms opt for "investment choice" Cash Balance plans
4. CB becomes a "must-have" for top medical/legal groups
5. CB assets surpass $1 Trillion, more investment products and income options will go to market

Cash Balance Innovation

Cash Balance market still very new, like the early days of 401(k). Opportunities and trends will include:
- Software innovations for plan design and actuarial work
- Participant technology, Daily Recordkeeping
- Investment and guaranteed income products

Daily Valuation & Participant Technology

- Taking Cash Balance out of the "black box"
- Participant-friendly technology
- 24/7 mobile access
Back Office Solutions for TPAs

Payden Kravitz Cash Balance Fund

Assets now close to $200M

How Can We Help?

Get a free plan design, connect with our Cash Balance community on social media:

(877) CB-Plans
www.CashBalanceDesign.com

@KravitzInc  LinkedIn
Cash Balance Consultants
Beyond the 401(k)

Order at Amazon.com
Free chapter at CashBalanceBook.com

Cash Balance Coach™ Certification

www.CashBalanceCoach.com
Fall session dates: Oct 6, 7, 13 & 15

Thank You!

www.CashBalanceDesign.com