

# Why Offer a Cash Balance Plan Instead of a Traditional Defined Benefit Plan?



Cash balance plans have proven to be an attractive alternative to traditional defined benefit plans for several key reasons.

By converting an existing defined benefit plan to a cash balance plan, the employer can avoid the need to terminate the defined benefit plan. Plan termination typically involves extensive actuarial calculations, government filings, and the need to purchase annuities to settle plan liabilities. The process usually generates significant fees from the plan's actuary, attorney and accountant.



## Reduce Costs

In addition, by converting a defined benefit plan to a cash balance plan, the employer is often able to reduce plan costs. Typically, traditional defined benefit plans are based on a participant's final average pay for a period just prior to retirement, whereas cash balance benefits are based on current salary so plan funding requirements are generally lower. In many cases, this restructuring of the benefits creates surplus assets or overfunding. This surplus can reduce or eliminate funding costs for a number of years.



## Flexibility

Furthermore, employees in today's workforce are increasingly more mobile. Cash balance plans have proven to be more attractive to short-term employees as they are structured to allow employees who terminate for any reason at any age to access their retirement monies upon termination. This allows employees to rollover their account balance to an IRA or to a new employer's qualified plan. Conversely, traditional defined benefit plans typically restrict access to retirement funds until employees reach retirement age, so depending on the participant's age at termination, their benefits could experience significant erosion over time, due to inflation.



## Greater Employee Appreciation

Since cash balance benefits are expressed in the form of an account balance, employees may feel more appreciative of the contributions being made on their behalf. The manner in which cash balance benefits are communicated is more straightforward and makes them easier to understand than in a traditional defined benefit plan. Beyond that, interest on an account balance is guaranteed, rather than dependent on the investment performance of an actual investment fund. The combination of these factors leads to greater employee understanding and appreciation of the retirement program with a lower employer cost.



## Conversion Advantages

The conversion of a defined benefit plan is especially advantageous where an employer maintains an overfunded defined benefit plan. In these cases, the defined benefit plan can be converted to a cash balance plan and the excess funds remaining in the plan can be used to fund the cash balance benefits. The period during which the excess funds are expected to cover annual normal costs is extended twofold by increasing the amount of excess assets and reducing the cost of annual accruals. In underfunded plans, a more positive funded status is created with lower annual normal costs.

Learn more about the Pentegra Cash Balance Advantage. For more information, contact the Pentegra Solutions Center at [solutions@pentegra.com](mailto:solutions@pentegra.com), or 855-549-6689.

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