SECURITY MUTUAL LIFE
The Company That Cares.®

Defined Benefit Plan
The "Next Level" in Retirement Planning

Unlike Profit Sharing 401(k) Plans, Defined Benefit Plans are not subject to a $58,000* individual allocation limit, nor is the employer tax-deductible contribution limited to only 25 percent of the "eligible compensation."

A Defined Benefit Plan is different from a Profit Sharing 401(k) Plan. That's because the retirement benefit is known (as a formula selected by the employer), and the necessary contribution is calculated to fund that benefit at "normal retirement age." By contrast, the profit sharing contribution is known, but the future retirement benefit will vary with investment performance.

A Defined Benefit Plan may include a pre-retirement survivor benefit funded by life insurance. The plan provides prudent flexibility in the choice of funding vehicles that may be used, allowing risk-averse individuals to choose guaranteed life insurance and annuity products. Plan trustees who have a higher level of risk tolerance may choose from other prudent products available for qualified plan investments.

Who Should Consider This Plan?

A Defined Benefit Plan will reward high-income, older participants (e.g., baby boomers will benefit far more than Generation X). Age is more important than salary when calculating the anticipated annual cost for the benefit because older individuals have fewer years to reach the assumed retirement age and benefit.

Making a Commitment

Unlike a Profit Sharing Plan, a Defined Benefit Plan must be funded each year. This means that even in a "bad year," the pension plan contribution must be made because the benefit is promised by the employer. The employer must fund for benefits that have been earned. Benefits typically are earned when a participant works the requisite number of hours defined in the plan document.

The stability of the employer is an important consideration. Because a Defined Benefit Plan is a fixed obligation and contributions are not discretionary, the sponsor should be profitable with stable earnings.

To make sure that each employee is guaranteed to receive a benefit, the federal government requires most Defined Benefit Plans to pay insurance premiums to the Pension Benefit Guaranty Corporation (PBGC).

The following example shows a sole owner, age 55, of an S-Corporation. He consistently earns more than the maximum IRS annual compensation limit of $290,000.*

Census Data			Contribution Amounts	
Position	Age	Salary Limit on Annual Compensation	Contribution	Survivor Benefit with Whole Life Insurance
Owner	55	$290,000	$320,913	$3,250,000

Retirement Benefits

The maximum benefit allowable in 2021 is 100 percent of compensation not to exceed $230,000 per year. This maximum amount is reduced if retirement occurs prior to age 62 or if the participant has fewer than ten years of participation in the Plan. The maximum benefit increases if retirement occurs after age 65.

Generally, the benefit is expressed in terms of monthly income at normal retirement age (e.g., $19,167 each month for a maximum plan). However, most small-business plans will offer a lump-sum option in lieu of a monthly benefit. In our prior example, this benefit is converted to a little more than $2 million, which may then be transferred to an IRA or successor Defined Contribution Plan. With all Defined Benefit Plans, the lump-sum limit is defined by IRC 415(b)(2).

Enhanced Survivor Benefits

A Defined Benefit Plan provides the plan sponsor flexibility in designing both the retirement and the income-tax-free survivor benefits.** Whole life and universal life insurance policies are permitted funding vehicles within the Defined Benefit Plan.

IRS rules limit the amount of life insurance that can be purchased. The premium must be less than 66 2/3 percent of the theoretical contribution that would be required under the individual level-premium funding method to fund benefits under the plan. The premium for universal life insurance cannot exceed 33 1/3 percent of the theoretical contribution. Another method is the "100 Xs Rule." This method allows the incidental life insurance benefit to be calculated as simply, 100 X the monthly projected retirement benefit.

Plan Administration

Before you can make contributions to a Defined Benefit Plan, a Plan and Trust must be established. The Plan must be adopted by the last day of the employer's tax year, with an **effective date** retroactive to the first day of that tax year, but not any earlier. Security Administrators, Inc. (SAI), a wholly owned subsidiary of Security Mutual Life Insurance Company of New York, can provide assistance at a competitive price.

Let Us Know How We Can Help You

*Internal Revenue Service (IRS) Limit for Defined Contribution Plans for 2021.

**The cash value minus the face amount is income tax free provided the participant reported the income benefit.

The hypothetical example shown within is for illustrative purposes only and does not guarantee or predict the results of any particular product. In preparing the example, we did not take into account the investment objectives, financial situation or particular needs of a specific person. The depicted strategy may not be suitable or appropriate to your individual circumstances. Accordingly, it does not constitute a personal recommendation to you.

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Product features and availability may vary by state.

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