



## Cash Balance Corner:

# “Complete Control” with Recommended Contributions

Welcome back to DWC’s Cash Balance Corner! If you’re joining us for the first time, our [Cash Balance Plans 101](#) is an FAQ that provides an overview. This and all subsequent editions of the Corner will use that as a foundation to build from. Where applicable, we include links for easy access to resources with additional information or explanation. If you are not familiar with cash balance plans (or if you would like a quick refresher), please check out that FAQ first. So, let’s get started!

Congratulations on making it through our [last installment](#) and to this one. We typically do not like to get that deep into the weeds, but hey, this is actuarial stuff after all, and you can’t always get what you want. To make up for the complexity of determining the Minimum Required Contribution (MRC), we are going to discuss Recommended Contributions, which requires just one simple mathematics exercise – subtraction.

We learned last time that the minimum amount required to be contributed to a cash balance plan will almost always leave the assets below the promised benefits, i.e. the sum of the hypothetical account balances. For example, in the first year of Robert Smith Inc.’s plan, the contribution credit is \$100,000 and the MRC is only \$80,873. Contributing the minimum will keep the plan in compliance, but not fully funded. That is where the recommended contribution comes into play.

There is no IRS guidance that defines the recommended contribution. Rather, it is simply an amount that, when contributed, increases the plan assets to a level equal to the plan liabilities (hypothetical account balance). Another way of putting it is that the plan sponsor is funding to a termination liability – meaning if the plan terminated after the contribution, the plan would have enough assets to pay out all of the promised benefits.

Let’s look at a few examples. Robert’s annual contribution credit is \$100,000. Since there is no interest credit in the first year of the plan, the recommended contribution is \$100,000. Now let’s jump ahead a couple of years like we did for the MRC examples. At the end of year three, we know that the hypothetical account balance will be \$309,090. Below are examples of the recommended contribution amounts assuming that the recommended contribution was made in each of the first two years.

1. If the plan’s actual investment returns each year are exactly equal to 3% (the plan’s interest crediting rate), the recommended contribution is always equal to the contribution credit.

Investment Return = 3%	Assets at the Beginning of the Year	Investment Earnings	(a) Assets at the End of the Year	(b) Hypothetical Account Balance	(b) – (a) Recommended Contribution
Year 1	\$0	\$0	\$0	\$100,000	\$100,000
Year 2	100,000	3,000	103,000	203,000	100,000
Year 3	203,000	6,090	209,090	309,090	100,000

2. If actual returns are less than the 3% interest credit, the recommended contribution increases to make up for the lower earnings.

Investment Return = 0%	Assets at the Beginning of the Year	Investment Earnings	(a) Assets at the End of the Year	(b) Hypothetical Account Balance	(b) - (a) Recommended Contribution
Year 1	\$0	\$0	\$0	\$100,000	\$100,000
Year 2	100,000	0	100,000	203,000	103,000
Year 3	203,000	0	203,000	309,090	106,090

3. If actual returns are greater than the 3% interest credit, the recommended contribution decreases as the “extra” earnings help fund the contribution credit.

Investment Return = 6%	Assets at the Beginning of the Year	Investment Earnings	(a) Assets at the End of the Year	(b) Hypothetical Account Balance	(b) - (a) Recommended Contribution
Year 1	\$0	\$0	\$0	\$100,000	\$100,000
Year 2	100,000	6,000	106,000	203,000	97,000
Year 3	203,000	12,180	215,180	309,090	93,910

So, the goal of the Recommended Contribution is to make sure today’s assets equal today’s promised benefits.

See, we promised there would be limited math in this one! Rest up, though, because we will dive into the Maximum Deductible Contributions next time, and that means some weird rules and more math.



**Want to get articles just like this one delivered to your inbox?**

[Subscribe](#) to receive regular updates from the [DWC 401\(k\) Q&A blog](#).

Helpful insights without the junk, delivered on your schedule.