Karel - Gordon & Associates

PENSION CONSULTANTS, PLAN ADMINISTRATORS AND ACTUARIES

Advisor Connect | Why Permitted Disparity Matters

MAKING IT ACTIONABLE

There are many ways to distribute a company's profit sharing contribution. It may be as straightforward as a proportional—"pro rata"—share to each eligible participant or it can be based on a formula that considers other factors such as age.

A simple formula might allocate 3% of compensation to all eligible employees. Participants share on a pro rata basis. However, the most simple option isn't always the most effective option.

A company might ask...

Q: Can my company include the contributions we make to social security as a factor in our formula?

A: Yes!

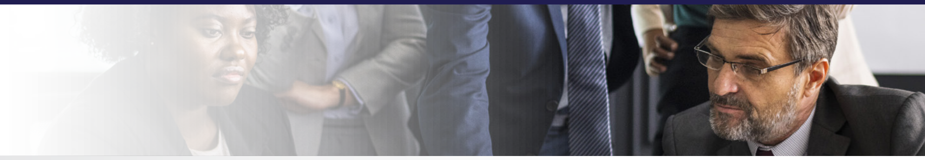
Employers make Social Security contributions of 6.2% up to the taxable wage base each year. On a percentage basis, the company actually contributes a smaller amount of pay for higher-paid employees than it does for those who earn less than the social security wage base threshold. To level this, the IRS allows companies to make an additional contribution on the excess. This method is called "Permitted Disparity" or "Social Security integration."

ACTION TO TAKE NOW

Familiarize yourself with how Social Security integration works in profit sharing contributions. This scenario can be broken down into just a few simple steps.

1. We allocate a contribution as a percentage of total pay to all eligible employees.
2. We allocate a percentage to the Excess Compensation, the amount over the social security taxable wage base, to those eligible participants.

Note: *The excess percentage cannot be more than the lesser of the base percentage or 5.7%.*



Keep in mind:

- The allocation method or formula for each retirement plan is spelled out in its plan document. The plan would need to adopt an amendment if this choice represents a change.
- Generally, the deadline for making a change like this is the end of the year for which the contribution will be made. However, you'll want to consult with us first to make sure this is the case for your client's specific plan.

Call on us any time to talk about optimizing profit sharing contributions or to request illustrations on how any of these methods may work best for a client's situation.