

WHAT ARE THEY?

Marketed as cross-tested or new comparability, these plans are not really a separate plan type. Instead, they are simply an allocation method that uses both age and compensation as the basis for allocating an employer contribution among eligible participants. This method that can be used in either stand-alone profit sharing plans or 401(k) plans. Cross-tested plans are subject to all the basic requirements and offer all the attributes of profit sharing or 401(k) plans.

WHAT ARE THE BENEFITS?

Because age is used as an allocation factor, cross-tested plans favor older employees who have fewer years to accumulate assets for retirement than younger employees. These plans work best when the key employees are older or when there is a significant spread between the age of the key employees and the average age of the other employees. In addition, cross-tested plans are used as companion plans for defined benefit or cash balance plans, when the owner wants to significantly increase retirement savings.



Under the right circumstances, this method can significantly favor specific employees, such as owners, officers, managers, tenured employees, etc. Taken a step further in design, employers can identify multiple groups of employees, and allow each group to receive a different contribution amount as a percentage of their pay.

When used in a 401(k) plan, the cross-tested allocation method can help address contribution limits imposed on highly compensated employees (HCEs) by the 401(k) deferral tests.

A significant advantage of profit sharing contributions is the financial flexibility retained by companies. This holds true with this method as well. As company conditions warrant, contributions can vary significantly from year to year, from nothing to the maximum allowed under the law. To fully realize the benefits of this plan design for the key employees, however, some minimum level of contribution is often required or desirable.

OTHER PLAN CONSIDERATIONS

Cross-tested allocations are subject to special nondiscrimination tests each year to verify that the key employees are not unduly favored in the plan. This results in two important considerations:

- 1) Administrative costs for these plans are somewhat higher to cover additional testing.
- 2) Changes in employee demographics, especially in smaller companies, can dramatically and/or negatively affect these tests.

Good planning before the end of each plan year can help alleviate the second problem, suggesting that close coordination is often critical for the success of this method.

LEARN MORE

Plans using the cross-tested allocation method have become very popular. They offer great financial flexibility for contribution levels each year, and contributions can often be targeted to favor the key employees. Contact your EGPS Sales Consultant to learn if cross-tested plans might be a good fit for you.