AB BERNSTEIN

CHANGE THE PLAN, NOT THE GOAL

A Business Owner's Guide to Selecting a Retirement Plan

50 YEARS OF INVESTMENT MANAGEMENT & RESEARCH

Bernstein does not provide tax, legal, or accounting advice. In considering this material, you should discuss your individual circumstances with professionals in those areas before making any decisions.

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EXECUTIVE SUMMARY

Securing long-term spending is the single most important goal for most savers in the developed world.

Yet, the best way to accomplish this is often unclear. Business owners and professionals know they should be saving, but how much? And how should they balance saving for the long term with investing in their business or practice and funding their current lifestyles?

How much to save is a function of how old you are now and how much you ultimately want to spend later. Our research shows that saving in a tax-deferred retirement plan can help, because the value of the deferral can be as much as an extra 2% per year in return.

Selecting the right tax-deferred retirement plan for your business or professional practice can meaningfully improve the amount of spending that owners, and their employees, can enjoy later. To help you make an informed decision, this guide explores the various plan types available, as well as their benefits and drawbacks.

While we have written this book for owners selecting plans for their companies, we cover the entire landscape to shed light on how various plans coordinate and interact.

OBSOLETE "RULES OF THUMB"

When it comes to securing long-term spending, conventional wisdom typically recommends that you save at least 15% of your gross income each year, assuming you start early at age 25. Other guidelines propose that your assets should grow based on a savings factor: for instance, six times your salary at age 50 and eight times your salary at age 60, assuming a retirement at age 67.

The appeal of these rules of thumb lies in their simplicity. Yet unfortunately, they are based on assumptions that no longer apply. Consider the following:

- Projected returns for equities and bonds are significantly below historical averages. This sobering reality requires an adjustment to conventional recommendations.
- For many people, especially business owners, building wealth may not be linear, which argues for a more tailored and nuanced approach.

OVERCOMING THE OBSTACLES

Given this new environment, what can be done to build wealth, secure long-term spending, and thrive in a world where investment returns are much lower? Several concrete actions, both today and over time, can help boost your chances of success:

- **Working longer.** Though often less desirable, this is usually the most significant variable, as it allows you more time to save along with fewer years of spending.
- **Lowering your expected spending or increasing your savings rate.**
- **Residing in tax-favorable states.** Depending on your taxable income, moving to a state like Florida can help lower your effective tax rate.
- **Maximizing retirement plan options and contributions.** These are essentially free benefits that can be taken, although they do limit the access and liquidity of your savings during your working years.

Building wealth is an extensive long-term process that requires discipline, persistence, and thoughtful choices. With the wide variety of retirement plan options and account types available, selecting the right type of savings vehicle can be a deciding factor in the ultimate wealth generated and the time it takes to secure a desired spending rate.

How Much Should I Save per Year?

How much you need to save each year depends on several factors. The three most important factors are when you start saving, when target spending starts, and the amount of spending expected:

- **Onset of Saving.** The younger you start, the less you will need to save, all things equal.
- **Onset of Spending.** Flexibility around the start of your spending from the portfolio will have a large impact on the amount of annual savings required.
- **Spending Levels.** Higher expected spending will require greater annual saving.

During saving years, be sure to consider factors that impact how much you can save and any variability in the savings rate:

- **Current Expenses.** Can you develop a realistic plan that will ensure regular contributions to savings? Keep in mind that one-time expenses such as the purchase of a house or significant investments in your business may challenge savings consistency.
- **Income Level.** Will your current and future income be enough to cover your savings rate? How do you expect your income to grow over time? Both are important when evaluating annual contributions.

> The right savings vehicle can impact the ultimate wealth generated and the desired spending rate.

Why Contribute to a Retirement Plan?

Put simply, investing in retirement plans creates more wealth compared to investing in a taxable account. The reasons behind this include:

- **Lower effective tax rates.** Many plans (e.g., 401(k)s) enable you to contribute pretax dollars, or allow for tax deductions for contribution amounts. By reducing your earned income, you can typically achieve a lower effective tax rate.
- **Forced Savings.** Many plans feature automatic payroll deductions, forcing you to make regular contributions.
- **Tax deferral worth 2%.** The benefits of tax deferral within retirement accounts cannot be overstated. By sheltering the retirement assets from taxation until their future withdrawal, you can obtain additional growth of roughly 2% per year.

Benefits of Tax Deferral

When we compare taxable and tax-deferred accounts, it is important to focus on the tax-equivalent value, or the amount of "spendable dollars" remaining after you liquidate the assets and pay any taxes due.

To illustrate how the benefit of tax deferral compounds over time, we start our analysis in **Display 1** with two portfolios—one taxable and one tax-deferred. Both start with a single contribution of $10,000 (the latter on a tax-equivalent basis). In 20 years, the tax-deferred account has compounded to almost 15% more.

Generally speaking, the longer the horizon, the greater the value of the tax deferral. **Display 2** (next page) illustrates what happens when $10,000 is contributed annually for 25 years. Not surprisingly, the saver would amass more wealth by age 65 on a pretax basis and would end up with more tax-equivalent value—resulting in a $20,100 advantage over taxable savings, as shown on the right side of **Display 2**.

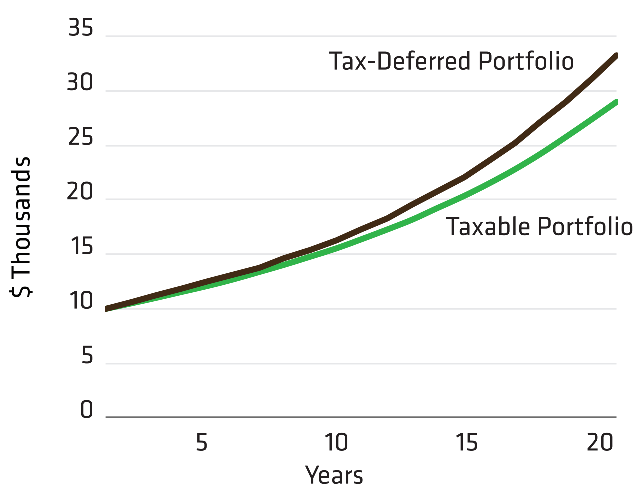
Keep in mind, the deferral period can be much longer than the retirement date. Even after accounting for required minimum distributions, saving via a tax-deferred, qualified plan has a meaningful positive impact on total wealth over a long horizon.

[Generally speaking, the longer the horizon, the greater the value of the tax deferral.]

Expected returns are forecast to be lower than normal in the decade to come, and are even worse when considered on an after-tax basis. In **Display 3** (page 5), we compare the historical returns for a balanced portfolio to expected returns over the next 10 years. Whether pretax or after-tax, there's a gap of nearly 1.7%. The power of tax deferral in retirement accounts can make up that difference.

DISPLAY 1: BENEFITS OF TAX DEFERRAL

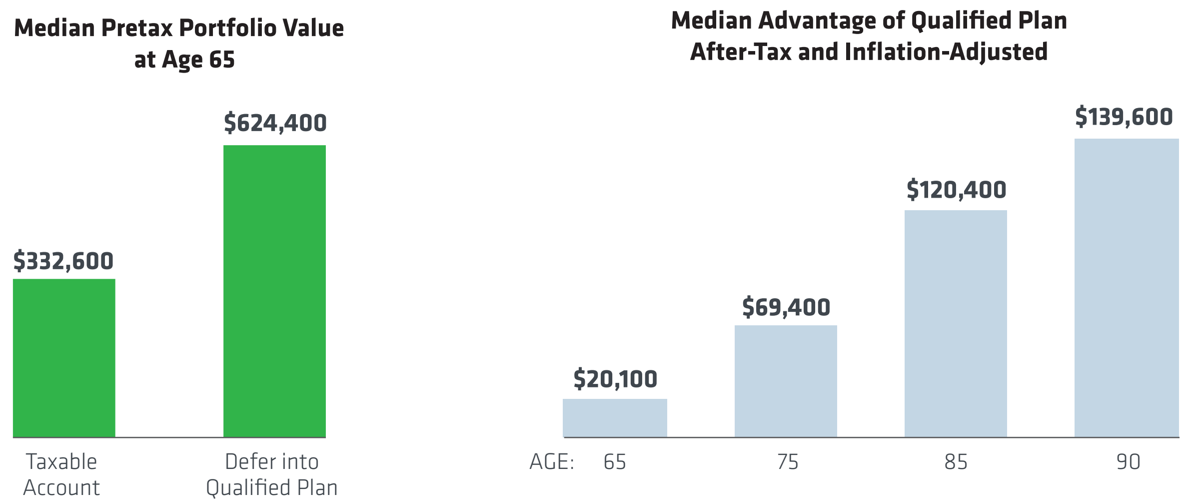
GROWTH OF $10,000: TAXABLE VS. TAX-DEFERRED PORTFOLIO (TAX-EQUIVALENT AMOUNT),* MEDIAN OUTCOME



Year	Taxable Portfolio	Tax-Deferred Portfolio	Benefit of Tax Deferral
5	$12,700	$13,100	$400
10	16,400	17,300	900
15	21,500	23,600	2,100
20	29,000	33,300	4,300

*After-tax portfolio amounts are net of implied capital gains tax for assets in taxable portfolio (where applicable) and ordinary income tax for assets in tax-deferred portfolio. Initial investment amounts are $10,000 for taxable portfolio and $15,385 (pretax equivalent) for tax-deferred portfolio. Assumes allocation of 60% stocks and 40% intermediate-term fixed income. Stocks are modeled as 21% US diversified, 21% US value, 21% US growth, 7% US small- and mid-cap, 22.5% developed international, and 7.5% emerging market. Bonds modeled as diversified municipal bonds in taxable portfolio and taxable bonds in tax-deferred portfolio. Income tax rate assumptions: federal 35% ordinary and 20% long-term capital gains/qualified dividends. Assumes investor is 40 years old and no required minimum distributions are due for the 20-year analysis. Based on Bernstein's estimates of the range of returns for the applicable capital markets over the periods analyzed. **Data do not represent past performance and are not a promise of actual future results or a range of future results.** See Notes on Wealth Forecasting System at the end of this guide for further details. Bernstein is not a legal, tax, or estate advisor. Investors should consult these professionals, as appropriate, before making any decisions.
Source: AB

DISPLAY 2: BENEFITS OF TAX DEFERRAL FOR STEADY SAVERS
VALUE OF $10,000 INVESTED ANNUALLY FOR 25 YEARS, FOR A 40-YEAR-OLD EMPLOYEE



After-tax portfolio amounts are net of implied capital gains tax for assets in taxable portfolio (where applicable) and ordinary income tax for assets in tax-deferred portfolio. Annual investment amounts are $10,000 for taxable portfolio and $15,385 (pretax equivalent) for tax-deferred portfolio. Allocation is 60% stocks/40% bonds. Stocks are modeled as 21% US diversified, 21% US value, 21% US growth, 7% US small- and mid-cap, 22.5% developed international, and 7.5% emerging market. Bonds are modeled as intermediate-term diversified municipals in taxable accounts and intermediate-term taxable bonds in retirement accounts. Income tax rate assumptions: federal 35% ordinary and 20% long-term capital gains/qualified dividends, with no state income taxes. Assumes investor is 40 years old and required minimum distributions are made starting at age 70½. To make a fair comparison, we assume that the tax-deferred portfolio is transferred to a taxable portfolio and that both taxable portfolios are liquidated and taxed at the age specified. Based on Bernstein's estimates of the range of returns for the applicable capital markets over the period analyzed. See Notes on Wealth Forecasting System at the end of this guide for further details. **Data do not represent past performance and are not a promise of actual future results or a range of future results.**
Source: AB

How Much Should I Save for a Given Level of Spending?

Tax-deferred retirement accounts provide significant benefits toward long-term spending, but how much will you spend and should you contribute? Here are some general guidelines:

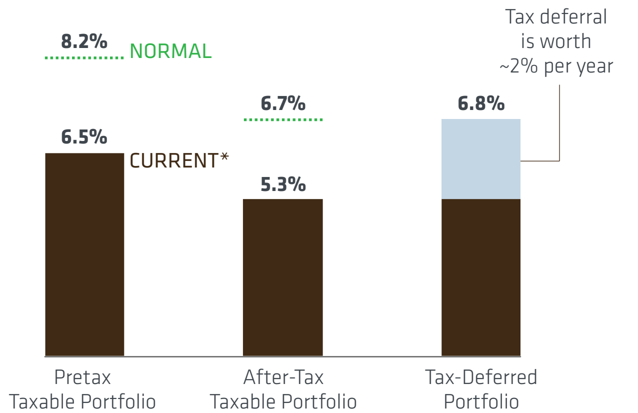
- Plan on needing to maintain 100% of your final salary level at first. While it is tempting to assume that you can manage with less, keep in mind that new expenses such as travel may arise right after you stop working. Healthcare and long-term assisted living costs may increase as you age.
- A typical recommendation is that you save at least 15% of your annual compensation (pretax) across your career (assuming ages 25 to 65) to ensure a high probability of maintaining your final salary level. Alternatively, late savers (ages 45 to 65) would need to contribute 30% per year.

Saving a moderate portion of income early in your career makes a significant difference in the likelihood of achieving your retirement goals. Consider the example below:

- **Start Saving at 25:** Investor making $150,000 saves 10% of pretax income in a taxable account with a goal of achieving $1 million when she retires at age 65. Assuming saving starts at age 25, she will be able to grow her assets to that level in the median case.
- **Start Saving at 45:** Investor waits until age 45, but must more than double her savings to $37,500 in after-tax income. With this increased level of funding, she is able to make up the gap and reach $1 million in assets by age 65.

In both cases, reaching a $1 million taxable portfolio at age 65 will support sustainable spending of $36,000 each year for the rest of the investor's life.

DISPLAY 3: FORWARD RETURN PROJECTIONS
NEXT 10 YEARS—60/40 ALLOCATION



*As of December 31, 2016
Allocation is 60% stocks/40% bonds. Stocks are modeled as 21% US diversified, 21% US value, 21% US growth, 7% US small- and mid-cap, 22.5% developed international, and 7.5% emerging market. Bonds are modeled as intermediate-term diversified municipals in taxable accounts and intermediate-term taxable bonds in retirement accounts. To make a fair comparison, we assume that the tax-deferred portfolio is transferred to a taxable portfolio and that both taxable portfolios are liquidated and taxed at the year specified. Tax rate assumptions: federal tax rates—43.4% earned/ordinary income (excluding IRA distributions), 39.6% IRA distributions, and 23.8% capital gains/qualified dividends; state tax rates—6.5% for all income and capital gains. Based on Bernstein's estimates of the range of returns for the applicable capital markets as of December 31, 2016. **Data do not represent past performance and are not a promise of actual future results or a range of future results.** See Notes on Wealth Forecasting System at the end of this guide for further details.
Source: AB

How Much Will Tax-Deferred Accounts Help?

Now let's consider how our example would change if we used tax-deferred accounts. Given that the investor will be able to use pretax dollars, we assume that she is able to contribute 40% more toward her annual savings: In this case, a 25-year-old investor would save $23,000 tax-deferred, which is the equivalent of $15,000 taxable:

- By using tax-deferred retirement accounts, the 25-year-old investor is able to double her nest egg to $2 million.
- Even though she will face taxes on her withdrawals when she begins to spend from the portfolio, the extra deferral results in an increase in sustainable spending. At age 65, she will be able to spend $63,000 per year, which is roughly 75% more.

How Much is a Tax-Deferred Dollar Worth?

Note that doubling dollars in a retirement plan doesn't translate directly into a doubled amount of sustainable spending.

That's because the value of a dollar saved in a tax-deferred retirement plan varies significantly based on the age of the participant at the time of the contribution. Given the longer period available for tax-deferred growth, contributions at an early age have a greater relative value compared to those made later in life.

Nevertheless, investing in tax-deferred assets can help you to catch up if you start later, as **Display 4** (next page) illustrates. For someone who plans to begin spending at age 65, investing in a tax-deferred account at age 35 can provide the same sustainable spending as saving equivalent amounts in a taxable account at age 25. In other words, the tax deferral can turn back the savings clock by a full 10 years.

> [Contributions at an early age have a greater relative value compared to those made later in life.]

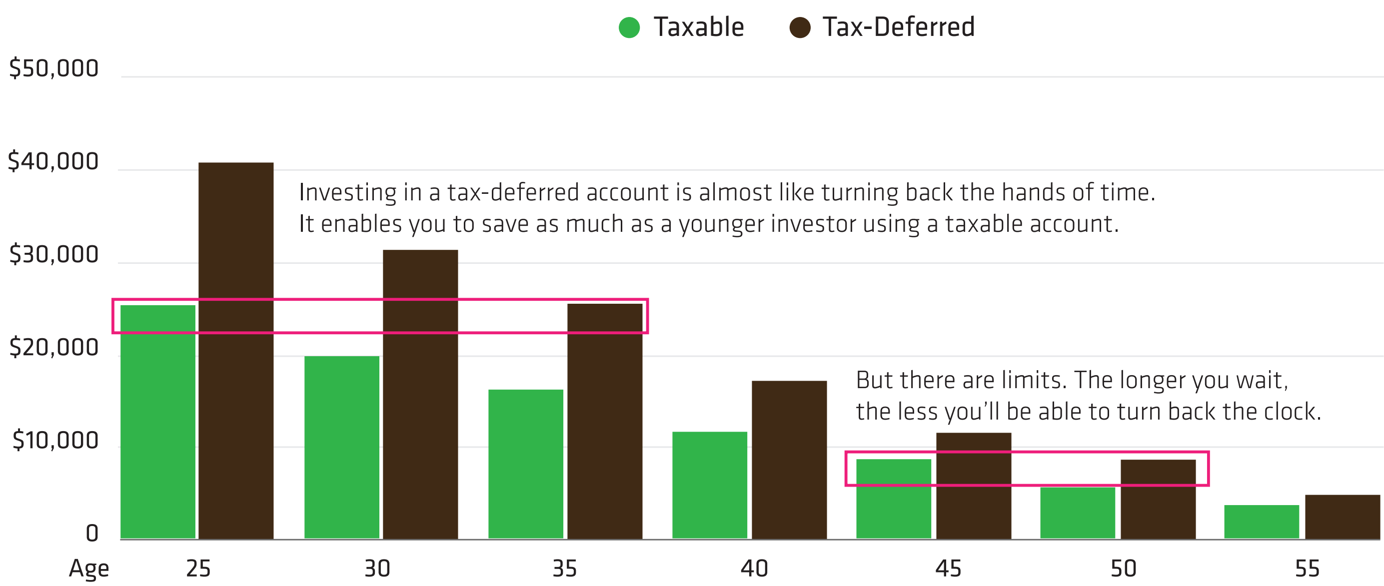
This effect is particularly noteworthy for business owners and professionals who may have spent their early careers reinvesting in their companies or paying off costly student loans. The ability to put more money away tax-deferred can help the owner recoup some of the advantage of early savings.

However, there is a limit to a tax-deferred account's ability to turn back time. A 50-year-old who starts saving today in a tax-deferred account will be able to spend only as much as a 45-year-old who starts saving in a taxable account.

How Much Will Social Security Help?

Many savers wish to consider the income they'll receive from Social Security when planning for after-tax spending. While in most cases the amounts will not be enough to meet your spending needs, these payments will provide an additional

DISPLAY 4: SUSTAINABLE SPENDING PER YEAR FOR $10,000 SAVED ANNUALLY*



*Assumes allocation is 60% stocks/40% bonds. Stocks are modeled as 21% US diversified, 21% US value, 21% US growth, 7% US small- and mid-cap, 22.5% developed international, and 7.5% emerging market. Bonds are modeled as intermediate-term diversified municipals in taxable accounts and intermediate-term taxable bonds in retirement accounts. Tax rate assumptions: federal tax rates—35% earned/ordinary income, and 20% capital gains/qualified dividends; no state or local taxes. We assume savings of $10,000/year for taxable accounts and $15,385/year for tax-deferred accounts, starting at each of the ages listed, and adjusted annually for inflation. Sustainable spending amounts listed are adjusted for inflation and based on the assumption that spending begins at age 65.
Source: AB

base on which to build. Here are some important points about how Social Security works:[1]

- Anyone who works and pays Social Security taxes earns "credits" toward Social Security benefits (based on the highest 35 years of earnings).
- The traditional "full retirement age" is typically between ages 66 and 67, depending on when the person was born, although you can start taking benefits as early as age 62 or as late as age 70. Starting benefits earlier will result in lower payouts, while delaying will provide higher payouts.
- Assuming you wait until the full retirement age for benefits and are able to max out your retirement credits, you should expect roughly $32,000 annually in benefits.

How Will Tax Changes Impact My Retirement Planning?

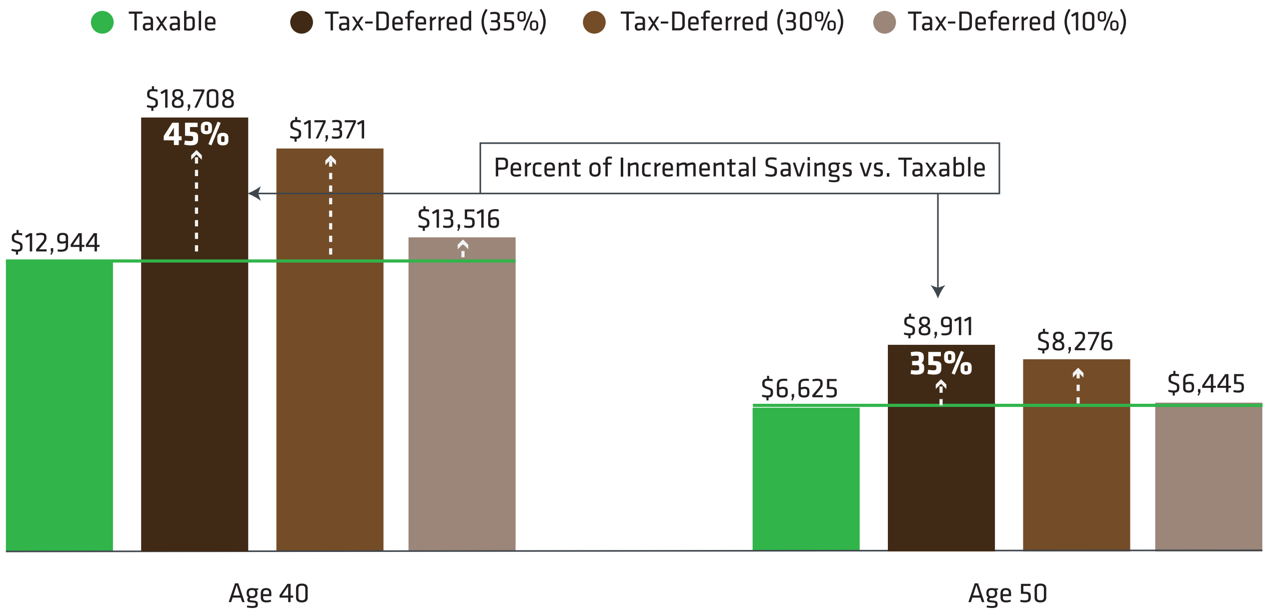
While changes to the tax code may impact your plan, it is important to understand that this possibility does not negate the importance of investing in tax-deferred plans.

The power of tax deferral remains consistent even when we lower the federal income tax rates.

In **Display 5**, we illustrate the sustainable spending advantage of tax-deferred savings over taxable savings assuming various hypothetical effective tax rates. Essentially, tax deferral continues to provide an advantage until federal tax rates on ordinary income sink to 10%.

[1] *Source: US Social Security Administration*

DISPLAY 5: SUSTAINABLE SPENDING PER YEAR FOR $10,000 SAVED ANNUALLY*



*Assumes allocation is 60% stocks/40% bonds. Stocks are modeled as 21% US diversified, 21% US value, 21% US growth, 7% US small- and mid-cap, 22.5% developed international, and 7.5% emerging market. Bonds are modeled as intermediate-term diversified municipals in taxable accounts and intermediate-term taxable bonds in retirement accounts. Assumes required spending from portfolio equivalent to the after-tax income at age 25, adjusted for inflation, where spending starts at age 65. Tax rate assumptions: Several federal tax rates for ordinary income are presented—35% earned/ordinary income, 30% earned/ordinary income, and 10% earned/ordinary income. In all cases, a 20% tax rate is applied to capital gains/qualified dividends, with no state or local taxes. Savings rate assumptions: All tax-deferred savings are adjusted to provide the taxable equivalent of $10,000/year, amounting to $15,385/year for the 35% tax scenario, $14,286/year for the 30% tax scenario, and $11,111 for the 10% tax scenario, respectively. Savings start at each of the ages listed and are adjusted annually for inflation. Sustainable spending amounts listed are adjusted for inflation and based on the assumption that spending begins at age 65.
Source: AB

Conclusion

For all savers, and in particular for business owners, the increased challenges of sufficient lifetime savings and the value of saving in a tax-deferred manner raise the logical question, "Which retirement plan is right for me or my firm?" The answer to this question is, not surprisingly, "It depends."

However, to simplify, the single most important factor in deciding upon a retirement plan is **how much income the owners are interested in deferring and able to defer**.

[The deciding factor in choosing a retirement plan is **how much income the owners are interested in deferring and able to defer**.]

There are two families of qualified retirement plans from which to choose: defined contribution and defined benefit. Defined contribution plans are flexible and relatively easy to implement, but their deferral potential is limited. Defined benefit plans, while allowing for significantly higher deferrals, are complex in nature and often require additional resources.

In the following section (pages 12–27), we describe in detail the various types of defined contribution and defined benefit plans. The main difference is that defined benefit plans allow for far greater deferral opportunities but require an actuary to draft and administer them due to the additional complexities.

In general, if the owners are looking to defer $54,000 per year or less, they can accomplish their goals with a defined contribution plan alone. If the owners are looking for deferral amounts exceeding $54,000 per year, they would need to establish a defined benefit plan, or a combination of both. What follows are case studies that address retirement needs for various business types.

STARTING A RETIREMENT PLAN: A CHECKLIST FOR BUSINESS OWNERS

- ☐ First, develop an emergency fund that can cover six months of expenses.

- ☐ Ensure all high-interest debt (e.g., credit cards) is paid down.

- ☐ Develop a realistic projection of expected long-term expenses:

    - ■ Using Bernstein's framework, find out how much you need to save to sustain those expenses—this is your goal.
    - ■ Look at your monthly and annual expenses, and determine how much savings you can put into tax-deferred retirement plans.
    - ■ Discuss with your partners or co-owners how much they would like to contribute.
    - ■ If the amount you wish to defer is $54,000 per year or less, consider a defined contribution plan.
    - ■ If you desire to defer more, engage an actuary to determine an initial defined benefit plan design:
        - How much can your partners contribute?
        - How much will the plan cost to cover eligible staff?
        - What should the return target be?
    - ■ Start saving via your plan or combination of plans.
    - ■ Review annually.

SPECIAL CONSIDERATIONS FOR BUSINESS OWNERS

As a business owner, you will need to consider a variety of additional factors when choosing the right retirement plans. Typically, the following factors are important to consider:

- **Ratio of Employees to Owners.** Typically, if you have more than 10 employees per owner, a 401(k) makes more sense. For employers with lower employee/owner ratios, there are more options, including selecting a cash balance plan with profit sharing agreements.
- **Administrative/Legal Costs.** The cost to administer plans, especially when managing larger numbers of participants, may be prohibitively expensive. Similar to evaluating your employee head count, it is important to factor in the operational costs of the various choices.
- **Sustainable Cash Flow.** Put simply, will your company have sufficient and sustainable cash flow to fund the relevant retirement plans that you select?
- **Current Age and Retirement Time Frame.** Two simple rules apply regarding age: (1) The older you are, the more you can defer, and (2) The closer you are to retirement, the more you will need to accelerate and load your retirement plans.

The following case studies illustrate these considerations for various types of businesses.

CASE STUDIES

Midsize Law Firm

Scenario: A midsize law firm with 30 partners and 170 other employees

CONSIDERATIONS:

- If deferring $54,000/year or less, a 401(k) combined with a profit sharing plan is the best option.
- Additional deferrals will require the addition of a cash balance plan.

Plan Type	Owner's Maximum Contribution	Capacity for Savings
401(k)	$18,000–$24,000	$0–$24,000
Profit Sharing	$36,000	$0–$60,000
Cash Balance*	Age Dependent (See Charts)†	Greater than $60,000/year per partner

*Rules to add cash balance plan: (1) need to provide staff benefits (in the profit sharing plan) between 5% and 7.5% of salary, and (2) need to include 40% (80 people in this example) of all eligible employees including owners.

†See the charts on pages 31 and 32 for maximum allowable contributions.

CASE STUDIES (CONTINUED)

Private Medical Practice

Scenario: A midsize medical practice with 10 partners and 40 other employees

CONSIDERATIONS:

- If deferring $54,000/year or less, using the 401(k) combined with a profit sharing plan is the best option.
- Additional deferrals will require the addition of a cash balance plan.

Plan Type	Owner's Maximum Contribution	Capacity for Savings
401(k)	$18,000–$24,000	$0–$24,000
Profit Sharing	$36,000	$0–$60,000
Cash Balance*	Age Dependent (See Charts)†	Greater than $60,000/year per partner

*Rules to add cash balance plan: (1) need to provide staff benefits (in the profit sharing plan) between 5% and 7.5% of salary, and (2) need to include 40% (20 people in this example) of all eligible employees including owners.

†See the charts on pages 31 and 32 for maximum allowable contributions.

Small Business

Scenario: A small business with two owners and eight other employees

CONSIDERATIONS:

- If deferring $54,000/year or less, using the trustee-directed profit sharing plan is the best option.
- Additional deferrals will require the addition of a defined benefit or cash balance plan.

Plan Type	Owner's Maximum Contribution	Capacity for Savings
401(k)/ Profit Sharing	$54,000	$0–$54,000
Defined Benefit/ Cash Balance*	Age Dependent (See Charts)†	Greater than $60,000/year per owner

*Rules to add cash balance plan: (1) need to provide staff benefits between 5% and 7.5% of salary, and (2) need to include 40% (four people in this example) of all eligible employees including owners.

†See the charts on pages 31 and 32 for maximum allowable contributions.

CASE STUDIES (CONTINUED)

Sole Proprietorship

Scenario: A sole proprietorship with one owner and no other employees

CONSIDERATIONS:

- For greater deferral above $54,000/year, use a profit sharing plan combined with a defined benefit plan.
- Note that any employees hired will need to be added into the SEP IRA within three years of employment.

Plan Type	Owner's Maximum Contribution	Capacity for Savings
SEP IRA	$54,000	$0–$54,000
401(k)/ Profit Sharing	$54,000–$60,000	$0–$60,000
Defined Benefit	Age Dependent (See Charts)*	Greater than $60,000/year per owner

At certain income levels, a 401(k), sometimes called a solo 401(k), may allow a sole proprietor more deferral than a SEP IRA. A solo 401(k) has the same rules and requirements as any other 401(k) plan.

*See the charts on pages 31 and 32 for maximum allowable contributions.

Owner with Multiple Businesses

Scenario: An owner with three businesses, where one company has 20 employees and the other companies have no employees

CONSIDERATIONS:

- Often, one of the businesses will have multiple employees, while the other businesses will have no employees. When considering a retirement plan, if the owner has at least 50% ownership of multiple companies, all of those companies will need to be considered in constructing retirement plans. The specific issues that the business owner needs to be concerned with are affiliated services and control groups.

Plan Type	Owner's Maximum Contribution	Capacity for Savings
Profit Sharing	$60,000	$0–$60,000
Defined Benefit/ Cash Balance*	Age Dependent (See Charts)†	Greater than $60,000/year per owner

*Rules to add cash balance plan: (1) need to provide staff benefits between 5% and 7.5% of salary, and (2) need to include 40% of all eligible employees including owners.

†See the charts on pages 31 and 32 for maximum allowable contributions.

INDIVIDUAL PLANS IN DETAIL

TRADITIONAL 401(k)

Benefits and Key Features:	Earnings grow tax-deferred Employer contributions are deductible for employer Employee contributions reduce employee's taxable income
Eligibility:	Employees typically must have one year of service, work 1,000 hours per year, and be at least 21 years old
Contributions:	Employee and employer
Maximum Contribution:	Employees under age 50: the lesser of $18,000 or earned income for the year Employees age 50 and over: the lesser of $24,000 or earned income for the year
Withdrawals:	Earnings and principal taxed as ordinary income Additional 10% penalty on withdrawals made prior to age 59½
Required Minimum Distributions:	RMDs begin at age 70½ unless still working; for a 5%-or-more owner, RMDs must begin at age 70½ even if still working

A traditional 401(k) is a retirement savings plan, sponsored by an employer, that lets workers save and invest a piece of their paycheck before taxes are taken out. Taxes aren't paid until the money is withdrawn from the account.

HOW IT WORKS

Participants contribute pretax salary earnings annually up to a maximum limit. For 2017, that limit is $18,000 for employees under 50 years old, and $24,000 for employees age 50 and over. Employers in some cases will also provide matching contributions in addition to the amount funded by the employee. Typically, the employees will maintain control over the investments, although selections are often limited by the employer. Earnings from investments in a 401(k) account (in the form of interest, dividends, or capital gains) are tax-deferred. The resulting compound return with delayed taxation is a major benefit of the 401(k) plan when held over long periods of time.

Withdrawals are taxed at ordinary income rates for both principal and earnings. Participants are restricted from taking distributions while employed at the company sponsoring the plan, except in the case of certain hardships. Furthermore, a 10% excise tax, on top of the ordinary income taxes, is assessed on any distributions when the participants are under age 59½. Once the participants reach 70½, they must start taking required minimum distributions (RMDs), although this is usually delayed if they are still working.

QUANTIFYING THE BENEFIT

The ability to use pretax salary income for contributions makes the 401(k) plan very attractive. For pretax contributions, employees do not pay federal income tax on the amount of current income they fund into their account, although they will ultimately pay taxes once distributions are made.

SIMPLE 401(k)

Benefits and Key Features:	Earnings grow tax-deferred Employer contributions are deductible for employer Employee contributions reduce employee's taxable income
Eligibility:	Employees of employers with 100 or fewer employees, or business owners, that do not currently maintain another retirement plan Employees typically must have one year of service, work 1,000 hours per year, and be at least 21 years old
Contributions:	Employee and employer
Maximum Contribution:	Employees under age 50: the lesser of $12,500 or 100% of pay Employees age 50 and over: the lesser of $15,500 or 100% of pay Employers must either match employee contributions dollar-for-dollar up to a maximum of 3% of the employee salary, or 2% of pay each year
Withdrawals:	Earnings and principal taxed as ordinary income Additional 10% penalty on withdrawals made prior to age 59½
Required Minimum Distributions:	RMDs begin at age 70½ unless still working; for a 5%-or-more owner, RMDs must begin at age 70½ even if still working

SIMPLE (Savings Incentive Match Plan for Employees) 401(k) programs are typically used by smaller companies with fewer than 100 employees. They provide an easy and cost-effective way for these businesses to offer retirement options, but are more limited in some respects compared with the traditional 401(k).

HOW IT WORKS

Participants contribute pretax salary earnings annually up to a maximum limit. For 2017, that limit is $12,500 for employees under 50 years old, and $15,500 for employees age 50 and over. Employers must also contribute; either matching employee contributions up to 3% of salary, or contributing 2% of pay. Typically, the employees will maintain control over the investments, although selections are often limited by the employer. Earnings from investments in a SIMPLE 401(k) account (in the form of interest, dividends, or capital gains) are tax-deferred. The resulting compound return with delayed taxation is a major benefit of the plan when held over long periods of time.

Withdrawals are taxed at ordinary income rates for both principal and earnings. Participants are restricted from taking distributions while employed at the company sponsoring the plan, except in the case of certain hardships. Furthermore, a 10% excise tax, on top of the ordinary income taxes, is assessed on any distributions when the participants are under age 59½. Once the participants reach age 70½, they must start taking required minimum distributions (RMDs), although this is usually delayed if they are still working.

QUANTIFYING THE BENEFIT

The ability to use pretax salary income for contributions makes the SIMPLE 401(k) plan very attractive. For pretax contributions, employees do not pay federal income tax on the amount of current income they fund into their account, although they will ultimately pay taxes once distributions are made.

403(b)

Benefits and Key Features:	Earnings grow tax-deferred Contributions can reduce employee's taxable income
Eligibility:	Employees of religious, charitable, educational, and other organizations described in IRC Section 501(c)(3), certain governmental organizations, and public school systems Contributions are deductible for employer
Contributions:	Employee and employer
Maximum Contribution:	Employees under age 50: the lesser of $18,000 or earned income for the year Employees age 50 and over: the lesser of $24,000 or earned income for the year For employees under age 50, total employer/employee contribution capped at $54,000; age 50 and over, capped at $60,000
Withdrawals:	Earnings and principal taxed as ordinary income Additional 10% penalty on withdrawals made prior to age 59½
Required Minimum Distributions:	RMDs begin at age 70½ unless still working For a 5%-or-more owner, RMDs must begin at age 70½ even if still working

The 403(b) plan, also known as a "tax-sheltered annuity plan" (TSA), is fundamentally equivalent to the traditional 401(k) program, but it is made available specifically for nonprofits, schools, and certain governmental and religious organizations that would not normally be eligible to participate in 401(k) programs.

HOW IT WORKS

Structurally similar to the 401(k) plan, the 403(b) allows individuals involved to contribute pretax amounts into investments that are then allowed to grow tax-free until eventual distribution and withdrawal. Annual contributions can be made by employees (up to $18,000 in 2017), or jointly between the employer and employee (up to $54,000 in 2017). Participants who are 50 or older can make additional catch-up contributions of $6,000. Employees who have worked for the same nonprofit for 15 years may also have access to an additional "catch-up provision" of $3,000 per year for up to five years, if they contributed an average of less than $5,000 per year previously.

Historically these plans have offered more limited investment choices than corporate 401(k) plans, although in recent years they've begun offering a broader array of investment options. One significant advantage of these plans is that they will frequently vest immediately, or over a shorter period of time, as compared to equivalent 401(k) plans.

Non-eligible withdrawals, such as when the participant is under age 59½, are subject to a 10% penalty in addition to 20% withholding.

QUANTIFYING THE BENEFIT

The 403(b) plan is effectively the 401(k) plan equivalent for nonprofits and other entities that would not normally be eligible for the 401(k) program. As with the corporate equivalent, it allows participants to defer current year income into a tax-advantaged account that can be accessed later in retirement.

ROTH 401(k)/403(b)

Benefits and Key Features:	Earnings growth is potentially tax-free Contributions are after-tax and not deductible Contributions do not reduce employee's taxable income
Eligibility:	Employees typically must have one year of service, work 1,000 hours per year, and be at least 21 years old For Roth 403(b) plans, see eligibility requirements for 403(b)s
Contributions:	Employers can match, but the amounts must go into a traditional 401(k) employee-only plan
Maximum Contribution:	Employees under age 50: the lesser of $18,000 or earned income for the year Employees age 50 and over: the lesser of $24,000 or earned income for the year
Withdrawals:	Earnings taxed as ordinary income, if taken before age 59½; distributions of principal and earnings are tax-free, if taken after age 59½ Additional 10% penalty on earnings growth against withdrawals made prior to age 59½
Required Minimum Distributions:	RMDs begin at age 70½ unless still working; for a 5%-or-more owner, RMDs must begin at age 70½ even if still working

Both the Roth 401(k) and the Roth 403(b) are retirement savings plans, sponsored by an employer, that let workers invest after-tax dollars. The primary benefit of these plans is that both the original principal and the earnings growth may be later withdrawn without any taxes. The Roth 403(b) plan provides the same benefits for nonprofit employers or public education organizations.

HOW THEY WORK

Participants contribute after-tax salary earnings annually up to a maximum limit. For 2017, that limit is $18,000 for employees under 50 years old, and $24,000 for employees age 50 and over. Employers in some cases will also provide matching contributions in addition to the amount funded by the employee, although these must be put into a traditional 401(k) account. Typically, the employees will maintain control over the investments, although selections are often limited by the employer.

Participants are restricted from taking distributions while employed at the company sponsoring the plan, except in the case of certain hardships. Similar to traditional 401(k) or 403(b) plans, a 10% excise tax is assessed on any distributions when the participant is under age 59½, although this penalty is applied only to the earnings and not to the original contribution. Starting at age 70½, participants must start taking required minimum distributions (RMDs), although this is usually delayed if they are still working.

WHEN DOES A ROTH IRA MAKE SENSE?

Compared to the traditional IRA, Roth accounts are funded with after-tax dollars but do not provide a tax deduction for the year when contributions are made. Their key feature is that they allow for both earnings and withdrawals to be taken out tax-free.

TRADITIONAL IRA

Benefits and Key Features:	Broad eligibility Earnings grow tax-deferred Contributions can be deductible
Eligibility:	You can contribute if you (or your spouse, if filing jointly) have taxable compensation, but not after you are age 70½ or older
Contributions:	Made by individual Can be made up until normal tax return filing deadline
Maximum Contribution:	Across all traditional and Roth IRAs, maximum contribution of: • $5,500 (for 2017), or $6,500 if age 50 or older by the end of year, or • Taxable compensation for the year
Withdrawals:	Earnings and principal taxed as ordinary income Additional 10% penalty on withdrawals made prior to age 59½
Required Minimum Distributions:	RMDs begin at age 70½ even if still working

A traditional IRA (individual retirement account) is a retirement plan, established directly by participants, that lets them invest their money in a tax-deferred savings account. The special treatment allows for dividends, interest payments, and capital gains to grow tax-free until the money is withdrawn from the account.

HOW IT WORKS

The traditional IRA is typically set up by an individual through an investment broker/dealer, and the account is grown through annual contributions. For 2017, the contribution limit is $5,500 for employees under 50 years old, and $6,500 for employees age 50 and over. Contributions are made using after-tax money, but the amount may be deductible if the participant meets certain income and filing status requirements. Additionally, IRAs are often funded via “rollovers” from other qualified retirement plans such as 401(k)s. Given that the plans are typically self-directed, the range of investment options is usually broad. Withdrawals made after age 59½ are taxed at ordinary income rates based on your tax bracket in the year when the distributions are made. Early distributions prior to that age should be avoided, given that a 10% excise tax, on top of the ordinary income taxes, is assessed on the withdrawals, although there are some exceptions made for hardships. Once the participants reach 70½, they must start taking required minimum distributions (RMDs), even if they are still working.

QUANTIFYING THE BENEFIT

A traditional IRA is a great option for retirement savings, particularly if the participants fall under the required limits to allow for a tax deduction on their contributions. This type of IRA is especially popular, given that it is easy to set up and administer directly by the IRA owner. It offers a greater degree of control of the timing and size of contributions, and the ability to control investment allocations.

SIMPLE IRA

Benefits and Key Features:	Earnings grow tax-deferred Contributions can be deductible
Eligibility:	Employees of employers with 100 or fewer employees, or business owners, that do not maintain another retirement plan Employees must have earned $5,000 or more in any of the prior two years and are expected to earn at least $5,000 in the current year
Contributions:	Employee and employer
Maximum Contribution:	Employees under age 50: the lesser of $12,500 or 100% of pay Employees age 50 and over: the lesser of $15,500 or 100% of pay Employer must match employee contributions up to 3% or contribute 2% of pay each year; can be 1% of employee compensation for two of five years For employees under age 50, total employer/employee contribution capped at $25,000; age 50 and over, capped at $31,000
Withdrawals:	Earnings and pretax contributions taxed as ordinary income Additional 25% penalty on withdrawals made within the first two years of participation and 10% thereafter prior to age 59½
Required Minimum Distributions:	RMDs begin at age 70½ even if still working

A SIMPLE (Savings Incentive Match Plan for Employees) IRA (individual retirement account) is a retirement plan typically established by employers or self-employed individuals (sole proprietorships and partnerships). Under the plan, eligible employees have the option to contribute part of their pretax compensation to the plan. All taxes on the assets contributed are deferred until the money is later distributed.

HOW IT WORKS

The SIMPLE IRA is a tax-deferral program that is typically used by smaller businesses. Contributions by employees are elective and get deducted from their salary. Employers are required to contribute to the plan, and they can provide matching contributions for the elective contributions made by employees, or they can commit to nonelective contributions that are made regardless of whether the employees make a contribution. Matching contributions are made dollar-for-dollar, up to a limit of 3% of compensation. Taxes are not applied to contributions or to any growth in the assets while still in the IRA.

Distributions from the plan are taxed at ordinary rates. During the first two years of participation, an additional 25% penalty is assessed on any withdrawals. Similarly, any distributions before age 59½ are subject to an extra 10% penalty. The participants must take required minimum distributions starting at age 70½, even if still working.

QUANTIFYING THE BENEFIT

The SIMPLE IRA is popular, given that it is easy to set up and administer compared to other qualified plans. It offers the participants a greater degree of control of the timing and size of contributions, and the ability to control investment allocations. Other attractive features for participants include the automatic vesting of all contributions, and the requirement that the employer provide matching contributions.

SEP IRA

Benefits and Key Features:	Earnings grow tax-deferred Contributions are deductible Higher contribution limit compared to traditional IRA Simple to set up and maintain
Eligibility:	Self-employed individuals and small firms Employees must be at least 21 years old, have worked for the company for three of the last five years, and earned at least $600 in the most recent year
Contributions:	Employer only
Maximum Contribution:	Up to 25% of compensation, but no more than $53,000 Lesser of approximately 20% of net earnings from self-employment or $53,000
Withdrawals:	Earnings and pretax contributions taxed as ordinary income Additional 10% penalty on withdrawals made prior to age 59½
Required Minimum Distributions:	RMDs begin at age 70½ even if still working

The SEP (Simplified Employee Pension) IRA (individual retirement account) is popular among self-employed individuals and small businesses, because it offers a streamlined and easy-to-set-up retirement plan with high contribution limits. These accounts can be created by any business owner or contractor with one or more employees.

HOW IT WORKS

The SEP IRA can be established by employers, including self-employed individuals (sole proprietorships or partnerships), and allows for the employer to make tax-deductible contributions on behalf of its employees. Participating employees must have a preestablished traditional IRA that will serve as the funding vehicle into which all contributions are funneled.

Given that this underlying account is a traditional IRA, all SEP IRA contributions follow the rules around taxation and distributions as established for traditional IRA accounts.

QUANTIFYING THE BENEFIT

The SEP IRA is popular, given that it is easy to set up and is less costly as compared to other qualified plans. One particularly desirable feature of the SEP plan is that employees may use the same account for their SEP contributions as for their regular traditional IRA contributions. The limits for the SEP employer contributions and the individual's traditional IRA contributions are different and do not affect each other. Note that this combining of the plans may impact the tax deductibility of the traditional IRA contributions. One drawback of this plan is that any employer wishing to implement a SEP in conjunction with another qualified retirement plan, such as a cash balance or profit sharing plan, must petition for specific approval from the IRS.

ROTH IRA

Benefits and Key Features:	Earnings grow tax-deferred and under certain conditions may be tax-free on withdrawal Contributions are not tax deductible
Eligibility:	Any individual with earned income and/or spouse with modified AGI at or below phaseout range Married Filing Jointly: $186,000–$196,000 in 2017 Married Filing Separately: $0–$10,000 Single or Head of Household: $118,000–$133,000 in 2017
Contributions:	Made by individual
Maximum Contribution:	Under age 50: the lesser of $5,500 or earned income for the year Age 50 and over: the lesser of $6,500 or earned income for the year
Withdrawals:	Distributions of earnings are tax-free if taken after age 59½ and if IRA is held for at least five years Earnings subject to ordinary income taxes Additional 10% penalty on withdrawals prior to age 59½
Required Minimum Distributions:	No RMDs during owner's life

A Roth Individual Retirement Account (Roth IRA) allows a person to set aside after-tax income, up to a specified amount each year.

HOW IT WORKS

The Roth IRA is a special retirement account where you pay taxes on money going into your account, and then all future withdrawals are tax-free.

Similar to the traditional IRA, the assets held in a Roth IRA are tax-deferred, allowing for all of your dividends, interest payments, and capital gains to compound each year without being hindered by taxes. This allows for an IRA to grow much faster than a taxable account.

Contributions are restricted by income limitations and can be made at any age, provided that the IRA owner has earned income for the year that is equal to or greater than the contributed amount.

QUANTIFYING THE BENEFIT

Unlike the traditional IRA, which gives investors a tax deduction for the year the contribution is made, the Roth version lets savers contribute after-tax money today and withdraw principal and earnings tax-free at retirement. This is significant, because it is one of the only investment vehicles that can ensure a stream of tax-free income in retirement. Another significant advantage is the plan's flexibility; given that the principal invested can be withdrawn penalty-free (not the earnings), it offers the ability to provide emergency cash if needed.

PROFIT SHARING AND MONEY PURCHASE PLANS

Benefits and Key Features:	Additional tax deferral of earnings beyond 401(k) and IRA contributions
Eligibility:	Employees typically must have one year of service, work 1,000 hours per year, and be at least 21 years old
Contributions:	Employer only
Maximum Contribution:	Employer contributions specified in plan documents Total contributions cannot exceed the lesser of $54,000 or 25% of pay
Withdrawals:	Earnings and principal taxed as ordinary income Additional 10% penalty on withdrawals made prior to age 59½
Required Minimum Distributions:	RMDs begin at age 70½ unless still working For a 5%-or-more owner, RMDs must begin at age 70½ even if still working

Profit sharing and money purchase plans are used by partners in professional practices and small business owners who are already contributing the maximum to their defined contribution plans.

HOW THEY WORK

Both profit sharing and money purchase plans are defined contribution plans where the employer determines the timing and payment amounts. The primary difference between the two is that profit sharing plans are discretionary and typically allocate a set amount to all eligible employees depending on the profit that year, while money purchase plans are mandatory and provide a fixed percentage of eligible employee salary regardless of the employer earnings. Contributions and any subsequent earnings accumulate on a tax-deferred basis. Distributions, typically made at retirement, or earlier if employment is terminated, are taxed as regular income. Prior to age 59½, participants receiving distributions are subject to a 10% penalty tax, although it is waived under certain circumstances (e.g., qualified plan rollover, medical expenses, disability).

Like IRAs, assets in these plans may be withdrawn beginning at age 59½ with no tax penalty, and must be regularly withdrawn beginning at age 70½. While some plans allow for participants to self-direct investment choices, the majority of plans are run by professional administrators, with funding through mutual funds, ETFs (exchange-traded funds), variable annuities, and life insurance products. Most plans have a vesting schedule between three and six years, under which participants leaving the plan prior to the full vesting timeline may forfeit all or part of the account value.

QUANTIFYING THE BENEFIT

Profit sharing and money purchase plans can be used in conjunction with other retirement plans to provide significantly higher tax-deferred contributions, as compared to using only traditional IRA and 401(k) vehicles. They retain a high level of flexibility, even on termination of employment, because the value of the plan can be transferred without penalty into a qualified IRA plan. Keep in mind that administrative costs may be higher than under more basic arrangements such as SEP or SIMPLE IRA plans. Limitations related to vesting schedules should also be considered, as they may require longer employment prior to the earning of benefits.

CASH BALANCE PLANS

Benefits and Key Features:	Earnings grow tax-deferred
Eligibility:	Employees of almost any employer, including corporations, self-employed individuals, or partnerships
Contributions:	Employer only
Maximum Contribution:	Contributions are age-based and can be up to four or five times higher than for DC plans Maximum for employees age 55: $184,000 Maximum for employees age 62: $268,000
Withdrawals:	Generally rolled into an IRA upon retirement If not rolled over, earnings and principal taxed as ordinary income
Required Minimum Distributions:	RMDs begin at age 70½ unless still working

For partners in professional practices and small business owners who are already contributing the maximum to their defined contribution plans, a cash balance plan can be a great opportunity for additional tax-deferred savings. Higher tax rates have increased the popularity of these plans—especially among older, high-earning doctors and lawyers saving for retirement.

HOW THEY WORK

A cash balance plan is an employer-sponsored defined benefit (DB) plan with some features similar to a defined contribution (DC) plan. Contribution limits are based on age and, for older individuals, can be four or more times higher than for DC plans, as the charts on pages 31 and 32 demonstrate.

Each partner/participant can choose his or her own level of contribution, but should commit to a contribution level for at least three years. Participants have a notional individual account balance that they can roll into an IRA when they leave the firm. To establish the plan, the professional practice or small business engages an actuary to determine how much the partners/owners could defer for a given level of contributions to the staff. Typically, businesses that already have an existing 401(k) or profit sharing plan and staff-to-owners ratio of less than 10 to one are good candidates for cash balance plans.

The plan could significantly increase the deferral potential for the principals while only modestly increasing firm contributions on behalf of the employees.

QUANTIFYING THE BENEFIT

As with a DB plan, assets in a cash balance plan are typically pooled and invested with the goal of matching a target rate of return. The target return can vary by plan design and demographics, but most cash balance plans have a return goal of 1% to 6%; many plans target a return of about 4%. Exceeding or falling short of the target return can cause over- or underfunding issues that plan sponsors would rather avoid. The chief benefit of these plans is not the modest return the partners earn while invested in them—it's the ability to defer substantially more income that can eventually be rolled into an IRA, or converted to a Roth IRA, for additional future tax-deferred or tax-free growth.

DEFINED BENEFIT PLANS

Benefits and Key Features:	Provides a fixed, preset benefit for employees upon retirement that is guaranteed by the company Benefits typically governed by length of employment and ending salary level
Eligibility:	Employees of almost any employer, including corporations, self-employed individuals, or partnerships
Contributions:	Employer or employer/employee
Maximum Contribution:	Funding contributions are made annually by the employer or employer/employee to support future benefits Maximum limit on annual contributions is $215,000 as of 2017
Withdrawals:	Annual distributions of pension benefits are taxed as ordinary income In some cases may be rolled into an IRA or other qualified plan
Required Minimum Distributions:	Not applicable

Defined benefit plans, also commonly known as pension plans, are retirement plans where a company guarantees that employees will receive payments upon their retirement. These payments are usually based on their length of service and the salary they earned at the time of retirement.

HOW THEY WORK

Defined benefit plans have a long history dating back to 1875. They are designed such that the employer takes on an obligation to provide a specific benefit to the employee at retirement. Benefits are typically calculated based on the years worked by the employee, salary levels, and the age at retirement. For instance, a plan could have an agreement to pay employees 2% of their ending year salary for every year worked. Contributions to support the growth of, and distributions from, these plans are typically funded annually by the employer alone, although in some cases the funding is jointly provided by both employer and employee.

Defined benefit plans distribute their benefits through life annuities. In a life annuity, employees receive equal periodic benefit payments (monthly, quarterly, etc.) for the rest of their lives. A defined benefit pension plan allows joint distributions so a surviving spouse can still receive 50% of an employee's payment.

QUANTIFYING THE BENEFIT

Earlier in US history, defined benefit plans were overwhelmingly the most popular retirement solution for professionals and workers, although moving into the 21st century, they have seen a significant reduction in use by most companies. The exception to this is for government-related entities, where approximately 85% of the workforce remains covered by defined benefit programs. For employees, these plans offer the promise of lifetime income with known amounts and timing. Many plans are structured such that the spouse of the participant is similarly covered in the event of early death. It should be noted, however, that these plans come with specific risks related to the employer. In cases where the sponsor entity goes into bankruptcy or financial distress, these plans could be at significant risk. In some noteworthy examples (Enron, WorldCom), the participants lost nearly all assets.

412(i) PLAN

Benefits and Key Features:	Guaranteed benefits (provided that there is funding) Contributions are deductible Must invest in life insurance or annuities Higher contribution limits compared to other qualified plans
Eligibility:	All business entities are eligible for a 412(i) plan. Includes sole proprietorships, partnerships, C corporations, S corporations, and limited liability companies
Contributions:	Employer/owner
Maximum Contribution:	Determined by multiple factors, including compensation of owner, age of owner, and expected retirement date
Withdrawals:	Distribution of benefits are taxed as ordinary income
Required Minimum Distributions:	Not applicable

The 412(i) plan is a defined benefit pension plan, typically used by small businesses, that is funded entirely through guaranteed annuities or life insurance. As a tax-qualified benefit plan, all contributions made by the business owner are available as an immediate tax deduction for the company.

HOW IT WORKS

Plan must be set up by business owners in coordination with the IRS, so they may obtain the tax-deductible and tax-exempt conditions.

Contributions for annuity-funded plans are determined by establishing the guaranteed purchase rate of the annuities, and using that to determine how much is needed to provide the promised benefit at retirement. Where life insurance contracts are contributed instead of annuities, benefits are based on the guaranteed cash accumulation of the policies. Depending on the age and retirement date used for the calculations, the maximum contribution levels are typically significantly higher than deductions allowed under most other defined contribution and defined benefit plans.

QUANTIFYING THE BENEFIT

The 412(i) plan is targeted for small business owners (five or fewer employees) who typically are nearing retirement and want to increase their retirement benefits through additional life insurance. All contributions are tax-deductible, making this an attractive option for those owners and private practices with significant taxable income to offset. Additionally, the plans allow for significantly higher contribution levels as compared to other small business-oriented plans, such as cash balance and profit sharing plans. Combined with the requirement that proceeds be invested in life insurance products, this vehicle typically can provide lower investment risk and tax risk as compared to equivalent retirement strategies.

457(b) PLAN

Benefits and Key Features:	Earnings grow tax-deferred Contributions are pretax and can reduce employees' taxable income Contributions can be made in addition to a 403(b) or 401(k)
Eligibility:	Employees and independent contractors of certain state and local governments and nongovernmental entities that are tax-exempt under IRC Section 501
Contributions:	Employee and employer
Maximum Contribution:	Employees under age 50: the lesser of $18,000 or earned income for the year Employees age 50 and over: the lesser of $24,000 or earned income for the year
Withdrawals:	Earnings and principal taxed as ordinary income Unlike most other retirement plans, withdrawals can be made at any age without penalty
Required Minimum Distributions:	RMDs begin at age 70½ unless still working

The 457(b) plan is used largely by state and local governments and tax-exempt organizations to give employees the option to defer their compensation into a tax-advantaged retirement plan. The employer provides the plan, while the employee is able to make pretax contributions to it.

HOW IT WORKS

A 457(b) plan provides tax deferral in addition to a 403(b) and 401(k) program. This plan is available to all employees or to contractors of the sponsoring entity. Contributions are made pretax annually, with the maximum deferral set similar to that used for the 403(b) or 401(k) plan ($18,000/year in 2017). Catch-up contributions are also allowed for participants age 50 and over, in addition to a special 457 catch-up provision that allows older participants to apply unused deferral amounts from previous years.

QUANTIFYING THE BENEFIT

The primary benefit of a 457(b) plan is flexible, tax-deferred savings. Unlike most other plans, withdrawals and distributions are allowed at any time. Distributions earlier than age 59½ do not incur extra penalties, unlike IRA and 401(k) plans.

Upon leaving employment after age 59½, employees have the option to roll the amounts into equivalent plans such as IRAs or 401(k) programs. Key benefits of the 457(b) plan, as compared to the 457(f) variant, include the ability for participants to self-direct investments in some cases, and protection against forfeiture of assets.

457(f) PLAN

Benefits and Key Features:	No contribution limit Earnings grow tax-deferred Contributions can be made in addition to a 403(b) or 401(k)
Eligibility:	Select or "top-paid group" in state/local government entities or any 501(c) tax-exempt organization
Contributions:	Employer
Maximum Contribution:	No maximum contribution so long as certain criteria are met
Withdrawals:	Benefits become fully taxable upon vesting
Required Minimum Distributions:	No required minimum distributions

The 457(f) plan is used largely by state and local governments and tax-exempt organizations to retain their top employees. Unlike the 457(b) program, this plan has no maximum contribution limit, provided that certain conditions are met.

HOW IT WORKS

The 457(f) plan may be offered to only the "top-paid group" within an organization, designated as "individuals who have the ability to affect or substantially influence the design and operation of the NQDC[2] plan." It is also used for salary continuation, income deferral, and death benefits.

Contributions are made by the employer annually and are reported on the W-2 for the employee as wages. The plans can be structured either as defined benefit (DB) or defined contribution (DC). Under a DB plan, the employer provides the participant with a specified percentage of final average compensation, similar to a pension plan. The benefit may be targeted as a total percentage, offset by the employer's qualified plan benefits. Under a DC plan, the employer makes specified annual contributions into a participant's account, based on a formula or metrics designed by the employer. Unlike the 457(b) plans, rollovers to other plan types are not permitted.

QUANTIFYING THE BENEFIT

These 457(f) plans are popular retirement vehicles used to compensate top executives in cases where limitations on other plans cannot provide adequate compensation. For instance, under the qualified 457(b) plan, participants currently have an $18,000 contribution limit, while the nonqualified 457(f) has no limits on contributions. The primary drawback of participating in a 457(f) is that the accrued amounts could be subject to forfeiture if the sponsoring company falls into financial distress, as these plans are considered unsecured creditors by the courts until the plans are vested.

[2]*Nonqualified deferred compensation*

RESTRICTED PROPERTY TRUST

Benefits and Key Features:	Allows for sizable transfer of income into a tax-deferred life insurance policy Does not impact limits on other qualified plans Contributions are tax-deductible to the employer or business owner
Eligibility:	Any S corporation, C corporation, limited liability company, or partnership can sponsor it and participation is completely discriminatory, enabling the business to limit the plan to only specific individuals
Contributions:	All contributions are made by the employer across a maximum period of five years Minimum contribution of at least $50,000/year
Maximum Contribution:	No set limit is mandated for these plans Contributions should provide “reasonable compensation,” a broad definition that would allow high earners to contribute significant savings
Withdrawals:	No withdrawals or loans allowed during funding After successful completion of funding period, policy is distributed to participant
Required Minimum Distributions:	Not applicable

The restricted property trust (RPT) is a life insurance plan initiated by employers that is typically offered to owners and key management.

HOW IT WORKS

Under this plan, the employer commits to making annual contributions to a life insurance policy benefiting the participant. These contributions are completely deductible to the employer, while only partially taxable to the participant. Once assets are in the plan, all asset growth is tax-deferred until the plan is ultimately terminated.

Given that the plan is not considered qualified, these contributions do not impact contributions to other qualified plans, nor are participants subject to the typical limits or tests. These plans typically have a funding period of no longer than five years, and any missed contributions during this time will cause the policy to lapse and all assets to be liquidated to a designated charity. Upon successful completion of the funding period, the policy is then distributed to the participant, who has the following options:

- Retain the policy for the eventual death benefit
- Leverage to provide nontaxable cash flow
- Exchange for annuity with larger income stream
- Exchange for life insurance policy with larger death benefit

Should the participant die prior to completion of the funding period, the death benefit remains intact and is passed along to the participant’s designated beneficiaries. Outside of these benefits, the plan also provides creditor protection and flexibility in terms of the amounts contributed per participant.

QUANTIFYING THE BENEFIT

This strategy is a popular retirement planning vehicle for business owners and upper management, given that it does not have stipulations on maximum contribution amounts. For an executive with significant earnings, this provides an alternate path to shelter large income amounts with tax-deferred growth.

The primary risk in this strategy is that all plan assets are subject to forfeiture (to a participant-designated charity) in the event that the employer fails to make an annual contribution across the planned funding period.

NONQUALIFIED DEFERRED COMPENSATION (NQDC) PLAN

Benefits and Key Features:	Allows for tax-deferred growth of salary contributions, with no limit on size of deferred amounts
Eligibility:	Any company can offer these types of plans, but they are typically only offered to top executives or key employees
Contributions:	All contributions made by employee in the form of salary deferrals
Maximum Contribution:	Plan allows for unlimited deferrals up to the salary earned by an individual
Withdrawals:	No withdrawals or loans allowed Plans may be structured to provide different forms of payout, such as a lump sum or graduated distributions
Required Minimum Distributions:	Not applicable All distributions are specified in the plan contract

A nonqualified deferred compensation plan (also known as a 409A plan) is an elective or nonelective plan, agreement, method, or arrangement between an employer and an employee to pay the employee or independent contractor compensation in the future.

HOW THEY WORK

The primary benefit of NQDC plans is that they allow for tax deferral of large blocks of income, well in excess of the 401(k) plan limits. This is especially important for those with higher salary levels, because it allows them to put aside significant tax-deferred savings. For instance, consider an executive making $300,000 per year. The maximum 401(k) contribution of $18,000 would represent only 6% of the executive's salary, but the addition of significant savings into a NQDC plan could bridge the gap toward achieving his or her retirement goals. Unlike qualified retirement vehicles, taxes are deferred for the participant, with the exception of Social Security and Medicare. Sometimes the assets may be segregated into a special trust (called a rabbi trust), but they still remain subject to creditor claims if the company becomes insolvent. Assets held within these plans are typically not available to participants until the contracted distribution date(s). Some plans allow for early distributions in cases of employment termination, or for shorter-term goals such as payments for college tuition, but these are specific to each individual plan agreement.

QUANTIFYING THE BENEFIT

This strategy has strong benefits and drawbacks that must be carefully considered. Given that NQDC plans allow for unlimited salary deferral into a tax-deferred structure, they are very popular for individuals who have maxed out traditional retirement options and still have significant amounts of excess income. This benefit, however, must be weighed against the substantial risk, given that the assets are owned by the sponsoring company. In the event of bankruptcy, these assets would be subject to the creditor's claims. As such, participants must weigh the potential benefits of the tax deferral against the strength of the sponsoring company, and their ability to lose that money in the event of future financial distress.

QUICK REFERENCE GUIDE: DC PLANS

	TRADITIONAL 401(k)/403(b)	SIMPLE 401(k)	ROTH 401(k)/403(b)	PROFIT SHARING AND MONEY PURCHASE PLANS
Key Features	Earnings grow tax-deferred Contributions are deductible for employer Contributions reduce employee's taxable income	Earnings grow tax-deferred Contributions are deductible for employer Contributions reduce employee's taxable income	Earnings grow tax-free Contributions are not deductible Contributions do not reduce employee's taxable income	Earnings grow tax-deferred Contributions are deductible for employer Profit sharing plan contributions are discretionary Money purchase plan contributions are mandatory
Eligibility	401(k): Employees must have one year of service, work 1,000 hours per year, and be at least 21 years old 403(b): Employees of religious, charitable, educational, and other organizations described in IRC Section 501(c)(3), certain governmental organizations, and public school systems	Employers with 100 or fewer employees that do not currently maintain another retirement plan Employees must have one year of service, work 1,000 hours per year, and be at least 21 years old	401(k): Employees must have one year of service, work 1,000 hours per year, and be at least 21 years old 403(b): Employees of religious, charitable, educational, and other organizations described in IRC Section 501(c)(3), certain governmental organizations, and public school systems	Employees must have one year of service, work 1,000 hours per year, and be at least 21 years old
Contributors	Employee and employer	Employee and employer	Employee only	Employer only
Maximum Contribution	Employees under age 50: the lesser of $18,000 or earned income for the year Employees age 50 and over: the lesser of $24,000 or earned income for the year Total employer/employee contributions for 403(b) plans are capped at $54,000 for employees under age 50; $60,000 for those age 50 and over	Employees under age 50: the lesser of $12,500 or 100% of pay Employees age 50 and over: the lesser of $15,500 or 100% of pay Employer must match up to 3% of employee contribution or 2% of pay each year	Employees under age 50: the lesser of $18,000 or earned income for the year Employees age 50 and over: the lesser of $24,000 or earned income for the year	Employer contributions specified in plan documents Total contributions cannot exceed the lesser of $54,000 or 25% of pay
Withdrawals	Earnings and principal taxed as ordinary income Additional 10% tax on withdrawals made prior to age 59½* RMDs begin at age 70½ unless still working; for a 5%-or-more owner, RMDs must begin at age 70½ even if still working	Earnings and principal taxed as ordinary income Additional 10% tax on withdrawals made prior to age 59½* RMDs begin at age 70½ unless still working; for a 5%-or-more owner, RMDs must begin at age 70½ even if still working	Earnings taxed as ordinary income, if taken before age 59½; distributions of principal and earnings are tax-free if taken after age 59½* Additional 10% tax (on earnings) for withdrawals made prior to age 59½* RMDs begin at age 70½ unless still working; for a 5%-or-more owner, RMDs must begin at age 70½ even if still working	Earnings and principal taxed as ordinary income Additional 10% tax on withdrawals made prior to age 59½* RMDs begin at age 70½ unless still working; for a 5%-or-more owner, RMDs must begin at age 70½ even if still working

Some exceptions apply

QUICK REFERENCE GUIDE: DB PLANS

	CASH BALANCE PLANS	DEFINED BENEFIT PLANS
Key Features	Earnings grow tax-deferred Higher contribution limits for older individuals	Earnings grow tax-deferred Higher contribution limits for older individuals
Eligibility	Almost any employer, including corporations, self-employed individuals, entities, or partnerships Best for closely held firms with highly paid partners, owners, or shareholders, such as law and accounting firms and medical practices	Almost any employer, including corporations, self-employed individuals, entities, or partnerships
Contributors	Employer only	Employer or employer/employee
Maximum Contribution	Contributions are age-based and can be up to four or five times higher than for DC plans Maximum for employees age 55: $184,000 Maximum for employees age 62: $268,000	Annually determined contributions, based on plan terms and actuarial calculations
Withdrawals	Generally rolled into an IRA upon retirement If not rolled over, earnings and principal taxed as ordinary income, and RMDs begin at age 70½ unless still working	Distributions are taxed as ordinary income Can be rolled into an IRA upon retirement, if plan permits Benefits are paid after a specified event and based on plan terms

QUICK REFERENCE GUIDE: IRA-BASED PLANS

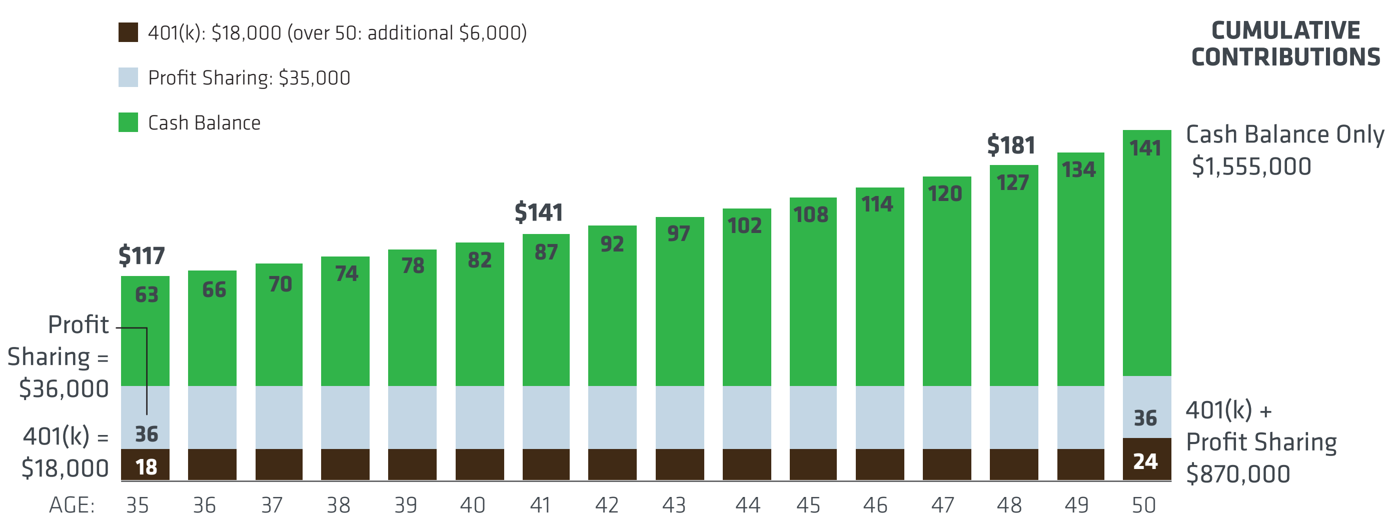
	TRADITIONAL IRA	SIMPLE IRA	SEP IRA	ROTH IRA
Key Features	Earnings grow tax-deferred Contributions can be deductible	Earnings grow tax-deferred Contributions can be deductible for employer and reduce employee's taxable income	Earnings grow tax-deferred Contributions can be deductible for employer Simple to set up and maintain	Earnings grow tax-deferred Contributions are not deductible and do not reduce employee's taxable income
Eligibility	Any individual under age 70½ can contribute Contributions are deductible for individuals with earned income and/or spouse with modified AGI at or below phaseout range Married Filing Jointly, with employer plan: \$99,000–\$119,000 Married Filing Separately, with employer plan (spouse): \$0–\$10,000 Single or Head of Household, with employer plan: \$62,000–\$72,000	Employers with 100 or fewer employees that do not maintain another retirement plan Employees must have earned \$5,000 or more in any of the prior two years and are expected to earn at least \$5,000 in the current year	Self-employed individuals and small firms Employees must be at least 21 years old, have worked for the company for three of the last five years, and earned at least \$600 in most recent year	Any individual with earned income and/or spouse with modified AGI at or below phaseout range Married Filing Jointly: \$186,000–\$196,000 Married Filing Separately: \$0–\$10,000 Single or Head of Household: \$118,000–\$133,000
Contributors	Employee only	Employee and employer	Employer only	Employee only
Maximum Contribution	Under age 50: the lesser of \$5,500 or earned income for the year Age 50 and over: the lesser of \$6,500 or earned income for the year	Employees under age 50: the lesser of \$12,500 or 100% of pay Employees age 50 and over: the lesser of \$14,500 or 100% of pay Employer must match up to 3% of employee contributions or 2% of pay each year; can be 1% of employee contributions for two of five years	Up to 25% of compensation, but no more than \$53,000 Lesser of 20% of net earnings from self-employment or \$53,000	Under age 50: the lesser of \$5,500 or earned income for the year Age 50 and over: the lesser of \$6,500 or earned income for the year
Withdrawals	Earnings and pretax contributions taxed as ordinary income Additional 10% tax on withdrawals made prior to age 59½* RMDs begin at age 70½ unless still working	Earnings and pretax contributions taxed as ordinary income Additional 25% tax on withdrawals made within the first two years of participation and 10% thereafter prior to age 59½* RMDs begin at age 70½ even if still working	Earnings and pretax contributions taxed as ordinary income Additional 10% tax on withdrawals made prior to age 59½* RMDs begin at age 70½ even if still working	Distributions of earnings are tax-free if taken after age 59½ and if IRA is held for at least five years Earnings subject to ordinary income taxes Additional 10% tax on withdrawals made prior to age 59½* No RMDs

**Some exceptions apply*

APPENDIX

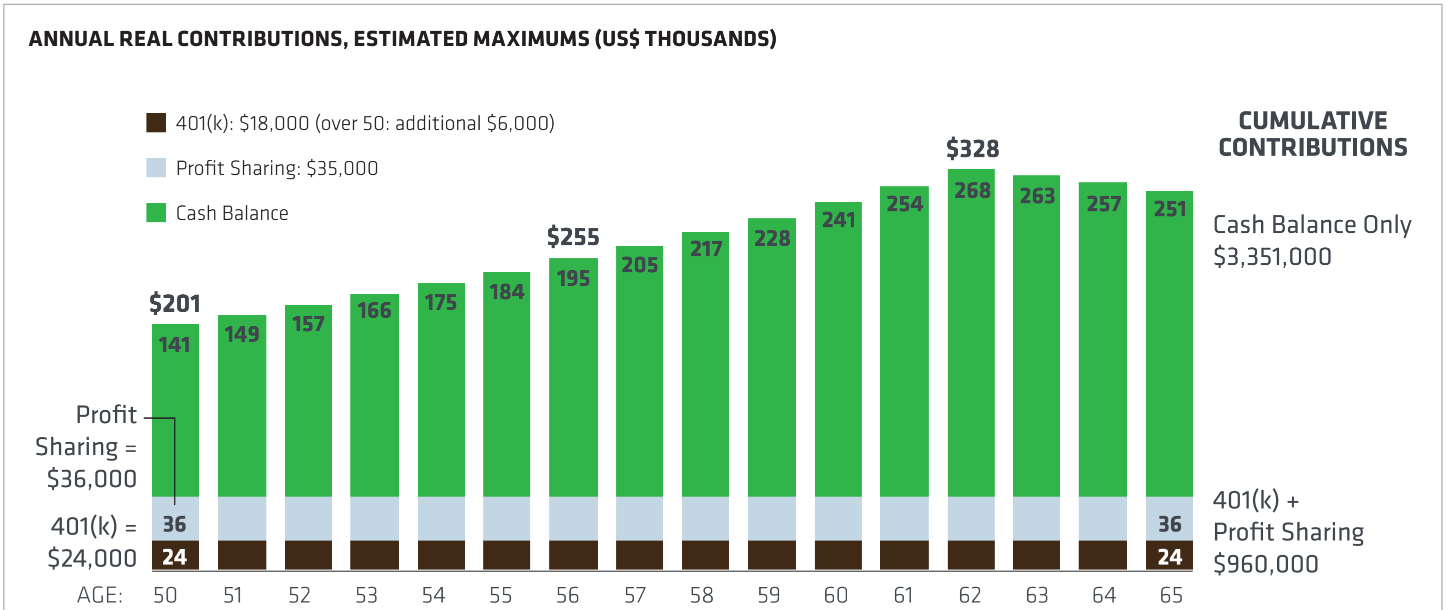
2017 Defined Benefit Contribution Limits

ANNUAL REAL CONTRIBUTIONS, ESTIMATED MAXIMUMS (US$ THOUSANDS)



Source: AB

2017 Defined Benefit Contribution Limits



Source: AB

NOTES ON WEALTH FORECASTING SYSTEM

1. **Purpose and Description of Wealth Forecasting System**
   Bernstein's Wealth Forecasting System[SM] is designed to assist investors in making long-term investment decisions regarding their allocation of investments among categories of financial assets. Our planning tool consists of a four-step process: 1) Client Profile Input: The client's asset allocation, income, expenses, cash withdrawals, tax rate, risk-tolerance level, goals, and other factors; 2) Client Scenarios: In effect, questions the client would like our guidance on, which may touch on issues such as when to retire, what his/her cash-flow stream is likely to be, whether his/her portfolio can beat inflation long term, and how different asset allocations might impact his/her long-term security; 3) The Capital Markets Engine: Our proprietary model, which uses our research and historical data to create a vast range of market returns, takes into account the linkages within and among the capital markets, as well as their unpredictability; and 4) A Probability Distribution of Outcomes: Based on the assets invested pursuant to the stated asset allocation, 90% of the estimated ranges of returns and asset values the client could expect to experience are represented within the range established by the 5th and 95th percentiles on "box-and-whiskers" graphs. However, outcomes outside this range are expected to occur 10% of the time; thus, the range does not establish the boundaries for all outcomes.

   Expected market returns on bonds are derived taking into account yield and other criteria. An important assumption is that stocks will, over time, outperform long bonds by a reasonable amount, although this is in no way a certainty. Moreover, actual future results may not meet Bernstein's estimates of the range of market returns, as these results are subject to a variety of economic, market, and other variables. Accordingly, the analysis should not be construed as a promise of actual future results, the actual range of future results, or the actual probability that these results will be realized.

2. **Retirement Vehicles**
   Each retirement plan is modeled as one of the following vehicles: traditional IRA, 401(k), 403(b), or Roth IRA/401(k). One of the significant differences among these vehicle types is the date at which mandatory distributions commence. For traditional IRA vehicles, mandatory distributions are assumed to commence during the year in which the investor reaches the age of 70½. For 401(k) and 403(b) vehicles, mandatory distributions are assumed to commence at the later of 1) the year in which the investor reaches the age of 70½ or 2) the year in which the investor retires. In the case of a married couple, these dates are based on the date of birth of the older spouse. The minimum mandatory withdrawal is estimated using the Minimum Distribution Incidental Benefit tables as published on www.irs.gov. For Roth IRA/401(k) vehicles, there are no mandatory distributions. Distributions from Roth IRA/401(k) vehicles that exceed principal will be taxed and/or penalized if the distributed assets are less than five years old and the contributor is less than 59½ years old. All Roth 401(k) plans will be rolled into a Roth IRA plan when the investor turns 59½ years old, to avoid minimum distribution requirements.

3. **Rebalancing**
   Another important planning assumption is how the asset allocation varies over time. Cash flows and cash generated from portfolio turnover are used to maintain the selected asset allocation between cash, bonds, stocks, REITs, and hedge funds over the period of the analysis. Where this is not sufficient, assets are assumed to be sold to rebalance.

4. **Expenses and Spending Plans (Withdrawals)**
   All results are generally shown after applicable taxes and after anticipated withdrawals and/or additions, unless otherwise noted. Liquidations may result in realized gains or losses, which will have capital gains tax implications.
5. **Modeled Asset Classes**
   The following assets or indexes were used in this analysis to represent the various model classes:

Asset Class	Modeled As	Annual Turnover
Cash Equivalents	3-month US Treasury bills	100%
Int.-Term Taxables	Taxable bonds of 7-year maturity	30
Int.-Term Diversified Municipals	AA-rated diversified municipal bonds of 7-year maturity	30
US Diversified	S&P 500 Index	15
US Value	S&P/Barra Value Index	15
US Growth	S&P/Barra Growth Index	15
US Small-/Mid-Cap	Russell 2500 Index	15
Developed International	MSCI EAFE Index (Unhedged)	15
Emerging Markets	MSCI Emerging Markets Index	20

6. **Volatility**
   Volatility is a measure of dispersion of expected returns around the average. The greater the volatility, the more likely it is that returns in any one period will be substantially above or below the expected result. The volatility for each asset class used in this analysis is listed in the Capital-Market Projections section at the end of these Notes. In general, two-thirds of the returns will be within one standard deviation. For example, assuming that stocks are expected to return 8.0% on a compounded basis and the volatility of returns on stocks is 17.0%, in any one year, it is likely that two-thirds of the projected returns will be between (8.9)% and 28.8%. With intermediate-term government bonds, if the expected compound return is assumed to be 5.0% and the volatility is assumed to be 6.0%, two-thirds of the outcomes will typically be between (1.1)% and 11.5%. Bernstein's forecast of volatility is based on historical data and incorporates Bernstein's judgment that the volatility of fixed income assets is different for different time periods.
7. **Technical Assumptions**
   Bernstein's Wealth Forecasting System is based on a number of technical assumptions regarding the future behavior of financial markets. Bernstein's Capital Markets Engine is the module responsible for creating simulations of returns in the capital markets. These simulations are based on inputs that summarize the current condition of the capital markets as of December 31, 2016. Therefore, the

first 12-month period of simulated returns represents the period from December 31, 2016, through December 31, 2017. A description of these technical assumptions is available on request.

8. **Tax Implications**
   Before making any asset allocation decisions, an investor should review with his/her tax advisor the tax liabilities incurred by the different investment alternatives presented herein, including any capital gains that would be incurred as a result of liquidating all or part of his/her portfolio, retirement-plan distributions, investments in municipal or taxable bonds, etc. Bernstein does not provide tax, legal, or accounting advice. In considering this material, you should discuss your individual circumstances with professionals in those areas before making any decisions.

9. **Capital-Market Projections**

Asset Class	Median 40-Year Growth Rate	Mean Annual Return	Mean Annual Income	One-Year Volatility	40-Year Annual Equivalent Volatility
Cash Equivalents	3.6%	4.0%	4.0%	0.3%	13.9%
Intermediate-Term Diversified Municipals	3.9	4.2	4.0	3.9	10.2
Intermediate-Term Taxables	5.0	5.4	6.6	4.9	12.0
Global International Taxable Bonds—Hedged	4.3	4.7	5.7	4.1	12.5
US Diversified Stocks	7.7	9.5	3.2	16.4	23.9
US Value Stocks	8.0	9.7	3.9	16.0	23.3
US Growth Stocks	7.5	9.6	2.6	18.2	25.4
US Small-/Mid-Cap Stocks	7.9	10.1	2.9	18.7	25.8
Developed International	8.5	10.8	3.5	18.1	24.6
Emerging-Market Stocks	6.7	10.8	4.7	26.1	31.3
Inflation	3.3	3.7	n/a	1.2	13.6

Note to All Readers:

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Based on 10,000 simulated trials, each consisting of 45-year periods. Reflects Bernstein's estimates and the capital-market conditions as of December 31, 2016. Does not represent any past performance and is not a guarantee of any future specific risk levels or returns, or any specific range of risk levels or returns.

Disclosure on Security Examples

References to specific securities are presented to illustrate the application of our investment philosophy only and are not to be considered recommendations by AllianceBernstein.

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