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Retirement Plan Contribution Limits in 2012

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Each year IRS makes cost of living adjustments to many of the limits on benefits from - and contributions to - qualified and non-qualified retirement plans. Here are the new limits for 2012:

- The maximum annual contribution to an individual's account (including the individual's 401(k) contributions, profit-sharing contributions and employer qualified non-elective contributions) in a defined contribution plan (a money-purchase, profit sharing or 401(k) plan) cannot exceed the lesser of 100% of the individual's compensation or $50,000. That amount is $1,000 more than the 2011 limitation and it includes employer contributions, employee 401(k) contributions and forfeitures. If your defined contribution plan has a fiscal year other than the calendar year, this new limit is effective for plan limitation years ending in 2012. An individual who is 50 or older in 2012 and participates in a 401(k) plan can make an additional 401(k) "catch-up" contribution of up to $5,500 over and above the $50,000 amount.

- The maximum annual 401(k) contribution an individual can make has been increased by $500 to $17,000. An individual who is 50 or older in 2012 can make an additional "catch-up" 401(k) contribution of up to $5,500 (unchanged from 2011) over and above the $17,000 limit. These limitations include Roth 401(k) contributions; in other words, total 401(k) contributions are limited to $17,000 (plus the $5,500 catch-up amount if applicable) regardless of how much of the total comes from "pre-tax" 401(k) contributions and how much from Roth 401(k) contributions.

- The maximum annual benefit which may be paid to an individual in a defined benefit plan is the lesser of 100% of the individual's average compensation for the highest paid three consecutive years of his or her employment, or $200,000. This is a $5,000 increase over the 2011 limitation. If your defined benefit plan has a fiscal year other than the calendar year, this limit is effective for plan limitation years ending in 2012.

- The maximum amount of an employee's annual compensation which may be taken into account for contribution or benefit calculation purposes is $250,000, effective for plan years beginning in 2012. This also represents a $5,000 increase to the 2011 limitation.

- For tax-exempt entities, the maximum amount which an individual may contribute to a 457(b) plan is increased by $500 to $17,000. The "catch-up" contribution of up to $5,500 over and above the $17,000 contribution limit for an individual who is age 50 or older in 2012 remains unchanged.

- Special rules apply to "topheavy" plans. A defined contribution plan is topheavy if the aggregate account balances of key employees exceed 60% of the aggregate account balances of all plan participants. A defined benefit plan is topheavy if the present value of the accrued benefits of key employees exceeds 60% of the present value of the accrued benefits of all plan participants. For 2012, the compensation paid to an officer that would cause him or her to be classified as a "key employee" is increased by $5,000 to $165,000.

- A retirement plan may not discriminate in favor of "highly compensated" employees. An employee is a highly compensated employee in 2012 if the employee either (1) owns greater than 5% of the ownership interests in the employer, or (2) earned over $110,000 in 2011 and, if applicable, is in the top 20% of employees when ranked by pay. For purposes of determining who will be a highly compensated employee in 2013, the dollar limitation has been increased by $5,000 from $110,000 to $115,000.

- The Social Security taxable wage base used in plans whose contribution formulas are integrated with Social Security is increased in 2012 from $106,800 to $110,100.

On a fairly regular basis, companies, associations and other organizations should review their plan's design to ensure that the key employees are benefiting from the increased contributions, and that the plan is operating as a valuable recruitment and retention tool. You may want us to review your current retirement plan to make sure it maximizes the potential benefits and is consistent with the overall business objectives of the organization.