Profit-sharing plans

Profit-sharing plans allow employers to make discretionary, tax-deductible contributions for their employees in a similar manner to that of the SEP IRA. However, profit-sharing plans provide employers with more control over eligibility requirements and vesting schedules. Its important to note that ALL 401(k)s are profit-sharing plans, but a profit-sharing plan does not require a 401(k) provision.

Advantages of a profit-sharing plan

High contribution limits: For 2024, employers may contribute up to the lesser of 25% compensation or $69,000. In 2025 it increases to $70,000.

Choice: The amount of the contribution can change from year to year and is up to the employer to determine.

Integration permitted: Contributions may either be a flat percentage of each employee's compensation, or they may be integrated with the Social Security taxable wage base ($168,600 for 2024 and $176,100 for 2025). Employees earning more than this receive a greater portion of the contribution to compensate for the smaller percentage of Social Security benefits they accrue.

Flexibility: Employer may establish a vesting schedule and decide whether or not to make loans and hardship withdrawals available to participants.

Eligibility: Part-time and seasonal employees may be excluded with eligibility requirements.

Other profit-sharing plan considerations

- Subject to ERISA reporting.
- Moderate administration.
- In general, the same percentage of compensation must be contributed on behalf of all participants.
- For 2024, if a 401(k) is offered in conjunction with a profit-sharing plan, the combination of employee deferrals and employer contributions (including matching contributions) is the lesser of $69,000 or 100% of compensation. For 2025, it increases to $70,000. These amounts do not include the catch-up amounts for the 401(k) - See the IRS chart for catch-up contributions if employee is age 50 or older.

See next page for alternate contribution options.

Profit sharing plan variations

Profit-sharing plans offer variations to accommodate the needs of different employers. These variations allow business owners to skew contributions toward older, more highly paid employees. Profit-sharing plan variations include age-weighted plans, new comparability plans and super comparability plans.

Age-weighted plans: Contributions are based on a formula that takes both age and compensation into account. Older employees receive larger contributions than their younger counterparts.

New comparability plans: Similar to an age-weighted plan, but instead of considering just age and compensation, new comparability plans allow employers to categorize employees by several criteria, including tenure, ownership, job function and age. Using these criteria, employers can determine an allocation formula to group employees as either “preferred” or “non- preferred.” The preferred group receives a greater share of the contributions.

Super comparability plans: A hybrid of the Safe Harbor 401(k) and the new comparability plan design, the super comparability plan allows employees to contribute to their own 401(k) accounts while also receiving profit-sharing contributions from their employer. A non-elective 3% employer contribution to all employees satisfies the Safe Harbor requirement and allows HCEs to make the maximum salary deferral to their own accounts ($23,000 in 2024; for 2025 it increases to $23,500). See IRS chart for catch-up contributions if employee is 50 or older.