UNDERSTANDING 401(K) AND PROFIT SHARING PLANS

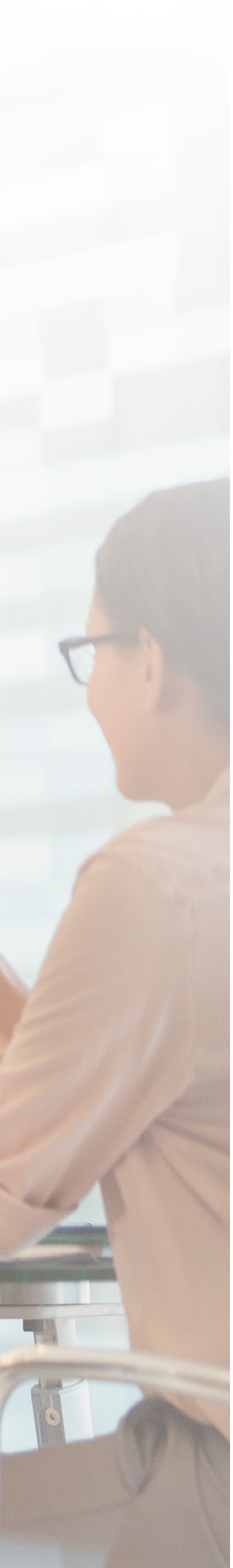
Choosing an option that benefits your business and your employees.

RAYMOND JAMES

As a business owner, you're likely concerned about retirement, for yourself and your employees.

Often, the issue isn't whether to implement a retirement plan but how to choose the one that will work best. This brochure is designed to help you decide which profit sharing plan is right for your business by comparing the most popular types available, including:

- Traditional profit sharing plans
- Age-weighted and new comparability profit sharing plans
- 401(k) plans and structures



PROFIT SHARING PLANS

Profit sharing plans offer employers both design flexibility and discretion with regard to contributions. Employer contributions are self-determined and can be allocated in a number of ways. If an employer makes little or no profit during a year, no contribution is required, although an employer is permitted to make contributions even if the company is not profitable.

An employer's maximum deduction is limited to 25% of the annual compensation paid to eligible employees. For 2022, the individual maximum contribution limit for employees applied to all defined contribution plans is 100% of compensation or $61,000, whichever is less. Depending on a profit sharing plan's allocation formula, the contributions for individual employees may exceed the 25% level as long as the aggregated employer contribution does not exceed the 25% maximum employer contribution limit.

There are three basic types of profit sharing plans: traditional, age-weighted and new comparability. The differences between the plans are the contribution allocation formulas used for each one. The following sections discuss the three types of plans.

TRADITIONAL PROFIT SHARING PLAN

A traditional profit sharing plan follows the salary ratio method, which is designed to allocate employer contributions to all participants on a uniform basis. For example, if one employee receives a 10%-of-pay contribution, all eligible employees would be allocated 10% of compensation as their share of the contribution. A profit sharing plan with a salary ratio formula is similar to a simplified employee pension (SEP) plan, but may be more attractive than a SEP plan in situations where an employer (a) does not wish to cover certain part-time employees, (b) wants to make employer contributions subject to a vesting schedule or (c) wants more control over the assets.

AGE-WEIGHTED

The age-weighted method allocates contributions based on both the age and compensation of eligible employees. It is similar to a defined benefit pension plan, but gives employers the option of making discretionary contributions. Since a participant's age or length of time until retirement is factored into the allocation formula, older participants receive a proportionately larger share of the contribution. This can be advantageous in situations where a company's key employees are significantly older than its other employees.

Although this type of plan is available to any size company, age-weighted plans are designed to be top heavy and are especially well-suited for small businesses and professional practices.

With an age-weighted plan, some employees receiving equal compensation could receive different profit sharing allocations, based on age. In addition, an older non-principal employee may receive a larger share than a younger principal.

NEW COMPARABILITY

The new comparability, or cross-tested, allocation method allows an employer to divide employees into different classifications for purposes of allocating contributions. If non-discrimination requirements are met, a larger share of a company's contribution may be made on behalf of those employees to whom the employer wishes to provide more significant benefits.

As with an age-weighted plan, non-discrimination testing is based on projected benefits at retirement, similar to a defined benefit plan. If the aggregated age of the favored employee group is higher than the other groups, the allocation of current dollars can be skewed proportionately toward the older group. This type of plan involves complicated calculations and may require actuarial consulting, but it is typically less expensive and more flexible than a defined benefit plan.

This plan may be appropriate in a situation where a business wants to favor older or highly paid participants. These plans may establish several "class" designations of employees, such as placing principals in the first group, officers in the second group and all other employees in the third group.

Eligible Employee	Age	W-2 Compensation	Traditional Profit Sharing Plan	Social Security Integrated	Age-Weighted	New Comparability
Officer 1	57	$305,000	$30,500	$31,814	$53,537	$33,296
Officer 2	38	$305,000	$30,500	$31,814	$11,363	$33,296
Employee 1	50	$40,000	$4,000	$2,832	$3,967	$1,515
Employee 2	35	$30,000	$3,000	$2,124	$875	$1,136
Employee 3	25	$20,000	$2,000	$1,416	$258	$757
TOTALS		**$700,000**	**$70,000**	**$70,000**	**$70,000**	**$70,000**

This chart is an example of the available allocation methods in a profit sharing plan using a 10% contribution.

Eligible Employee	Age	W-2 Compensation	Traditional Profit Sharing Plan	Social Security Integrated	Age-Weighted	New Comparability
Officer 1	57	$305,000	$61,000	$61,000	$61,000	$61,000
Officer 2	38	$305,000	$61,000	$61,000	$12,947	$61,000
Employee 1	50	$40,000	$8,000	$6,659	$4,519	$2,772
Employee 2	35	$30,000	$6,000	$4,994	$997	$2,079
Employee 3	25	$20,000	$4,000	$3,330	$294	$1,386
TOTALS		**$700,000**	**$140,000**	**$136,983**	**$79,757**	**$128,237**

This chart is an example of the available allocation methods in a profit sharing plan designed to maximize contributions for the oldest owner.

CONSIDER A 401(K) PLAN FOR YOUR COMPANY, YOUR EMPLOYEES AND YOURSELF

Your company's success depends on quality employees. Attracting and retaining them often takes more than a competitive salary or a satisfying environment. Workers today expect added benefits including the means to save for retirement through options such as a 401(k) plan.

As a business owner, you likely already recognize the importance of offering – and receiving – such a benefit. Establishing a 401(k) plan can provide you and your employees with the means for achieving secure retirements, while also helping you gain tax* advantages for your business and ultimately benefiting your company's bottom line.

However, deciding which 401(k) arrangement is best for your organization – and then maintaining the plan – can be a challenge. That's where we can help. Our goal is to work with you to determine the best approach for your business and then identify the plan that best meets your company's unique needs.

We not only assist in evaluating options, but work with you on an ongoing basis to coordinate the different components of the 401(k) process. We believe that establishing a 401(k) plan for your company also means creating long-term relationships with your employees – helping them understand how to invest and coordinate their 401(k) allocations with their other assets to develop complete financial plans.

The next few pages offer an overview of 401(k) plans and the decisions needed to ensure your company's program is effective.

ABOUT 401(K) PLANS

A 401(k) is a profit sharing retirement plan that allows employees to make elective salary deferrals while avoiding current taxes on that portion of their incomes. Most employers, including not-for-profit organizations but excluding government entities, can offer a 401(k) plan to their employees.

The Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) allowed employees to add qualified Roth contributions to 401(k) plans starting January 1, 2006. The Roth 401(k) contributions only apply to employees' elective salary deferrals.

An employer should consider several basic factors when evaluating whether a 401(k) plan is right for his or her company:

ELIGIBILITY REQUIREMENTS

Employees who are at least 21 years old and who have completed one year of service are generally eligible to participate. Certain employees, such as those covered by a collective bargaining agreement, may be legally excluded.

Funding the 401(k) plan

A 401(k) plan can be funded from one or more of the following sources:

- EMPLOYEE ELECTIVE SALARY DEFERRAL
  All 401(k) plans permit employees to voluntarily contribute, or "defer," a portion of their salaries to the plan, as either pre-tax or after-tax Roth contributions.

- MATCHING EMPLOYER CONTRIBUTION
  To provide an incentive to participate, many employers match a portion of each participant's elective salary deferral. This discretionary matching contribution is tax deductible for the company. An employer may not make the matching contribution in the form of an after-tax Roth contribution.

- EMPLOYER PROFIT SHARING CONTRIBUTION
  Employers may also make discretionary contributions to all eligible employees, regardless of whether the employees make elective salary deferrals. The employer profit sharing contribution must be pre-tax and not an after-tax Roth contribution.

*Raymond James does not offer legal or tax advice. Please speak with your appropriate professional.

Individual contribution limits

The maximum 401(k) deferral for 2021 is the lesser of 100% or $20,500 of each employee's eligible payroll. Plan documents may limit salary deferrals to less than 100%.

Employer contribution limits

The employer's contribution limit is 25% of each employee's eligible payroll. While an employee can contribute more than 25%, total combined contributions from deferrals, matching employer contributions and employer profit sharing contributions cannot surpass the $61,000 maximum.

Non-discrimination requirements

401(k) plans may not discriminate in favor of highly compensated employees (HCEs) – employees who own 5% or more of the company or who earn a minimum of $135,000. Each plan is subject to an annual non-discrimination test, commonly referred to as the actual deferral percentage (ADP) test, which is intended to prevent the plan from benefiting only an HCE group. In essence, the amount that an HCE may defer is controlled by the deferral rate of the non-highly compensated employee (NHCE) group.

In addition, every 401(k) plan has a number of different components that must be coordinated to optimize employee benefits.

ACTUAL DEFERRAL PERCENTAGE (ADP) TEST

This chart illustrates the highest deferral percentage available to the HCE group, as an average, if the ADP for the NHCE group is at a specific level.

Highly compensated employees include:

1. Employees with 5% or more ownership stake and
2. Any employee who earns $135,000* or more.

*Indexed figures for 2022

HCE	NHCE
2%	1%
4%	2%
5%	3%
6%	4%
7%	5%
8%	6%
9%	7%
10%	8%
11.25%	9%
12.5%	10%

Investment alternatives

Most 401(k) plans enable participants to choose from a variety of investment alternatives. An effective plan should allow employees to move freely among available funds to create the best asset allocation for their needs.

Recordkeeping

Allocating contributions and earnings among different investment alternatives, calculating vesting amounts, and generating participant statements are usually referred to as participant level accounting. These functions are critical to keep the plan running smoothly.

Plan administration

Regulatory functions, such as plan qualification, non-discrimination testing, reporting to the IRS and disclosure to employees, must be performed on an annual basis. In addition, participant-level information must be incorporated into plan-level accounting as part of IRS reporting.

Employee communication

From the long-range perspective of creating a means for employees to accumulate retirement assets, effective communication is the most important component of the 401(k) plan structure. Each employee must have a basic understanding of the concepts of investing and how the plans work.

Trustee selection

Unlike in a traditional pension plan, in a participant-directed 401(k) plan an outside trustee mainly performs custodial functions – such as distributions and the related reporting functions – but assumes no fiduciary liability.

STRUCTURING YOUR PLAN

While many factors influence 401(k) decisions, choosing a structure is often determined by the maintenance and fees involved. The three basic structures are:

SINGLE SOURCE

This arrangement is a full-service package that provides single-source responsibility – as well as a single source of fees – for all functions. Frequently referred to as a "bundled" plan, this format has the fewest components and is the simplest to maintain.

MULTIPLE SOURCE

This is also a packaged arrangement, but adds a third-party administration firm that can be electronically linked to the mutual fund family or insurance company that provides the investment selections. The recordkeeping functions, plan administration and investments must be integrated for the plan to run efficiently. While this arrangement is more complex than the single-source option and fees are incurred from multiple sources, it provides additional flexibility that may be critical to meeting the plan's objectives.

UNBUNDLED

In this arrangement, many components operate independently, and no single source is responsible for the process as a whole. As a consequence, although this option offers total investment flexibility, it has the greatest potential for operational breakdowns and poor service. In addition, the unbundled approach may require more day-to-day employer involvement.

While your company's needs dictate the type of plan that is most appropriate, the majority of small businesses tend to select the single- or multiple-source arrangements to reduce management responsibility, as well as the likelihood of problems coordinating the different facets of unbundled plans.

In addition to the general structure of your plan, there are also two investment arrangements from which to choose:

SINGLE MUTUAL FUND FAMILY

Providing investment choices from a single company typically offers the lowest overall cost since all functions are controlled by one entity. Choosing a fund family with investment alternatives across different asset classes can deliver a cost-effective retirement plan structure while potentially minimizing your fiduciary liability.

MULTIPLE FUND MANAGERS

This option, usually provided through an insurance company or an alliance arrangement with an independent plan administration firm, employs investment managers from different fund families. The goal of this approach is to provide more choice and greater diversification.*

The trading platform alliances, in which an independent plan administration firm is linked to a transfer agent trading platform that processes trades across fund family lines, may allow a wider selection of fund choices, but can also be more complex. In addition, the overall accountability is divided among several sources, which can lead to communication problems.

THE SAFE HARBOR 401(K) PLAN ALTERNATIVE

Because of the potential complexities of traditional 401(k) plans, some business owners – especially those with fewer employees – may choose to explore options better suited to their needs. In the past, this often meant choosing to offer no retirement plan at all. However, newer alternatives can replace or supplement more conventional plans, reduce administration efforts and costs involved, and/or provide added benefits for business owners.

A Safe Harbor 401(k) plan is similar to a traditional 401(k). However, its key benefit is that low employee participation does not keep the business owner from achieving the maximum pre-tax payroll deferral limit. This is because a Safe Harbor 401(k) allows the business owner to avoid non-discrimination, ADP and ACP testing. However, the company must be willing to make contributions on behalf of its employees. There are two options:

- A dollar-for-dollar match for the first 3% of compensation and $0.50 per dollar on the next 2%. If an employee contributes 5% of his or her salary to a Safe Harbor 401(k), the employer match obligation is 4%.

*Diversification does not guarantee a profit nor protect against loss.

- A 3% of compensation non-elective contribution to all employees eligible to contribute to the Safe Harbor 401(k). Each will receive the 3% regardless of plan participation.

The company can make additional contributions, up to 25% of eligible compensation per participating employee (reduced by its match or non-elective contribution).

Profit sharing plans offer employers both design flexibility and discretion with regard to contributions.

SAFE HARBOR CONTRIBUTION (3% NON-ELECTIVE OPTION)

Eligible Employee	W-2 Compensation	Pre-Tax Payroll Deferral[1]	3% Safe Harbor Employer Contribution[2]	Additional Profit Sharing Contributions[3]	Total Contributions[1]
Owner	$305,000	$20,500	$9,150	$31,350	$61,000
Employee 1	$40,000	$4,000	$1,200	$3,312	$8,512
Employee 2	$30,000	$3,000	$900	$2,484	$6,384
Employee 3	$20,000	$2,000	$600	$1,656	$4,256
TOTALS	**$395,000**	**$29,500**	**$11,850**	**$38,802**	**$80,152**

[1]This illustration assumes that no employees qualify for the catch-up contribution. [2]Owner satisfies Safe Harbor and top-heavy requirements by making a 3% fully vested contribution to all participants, including both contributing and non-contributing employees, as well as himself/herself. [3]Owner makes an additional 10.3% contribution to all participants, subject to a vesting schedule, to achieve the maximum contribution of $61,000 for himself/herself.

SAFE HARBOR CONTRIBUTION (4% MATCHING OPTION)

Eligible Employee	W-2 Compensation	Employee Pre-Tax Payroll Deferral[1]	4% Safe Harbor Employer Contribution[2]	Additional Profit Sharing Contributions[3]	Total Contributions[1]
Owner	$305,000	$20,500	$12,200	$28,300	$61,000
Employee 1	$40,000	$4,000	$1,600	$3,156	$8,756
Employee 2	$30,000	$3,000	$1,200	$2,367	$6,567
Employee 3	$20,000	$2,000	$800	$1,578	$4,378
TOTALS	**$395,000**	**$29,500**	**$15,800**	**$35,401**	**$80,701**

[1]This illustration assumes that no employees qualify for the catch-up contribution. [2]Owner satisfies Safe Harbor and top-heavy requirements by making a 4% fully vested contribution to all participants, including both contributing and non-contributing employees, as well as himself/herself. [3]Owner makes an additional 9.3% contribution to all participants, subject to a vesting schedule, to achieve the maximum contribution of $61,000 for himself/herself.

The charts below illustrate how the addition of a Safe Harbor 401(k) to a traditional, age-weighted or new comparability profit sharing plan permits business owners to fully contribute up to the IRS limit while reducing the amount they must contribute on behalf of the plan's participants. The first chart illustrates the three types of profit sharing plans with only employer contributions. The second chart adds a Safe Harbor 401(k) with the matching option, taking advantage of an employee salary deferral contribution and limiting the total employer contribution to the plan.

ENHANCED PROFIT SHARING CONTRIBUTION

Eligible Employee	Age	Class	W-2 Compensation	Regular	Social Security Integrated	Age-Weighted	New Comparability
Owner 1	57	1	$305,000	$61,000	$61,000	$61,000	$61,000
Owner 2	38	1	$305,000	$61,000	$61,000	$12,947	$61,000
Subtotals			**$610,000**	**$122,000**	**$122,000**	**$73,947**	**$122,000**
Class two	50	2	$40,000	$8,000	$6,659	$4,519	$2,772
Class two	35	2	$30,000	$6,000	$4,994	$997	$2,079
Class two	25	2	$20,000	$4,000	$3,330	$294	$1,386
Subtotals			**$90,000**	**$18,000**	**$14,983**	**$5,810**	**$6,237**
TOTALS			**$700,000**	**$140,000**	**$136,983**	**$79,757**	**$128,237**

ENHANCED 401(K) CONTRIBUTION

Eligible Employee	Age	Class	W-2 Compensation	Salary Deferral	Match (4%)	Catch-Up	Regular	Social Security Integrated	Age-Weighted	New Comparability
Owner 1	57	1	$305,000	$20,500	$12,200	$6,500	$28,300	$28,300	$28,300	$28,300
Owner 2	38	1	$305,000	$20,500	$12,200	$0	$28,300	$28,300	$6,006	$28,300
Subtotals			**$610,000**	**$41,000**	**$24,400**	**$6,500**	**$56,600**	**$56,600**	**$34,306**	**$56,600**
Class two	50	2	$40,000	$4,000	$1,600	N/A	$3,711	$2,371	$2,097	$1,444
Class two	35	2	$30,000	$3,000	$1,200	N/A	$2,784	$1,778	$463	$1,083
Class two	25	2	$20,000	$2,000	$800	N/A	$1,856	$1,185	$136	$722
Subtotals			**$90,000**	**$9,000**	**$3,600**	**$0**	**$8,351**	**$5,334**	**$2,696**	**$3,249**
TOTALS			**$700,000**	**$50,000**	**$28,000**	**$6,500**	**$64,951**	**$61,934**	**$37,002**	**$59,849**

THE ROLE OF THE 401(K) ADVISOR

Maintaining an appropriate retirement plan for your company often seems like a daunting task – especially when you consider everything else that goes into running a successful business. For us at Raymond James, it's one of our specialties. In general, the role of a 401(k) advisor can be segmented into:

Clearly defining the parameters of the specific client relationship and establishing reasonable expectations for both the client and the advisor. Developing an overall retirement plan strategy with specific goals is critical in ensuring success.

Evaluating and recommending service providers. A qualified 401(k) advisor can diagnose the particular aspects of the service delivery that are critical to your situation and recommend the most appropriate alternatives. Since Raymond James advisors are not tied to a particular provider, we're free to recommend what is best for your company and employees.

Performing plan design consulting. A review of the plan design is very important because plan design provisions can make a big difference in whether your plan meets your needs. These provisions address matching contribution formulas, cross-tested profit sharing allocations, qualification and eligibility issues, and merger and acquisition situations. Raymond James 401(k) advisors will work closely with the provider's administration experts to ensure that all available aspects of plan design are considered.

Managing the implementation and transition to new provider(s). This is perhaps the most challenging function of all, and is usually where most problems begin. Most "fired" providers are not overly anxious to cooperate with new providers, so it takes a dedicated effort to ensure a smooth transition. Having one individual responsible for coordination makes the process more user-friendly for you.

Serving as the primary contact for all aspects of plan servicing. No longer will you or your employees need to wonder who to call when problems or questions arise. We'll act as the single source responsible for managing all the moving parts and will troubleshoot as needed. Moreover, we will monitor the service providers to ensure that they continue to meet your retirement plan needs, replacing them if necessary.

Providing ongoing plan reviews. This includes: discussing overall plan service, operation and results, such as participation levels, deferral percentages, loans, non-discrimination testing, enrollment and communication strategies, and any other items of relative importance; offering a performance analysis at least annually of investments utilized by the plan versus benchmarks and/or peer groups; monitoring funds selected by the plan sponsor for style drift and correlation with fund investment objectives stated in the IPS; and providing regulatory updates such as information on legislative, Department of Labor and IRS matters of relevance to retirement plans.

Managing employee communication and investment education. We believe that coordinating enrollment meetings and providing ongoing investment education for participants regarding plan options is a valuable part of our service. That's why Raymond James 401(k) advisors will be available to your employees by phone and, periodically, in person for individual consultation. If enrollment and/or education teams from the provider are necessary due to multiple company locations, we will coordinate those efforts. We also provide supplemental educational materials if desired.

In addition, we can integrate qualified plan goals into a personal customized financial and estate plan as necessary. Finally, we will educate plan participants about plan distribution alternatives, provide retirement cash flow analysis, and, whenever necessary, consult with retirees regarding investment asset allocation.*

*Asset allocation does not guarantee a profit nor protect against loss.

Frequently Asked Questions About Profit Sharing Plans

CAN A PROFIT SHARING PLAN BE COMBINED WITH A 401(K) PLAN?

A 401(k) plan is simply a profit sharing plan with a provision allowing employee salary deferrals. Most 401(k) plans provide employer matching contributions based on a participant's contribution, with an additional option for a profit sharing allocation. Although most 401(k) plans use a salary ratio formula for profit sharing plan allocations, any of the other formulas could be used.

WHAT ARE THE COSTS OF IMPLEMENTING AND MAINTAINING A PROFIT SHARING PLAN?

Cost can vary significantly depending on the design complexity of the plan, the number of employees and the structure of the investment portfolio.

CAN AN IRA BE ROLLED INTO A PROFIT SHARING PLAN?

Yes. An IRA can be rolled into a profit sharing plan as long as the profit sharing plan permits such a rollover.

DO ALL EMPLOYEES HAVE TO BE INCLUDED IN A PLAN?

Certain employees may be excluded, but strict coverage rules prevent the plan from discriminating in favor of highly compensated employees.

WHAT IS THE DIFFERENCE BETWEEN A PROFIT SHARING PLAN AND A SEP PLAN?

The profit sharing plan allows vesting schedules, while SEP plans require 100% immediate vesting. A profit sharing plan can require employees to work at least 1,000 hours to share in the contribution, but a SEP plan covers all eligible employees, regardless of hours worked.

WHAT ARE THE ADMINISTRATIVE REQUIREMENTS?

All profit sharing plans are subject to IRS reporting requirements. This includes keeping the plan up to date with new laws, performing non-discrimination tests, filing an IRS Form 5500 return each year, and providing benefit statements and other plan information to participants at least annually. Self-employed persons with no employees are not required to file returns until the plan has $250,000 in assets. A professional pension plan administrator should usually be retained to perform these annual reporting functions.

LIFE WELL PLANNED.

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