

401(k) plan

The 401(k) plan is one of the most popular types of employer-sponsored retirement plans available.



Wealth
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How it works

401(k) plans center around employee contributions through pre-tax or Roth payroll deductions. These contributions are put at the employee's discretion into investment options available through the plan. Additionally, employers have the option of matching employee contributions, making a profit-sharing contribution, or both. This type of plan offers tremendous plan design flexibility.

401(k) plans are most appropriate for:

- Employers who want a plan that offers employees the ability to save for their own retirement.
- Companies desiring a vesting schedule on employer contributions.
- Employers who don't want to be required to make contributions each year.

Key advantages for the employer

- Company contributions are tax-deductible.
- You have the flexibility to change the amount of contributions you wish to make each year.
- Various vesting schedule options are available for employer contributions.

- Contributions can be made in amounts up to 25% of eligible payroll.
- A 401(k) plan is an attractive benefit to offer prospective employees while building loyalty among existing employees.

Key advantages for employees

- A 401(k) plan can help provide for your employees' retirement.
- Employees can reduce their taxable income and their taxes by contributing up to \$23,500 in 2025.
- Employees age 50 or older may be allowed to contribute an additional \$7,500 pre-tax catch-up amount in 2025.
- Earnings grow and compound tax-deferred.
- Early withdrawals in cases of hardship may be permitted.
- Employees have the flexibility to choose from a broad range of investment options.
- Employees can participate in the profits of the company, if the contribution formula is based on profits.
- A loan program may be offered to participants to help meet short-term needs.

What else you should know about 401(k) plans

Income limits

Contributions can only be based on the first \$350,000 of an employee's income in 2025. The sum of the employer's contribution and the employee's salary deferral contribution cannot exceed \$70,000* in 2025 or 100% of the employee's compensation, whichever is less.

Other plan design considerations

There are various 401(k) plan design features that can help your company meet your retirement planning objectives for employees. The IRS issued regulations that allow a 401(k) plan to offer Roth after-tax contributions by participants. The earnings on these Roth contributions will grow tax-free, and by adding this feature your company will give participants the opportunity to diversify their tax risk by choosing from pre-tax, Roth after-tax, or blended contributions in the same plan.

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Key features of a Roth 401(k):

- Available to employees at any income level.
- Aggregated and subject to one combined deferral limit (\$23,500 in 2025, or \$30,500 for employees age 50 or older).
- Tax-free distribution of earnings.
- Tax-free distribution of earnings if made after five years following the first Roth 401(k) contribution and the attainment of age 59 ½.
- Contributions may be available for loans.
- Contributions may be matched on a pre-tax basis.
- Employee Roth contributions are 100% vested immediately.
- All or a portion of the 50+ catch-up contribution can be designated as a Roth contribution.
- Terminated employees have the option of rolling over their Roth 401(k) account to a Roth IRA or another plan with a Roth 401(k) or Roth 403(b) feature.

Safe harbor

- Requires employer match contributions and immediate vesting of employer contributions.
- Automatically satisfies certain nondiscrimination testing, including average deferral percentage (ADP) and actual contribution percentage (ACP) if safe harbor guidelines are met.
- Fewer restrictions on salary deferral contributions for higher compensated employees.

New comparability

- Employer contributions are discretionary and are calculated using a formula based on estimates of lifetime benefits.
- Maximizes contributions for owners and key employees without increasing overall plan costs.
- Allows key employees the potential to build retirement savings more quickly.

Auto programs

Incorporating auto programs into your plan may help employees, who otherwise might not choose to join or fully participate in the plan, invest in their futures. Automatic programs are flexible and can be tailored to meet the needs of your company and your employees.

- Automatic enrollment helps employees meet their retirement goals by enrolling them in the plan as soon as they are eligible.
- Automatic enrollment deferral increase is an easy solution to help participants contribute more and increase savings rates.
- Automatic investment helps confirm participant contributions are reasonably invested when the participant does not actively select an investment option.

Qualified Automatic Contribution Arrangement (QACA)

- Combines the benefits of safe harbor and auto enrollment/auto increase into a 401(k) plan.
- Offers lower employer match contribution than safe harbor alone.
- Automatically satisfies ADP and ACP testing.
- Eliminates contribution restrictions for key employees.

Compliance requirements

401(k) plans require annual nondiscrimination testing and top-heavy testing, and IRS 5500 annual tax filings are required. Your recordkeeper or administrator can provide these services.

How RBC Wealth Management can help you

Your RBC Wealth Management financial advisor can work closely with you to help design the right 401(k) plan for your company. He or she can provide you and your tax advisor with the most popular and efficiently administered 401(k) options available in the market.

In addition, your financial advisor can provide you and your employees with a full range of investment options to help implement each employee's retirement strategy.

* \$76,500 in 2024 if age 50 or older.

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