
Employees' Profit-Sharing & Retirement Trusts

-
- WHAT THEY ARE —
 - WHAT THEY ACCOMPLISH —
 - THEIR TAX STATUS —
 - THEIR RELATION TO PENSION PLANS —
 - HOW TO SET THEM UP —
-

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WHAT THEY ARE

An Employees' Profit-Sharing and Retirement Trust is a retirement trust fund established by an employer for the exclusive benefit of employees.

CONTRIBUTIONS to the trust fund are made by the employer based on the employer's profits and on the employees' pay. These contributions are invested, and the investments are held by a Trustee.

The executives and employees who are designated as Participants in the Trust share in its benefits in proportion to their annual total compensation from the employer. Their benefits are paid to them when they reach a specified retirement age (or are disabled) and are paid to their beneficiaries in case of death.

In case a Participant voluntarily leaves his job or is discharged for cause, he forfeits his participation, or such portion of it as may be specified, and *the amount so forfeited serves to increase proportionately the interests of the other Participants*. In case he is discharged through no fault of his own, the value of his participation at that time is paid to him in full.

The employer may be a corporation, partnership, or proprietorship but neither partners nor sole proprietors may be Participants in the Trust. Executives of corporations, whether or not they are shareholders, may be Participants.

THEIR PURPOSES

The primary purpose of an Employees' Profit-Sharing and Retirement Trust is to supplement Social Security in making provision for employees at the age of retirement.

In case of death or disability the employee's participation in the Trust serves as a supplement to his insurance. In case of termination of employment it supplements his severance pay. It is of especial benefit to the more-than-\$3,000 employee and executive since Social Security

benefits do not increase above that level. Participation may be *confined* to this class of employee if desired.

The Trust serves the additional purpose of creating employee good-will and solidarity. Since contributions are in proportion to the prosperity of the business, the executives and employees have a *direct financial interest* in making the business prosper. Personnel turnover is reduced, since the benefits soon become too large to be lightly abandoned.

Employees' Profit-Sharing & Retirement Trusts

THEIR TAX STATUS

TO THE EMPLOYER . . . Contributions made by an employer to an Employees' Profit-Sharing and Retirement Trust which conforms to the provisions of the Internal Revenue Code as being bona-fide and nondiscriminatory are a *business expense* of the employer, deductible before computing Federal income taxes. Such contributions are therefore made, in effect, by the Government to the extent of the *highest* tax rate paid by the employer.

The maximum of contributions so deductible in any one year is 15% of the total annual compensation of participants. However, additional contributions in that year may be carried over and used as deductions in the following year.

Each year's contribution by the employer, and the amount, is optional with the employer. In years where the employer's earnings are so low that no tax is payable, any contribution that it may elect to make for that year may be carried over as a tax deduction in the following year. So the fact that earnings are low in the present

year does not necessarily mean the loss of tax advantages on this year's contributions to a Trust.

TO THE TRUST . . . A properly drawn Trust is exempt from Federal income tax either on its investment income or on profits realized from the sale of its investments.

TO THE EMPLOYEE . . . The Participant is taxed only when he *receives* his benefits, which normally occurs when he reaches the retirement age. At that time the absence of former regular income would presumably bring his personal income tax rate considerably below its present level. Under the provisions of Section 165b of the Internal Revenue Code, if the total amount payable to an employee on retirement, total disability, or severance of employment is paid in a lump sum, or in one taxable year, *it is taxed as long-term capital gain*. If the amount payable is paid in installments over a period of years, it is taxed as ordinary income.

A VALUABLE COMPANION TO PENSION PLANS

The basic difference between Profit-Sharing Trusts and Pension Plans are such that the two arrangements combined have advantages not offered by either one alone. The tax rewards offered for each do not cancel out the other but are added. Thus while 15% of total compensation of participants is the deductible limit for a Profit-Sharing Trust, the deductions per-

mitted for a Trust plus a Pension Plan may run as high as 25% to 30% of payroll.

The difference to the beneficiary is that a Pension Plan provides for a stipulated amount of dollars to be paid him irrespective of changes in the purchasing power of those dollars. The Profit-Sharing Trust can adapt its investment policy to compensate for such changes; during

Employees' Profit-Sharing & Retirement Trusts

inflationary periods it can hold mostly common stocks, in deflation mostly Government bonds. Together the Pension Plan and the Trust offer the same protective combination to the beneficiary as is employed by the prudent individual who has both life insurance and investments.

The most important difference to the employer is in *flexibility*. The Profit-Sharing Trust is far more flexible from the employer's standpoint than the Pension Plan, since it is not practicable from year to year to change or to reduce Pension contributions. After a succession of bad years the Pension Plan is likely to become a burden that has to be abandoned, whereas con-

tributions to a Profit-Sharing Trust are optional from year to year and if desired may be made only in profitable years.

In cases where, for special reasons, only one of the two arrangements is desired the Profit-Sharing Trust should be selected. Flexibility is by no means its only advantage. It is less expensive. Where turnover of employees is, or might be, substantial, it offers far greater advantages to the remaining beneficiaries since the abandonment of not-yet-vested interests in a Profit-Sharing Trust may very substantially increase the values to be shared by the other Participants.

HOW TO SET UP A TRUST

IN establishing an Employees' Profit-Sharing and Retirement Trust a number of essential elements must be combined. There must be a formally executed Trust Agreement with a Trustee, either an individual or a bank or trust company. There must be a Plan—also a formal document—embodying all the terms decided upon by the employer, such as what portion of total employees are to participate, what is to be the age of retirement, how benefits are to be disbursed, etc. The Plan and Trust Agreement must be filed with the Commissioner of Internal Revenue and the Collector of Internal Revenue and meet the requirements of the Internal Revenue Code and regulations or the tax advantages (both to employer and employee) will be lost. If the employer is a corporation certain corporate action is required.

TO simplify what might otherwise appear to be a complex subject a *Standard Plan and Trust Agreement* has been developed for Distributors Group, Incorporated, of New York, professional managers of investment funds, and for investment dealers, banks and trust companies associated with them. Procedure is so organized that all the necessary elements have been brought together yet there is ample leeway, within this Standard Plan, for practically every employer to adapt it directly to his own particular situation.

ON request, and without charge or obligation, we shall be glad to submit a summary, in layman's language, of the Distributors Group, Incorporated, Standard Plan. Your decisions, as an employer, on the 7 points indicated in this summary adapts this Plan directly to your specific requirements. The degree of latitude possible for each such decision is plainly stated.

