



## Nonqualified Deferred Compensation Plans

# Six Primary Uses for Deferred Compensation

A properly designed executive benefit program can help your highly compensated employees bridge their retirement gap caused by qualified plan limitations. By offering this benefit, you can help them maintain their standard of living in retirement, which is something that 49% of highly compensated employees are concerned about\*.

A nonqualified deferred compensation (NQDC) plan is such a benefit program. This benefit program can help you recruit, retain and reward those select key employees on whom the success of your business depends. Take a look at these six ways that a deferred compensation plan can be used to help benefit your business and your key executives.

### 1 401(k) repair

- Eligible executive is allowed to defer into an NQDC plan any amount restricted by qualified plan nondiscrimination testing, up to the maximum qualified plan amount.
- Company contributions follow executive deferrals.

Deferral Limit (2009)	Limits of Qualified and Nonqualified Plans	Company Match	Amounts Available for Qualified and Nonqualified Plans (Company Totals)
Qualified limit \$16,500	\$7,500 testing limit for qualified plan	50%	\$3,750 into qualified plan
	\$9,000 could go to NQDC plan	50%	\$4,500 into NQDC plan

### 2 Retirement savings

- This works like 401(k) repair, but the deferral limits are raised, or more commonly eliminated.
- May or may not include company matching amounts and/or discretionary profit share contributions.

Three Levels of Executive	Executive Deferral Limit	Company Match
Low tier	\$50,000	Any amounts restricted by qualified plan testing
Middle tier	Unlimited	Any amounts restricted by qualified plan testing
Top tier	Unlimited	All deferrals

\*The Principal Well-Being Index<sup>SM</sup>, 2008

### 3 Taxation timing

- With the guidance of their tax advisors, eligible executives with variable income components may use the NQDC plan to choose when they take receipt of money and, thereby when they pay taxes on that money.
- Income tax would be payable in the year the money is actually received by the executive.

Executive objectives:				
		• Provide college money for two kids	• Purchase second home	• Build retirement
	Annual Amount	Elected Deferral %	Deferral Amount	
Executive Base Income	\$140,000	10%	\$14,000	
Executive Bonus	\$90,000	50%	\$45,000	
Total Deferral			\$59,000	

#### Annual deferral elections allocation:

20% College: Mary	20% College: Mike	20% Beach House	40% Retirement
\$11,800 June 2014	\$11,800 June 2016	\$11,800 January 2020	\$23,600 NRD
4 PAYMENTS	4 PAYMENTS	1 PAYMENT	7 PAYMENTS

### 4 Compensation control

- Employers can use performance-based contribution and performance-based vesting to induce the behavior they desire from key performers.
- Employer designates a bonus pool that is allocated based on the performance of each eligible executive. Bonuses are paid into each executive's NQDC account.

Selected Eligible Executives	Bonus	Vesting Schedule
Executive 1	\$15,000	100% vested in 2015
Executive 2	2% gross profit	100% vested upon completion of set goals
Executive 3	\$30,000	20% vesting every two years

## 5 Ownership experience

- Contributions and vesting measured by phantom stock values are like “compensation control”
- Executive shares in both increases and decreases in the valuation of the company, which creates an ownership experience without the dilution that comes from actual equity grants.

Company	Formula	Value	Vesting
Contributes phantom stock shares to participating executives	# of phantom shares determined by annual gross profit	Declared by board quarterly	20% per year based on meeting goals

## 6 Insider transition

- Closely held corporation funds an NQDC plan account for current executives who are possible future owners.
- Account is set to vest and distribute on a “change in control” of the company.
- Provides incentives/rewards for key executives and retains options for current owner.

Sale of Business	Change of Control	Vesting
Sale to insiders	YES	Account vests and distributes to executives and is used to execute purchase
Sale to outsiders	YES	Account vests and distributes to executives as reward for years of service
NO	NO	Optional triggering event can be retirement

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