

Nonqualified Deferred Compensation Plans

Primary Uses for Deferred Compensation

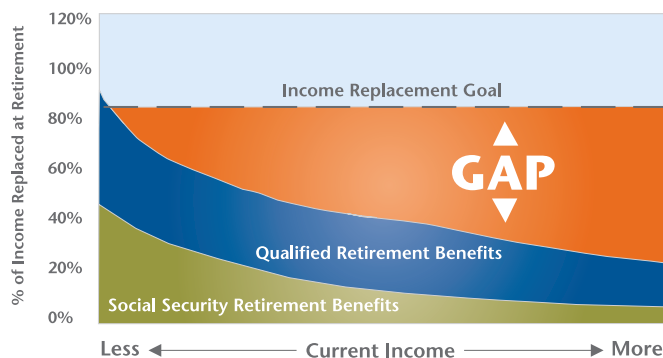
The following uses of nonqualified deferred compensation (NQDC) demonstrate the flexibility in plan design employers have used to support their organizational goals.

40% of highly compensated employees say they're concerned about **maintaining their standard of living** in retirement.*



401(K) RESTORATION AND RETIREMENT SAVINGS

Qualified plans, 403(b) plans and Individual Retirement Accounts (IRAs) have limits on the amounts that can be contributed to them. Also, qualified plans and 403(b) plans are subject to coverage and non-discrimination testing that may limit both employee and employer contributions to the plans. Nonqualified deferred compensation plans can **help key employees bridge the retirement gap** through 401(k) restoration and additional retirement savings opportunities.



This information is from the Principal Financial Group® Replacement Ratio Calculator with source information from the Annual Statistical Supplements to the Social Security Bulletin (www.ssa.gov). It is intended to demonstrate the potential impact of Social Security and 401(k) plan benefits at various income levels. For more information on your individual circumstances, please speak with your financial or tax professional. ©2015 Principal Financial Services, Inc.

401(k) restoration

Employer contributions can “restore” benefits that are limited under a qualified retirement plan.

- 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.

Retirement savings – going beyond 401(k) restoration

Addressing the retirement gap higher earners face.

- Deferral limits can be raised, or more commonly, eliminated.
- May or may not include company matching amounts and/or discretionary profit share contributions.
- Employer has the ability to choose who to reward and how much. Plan design may allow ability to create tiers of the Top Hat Group with different deferral limits, employer contributions and vesting schedules.



TAXATION TIMING

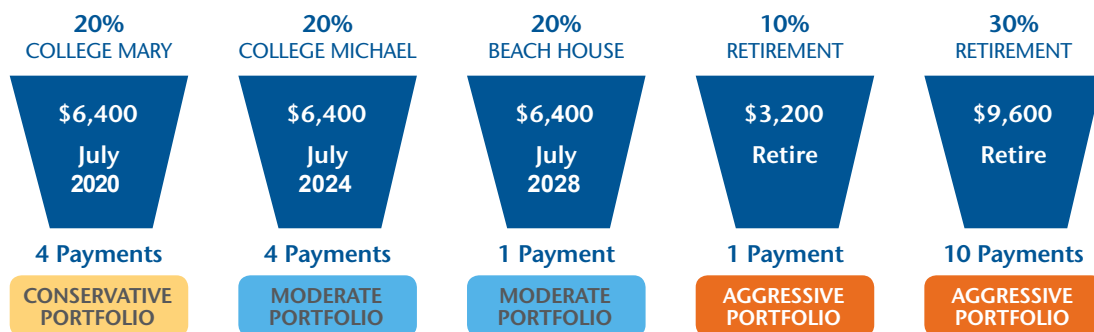
NQDC offers participants considerable flexibility and control over distributions to meet their objectives and timing needs. This increased control allows them not only to create accounts to meet different objectives but also provides the distribution flexibility to control when they take receipt of the money; and thereby the amount of taxes they pay (example below).

- With the guidance of their tax advisors, eligible executives with variable income components may use the NQDC plan to choose when they take distributions including the option to take installments. In addition, plan participants have the flexibility of delaying distributions beyond the originally scheduled timing.
- Participants have the ability to coordinate their NQDC distributions with distributions from Social Security or other pre-tax retirement plans such as a 401(k) plan. Often participants will fund their retirement with NQDC distributions first, then receive qualified plan distributions later.
- Participants can defer distributions while they're working and their marginal tax rates are potentially high and then take the distribution during retirement when their *effective tax rate* may be lower.
- Income tax would be payable in the year the money is actually received by the executive.

KEY EMPLOYEE BASE INCOME

\$120,000, Bonus \$40,000

	OBJECTIVES	DEFERRAL AMOUNTS
Key Employee elects to defer 10% OF BASE PAY and 50% OF BONUS	<ul style="list-style-type: none"> • Provide college money for two kids • Purchase second home • Build retirement 	<ul style="list-style-type: none"> • BASE: \$12,000 • BONUS: \$20,000 • TOTAL: \$32,000



*More than 9 in 10 participants say NQDC plans are important in reaching retirement goals**

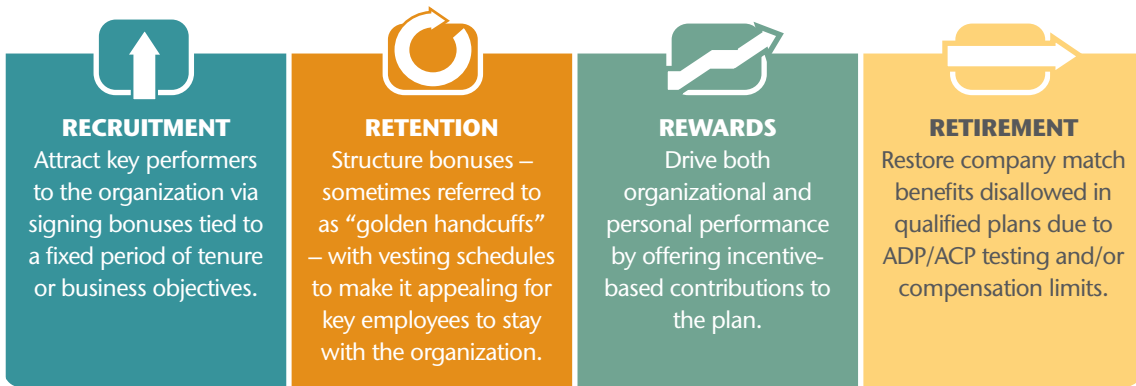


COMPENSATION MANAGEMENT

NQDC plans can also provide employers with a **program to help recruit, retain, reward and/or provide incentives for the people on whom the success of your business depends.** You can use performance-based contribution and performance-based vesting to influence the behavior you want from key performers. You can customize contribution and vesting schedules to use as performance rewards for executives.

Recruit, retain, reward and retire

Use discretionary employer contributions based on the particular needs of your organization. NQDC plans can be customized to fit a wide variety of organization goals.



OTHER PLANNING OPPORTUNITIES

NQDC plans can be valuable to an organization planning for the future. Whether using NQDC to **create phantom shares and provide an ownership experience – or using it to create opportunities for executives to be potential future owners –** NQDC plans have much flexibility and offer many options.

OWNERSHIP EXPERIENCE – Employers can customize contribution and vesting schedules measured by phantom stock values – similar to “compensation management.” That way the 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 (example on right).

COMPANY	FORMULA
Contributes phantom stock shares to participating executives	# of phantom shares determined by annual gross profit
VALUE	VESTING
Declared by board annually	20% per year based on meeting goals

INSIDER TRANSITION – Closely held corporation funds an NQDC plan account for current executives who are possible future owners, setting an account to vest and distribute on a “change in control” of the company. This not only provides incentives and rewards to key employees, it also retains options for the current owner (example below).

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
NONE	No	Optional triggering event can be retirement

However you choose to design your plan, some key benefits are universal.

An NQDC plan:

- Allows participants the opportunity to defer compensation in excess of qualified retirement plan limits on a pre-tax basis (up to 100 percent deferral depending on plan design)
- Can allow organizations to make discretionary contributions to retain and motivate key employees — including incentive-based contributions.
- Restores contributions/benefits limited by IRS restrictions in retirement plans
- Can give participants more flexibility in tax planning with flexible distribution options
- Offers flexible distribution options including ability to take prior to age 59½
- Allows participants to design an individualized investment strategy
- Is not subject to contribution and participation limits
- Has simplified government reporting and disclosure rules, or none at all, depending on plan design

YOU'LL GET AN EDGE WITH THE PRINCIPAL®

These uses for deferred compensation plans are just a few of the many flexible plan designs that could help you address various business and executive needs. When you and your financial advisor work with the Principal Financial Group®, you'll benefit from the expertise of an experienced plan provider. This will help ensure that you receive a plan designed to meet your specific goals. You'll also gain the resources and support needed to make the implementation and administration of your plan as easy as possible.

* 2013 Trends in Nonqualified Deferred Compensation; Spotlight on Plan Participants, the Principal Financial Group.



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