Nonqualified Executive Benefit Plans
SALES KIT

In this kit:
Prospecting guides | Implementation guide
Producer guides | Toolkits | Consumer guides

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Nonqualified Deferred Compensation

CONCEPT APPLIED:

A nonqualified deferred compensation arrangement allows an employer to provide retirement income and often death and disability benefits to an exclusive employee group, often with benefits in excess of those permitted under qualified plans.

HOW IT WORKS:

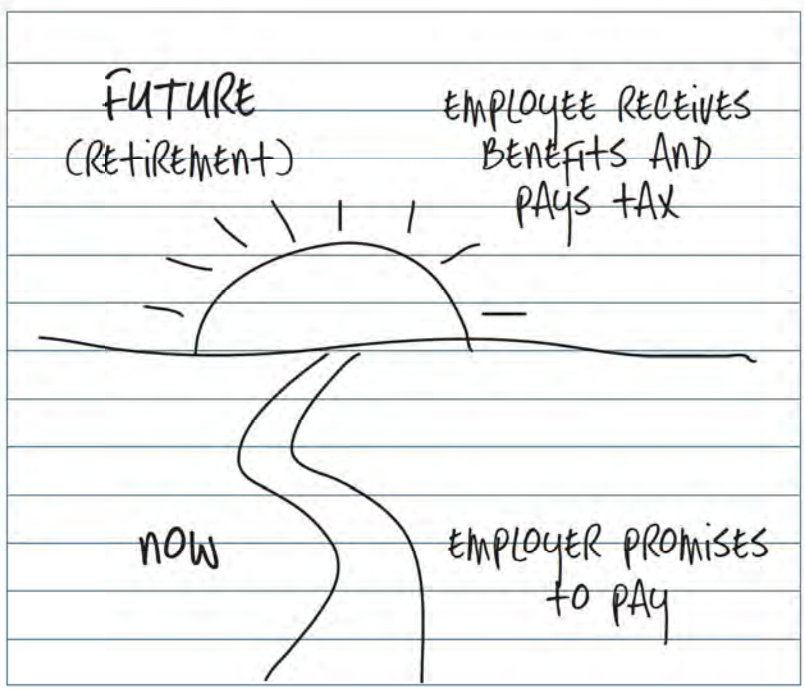
True deferred compensation plans offer future income in exchange for current salary reduction. Customarily, however, employers use "salary continuation" arrangements that promise future compensation without reducing current compensation.

Deferred compensation arrangements must be unfunded to ensure current income tax deferral for employees. Employers may not set up a specific reserve fund in which a participant has a vested right. A life insurance policy is uniquely suited to informally finance a nonqualified deferred compensation plan.

50 words or less

Deferred compensation is a contract between an employer and employee that specifies future compensation. A nonqualified deferred compensation arrangement:

- Is exempt from ERISA's regulatory requirements
- Can discriminate in favor of select employees
- May provide different benefits to individual employees
- Does not require IRS approval



WHY IS IT USEFUL?

Nonqualified deferred compensation arrangements can be designed to reward and retain valuable, highly compensated employees. Life insurance is useful in that it can ensure that funds will be available to pay promised benefits.

Nonqualified deferred compensation plans

Identifying deferred comp prospects

Employers open doors to good ideas – and you have one!

Employers want effective ways to recruit and keep the best employees. And key employees want to work for companies that care about their future. This motivates employers to provide valued and competitive benefits.

Reaching out to employers about a nonqualified deferred compensation plan is well-worth your time. Research shows that employers **and** key employees value deferred comp for many reasons[1]. We can help you find what doors to knock on … and how to start a conversation with employers about the benefits of deferred comp!

Check here for the best prospects.

Organizations looking for a competitive advantage in benefits for key employees are ideal prospects for deferred comp if they meet **each** of these criteria.

- ○ **Are one of these business types:**
  - Public
  - Private C corporation
  - Pass-through tax entity (S corporations, Limited Liability Corporations or partnerships) – wanting to provide benefits for non-owners
  - Non-governmental tax-exempt organization
- ○ **Have a strong business-continuation plan in place.**
- ○ **Are profitable, have good cash flow and a proven record of financial stability.**
- ○ **Have key employees falling short in retirement planning due to:**
  - Limits on how much they can contribute in their 401(k) or 403(b) plan
  - Qualified plan testing issues
  - Exclusion from the 401(k) plan
- ○ **Are willing to be a plan sponsor and:**
  - Pay the administrative service fees
  - Want the option of making employer contributions to select key employees

Take a closer look at the prospect.

Once you've spotted an organization that fits the characteristics above, dig deeper to learn about it and its key employees. The **more** of these attributes you can check, the **more likely** a deferred comp plan is a good fit for them.

Does the organization have …

- ○ Success for five years or more – and a stable or growing business?
- ○ Revenue greater than $10 million?
- ○ More than 100 employees – with key employees over age 50?
- ○ 10+ key employees earning over $150,000 or 5+ key employees earning over $250,000?
- ○ Issues with losing key employees at a higher rate compared to competitors?
- ○ To consistently provide refunds due to failed plan nondiscrimination testing?
- ○ Challenges in filling key employee positions due to a non-competitive benefits package?

There's much to talk about

Deferred comp gives you a lot to talk to employers about. You can explain how the plan helps their key employees save beyond 401(k) or 403(b) plan limitations – and provides employers with a competitive advantage in recruiting, rewarding and retaining them.

This chart shows that key benefits of deferred comp will get – and keep – employers' attention.

Deferred comp plans allow employers to[1]:

90%	Help participants save for retirement in excess of qualified plan limits
85%	Retain key employees
83%	Provide competitive benefits package when recruiting key employees

For key employees

- Take advantage of pre-tax deferrals, tax-deferred growth and compound earnings.
- Enjoy flexibile distributions without the same restrictions as 401(k) plans.
- Design an individualized investment strategy.

For employers:

- Provide a valued benefit that helps their key employees remain satisfied and motivated.
- Use additional employer contributions to retain or reward select key employees.
- Receive a tax deduction when benefits are paid.
- Benefit from assets on the balance sheet – money to finance the plan accumulates until benefits are paid.

Help your clients continue their business success and keep their top employees loyal by adding a deferred comp plan to their benefits program today.

Let's connect.

For deferred comp prospecting and marketing tools, or to discuss potential sales opportunities with these plans, contact your regional vice president – nonqualified plans (BB9718).

[1] 2015 Trends in Nonqualified Deferred Compensation, Principal®, published June 2016.

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Salary Deferral

CLIENT SNAPSHOT

BUSINESS PLANNING

A salary deferral plan is a type of employer-sponsored non-qualified deferred compensation plan available for highly compensated executives. Under a salary deferral plan, a key executive agrees to defer a portion of his/her compensation and the employer agrees to return the deferred amounts, with interest, at a future point in time.

A salary deferral plan is a non-qualified plan, which means the employee is allowed to defer as much income or compensation as the plan permits and the plan is not subject to qualified plan limits or caps. Accordingly, employees ordinarily participate in deferral plans when their current income substantially exceeds their current needs. Elective deferred compensation is designed as a supplemental benefit, so that key employees have an opportunity to accumulate wealth for retirement with tax deferred savings in excess of their qualified plan contributions.

How it Works

STEP 1

The employer decides which key executives to include in the plan.

STEP 2

Each participating employee and the employer enter into a deferral agreement, whereby the employee agrees to defer a portion of his/her compensation for the current year with an expectation to make additional deferrals of income in future years. The employer will agree to repay the money with interest at a specified time, usually at retirement. The employer may choose to match the employee's contributions to the plan, in whole or in part.

STEP 3

The employer decides how interest will be credited to the employee's deferral account and what options, if any, to offer. For example, the employee may be given phantom investment options with results applied to the deferral account.

STEP 4

The employer may choose to informally fund the plan. Salary deferral plans may be funded in several ways, but are commonly informally funded with a life insurance policy owned by the business on the employee's life.

STEP 5

At retirement, the employer can access the life insurance policy cash value via tax-free loans and withdrawals to pay the retirement benefit. At the time the benefit is paid, it will be taxable income to the employee and tax deductible to the employer.

Key Benefits

FOR THE EMPLOYEE

- **Deferral of taxation:** If properly structured, the employee will only pay income taxes when he/she actually receives the retirement benefit. Pre-tax retirement contributions maximize the compounding of savings. Moreover, the employee may receive tax benefits if he/she is in a lower marginal income tax when the deferred payments are received.
- **Supplements income from qualified plan savings:** Provides key executives with a vehicle to make tax-deferred savings beyond what he/she could contribute in a qualified plan.
- **Matching contributions:** An employer may choose to match an employee's contributions, thus increasing the value of the benefit received in retirement.
- **Investment options:** The employer may offer phantom "investment options" that align with the employee's investment goals and then allocate the plan assets (owned by the employer) in accordance with these goals.

FOR THE EMPLOYER

- **Increased competitiveness/loyalty:** Enhances a key executive's total compensation package.
- **Flexibility:** Deferral plans are flexible in terms of plan design, coverage, and implementation within the rules of §409A.
- **Golden handcuffs:** The employer may add a vesting schedule on employer contributions to the plan to encourage a key employee to stay with the company on a long-term basis.
- **Discrimination:** The employer may handpick the employees to participate in the plan and is not subject to the discrimination rules associated with qualified plans.
- **Cost recovery:** If informally funded with life insurance, the income tax-free death benefit can provide the employer with cost recovery.[1]
- **Ease of administration:** Minimal IRS, ERISA, accounting and other reporting/ regulatory requirements.

Important Considerations

- **Income Taxation:** If properly structured, the employee will only pay income taxes when he/she actually receives the retirement benefit. At that time, the employer may take a corresponding deduction. Note that the premium payments on a life insurance policy are not deductible to the employer.

- **Creditors:** Because a salary deferral plan is a non-qualified deferred compensation arrangement, plan assets may not be segregated (like in a qualified plan) without causing taxation to the employee. If the business becomes bankrupt and is unable to repay the benefit in the future, the employee will be considered an unsecured, general creditor of the business and will not receive preferential treatment in recovering his/her benefit.

- **Insurance Ownership and §101(j):** If the plan is informally funded with life insurance, the employer owns and is the beneficiary of a policy on the employee's life – the employee has no rights to the policy. When life insurance is owned by an employer on the life of an employee, §101(j) of the tax code requires that certain conditions and Notice and Consent requirements be met to keep the death benefit proceeds income tax-free.

- **§409A:** Section 409A of the Internal Revenue Code applies to all non-qualified executive benefit plans that provide for the deferral of compensation, such as a salary deferral plan. Failure to comply with Section 409A may subject the employee to immediate income taxation of the deferred amounts as well as interest and a 20% excise tax on the taxable income.

- **ERISA:** The possible application of ERISA should be considered for all non-qualified executive plans, including a salary deferral plan. In most instances, a salary deferral plan may be exempt from most ERISA requirements as a "top hat" plan. If ERISA applies, advisors should note that they may be considered a fiduciary and should take appropriate steps to comply with ERISA requirements, including conflict of interest rules.

Conclusion

A salary deferral plan can be a simple, flexible way for employers to reward a key executive's hard work and loyalty to the company, especially in cases where qualified plan income and contribution limits can hinder the executive's ability to fully save for retirement. Key employees should consider participating in a salary deferral plan if they are looking to bridge the gap between the tax-deferred retirement income they are eligible to save in qualified plans and the amount of retirement income they will need.

Talk to your financial professional to determine how a Salary Deferral Plan might work for you.

1. At the employee's retirement, the employer may be able to recover the cost of the benefit from the potential policy cash value via policy loans and withdrawals. Loans and withdrawals will reduce the death benefit and the cash surrender value, and may cause the policy to lapse. Lapse or surrender of a policy with a loan may cause the recognition of taxable income. Withdrawals in excess of the cost basis (premiums paid) will be subject to tax and certain withdrawals within the first 15 years may be subject to recapture tax. Additionally, policies classified as modified endowment contracts may be subject to tax when a loan or withdrawal is made. A federal tax penalty of 10% may also apply if the loan or withdrawal is taken prior to age 59½. Cash value available for loans and withdrawals may be more or less than originally invested. Withdrawals are available after the first policy year.

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Life insurance death benefit proceeds are generally excludable from the beneficiary's gross income for income tax purposes. There are few exceptions such as when a life insurance policy has been transferred for valuable consideration.

Loans and withdrawals will reduce the death benefit, cash surrender value, and may cause the policy to lapse. Lapse or surrender of a policy with a loan may cause the recognition of taxable income. Policies classified as modified endowment contracts may be subject to tax when a loan or withdrawal is made. A federal tax penalty of 10% may also apply if the loan or withdrawal is taken prior to age 59 1/2.

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Non-qualified benefit plan features at a glance

BUSINESS PLANNING

PLAN	162 BONUS PLAN	REBA	SALARY DEFERRAL	SERP	KEY PERSON COVERAGE
Target Employer	• Wants to reward selected key employees • Wants to avoid plan administration • Wants a current tax deduction	Same as 162 Bonus, plus: • Wants some control over how employee uses policy cash values • Wants to potentially recover costs if employee leaves early	• Wants to reward selected key employees • Wants maximum control of plan and assets • Wants cost recovery of plan outlay • Does not need immediate tax deduction • Does not mind some plan administration • Wants employee to contribute to plan costs	• Wants to reward selected key employees • Wants complete control of plan and assets • Wants cost recovery of plan outlay • Does not need immediate tax deduction • Does not mind some plan administration • Is willing to fund plan without employee contributions	• Has a key executive whose loss would cause great harm to business • Loss of key executive would disrupt sales, creditors, and/or customers • Would incur great expense to replace and train replacement
Target Employee	• Highly compensated and/or key employee that employer is looking to provide with an additional benefit • Has life insurance need, and may want to supplement retirement income as well • Wants maximum control over plan assets	Same as 162 Bonus	• Highly compensated employee • Maxed out on 401(k) plan • In a high tax bracket and wants to defer more income	• Highly compensated employee • Maxed out on 401(k) plan	• Key executive • Has special knowledge of the corporation's operations and products or has special creative talents • Is a "rainmaker" • Has special relationship with customers or creditors
Benefits	• Possible welfare benefit plan – minimal ERISA compliance • Can be selective in terms of who participates • Can have different bonus amounts for each selected employee • Tax-deductible • Minimal administration • Cost effective to employee • Policy can be outside of insured's estate	• Possible welfare benefit plan – minimal ERISA compliance • All the benefits of a 162 Bonus Plan, with added protection for the employer (golden handcuffs) • Potential cost recovery of unvested benefits • Easy to set up and administer • Encourages employee loyalty	• Top-Hat Plan – minimal ERISA compliance • Can discriminate in participants, vesting, and corporate match • Can provide employer cost recovery • Immediate plan funding with life insurance • Employee deferral of income, as much as employer will allow • Employee receives additional retirement benefit	• Top-Hat Plan – minimal ERISA compliance • Can discriminate in participants, vesting, and funding • Can have different benefit levels for different employees • Can provide employer cost recovery • Immediate plan funding with life insurance • Employee receives an additional retirement benefit	• Provides source of income to cover death of key person • Provides access to policy cash values in case of unexpected expenses • Could use policy cash value at retirement to fund a benefit for employee • Where available, policy may include a "critical illness benefit rider" that provides an additional pool of tax-free income in case key person is diagnosed with a covered critical illness (e.g., cancer, stroke, etc.)

PLAN	162 BONUS PLAN	REBA	SALARY DEFERRAL	SERP	KEY PERSON COVERAGE
Policy Owner	Employee	Employee	Employer	Employer	Employer
Plan Administration	Little to none	• Little to medium - employer must keep track of vested and unvested amounts • Must comply with 409A regulations but impact of 409A is generally minimal for a REBA	• High • Must comply with 409A regulations • Employee must sign consent to insure (101(j) compliance)	• High • Must comply with 409Aregulations • Employee must sign consent to insure (101(j) compliance)	• Little to none • Employee must sign consent to insure (101(j) compliance) • If used to fund a retirement benefit, must comply with 409A
Employer Deductibility	Yes	Yes, as benefit vests to employee	• Pre-retirement contributions to the funding vehicle are not deductible • Retirement benefit payments are deductible as they are paid out	• Pre-retirement contributions to the funding vehicle are not deductible • Retirement benefit payments are deductible as they are paid out	No
Employer Cost Recovery	No	Yes, for unvested portion of bonuses paid if employee terminates employment early	Yes	Yes	Yes
Employee Tax Deferral	• Premiums are reportable as income but policy cash values grow tax deferred. • Employer could pay tax cost via a double-bonus.	• Premiums are reportable as income but policy cash values grow tax deferred. • Employer could pay tax cost via a double bonus.	Yes, amounts contributed are tax deferred until received by employee	Yes, amounts contributed are tax deferred until received by employee	N/A
Degree of "Golden Handcuffs"	Low	Medium	High	High	N/A

Section 409A of the Internal Revenue Code imposes extensive substantive requirements on arrangements that purport to accomplish a deferral of income or the taxation of income. By its own provisions, failure to satisfy these requirements will result in the loss of deferral of recognition and taxation of the income. Section 101(j) of the Internal Revenue Code imposes income tax on the death benefit of life insurance contracts owned by the employer of the life insured unless certain exceptions apply. All such exceptions include satisfaction of notice and consent requirements set forth in the section. IRS Notice 2009-48 provides additional clarification of the rules for employer-owned life insurance.

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BECAUSE YOU ASKED

ADVANCED MARKETS

Implementing Non-Qualified Executive Benefit Plans

Don't let the fear of implementing non-qualified executive benefit plans prevent you from selling them.

The Advanced Markets group receives many calls from producers who are apprehensive about implementing non-qualified executive benefit plans, including Section 162 bonus plans, Restrictive Endorsement Bonus Arrangements (REBA), Salary Deferral plans, and Supplemental Executive Retirement Plans (SERP). This piece covers the key components of this important process. Use this document as a resource and adjust any of the components to meet the needs of specific cases.

Lay the Groundwork

During the sales process, be sure to mention the importance of implementation considerations and plan administration to the employer. You want the employer to be actively engaged in these activities, so bringing it to their attention early will help. A well-designed implementation strategy can boost participation levels among the eligible executive group because it will communicate the plan benefits effectively and demonstrate that the employer strongly supports the plan. In essence, it amounts to selling the plan to the eligible executives.

Many companies have a "style" to their communication with executives and you will want to understand how you will need to adapt the plan implementation to that style. For example, many executives work remotely from the main headquarters. Therefore, a combination of written materials mailed or sent electronically along with a webinar-type meeting to introduce the plan to the eligible participants may be needed. Also, you may need to conduct either a group meeting or individual meetings with the eligible plan executives to introduce the plan. You may have ideas to offer the employer to enhance the success of the implementation process, but ultimately the employer will want you to work within their guidelines. The employer may want certain people, perhaps from Human Resources, to attend all the meetings, or they may want only their staff to conduct the meetings without your involvement.

Keys to Successful Plan Implementation

Knowledge and communication are the keys to implementing a non-qualified benefit plan. Obviously, you need to know and understand the details of the plan and how it works, but what we are referring to here is the knowledge of what the employer's goals are for the plan and how they want it to benefit the participants. Understanding the employer's goals and needs will help you to offer the proper plan options to make it more effective for the company.

Typically, your role will be to serve as the hub for all the activities pertaining to implementing the plan. This requires you to effectively communicate with the employer, his/her accountant, attorney, Human Resources and Benefits departments, and the plan administrator to ensure that the plan is implemented as smoothly as possible. Other vendors may be involved, such as an outside graphics artist hired by the client to design and print enrollment brochures. It will be your job to harness all the various resources and keep them moving in the right direction. To do that, you must stay in regular contact with all parties until they complete their respective task(s). For example, the employer will not sign off on plan documents until the attorney has approved them. This may take several revisions, which can take time. This may delay the preparation of enrollment kits and could delay the plan enrollment if you do not keep the employer and attorney focused on completing that task.

After you have gathered the necessary information, here are the action steps to take in order to implement the plan.

Step 1:

The first step in the implementation process is to develop a schedule of the tasks that need to be done, including listing who is responsible for completing each task and a date for completion. A general rule of thumb is that it takes a minimum of three months to properly complete a plan implementation, and expect that there will be changes to the schedule. A variety of legitimate reasons can delay completion of specific tasks. Sometimes it's the employer who is slow to complete tasks, and there is only so much pressure you can put on them. So don't try to design a schedule with rigid completion dates. Build in some cushion for delays. A sample schedule is shown on the next page.

Step 2:

The next step is to begin designing the enrollment kits and formal presentation for the participants. As documents are completed they can be prepared for the kits. If an outside vendor has been hired to design enrollment kits, then your workload is lighter. However, the vendor will need your help to be sure the plan is appropriately described in the enrollment materials. This will likely require many phone calls and several hardcopy revisions. More than likely you and your staff will produce the enrollment kits. In most cases a simple, professional looking kit will serve very well. Successful enrollment kits often use a neutral-colored (dark blue or green, or white) folder with pockets on the inside. Personalizing the kit is important — the folder should have a label on the front with the participant's name. On the inside left pocket would be another label listing the documents included in the kit in the order they are placed. Typical items found in the kit include:

ENROLLMENT KIT

LEFT SIDE	RIGHT SIDE
Instruction Page	Personalized Illustration
Plan Election Form	Current Portfolio Review of VUL Subaccounts (if applicable)
One or two page Executive Summary of the Plan using bullet points	Glossy VUL Investment Brochure (if applicable)
Detailed Plan Description (not legalese)	VUL Prospectus (if applicable)
Plan Agreement(s) prepared by Attorney	

Step 3:

An equally important step is the enrollment presentation. This is typically a PowerPoint presentation in bullet point format. This piece is used for group enrollment meetings where the plan is explained to the participants and they are invited to participate. Executives often like these presentations because they can get to meet you personally. These presentations are often critical to the initial level of participation in voluntary plans (such as a salary deferral plan).

Step 4:

The last step is the actual enrollment period itself. During this time the participants will review their kits, complete the paperwork, return it, as well as call you for clarification of the plan features. During your discussions with the participants, you will learn firsthand what they liked and didn't like about the enrollment materials. This helps you to modify the materials for next year's enrollment. After the enrollment period is over, we recommend meeting with your client to learn what they liked about the enrollment process and what changes they want to make for next year.

Plan Administration

After the plan is implemented, it will require some level of administration. Also, you will want to maintain your relationship with the employer. At the very least, you should be prepared to meet with the employer annually to get their feedback on how the plan is performing and to determine if any changes are needed or if goals have changed. For example, the employer should be interested in how the life insurance policies are performing compared to how they were illustrated at plan implementation.

If the plan design is simple, such as a Section 162 bonus plan, you will probably acquire and prepare the illustrations and information needed for these meetings. However, if the plan is complicated, like a SERP, you will have to make a decision about your role in ongoing administration. The employer will want regular reporting on the status of the plan and will need specific information that is critical to their accounting and tax departments at the end of the year. Unless you have the specialized knowledge and staff needed for this level of plan administration, you will be well served to recommend the employer hire a Third Party Administrator (TPA) for these services. The employer's cost for these services is tax deductible as a service fee. The employer can use a TPA of their choice for this work. John Hancock has a relationship with a nationally recognized TPA as well.

SAMPLE SCHEDULE

TASK	PRIMARY PARTY RESPONSIBLE (OTHERS INVOLVED)	DUE DATE
Receive Final Census Data	Client (Producer, Attorney)	October 1
Announcement Letter to Participants	Client (Producer, Attorney)	October 15
Legal Document Preparation	Attorney (Client, Producer)	October 1 to November 22
Plan Description Preparation	Producer (Client, Attorney)	October 1 to November 22
Executive Summary Preparation	Producer (Client, Attorney)	October 1 to November 22
Personalized Illustrations	Producer (Client)	October 1 to November 22
Enrollment Kits Finalized	Producer (Client)	November 22
Enrollment Kits Delivered to Client	Producer	November 25
Enrollment Group Presentations	Producer (Client)	December 2 to December 6
Enrollment Period		December 2 to December 23
Published Date to Return Forms		December 23
Unpublished Date to Return Forms		December 31
Underwriting Period (if needed)		December 20 to January 15

For more information on implementing non-qualified executive benefit plans, contact the Advanced Markets Group at 888-266-7498, option 3.

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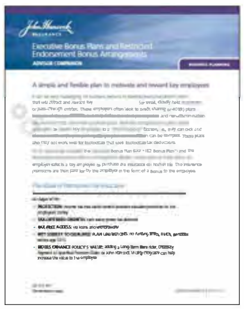
Executive Bonus Plans

TOOL KIT

The following materials were designed to help promote Executive Bonus Plans. Executive Bonus plans can provide long term value to the most productive employees in a way that is flexible, cost effective, and simple to administer.

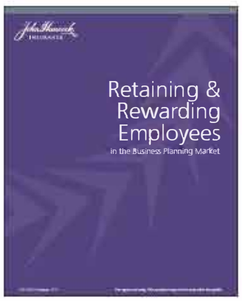
Download the documents below here:
https://pinneyinsurance.com/docs/JohnHancockExecutiveBonusPlansToolkit.pdf

Executive Bonus Client Snapshot
(Client Approved)



Executive Bonus/ REBA Advisor Companion

Executive Bonus/ REBA Employer Guide
(Client Approved)



Retaining and Rewarding Key Employees

Executive Bonus Plans/ REBA Fact Finder

JH Solutions Sample Presentation
(Client Approved; Customizable)

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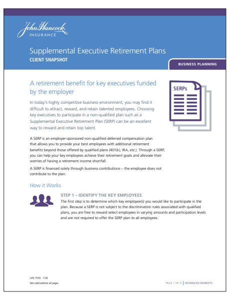
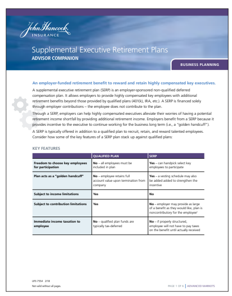
Supplemental Executive Retirement Plans
TOOL KIT

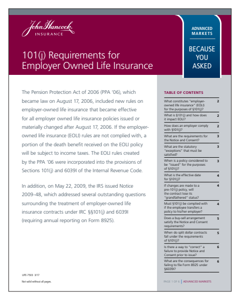
The following materials were designed to help promote Supplemental Executive Retirement Plans (SERP). A SERP might be an ideal solution to help fund a retirement benefit for the employee and also be used to retain the employee until retirement.



Client Snapshot
(Client Approved)



Advisor Companion



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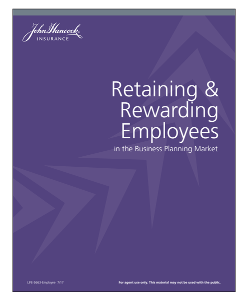
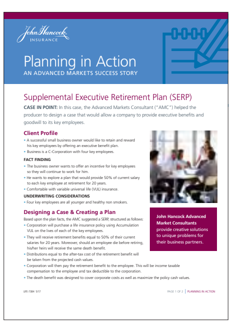
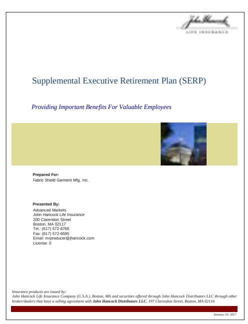


Retaining and Rewarding Employees



Planning in Action: SERP



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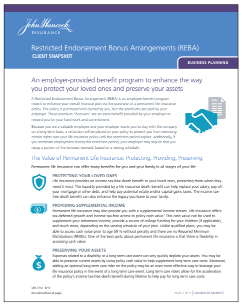
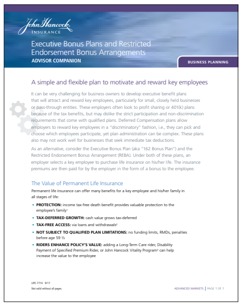
Restricted Endorsement Bonus Arrangements

TOOL KIT

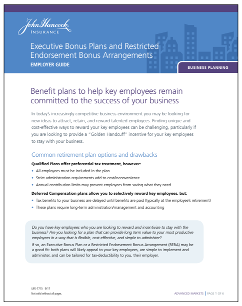
The following materials were designed to help promote Restricted Endorsement Bonus Arrangements (REBA). REBA plans can provide long term value to the most productive employees in a way that is flexible, cost effective, and simple to administer.



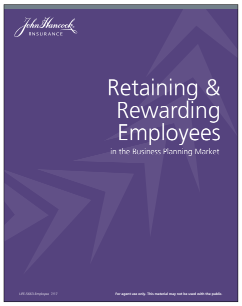
REBA Client Snapshot
(Client Approved)



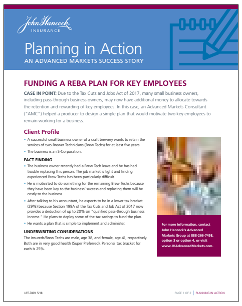
Executive Bonus/REBA Advisor Companion



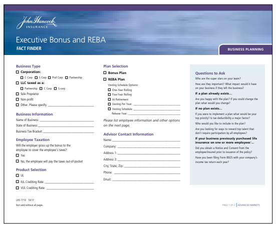
Executive Bonus/REBA Employer Guide
(Client Approved)



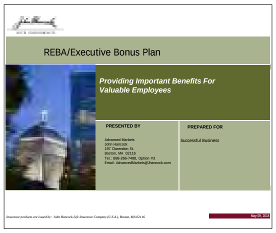
Retaining and Rewarding Key Employees



REBA Planning in Action



Executive Bonus Plans/REBA Fact Finder



JH Solutions Sample Presentation
(Client Approved; Customizable)

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Principal®

Nonqualified deferred compensation plans

Plan designs that drive business success

Strategies behind the plan's primary uses

A versatile tool that helps enhance your benefits package, and so much more

A nonqualified deferred compensation plan gives you options and flexibility to drive progress toward many types of organizational goals and strategies that impact your success.

First, take a look at the primary business needs that many plan sponsors want to solve. Then keep reading to see how the flexibility in plan design can be used to implement a deferred comp solution tailored to your specific business drivers and strategies.

Primary business needs

Help key employees save more
Qualified plans are a great start in saving for retirement, but they have limits and coverage testing requirements that cause problems for highly compensated employees. They don't allow them to defer the same percentage of income as other employees, limit incentive choices and flexibility, contribute to 401(k) participation testing, and possibly even result in contribution refunds. A deferred comp solution offers a supplemental savings approach.

Give key employees more control over the timing of benefit payments (and taxes)
For high earners or those with fluctuating income, their tax rate is an important component in their financial planning. With more control over when they get paid, they could manage taxation timing, save for big moments and be more strategic to meet retirement and other savings goals.

Support efforts to recruit, reward, retain and help key employees retire
To attract, keep and reward key employees, sometimes you need something more than your competitive benefits package. Having a flexible component can help ensure your top talent remains committed to you – and not the competition.

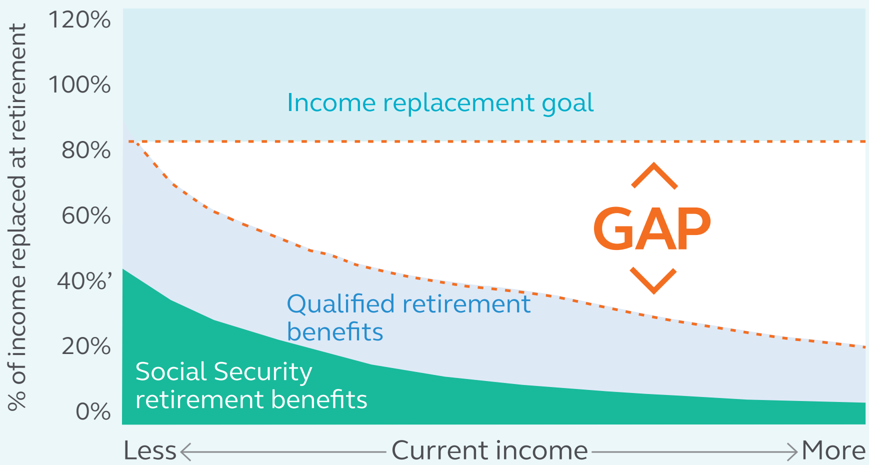
Imitate employee ownership and transition platforms
It's easy to envy the vested interest achieved with formal employee ownership scenarios. But that isn't always the best option. Imitating shares for purchase or an insider transition plan can create an ownership experience without dilution or premature decisions.

Let's take a look at how a deferred comp plan could be designed to address these four primary business needs.

Bridge employee's retirement gap

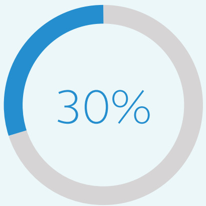
Deferred comp plans offer a secondary pre-tax savings account that can be used to bridge the retirement savings gap that often burdens highly-compensated employees. Not only can participants set aside more income for retirement, but this plan gives you another way to reward them, too. If your contributions are held back by qualified plan limits or risk of failing non-discrimination and coverage testing, you can contribute additional savings to a deferred comp plan.

Customize your plan by setting deferral limits (if any), employer contribution amounts and vesting schedules to fit your need. You can also do this for various participant tiers. You ultimately choose who to reward and how much, without worrying about the testing and compliance concerns that come with qualified plans.



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.

Expected retirement income by deferred comp plan participants



of participants anticipate the plan will provide **10–24%**[1]

[1] 2017 Principal Trends in Nonqualified Deferred Compensation report.

Manage the timing of income and taxes

Deferred comp plans can be designed to give employees more strategic control over when their benefits are paid to meet their objectives and timing needs. And since taxes are due when benefits are received, they also have some control over taxation timing.

This flexibility gives them a plan that better fits their financial goals. You can set parameters around options like multiple savings accounts, getting paid while still working or in retirement, lump sum or installment payments, delaying payouts, and investment risk – all at the individual account level.

As shown in the example scenario below, this kind of flexibility in plan design could allow participants to:

- Coordinate with other retirement income sources
- Lower overall tax rates
- Fund life's big events

Income and deferral elections	Objectives	Tax strategy
• 10% of $120,000 base pay ($12,000) • 50% of $40,000 bonus ($20,000) • Total: $32,000	• Provide college money for two kids • Purchase second home • Build retirement	• Lower income when marginal tax rates might be higher • Take distribution when effective tax rate might be lower

20% Mary's college	20% Michael's college	20% Beach house	10% Retirement	30% Retirement
$6,400 **July 2020**	**$6,400** **July 2024**	**$6,400** **Jan 2028**	**$3,200** **Retire**	**$9,600** **Retire**
4 payments	4 payments	1 payment	1 payment	5 payments
Conservative portfolio	Moderate portfolio	Moderate portfolio	Aggressive portfolio	Aggressive portfolio

This is a hypothetical example to illustrate how multiple savings accounts work within a nonqualified deferred compensation plan. It is intended to be educational in nature and not intended to be taken as a recommendation.

Recruit, retain, reward and retire key employees

Flexible options in deferred comp plans allow you to give back to your key employees, whose leadership and expertise are hard to match – and hard to find. This boost in your benefits package can even be flexible enough to cater to different stages of employee management, as well as the different ways your top talent is motivated.

Recruit
Attract top talent via signing bonuses tied to tenure or performance.

Retain
Influence tenure with structured bonuses that use vesting schedules.

Reward
Drive both organizational and personal performance with incentive-based contributions to the plan.

Retire
Restore company match benefits you're unable to make in qualified plans due to testing or compensation limits.

> If key employees are offered a unique benefit…it ties them to the company that much more.
>
> – Dan Kowalczyk, retired business executive, nonqualified plan participant

Create an ownership experience

Deferred comp plans can be a valuable tool in mimicking an ownership experience without the formality that can get in the way of the value you want to capture. Plans can be designed to create a performance-driven shares scenario, a transition plan for successors or something else that suits your business needs.

Performance-driven shares
Employers have the option of using employer contributions or phantom shares to incent employee performance. Similar to shares of stock, employers can customize contribution and vesting schedules measured by phantom stock values. With this compensation management strategy, the employee is given phantom shares that increase and decrease based on the valuation of the company, as shown in the example. But you aren't subject to the dilution that comes from actual equity grants. Or, employers can simply set up contributions based on company profitability.

Company	Formula
Contributes to plan or provides phantom stock shares to participating key employees	Number of phantom shares or contributions determined by annual gross profit
Value	**Vesting**
Declared by board annually	20% per year based on meeting goals

Transition planning
Give possible future owners of the company a way to purchase the business, without limiting your options. You can contribute to a potential future owner's account and establish the vesting and distribution to occur based on the sale of the company as shown in the example. If you're unsure how the sale will happen, that's ok. You can build in various circumstances.

Sale of business	Vesting event	Vesting
Sale to insiders	Change in control	Account vests and distributes to executives and is used to execute purchase
Sale to outsiders	Set duration after the sale	Account vests and distributes to executives as reward for years of service
None	Retirement	Optional triggering event can be retirement

So many options with widespread benefits

No matter what role a deferred comp plan plays in your overall strategy, it offers some universal benefits that both you and your employees can enjoy.

Benefits for your key employees:
- Take advantage of pre-tax deferrals, tax-deferred growth and compounded earnings
- Defer up to 100% of compensation to meet savings goals
- Design a personalized investment strategy
- Enjoy flexibility and take payouts from the plan without the same age restrictions as 401(k) plans

Benefits for you:
- Make optional company contributions
- Restore 401(k) plan contributions limited by IRS testing
- Easily administer with no discrimination testing, minimum participation or Form 5500 filing, if set up properly by the employer

An industry leader in your corner

Our history speaks for itself. We've been providing deferred comp plans for more than 25 years, and have over 75 years of retirement plan experience. We're the No. 1 provider of deferred comp plans[2] and a leading provider of defined contribution plans[3].

[2] Based on total number of NQDC plans, PLANSPONSOR 2015 NQDC Buyer's Guide.
[3] Based on number of Recordkeeping plans, PLANSPONSOR Recordkeeping Survey, June 2016.

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Principal℠

Nonqualified deferred compensation plan

Keep your business strong and key employees motivated

A retirement benefit that helps you recruit, retain and reward key employees

What is a deferred comp plan?

It's much simpler than you may think. A deferred compensation plan is an employer-sponsored benefit for the key employees you choose. It's basically an agreement between you and your key employees.

Those who participate defer a portion of their annual compensation into the plan before taxes. And you promise to distribute that money, plus any earnings and additional employer contributions, to them at a future time.

Keep your key employees satisfied with benefits they need and value

Things are going well for your organization. Much of this success is credited to your key employees. Their leadership and expertise are hard to match – and hard to find! What can you do **now** to help ensure your top talent remains committed to you – and **not** the competition?

Enhance your benefits package with a **nonqualified deferred compensation plan**. It can give you a competitive advantage by:

- Encouraging the best employees to join your organization as it grows.
- Keeping your key employees satisfied and motivated for the long term.
- Rewarding them for reaching goals.
- Helping employees bridge the retirement gap resulting from 401(k) plan testing and limitations.

No matter which of the areas above you are trying to address, we have a solution for your organization. To help you select the right plan, we'll listen to your challenges, understand your needs and goals, and work with you and your financial professional to:

Discover – Identify the issues your organization wants to resolve and what you want to achieve.

Solve – Learn how this plan can help solve problems and achieve your objectives.

Design – Use the plan's flexibility to tailor a plan to your organization's and participants' needs.

Partner – Trust the service and expertise we'll provide to you and your key employees every step of the way, year after year.

Stay current – Make changes to your plan as your organization's needs and goals change.

Discover

What are the organization's goals?

It's important to your organization to have a valued and affordable benefits package – plus a little more for your key employees. So think about the goals you want your benefits package to achieve – both short- and long-term, such as:

		Notes
Recruit	Attract the best employees as part of a competitive benefits package.	
Retain	Encourage key employees to remain loyal to your organization.	
Reward	Provide performance-based contributions to achieve organizational goals.	
Ownership experience	Create phantom shares to provide an ownership experience without the dilution that comes from actual equity grants.	
Retire	Help your key employees save enough for retirement above what 401(k) plans allow.	

What are your key employees' goals?

To have a successful plan, you need to address what your top employees want. Our annual trends survey shows participants consider deferred comp most important in reaching retirement goals. But you can customize the plan to help your key employees with a variety of goals, including:

		Notes
Retirement savings	Save beyond 401(k) plan limitations with employee deferrals or optional employer contributions.	
Other savings goals	Control timing of payouts to meet other savings goals before or after retirement, such as college education or second home.	
Managing taxes	Help manage the impact of taxes using the plan's flexibility for when benefits are paid.	
401(k) restoration	Use employee deferrals or employer contributions from deferred comp to restore benefits limited under a 401(k) plan.	

Solve

Is deferred comp right for you and your key employees?

Once you've identified the most important goals, then consider the role that a deferred comp plan can play in helping achieve those goals. The plan offers benefits and considerations for both the organization and the key employees.

Benefits for your key employees:

- Take advantage of pre-tax deferrals, tax-deferred growth and compounded earnings.
- Defer up to 100% of compensation to meet savings goals.
- Design a personalized investment strategy.
- Enjoy flexibility and take payouts from the plan without the same age restrictions as 401(k) plans.

Benefits for you:

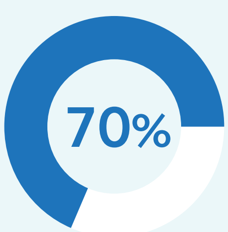
- Make optional company contributions.
- Restore 401(k) plan contributions limited by IRS testing.
- Easier to administer with no discrimination testing, minimum participation or Form 5500 filing, if set up properly.

Considerations for your key employees:

- There are no rollovers or loans like qualified retirement plans.
- Compensation deferred into the plan isn't protected in the event of company bankruptcy.
- The decision to defer compensation must be made the year ahead of earning the income.

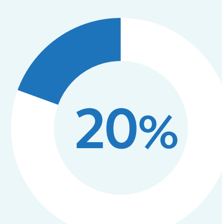
Considerations for you:

- The corporate tax deduction is deferred until benefits are paid, rather than a current deduction.
- There's a potential charge to earnings on assets purchased to finance the plan.



Plan sponsors view deferred comp benefits as a **supplement to their benefits package** to help recruit, retain and reward top talent. In addition, over 70% want to help them have sufficient retirement income[1].

Participants expect their deferred comp plan to account for **20% of their retirement income**, on average[1].



Design

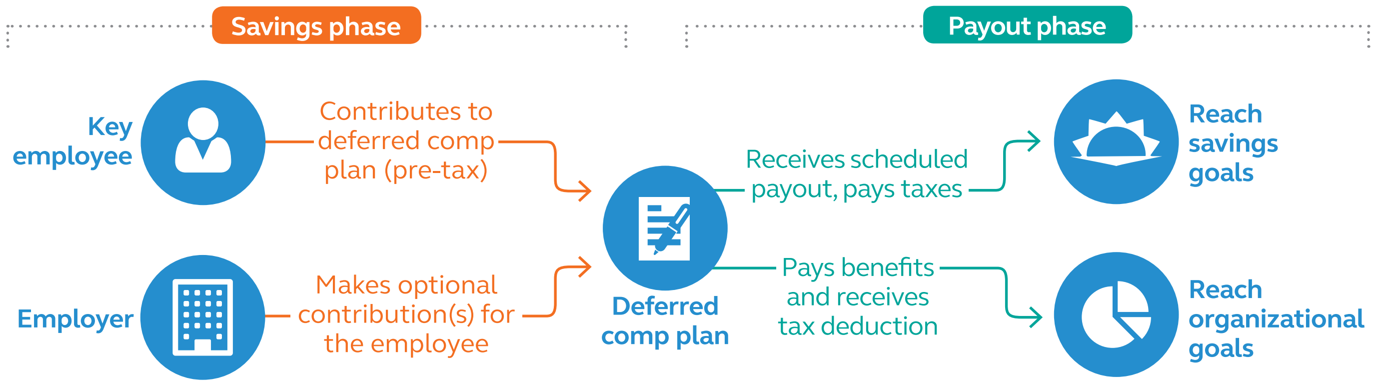
How's the plan created?

You're in control of making the plan yours – it's based on the specific goals of your organization and unique needs of your key employees. Together with your financial professional, we'll walk you through the decisions that need to be made to design a plan that makes sense for your organization:

		Notes
Who participates	Select the groups of key employees ("Top Hat" employees or independent contractors) to participate in this plan.	
What can be contributed	You can allow key employee deferrals (up to 100% of compensation) and/or provide employer contributions with the flexibility to vary benefits by employees.	
What happens with the contributions	You can select a reference investment line-up for participants from a broad range of options. In addition, you can decide how and when key employees may receive the benefits based on organizational needs.	
How benefits are paid	Decide how payouts can be received from the plan. Benefits can be distributed as a lump sum or in annual installments.	

How it works

This chart shows how money is contributed to the deferred comp plan and paid out at a later date. It also points out that when the benefit is distributed to the key employee, the employer receives an income-tax deduction and the key employee pays income tax on it.



How does an organization pay for it?

How the plan is financed

Keeping your promise to pay benefits to participants in the future is important. Any one of these three (or combination of) financing options can help you do that. Plus, we'll provide a detailed financial model comparing the options to help you make this decision.

- **Company cash** – No specific plan assets are set aside. Instead, benefits are paid through the company's cash flow.
- **Taxable investments** – The company invests in mutual funds and/or individual securities.
- **Corporate-owned life insurance (COLI)** – The company purchases a policy to pay future obligations.

Notes

Partner

How do we work with your organization and key employees?

You want to offer key employees the benefits they value – and those that will have a positive influence on them and your organization. Our team of experts will work closely with you and your financial professional to develop a strategy for implementing and servicing your deferred comp plan.

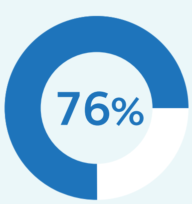
But we don't stop there. Year after year, we'll continue to work closely with you and your financial professional to fine-tune your plan to ensure your organization's goals are met – and your plan is administered as efficiently as possible.

Keeping you in-the-know

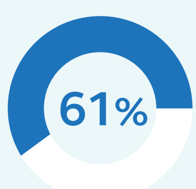
To help you stay on top of your plan, a range of information is available on our website and corporate accounting reports. You also have easy access to plan asset and liability reporting, investment resources and other tools to assist with administering your plan. Plus, depending on your plan type and design, you'll receive:

- Access to plan participants' account information.
- Daily valuation of assets/liabilities.
- Asset/liability information and rebalancing services.
- Financing reviews to assess plan performance.
- Updates on enrollment progress.
- Quarterly newsletter featuring legislative news, service updates and more.

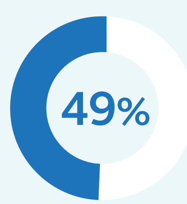
Participants tell us they consider the deferred comp plan most important in[1]:



Reaching retirement goals – 76%.



Considering taking a new job with a new employer – 61%.



Deciding to stay with a current employer – 49%.

› Turning your key employees into plan participants

Understanding the benefits of this exclusive plan is the first step – it's what will encourage your key employees to participate. We're here to help every step of the way:

Step 1: Introduce the plan

Whether this is a brand-new benefit or employees are familiar with this type of plan, we offer award-winning* custom education to introduce plan basics. We'll help you make sure your employees are aware they are eligible so they can make an informed decision to participate.

Step 2: Enrollment

Participants can conveniently enroll online at principal.com. Our deferred compensation plan specialists are available to answer questions Monday-Friday.

Step 3: Ongoing education and planning

Your participants need support to stay on track. We can also provide you with additional communication and education to promote greater understanding and appreciation of the benefit. Participants can find information about their accounts, investment strategy, contributions and scheduled distributions at principal.com.

* 2016 International Financial Communicators Awards Competition

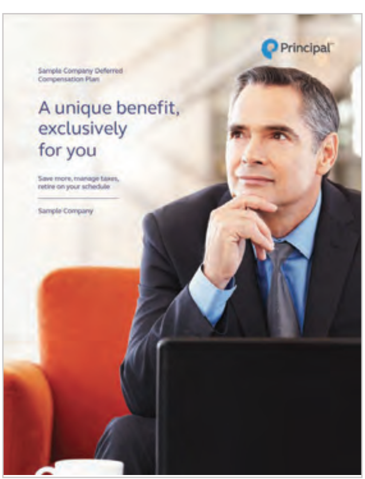
Participants set savings goals and see the impact of their contributions through our Deferred Compensation Planner.

The first question is simple. Can you afford to defer some current income? If you can, these additional questions will help you learn more.

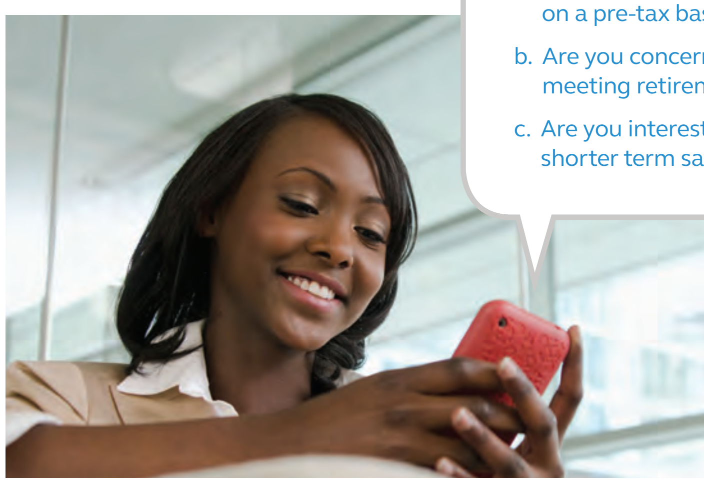
a. Are you interested in saving on a pre-tax basis?

b. Are you concerned about meeting retirement goals?

c. Are you interested in meeting shorter term savings goals?



Education materials prepare participants for the decisions they'll make at enrollment.



Employees create their own tailored experience through dynamic, interactive digital education.

Stay current

How does the plan keep up with your organization's needs and goals?

The deferred comp plan is your plan. Its long-term success depends on how well it keeps pace with your organization's needs and goals -- today and tomorrow. So once your plan is in place, we'll make sure to provide:

Close attention to the plan over time, such as a participant's account balance from the beginning of the plan until payout at retirement.

Experienced specialists who offer feedback on factors that can influence the plan, such as plan design changes and regulatory updates.

Analytical tools and resources are available for new and existing plans – all while watching out for your bottom line.

Periodic financial reviews help ensure the plan's financing continues to meet your goals.

Annual service reviews to discuss how the plan is doing.

Access to online dashboards of information.

"(We receive a) fantastic experience from our service team representatives and on up to our client relationship manager. We have a great working relationship. They understand our complicated structure, are well-respected by our senior leadership team and very responsive."

– Plan sponsor quote from Principal research survey, April 2016

Ready to start?

Once you decide that a deferred comp plan is right for your organization and key employees, we'll bring our expertise and resources to the table to help you put this plan in place within your desired timing. We'll begin by:

- Gathering information from you about your organization.
- Tailoring the plan to your specific needs and goals.

Thousands of employers value the solutions and services we provide. You and your financial professional can count on us, too. We'll do our best to deliver a positive experience for everyone involved.

An industry leader in your corner

Our history speaks for itself. We've been providing nonqualified deferred compensation plans for more than 20 years, and have over 75 years of retirement plan experience. We're the No. 1 provider of deferred comp plans[2] and a leading provider of defined contribution plans[3].

What sets us apart from others is our:

- Commitment to and experience in the business and retirement plan markets.
- Unique plan design and flexibility to tailor it to specific needs and goals.
- Specialized team of legal, accounting and financing resources with more than 200 years of experience to provide support.
- Service and commitment to building long-lasting relationships.

A member of the FORTUNE 500®, our employees are passionate about helping clients of all income and portfolio sizes achieve their goals. You can count on us to offer innovative ideas, investment expertise and real-life solutions to help make financial progress possible.

Learn more

Contact your financial representative for more information or to help with the next steps in putting a plan in place.

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[1] 2015 Trends in Nonqualified Deferred Compensation, Principal®, published June 2016.

[2] Based on total number of NQDC plans, PLANSPONSOR 2015 NQDC Buyer's Guide.

[3] Based on number of recordkeeping plans, PLANSPONSOR Recordkeeping Survey, June 2016.

NONQUALIFIED DEFERRED COMPENSATION

Presented for

Client Name Fillable

Presented by

Agent Name Fillable

Line 1 Contact Information

Line 2 Contact Information

Line 3 Contact Information

TITLE HERE (in Options)

The Concept…

- Nonqualified deferred compensation is an arrangement employers use to provide retirement income—and often death and/or disability benefits—to a select group of executives or highly paid employees.
- The arrangement is a contractual agreement between an employer and an employee (or independent contractor) specifying when and how future compensation will be paid.
- When properly set up, the employee can postpone income taxation on the deferred amounts until the benefits are paid.
- Deferred compensation arrangements are “nonqualified,” meaning they don’t have to be preapproved by the IRS, and employers can favor selected employees without risking claims of discrimination.
- Properly arranged, they’re exempt from nearly all of ERISA’s regulatory requirements.

The Rationale…

- Providing attractive compensation and benefits to owner-employees and key executives is a continuing source of concern for large and small businesses.
- In this environment, strict regulations surrounding qualified retirement plans—coupled with high administrative costs, anti-discrimination rules, and caps on benefits and contributions—have steered many businesses toward supplemental arrangements for key executives.
- Nonqualified deferred compensation permits employers to reward selected executives without taking on the administrative burden of a qualified plan.
- Deferred compensation is typically viewed as an added benefit, and is used in conjunction with a qualified retirement plan, group life and health insurance coverage, and other broadly based employee benefits.

Prospect Profiles…

- An employer who wants to benefit a select, highly compensated employee or group of employees
- C-corporation executives who are looking for ways to improve compensation and benefit packages
- An employer who needs to attract, retain, or reward one or more key employees

Section Here (in Options)

TITLE HERE (in Options)

- A key employee who is already contributing maximum amounts—or accruing maximum benefits from—a qualified retirement plan
- An employer who does not want to establish a qualified retirement plan

Unique Flexibility…

- Nonqualified deferred compensation permits a business to pick and choose among "top-level" employees with no danger of running afoul of anti-discrimination rules or minimum funding requirements.
- A business can provide a different level of benefits for different employees.
- No government-mandated vesting rules apply.
- Deferred compensation can be customized to suit individual situations.
- Paperwork and administrative costs are kept to a minimum.

The Process…

- Nonqualified deferred compensation typically provides that an employee will receive a stipulated sum for a fixed period of time, or for life, beginning at a future date—the employee's scheduled retirement, for example.
- If the employee dies after payments have begun, the agreement may direct that remaining benefits be paid to the employee's designated beneficiary.
- A "true deferral" arrangement provides that the employee will receive future compensation as a result of a current salary reduction agreement, or in lieu of a future bonus or expected salary increase.
- In contrast, a "salary continuation" arrangement commits the employer to pay future compensation to the employee without a reduction in current compensation.

Funding…

- In a "funded" arrangement, the employer sets aside specific assets to meet this future obligation, out of the reach of general creditors and with the employee as beneficiary. However, a funded arrangement results in the current inclusion of the deferred amounts in the employee's income unless the funds are subject to a "substantial risk of forfeiture."

TITLE HERE (in Options)

- An “unfunded” arrangement is therefore more common, giving the employee only a contractual, unsecured right to future income—either there are no reserves set aside to pay promised benefits, or reserves remain within the reach of general creditors or as a general asset of the business. The employee may not have beneficial ownership rights in any reserved assets.
- In an unfunded arrangement, deferred amounts are included in the employee’s gross income only when benefits are actually or constructively received.
- The employer can purchase life insurance to unofficially fund the arrangement without losing the income tax deferral. The policy must be available to the employer’s creditors and the employee has no beneficial ownership rights in the policy.
- To avoid taxation of death proceeds, the employer must meet the notice and consent requirements of IRC Sec. 101(j).

Acceleration of Benefits…

- Historically, participating employees were generally not taxed until they actually received payments as long as three conditions were met: (1) the deferral was agreed upon before compensation was earned, (2) the deferred amount was not unconditionally placed in trust or escrow, and (3) the employer’s promise to pay was merely a contractual obligation and not evidenced by notes or secured in any other way.
- The employee can lose income tax deferral if the arrangement doesn’t follow the rules of IRC §409A (for example, if an employee has control over deferred amounts or has a right to early access to benefits).
- Moreover, if the statutory requirements are not met, the employee must pay a 20% penalty on the amounts included in gross income, plus interest charged at one percent over the normal rate on underpayments.
- Deferred amounts are generally includible in the employee’s gross income—for all tax years in which they are not subject to substantial risk of forfeiture—if the plan fails to meet: (1) distribution requirements, (2) no-acceleration-of-benefits requirement, and (3) election of deferral requirements.
- Distributions are permitted only upon separation from service, death or disability, a fixed time specified in the plan, a change in an employer’s ownership or control, or an unforeseeable emergency such as severe financial hardship. Distributions at any other time will result in the loss of income tax deferral.

- Any changes in distribution methods that create an acceleration of payments will result in loss of income tax deferral, as will adopting an arrangement that gives the plan administrator discretion over the timing of benefit payments that could result in accelerated payments.

The Timing…

- To achieve income tax deferral, the employee must generally make the election to defer compensation no later than the end of the preceding tax year.
- In the first year of eligibility, the employee can make the initial deferral election within 30 days of becoming eligible and it will apply to compensation for services subsequently performed.

The Bottom Line…

Even though the tax law places restrictions on the distribution of benefits, nonqualified deferred compensation arrangements are an effective way to reward and retain valuable, highly compensated employees on a selective basis.

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SUMMARY

What Is Nonqualified Deferred Compensation?

Nonqualified deferred compensation is an arrangement established by employers to provide retirement income and often death and/or disability benefits to selected managers or highly compensated employees. When it's properly arranged, the employee can defer income taxation until the benefits are paid.

Deferred compensation arrangements are "nonqualified," which means they don't have to be preapproved by the IRS, and employers can favor selected employees without risking claims of discrimination. Also, when properly arranged, they are exempt from nearly all of ERISA's regulatory requirements.

How Does It Work?

A nonqualified deferred compensation arrangement typically provides that an employee will receive a stipulated sum for a fixed period of time—or for life—beginning at a future date, such as the employee's retirement. If an employee dies after payments have begun, the arrangement may direct that the remaining benefits be paid to the employee's beneficiary.

The arrangement may provide that the employee will receive future compensation as a result of a current salary reduction or in lieu of a bonus or salary increase. This is sometimes called a "true deferral arrangement."

An alternative is a "salary continuation arrangement." Here, the employer commits to pay future compensation to the employee in addition to current earnings, which aren't reduced by participation in the arrangement.

What's the Tax Picture?

Generally speaking, the deferred amounts in an unfunded plan are includible in the employee's gross income when they are actually or constructively received. The deferred amounts in a funded plan are currently includible in the employee's gross income unless they are subject to a substantial risk of forfeiture.

The employee can lose income tax deferral if the arrangement doesn't follow the rules of IRC §409A (for example, if an employee has control over deferred amounts or has early access to them).

Amounts deferred under a deferred compensation plan will be includible in the employee's gross income for all tax years in which such amounts are not subject to a substantial risk of forfeiture if the plan fails to meet (1) distribution requirements, (2) no-acceleration-of-benefit requirements, and (3) election requirements.

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The rules only permit distributions upon separation from service, death, disability, a fixed time specified in the plan, a change in ownership or control of the employer, or an unforeseeable emergency such as a severe financial hardship. Distributions at any other time will result in loss of income tax deferral.

The plan must not permit a prohibited acceleration of any payment or schedule of payments. Therefore, the plan administrator may not be given discretion over the timing of benefit payments that could result in an acceleration of payments

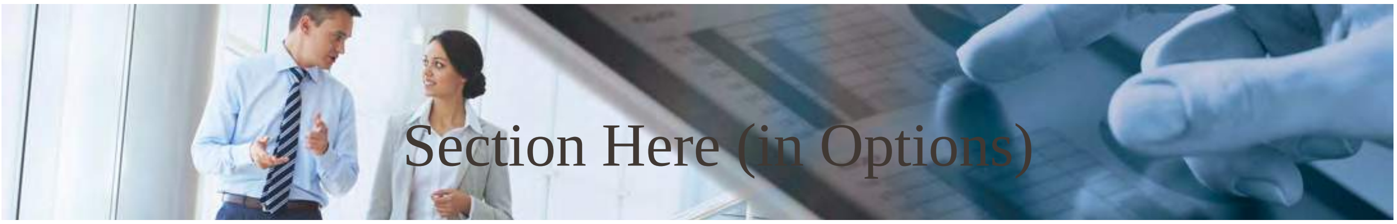
When Should the Deferral Election Take Place?

To achieve income tax deferral, the employee must generally make the election to defer compensation no later than the end of the preceding tax year.

In the first year of eligibility, the employee can make the initial deferral election within 30 days of becoming eligible and it will apply to compensation for services subsequently performed.

What’s the Conclusion?

Even with the tax law placing restrictions on the distribution of benefits, nonqualified deferred compensation arrangements remain an effective way to reward and retain valuable, highly compensated employees on a selective basis.



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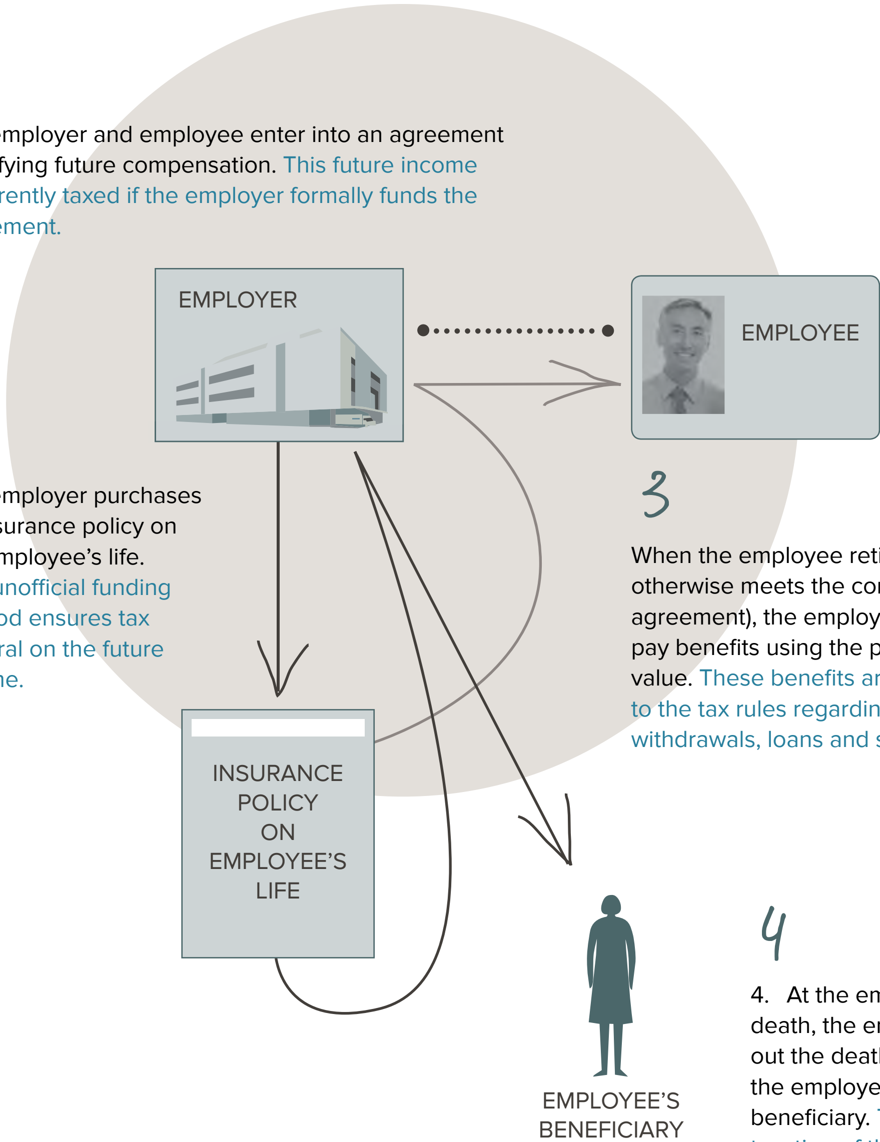
1

The employer and employee enter into an agreement specifying future compensation. This future income is currently taxed if the employer formally funds the agreement.



2

The employer purchases an insurance policy on the employee's life. This unofficial funding method ensures tax deferral on the future income.

3

When the employee retires (or otherwise meets the conditions of the agreement), the employer begins to pay benefits using the policy's cash value. These benefits are subject to the tax rules regarding policy withdrawals, loans and surrenders.

4

4. At the employee's death, the employer pays out the death benefits to the employee's named beneficiary. To avoid taxation of these death benefits, the employer must meet the notice and consent requirements.

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