QUALITY QUOTE
INSURANCE SOLUTIONS
INNOVATIVE ADVISOR SERVICES

Various Methods to Support Deferred Compensation Plans

Because highly compensated employees are limited in their yearly contribution to the employer's qualified retirement plans, their potential retirement income, as a percentage of their pre-retirement income, may be lower than that of an employee compensated at a lower salary. Thus, to provide incentive and reward as well as equitable treatment at retirement, many employers develop separate non-qualified deferred compensation plans. These informally funded plans may contain promises to pay a select amount of post-retirement income to the executive if he lives, or pre-retirement death benefits to the executive's beneficiary if he dies early.

	Income Tax	Benefits	Disadvantages
Employer Funds	Deductible to ER when benefits are paid to EE. Taxable to EE when benefits are received.	No capital commitment during deferral phase. Deductibility when paid out reduces employer's net cost. No taxation until funds are received as benefits by employees.	Drain on capital that might help the business grow. No assurance cash will be available to fund the obligation to the EE when needed.
Sinking Funds	Growth may be taxed annually on underlying assets.	Flexibility in investment options and funding	No assurance the funds will be available to meet the promised obligation to the EE. The underlying assets' rate of returns may fall short.
Mutual Funds	Growth may be taxed annually, depending. on underlying assets.	Flexibility in investment options and funding	No assurance the funds will be available to meet the promised obligation to the EE. The underlying assets' rate of returns may fall short. Taxes may be burdensome in later years.
Annuities	Annuity growth is taxed annually. Business, as annuity owner, falls under the "non-natural person rule."	Option to consider if the EE is uninsurable. Establishes a plan to fund the EE obligation.	No assurance the funds will be available to meet the promised obligation if EE dies early in accumulation phase.
Life Insurance	Growth in the life insurance policy is tax deferred. Access to policy values may be tax-favored to the business.	If the EE dies early in the accumulation phase, the death benefit will help to fund the promised benefits. Aggregate funding could be used for older or uninsurable employees.	No assurance the funds will be available to meet the promised obligation to the EE. The underlying assets' rate of returns may fall short.

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General Information on Underlying Assets

If there are older or uninsurable participants in the plan, and the desired asset for informal funding is life insurance, consider an aggregate funding approach. In essence, insure the younger, healthier employees with the goal to accumulate policy cash values in the life insurance to meet the overall employer-promised deferred compensation obligation.

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