2015

Non-Qualified Plans

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Successful privately held businesses face these issues:

1) Qualified retirement plans are not adequate programs for reward and retention of key personnel;
2) Plans which involve stock or equity in private companies are often perceived as being of little value to executives while adding complexity to majority owners;
3) High rates of income and capital gains tax create impediments to personal and business wealth creation.

Did you know that…
Qualified Retirement Plans often discriminate AGAINST the highly compensated?

Regulations and restrictions placed on qualified retirement plans limit the size of the benefits that can be accrued for highly-compensated employees, producing a "reverse discrimination" effect.

The following table illustrates a typical retirement income replacement percentage when including both social security and 401(k) plans:

	Starting Salary	Social Security Payments Starting at 67	Annual 401k Withdrawal Starting at 67	Combined S.S. + 401k	Future Value of Salary at 67	Income Replacement Ratio
Avery Albertson	$25,000	$17,268	$18,723	$35,991	$52,017	69.19%
Bradley Baker	$50,000	$25,080	$37,443	$62,523	$104,034	60.10%
Cindy Conrad	$100,000	$33,312	$70,190	$103,502	$208,069	49.74%
David Donaldson	$250,000	$33,312	$78,425	$111,737	$520,171	21.48%
Elaine Etherton	$500,000	$33,312	$78,425	$111,737	$1,040,343	10.74%
Frederick Fillmore III	$1,000,000	$33,312	$78,425	$111,737	$2,080,685	5.37%

Assumptions

Salary growth at 2% annually
Current age 30; retiring at age 67
Employees contribute 5% of salary to the 401(k) up to the maximum
These calculations use today's dollars and do not illustrate inflation
Current maximum 401k contribution of $18,000 is assumed until age 50; $24,000 assumed from age 50-67
The 401k balance grows at 7% annually pre-retirement and 5% thereafter
Social Security payments and 401k withdrawals are illustrated on a pre-tax basis
Social Security contributions based on salary at median age of 47
401k withdrawals are level at 6.9% of account value upon retirement which should deplete account at age 90
"Top Heavy" employee 401k contributions limited to 2.5% of IRS annual compensation limit of $265,000

What can privately held businesses do to attract and retain top talent when:

- Qualified plans discriminate against the highly compensated;
- Salary alone is often not enough; and
- Private employers lack the wider variety of long term compensation and incentive options available to publicly traded companies.

Non-Qualified Plan Solution

There is a solution; however, to the inadequacy of qualified retirement plan benefits… one that can also help a corporation attract and retain key executives as well as meeting other company goals.

Key employees can be rewarded for increasing the value of the business upon retirement or sale, while additional company objectives are met through phantom stock/equity plans and equity appreciation rights.

A non-qualified plan is an arrangement between a corporation and select key executives in which the corporation agrees to defer a portion of the executive's salary in exchange for the promise of future benefits. By deferring current compensation, the participating executives also defer income taxes until benefits are actually received in the future.

The primary purpose of the plan is to provide a retirement benefit to those key executives who will remain with the corporation until retirement. Life insurance/survivorship can also be provided for in a non-qualified plan.

These custom tailored benefits are over and above those provided to all employees by a qualified retirement plan or any other employee benefit plan. This fosters and maintains the loyalty of a corporation's most highly valued key executives, while providing key benefits to these executives both prior to, and after, retirement.

The right non-qualified plan can add significant value to the company where expertly designed.