

EXECUTIVE BENEFITS INSIDER



NONQUALIFIED DEFERRED COMPENSATION PLANS

Qualified plans have contribution caps and other restrictions that limit pre-tax savings opportunities for highly compensated employees.

An NQDCP helps bridge the retirement income gap and is key to a company's ability to successfully recruit, retain, and reward top talent.

INTRODUCTION

A nonqualified deferred compensation plan (NQDCP) is a company-sponsored benefit program that allows employees to defer pre-tax income until retirement or another specified future date or event.

Unlike a 401(k) or other qualified plan, NQDCPs are generally only offered to a select group of management and highly compensated employees. As they are exempt from most ERISA provisions and have no contribution limits, NQDCPs are a more flexible and powerful tool for engaging top talent, rewarding peak performance, and achieving company goals.

Eligible NQDCP participants elect to defer various types and amounts of compensation as allowed by the plan sponsor. Companies can make matching or discretionary contributions as well, with the option to have benefits subject to vesting schedules or contingent on the achievement of specific performance goals.

All contributions and their investment returns are tax-deferred, which effectively increases the earning power of the benefit.

In addition to serving as a retirement savings tool, NQDCPs offer the design flexibility to help participants meet short-term financial goals. Penalty-free distributions can be scheduled while employed to help fund a child's tuition, buy a home, or make other significant purchases.

While many crediting rate options are available, most NQDCPs offer a wide selection of deemed investments in which to allocate deferrals. The funds themselves are only used to track returns that determine the increase or decrease in the plan's balance; participants have no ownership interest in the investments themselves.

As with other nonqualified plans, NQDCPs are unsecured promises of the employer to make future distribution payments as they come due, and they would be subject to the claims of creditors in the event of company bankruptcy or insolvency. To enhance benefit security for participants, companies may choose to informally fund the NQDCP by setting aside assets in a rabbi trust to cover their plan obligations.

NQDCP BENEFITS

FOR THE EMPLOYER

Flexible plan design options to align with company objectives

- Able to set specific eligibility criteria
- May provide a company match or discretionary contribution to boost participation and loyalty
- Can incorporate custom vesting schedules to encourage retention

Powerful tool to recruit, retain, reward

- An elite benefit that sets a company apart from its competitors
- Enables employers to provide valuable incentives and awards without current taxation to the individual
- Rewards and encourages leadership's long-term stability and commitment

Cost-effective

- Offers a meaningful financial benefit without increasing current payroll
- Requires minimal reporting and filing and is typically less costly to implement and administer than qualified plans
- Can be informally funded to help recover benefit costs
- Benefits are deductible to the company when paid

FOR THE EMPLOYEE

Address the retirement savings gap

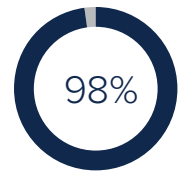
- Helps key employees contribute more pre-tax income to make up for limitations and discrimination testing restrictions imposed on qualified plans
- Offers a deferral opportunity commensurate with compensation that enables high-earning employees to achieve their financial goals

Enjoy a tax-favored benefit

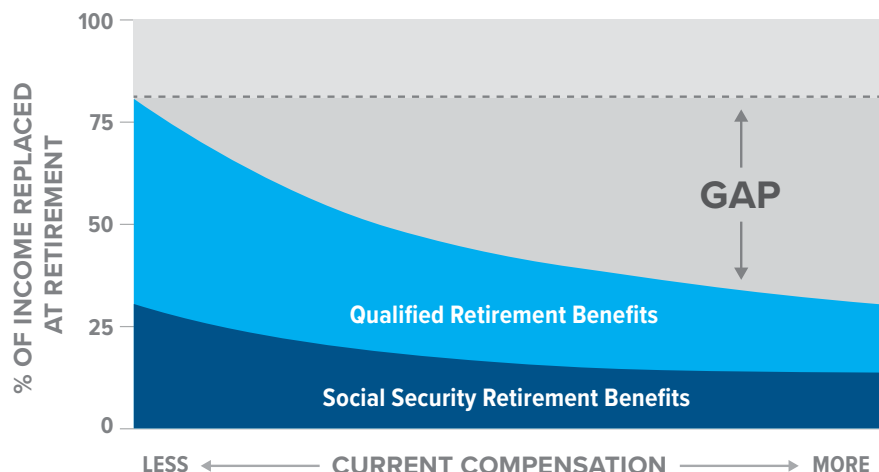
- Contributions and earnings are tax-deferred
- Reduces current taxable income, providing more control over income tax liability
- Benefits are subject to ordinary income tax only when distributed

98% of companies – from smaller firms in emerging growth mode to multibillion-dollar businesses – utilize NQDCPs to help select employees plan for retirement and other personal financial goals.

2020 Newport/PLANSponsor
Executive Benefit Survey



Retirement Savings Gap





DESIGN

When appropriately structured, an NQDCP can help address the income replacement inadequacies of qualified plans for highly compensated leaders while positively impacting employee productivity and motivation to produce tangible results for the company.

A wide array of features can be customized to be especially advantageous for both the company looking to optimize its return on talent investment and the executive securing a valuable financial planning benefit in exchange for their hard work and dedication:

- Eligibility
 - Title
 - Job grade
 - Base salary
 - Total compensation
- Contribution types
 - Employee
 - Salary
 - Bonus
 - Commissions
 - Short- or long-term incentives
 - Employer
 - Company match
 - Tied to company performance
- Crediting rates
 - Fixed
 - Variable (tied to underlying index)
 - Company stock
 - Market-based investments
- Vesting (immediate, graded, cliff)
- Benefit-triggering events
 - Scheduled in-service distribution
 - Retirement
 - Separation from service
 - Death
 - Disability
 - Change in control/management

An NQDCP is a powerful tool for elevating a company's ability to:

- Attract
- Motivate
- Retain
- Reward
- Replace income

SUMMARY

A competitively designed NQDCP satisfies an organization's recruitment, reward, and retention objectives while serving as the primary retirement savings benefit for highly compensated employees. It is an important consideration for any plan sponsor and can be the deciding factor for whether or not a valued employee pursues other career opportunities.

A company ready to implement a nonqualified deferred compensation plan will require an executive benefit specialist with expert services and capabilities and a depth of knowledge in the rules and regulations governing compliant design and operation.

To that end, accurate record keeping is crucial. The systems used in benefits administration must be flexible to accommodate unique plan provisions and election choices for deferral amounts, distribution events, and investment choices.

The plan must also be communicated in an easy-to-understand way that facilitates well-informed decision-making on the part of the participant and follows through with a user-friendly online enrollment experience.

A plan sponsor would be well advised to work with a skilled partner that has expertise in deferred compensation plan design, implementation, communication, education, administration, accounting, reporting, and informal funding to help the plan achieve its stated objectives.

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