

MERCER

Human Resource Consulting



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Executive Retirement Benefits





Deferred Compensation Basics

Terminology 101

What is it?

Names

Excess Plan

Restores benefit limit

- **Deferred compensation**
- “True” excess plan
- 415 excess plan

Restoration Plan

Restores all limits

- **Deferred compensation**
- Excess plan
- SERP

SERP

Provides benefits in excess of the qualified pension formula

- **Deferred compensation**
- Executive retirement plan

Voluntary Deferred Compensation

Allows deferral of pay in excess of 401(k) limits

- **Deferred compensation**
- 401(k) excess/mirror



Hidden Value and Optics

Cost of Voluntary Deferred Compensation

There is a cost to providing deferred compensation plans to executives.

Participant defers \$1,000,000 for one year with a 6% return. Company's after-tax cost of funds is 3.6%.

Company cost

(\$1,060,000)	Pre-tax payment (deferral & return)
<u>424,000</u>	Company tax savings at 40%
(\$636,000)	<i>After-tax</i> cost to company

Company assets

\$1,000,000	Deferral
<u>(400,000)</u>	Foregone tax deduction on current compensation
600,000	<i>After-tax</i> cash to invest
<u>21,600</u>	<i>After-tax</i> investment earnings at 3.6%
621,600	Accumulated asset at end of year

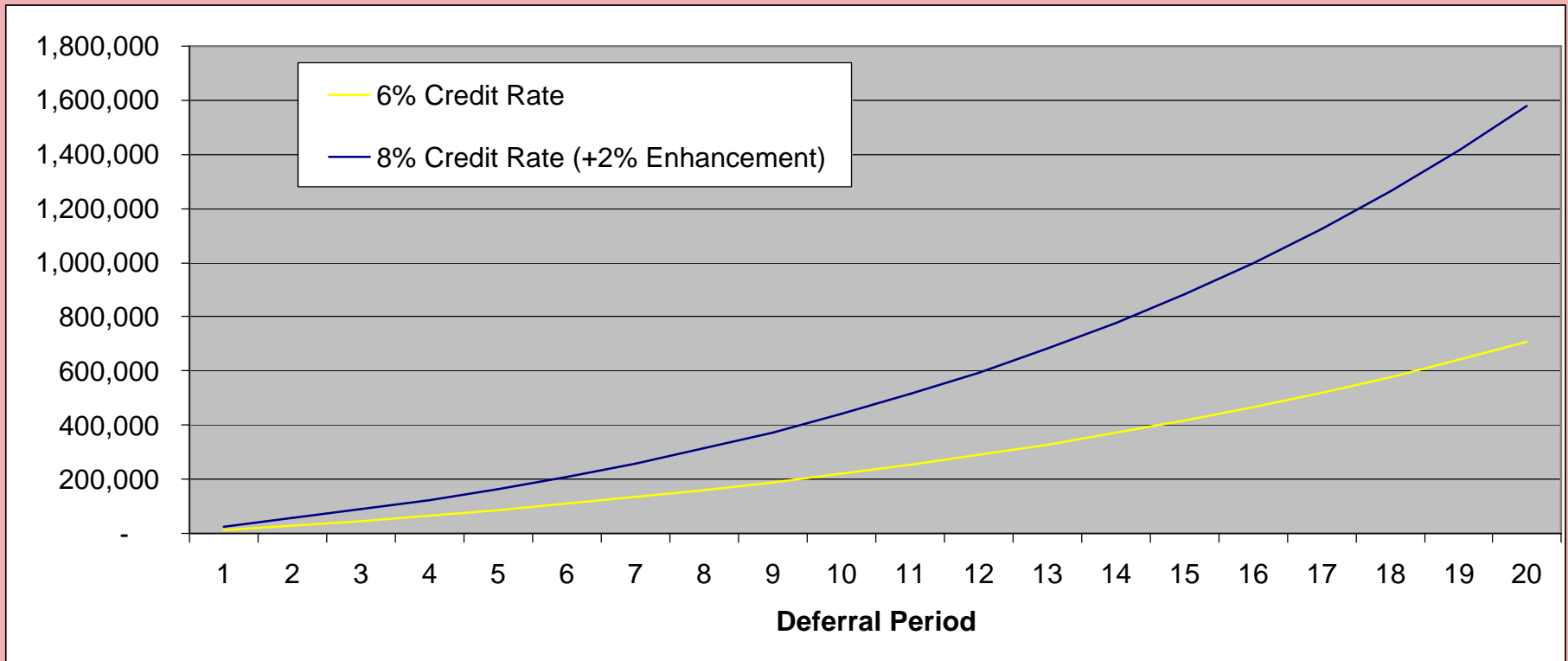
<i>After-tax</i> cost	(636,000)
Asset	<u>621,600</u>
Company's net cost =	(14,400)



Hidden Value and Optics

Cost of Voluntary Deferred Compensation

Participant makes one-time deferral of \$1,000,000. Company's after-tax cost of funds is 3.6%. Net Deferred Comp cost is shown as the accumulated after-tax asset less after-tax cost of deferred comp





Hidden Value and Optics

Value of “Plain Vanilla” SERP

CEO – Current Age 57

Base Pay	▪ \$1 million (pensionable)
Annual Bonus	▪ \$1 million (pensionable)
LTI	▪ \$3 million (not pensionable)
Service	▪ 25 years
Normal Retirement Age	▪ 62
Early Retirement Age	▪ 57 (75% early retirement factor)
Retirement Benefit	▪ 2% x years of service x final average pay (offset by qualified plan)
Qualified Plan	▪ \$75,000
SERP	▪ \$675,000
Current Lump Sum Value	▪ \$9.5 million



Hidden Value and Optics

Lump Sum Value of SERP at Age 57

