Advantages of Non-Qualified Deferred Compensation Plans

Non-qualified deferred compensation ("NQDC") arrangements are one of the most common and attractive plans for businesses seeking to reward and retain their top performers because they are flexible and customizable to the executive. These plans can be designed in a variety of ways. Regardless of the type of plan selected, non-qualified deferred compensation arrangements offer advantages to the business sponsoring the plan as well as those who are selected to participate.

NQDC plans come in two basic forms. The first is often referred to as a "Supplemental Executive Retirement Plan" or SERP. As the name implies, a SERP is an agreement where the business promises to supplement the executive's income at retirement.

The second form of NQDC plan is commonly referred to as a "Salary Reduction/Deferral Plan." As the name implies, the executive defers his or her own salary to fund the plan. The salary amounts deferred are not currently taxable to the executive, but will be at retirement and then deductible by the business.

Advantages to the Sponsoring Business

- Unlike qualified retirement plans where there are rigid coverage and participation rules, the business owner has the flexibility to decide who, among its executives and highly compensated employees, are allowed to participate in a non-qualified deferred compensation plan.
- Deferred compensation plans provide a business with an excellent tool to recruit, retain and reward employees who are vital to its business.
- Salary reduction plans coordinate with existing qualified plans and can be individually tailored to complement other benefit programs.
- There is significant flexibility over the design and structure of benefit payments.
- The company retains significant flexibility regarding funding options.
- Benefits are tax deductible by the business when paid.
- Where corporate-owned life insurance is used to informally fund the plan:
  - Tax-deferred accumulation and high early cash value can offset the impact to earnings charges;
  - Policy cash values are subject to business control and can be used for general business purposes;
  - Death benefits are generally received income-tax free*;
  - Any excess insurance proceeds left over after all benefit obligations are satisfied can be retained by the business; and
  - With the proper plan design, plan expenses can be fully recovered by the business from the insurance death benefit proceeds.
- A vesting schedule can ensure that employees who leave the business receive no benefits, and delayed vesting schedules can encourage participants to stay with the business.
- The plan can be designed with a "cost of money" factor so the business can actually profit from the plan.

Executive Benefits

- Compared with qualified retirement plans, there is minimal government reporting requirements.

- The plan can help to align a participant's job performance with long-term corporate goals, and helps to maintain corporate continuity and stability within the business's senior management team.

Advantages to the Participant

For the participant, non-qualified deferred compensation plans offer a variety of advantages:

- Wage deferrals into salary reduction deferred compensation plans have the effect of lowering the amount that would be reported as "gross income" on line 1 of a participant's Form 1040 income tax return. Thus, salary reduction plans can be a very attractive alternative for business owners and executives who find themselves suddenly bumped into a higher bracket, or when changing tax laws increase the income tax rates.

- There is an opportunity for tax-leverage at retirement if the executive is in a lower tax bracket when the benefits are received.

- The benefits of tax-deferred growth can result in increased retirement income, and a pre-retirement death benefit can be provided for designated beneficiaries.

- With the proper planning, a participant's retirement income shortfall can be reduced or eliminated.

- Plans can be individually tailored to fit the needs and production goals of specific participants, and employers can make discretionary contributions to reward individual or team performance.
- Unlike qualified retirement plans, there are no deferral or contribution limits with non-qualified deferred compensation plans.

- Benefit payments can be flexibly designed to meet the needs of participants at any point in their lives (e.g., separation from service, death, disability, change of control or unforeseeable emergency).

- Informal funding with corporate-owned life insurance (COLI) allows participants to allocate account balances in a manner that is similar to 401(k) plans.

* Subject to alternative minimum taxes.

For further information on NQDC plans, please ask your Guardian Financial Representative for our informational bulletin entitled "*Non-Qualified Deferred Compensation*". Please consult with your Guardian Financial Representative if you have any questions concerning this document.

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Guardian Financial Representatives may call the Business Resource Center for Advanced Markets, at 1.800.871.7780, Option 3, for additional information.