

Bonus Plans Built for Key Executives



Limits and restrictions on the amount that employees and employers can contribute toward qualified benefit plans leave many **highly compensated executives with a gap which means they'll have insufficient assets to maintain their standard of living when they retire.** Many executives also fail to adequately protect their loved ones through the use of life insurance. **An executive bonus plan that's assembled using life insurance can help put key employees in a better position.**

A life insurance bonus plan is a simple, straightforward method of rewarding key executives over and above traditional salary, bonus and other benefits such as group life insurance. The plan sponsor enters into an agreement with the executive to pay the premium for a life insurance policy owned by the executive. The premium payment is considered income for the executive, taxed at normal income and other payroll tax rates. The plan is considered additional compensation paid to the executive therefore the premium payments are tax deductible to the plan sponsor. **Many varieties of life insurance contracts can be used.** The type of insurance contract ultimately selected will depend on the goals of the executives, the employer or both. Newer life insurance policies may include long term care benefits. In some cases streamlined underwriting is available; however, proof of good health is often required.

Life Insurance Bonus Plans

Plan Advantages for both Employers and Employees

- Provides permanent, portable life insurance coverage to a group of key management talent
- Helps executives build an asset that can supplement retirement income or be used for other financial goals
- Creates a flexible benefit plan that can be customized to the needs of the organization
- Helps attract and retain a competent, talented team of executives
- Reduces discrimination against highly compensated executives that's inherent in qualified plans and government benefits

How Executives Benefit from a Life Insurance Bonus Plan

Highly compensated executives can often benefit from having some permanent life insurance coverage, including:

- An asset that generates income-tax-free cash surrender value and death benefits
- A benefit that is not subject to company creditors
- Income replacement during retirement
- Estate planning and wealth transfer
- Philanthropic wishes
- Payment for long-term care and nursing home stays

CONSIDERATIONS

Taxation Laws

The Tax Cut and Jobs Act of 2017 (TCJA) did not change the tax treatment of such plans to the employer or the employee. Compensation payments remain tax deductible by the employer at the employer's corporate tax rate. Employees will report the premium bonus as taxable income. Under TCJA, the maximum personal federal tax rate was reduced from 39.6% to 37%.

Under longstanding tax law, permanent life insurance policies generate tax-deferred cash value growth and tax free death benefits. Additionally, if properly structured, tax free cash can be extracted from the policy's cash value during the employee's lifetime.

Some employees may experience an increase in their effective combined federal and state personal tax rate, which will increase the after-tax cost of acquiring the policy. If other nontaxable or deferred income alternatives are not a viable solution, they may want to consider redeploying a portion of their other personal assets that generate taxable income towards the purchase of the policy.

Executive Bonus Plans — And a Whole Lot More

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