

Great Idea...Lousy Name

Contributed by Ken Morris
Sunday, 04 February 2007

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{bot_wrgoogle}Non-qualified deferred compensation (NQDC) is a powerful retirement planning tool, particularly for owners of closely held corporations (for purposes of this article, I'm only going to deal with "C" corporations). NQDC plans are not qualified for two things; some of the income tax benefits afforded qualified retirement plans and the employee protection provisions of the Employee Retirement Income Security Act (ERISA). What NQDC plans do offer is flexibility. Great gobs of flexibility. Flexibility is something qualified plans, after decades of Congressional tinkering, lack. The loss of some tax benefits and ERISA provisions may seem a very small price to pay when you consider the many benefits of NQDC plans.

A NQDC plan is a written contract between the corporate employer and the employee. The contract covers employment and compensation that will be provided in the future. The NQDC agreement gives to the employee the employer's unsecured promise to pay some future benefit in exchange for services today. The promised future benefit may be in one of three general forms. Some NQDC plans resemble defined benefit plans in that they promise to pay the employee a fixed dollar amount or fixed percentage of salary for a period of time after retirement. Another type of NQDC resembles a defined contribution plan. A fixed amount goes into the employee's "account" each year, sometimes through voluntary salary deferrals, and the employee is entitled to the balance of the account at retirement. The final type of NQDC plan provides a death benefit to the employee's designated beneficiary.

The key benefit with NQDC is flexibility. With NQDC plans, the employer can discriminate freely. The employer can pick and choose from among employees, including him/herself, and benefit only a select few. The employer can treat those chosen differently. The benefit promised need not follow any of the rules associated with qualified plans (e.g. the \$44,000 for 2006) annual limit on contributions to defined contribution plans). The vesting schedule can be whatever the employer would like it to be. By using life insurance products, the tax deferral feature of qualified plans can be simulated. Properly drafted, NQDC plans do not result in taxable income to the employee until payments are made.

To obtain this flexibility both the employer and employee must give something up. The employer loses the up-front tax deduction for the contribution to the plan. However, the employer will get a deduction when benefits are paid. The employee loses the security provided under ERISA. However, frequently the

employee involved is the business owner which mitigates this concern. Also there are techniques available to provide the non-owner employee with a measure of security. By the way, the marketing guys have gotten hold of NQDC plans, so you'll see them called Supplemental Executive Retirement Plans or Excess Benefit Plans among other names.

“Can somebody please help me watch, manage, invest or oversee my 401k” is the question Mr. Morris hears most often that causes him the most concern. Fearing the American worker is being left in the dark, Mr. Morris, a fee based Investment Advisor Representative, based in Central Ohio, with Raymond James Financial Services, Inc., helps (<http://www.investmy401k.com>) 401k participants get the most out of their retirement plan. Let Ken Morris be your 401k Watchdog, with InvestMy401k.