DEFINED CONTRIBUTION PLAN

IRC SECTION 409A COMPLIANCE

- Protects a company from financial costs related to the loss of a key employee
- Informally funds the cost of employee benefits
- Policy cash value is available to fund company obligations
- Can earn a competitive after-tax yield compared to other investments
- Can be retained after an insured employee leaves the company in order to cover the liabilities the company has to other employees
- Can favorably impact a company's financial performance when it increases net after-tax income
- No cost to the employee

KEEP IN MIND

- Premiums are NOT tax-deductible
- Policies can be surrendered for cash value at any time (early surrender penalties may apply)
- Coverage can be transferred to another carrier or insured as company needs change
- Employee consent (for IRC 101(j) purposes) must occur PRIOR to the issuance of coverage
- The company (or Trust) must be the owner and beneficiary of the policies
- A company purchasing insurance on employees must demonstrate an insurable interest in those employees

WHAT IS A DEFINED CONTRIBUTION PLAN?

A defined contribution plan is a type of nonqualified plan sponsored by an employer that promises certain key executives or independent contractors a tax-deferred benefit based on the value of an account at the time of payout. The design of the plan and the accumulation of the participant's account balance is derived from three major elements:

(1) **Source of Plan Contributions**. Contributions can be derived from employee deferral of compensation (e.g., base salary, bonus, commission) and/or company contributions (e.g., matching or discretionary).

(2) **Account Growth**. Various methods are used in determining growth on the plan contributions. The most common methods include a plan directed interest rate, participant directed "deemed" investments, or benchmarking the account value to a corporate owned asset such as a brokerage account or corporate owned life insurance policy.

(3) **Account Distributions**. Plans can be designed to payout upon the earliest of separation from service, death, disability, change in control, a specified date or age, and/or an unforeseeable emergency.

NONQUALIFIED PLAN FINANCING

Nonqualified plans, by nature, cannot be formally funded (i.e., companies cannot set money outside the scope of general creditors for plan purposes). Most prudent companies, however, set aside (or "earmark") certain corporate assets to offset liabilities generated as a result of plan benefits. The most common methods for plan financing are corporate owned life insurance or corporate owned mutual funds. Plans are not required to have any assets earmarked for the plan as some companies fund out of current cash flows. If a corporate asset is used, it is typical that the participant's account growth is based on a similar method of growth as the corporate asset.