VisionLink

"Driving Productivity and Profits Through Deferred Compensation"

The "Learn & Earn" Series™

Building Unified Financial Visions

THE VISIONLINK ADVISORY GROUP

July 21, 2009

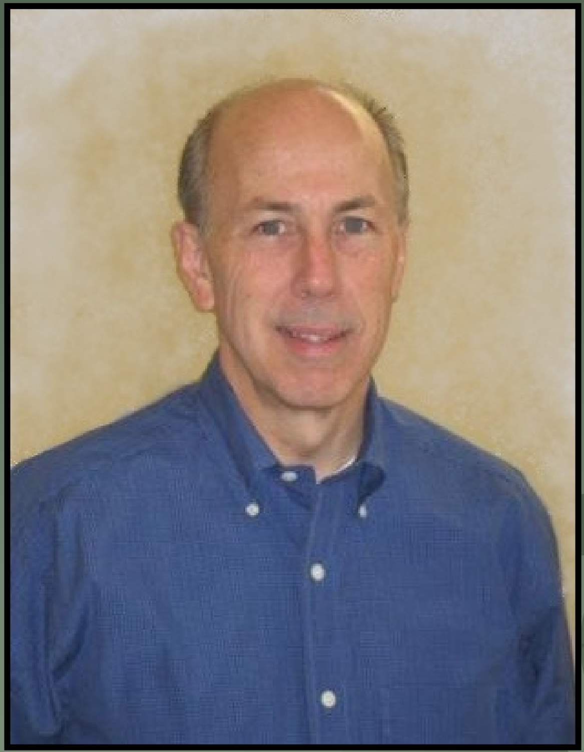
Today's presenter:

Ken Gibson

Senior Vice-President

949-265-5703

kgibson@vladvisors.com



THE VISIONLINK ADVISORY GROUP

Building Unified Financial Visions

Course Credit

Per State Requirements:

To receive CPE credit for today's course, you must respond to at least 75% of the monitoring events – given in the form of polls.

Each person taking the course must respond to the monitoring events from their own computer. You may not share a computer when taking the course

Next CPE Course:

“How Does My Client Get Sustained Performance From his Key People?”

To be held on:

Tuesday, August 18th, 2009

Building Unified Financial Visions

We're happy to provide a copy of today's slides, course syllabus/summary, and a CD of the presentation. Information will be provided at the close of the presentation about requesting these.

For questions during today's presentation:

Use the question panel
to the right of your screen

Building Unified
Financial Visions

Key Concepts

- Any compensation program should improve key performance indicators
- There is a difference between most traditional deferred compensation and an incentive approach
- Deferred compensation should be measured as any other rewards strategy
- Deferral plans (and SERPs) are uniquely positioned to meet multiple rewards targets

Course Objectives

- Chart the evolution of deferred comp—what got us here
- Understand how and why deferred compensation works
- Define the role of 409 A and how it has changed the deferred comp landscape
- Understand the strategic use of deferred compensation as an incentive plan
- Review the plan designs that are most effective at driving key results

Building Unified Financial Visions

Poll #1

QUICKPOLL

I would rate my exposure to, experience with and/or understanding of deferred compensation plans as follows:

Please select one:

- No experience
- Some experience
- High experience
- Expert

QUICKPOLL

I would rate my exposure to, experience with and/or understanding of deferred compensation plans as follows:

Poll Results (single answer required):

No experience	0%
Some experience	50%
High experience	50%
Expert	0%

The Premise

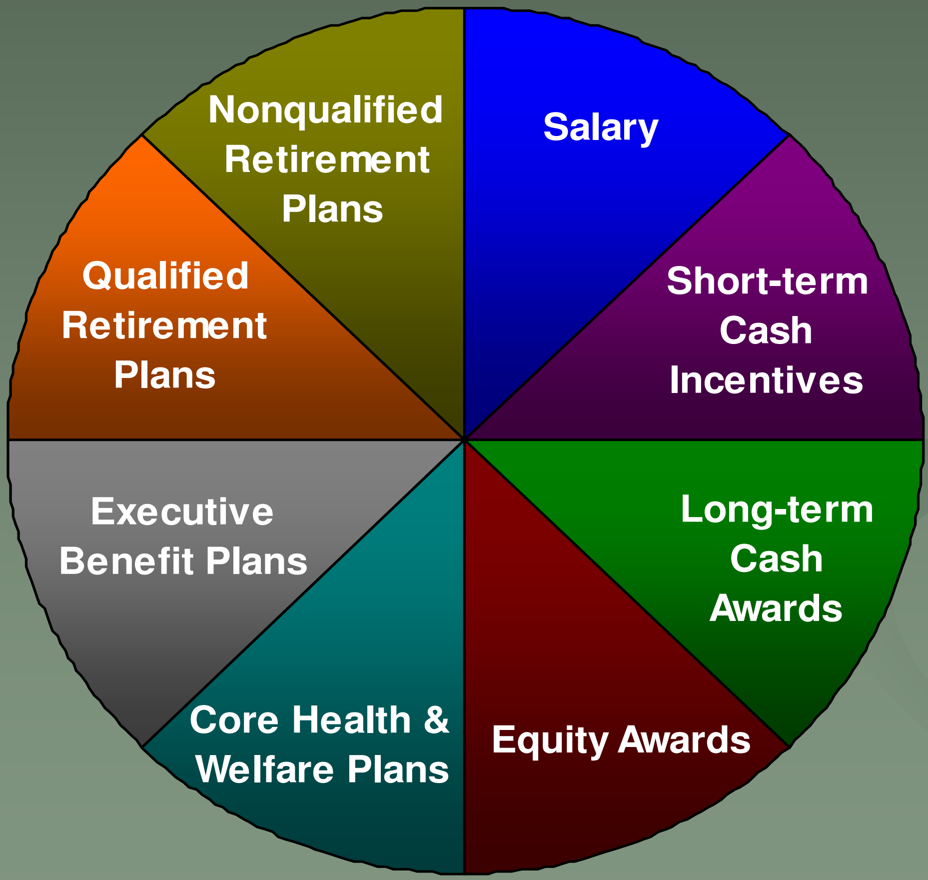
Three Things All Rewards Plans Should Help Accomplish

- Win the talent wars—help attract and retain great people
- Improve employee productivity—focused, engaged and executing consistently
- Increase (good) profits—and improve shareholder value

Which plans accomplish this?

1. Win the Talent Wars

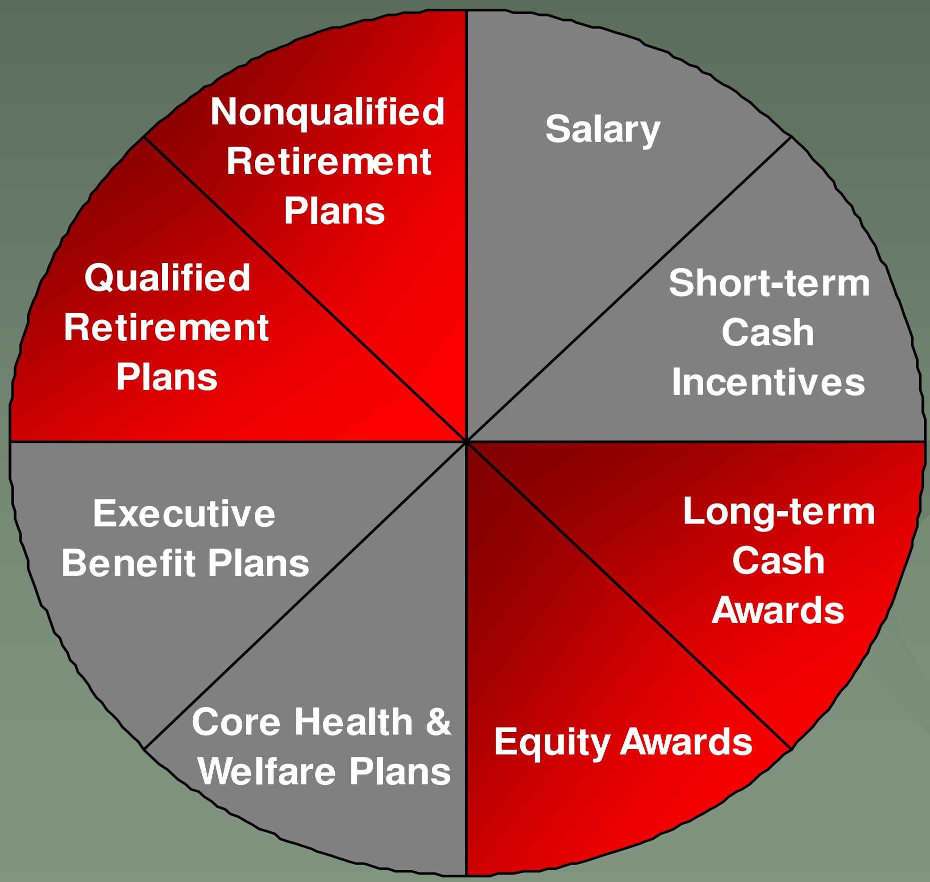
(Attract and retain great people)



Building Unified Financial Visions

1. Win the Talent Wars

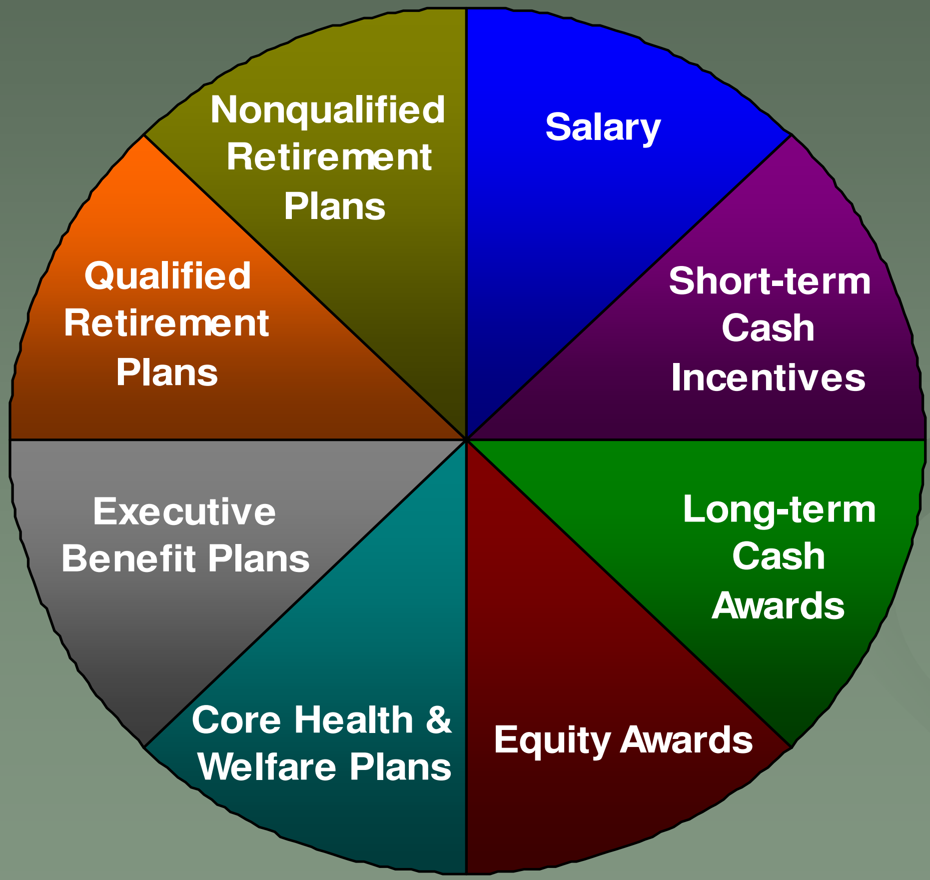
(Attract and retain great people)



Building Unified Financial Visions

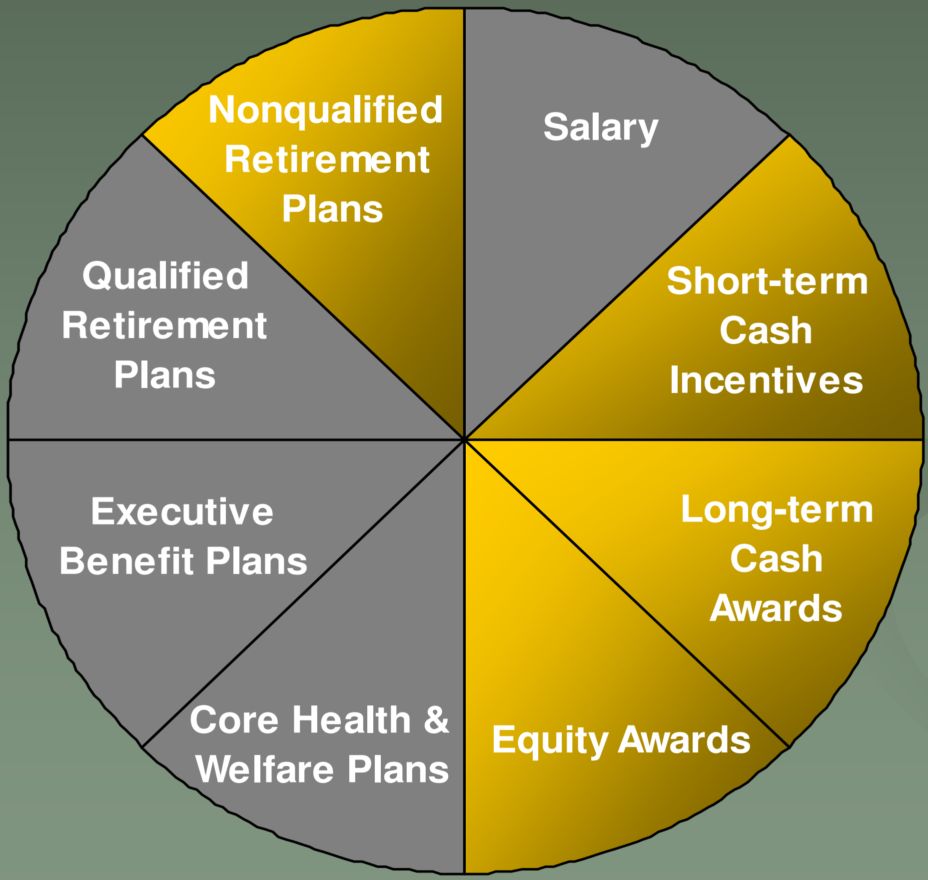
2. Improve Employee Productivity

(Point people to the "right" results)



2. Improve Employee Productivity

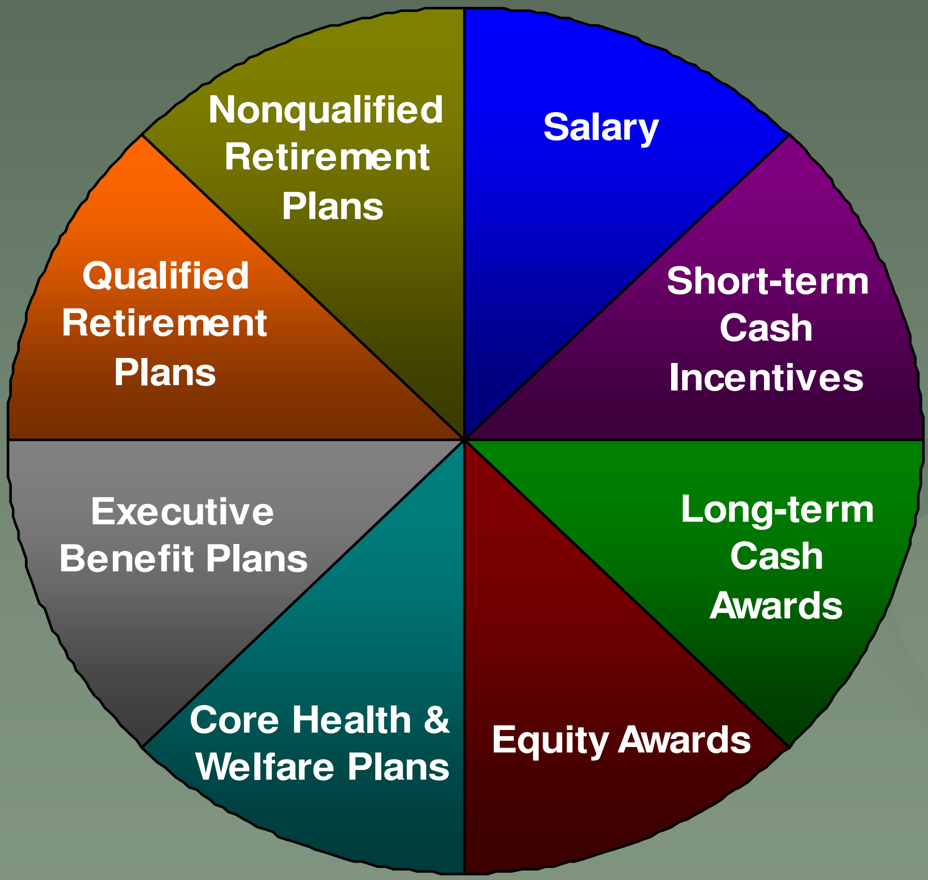
(Point people to the “right” behavior)



Building Unified Financial Visions

3. Increase Profits

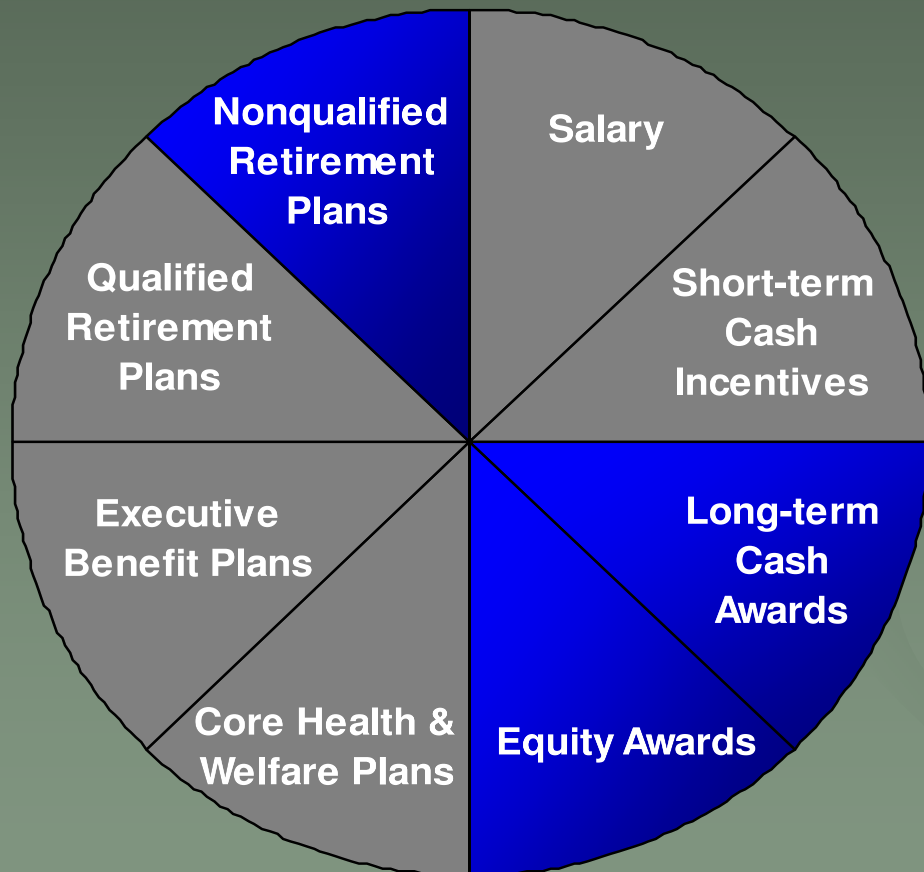
(Produce a measurable return on investment)



Building Unified Financial Visions

3. Increase Profits

(Produce a measurable return on investment)

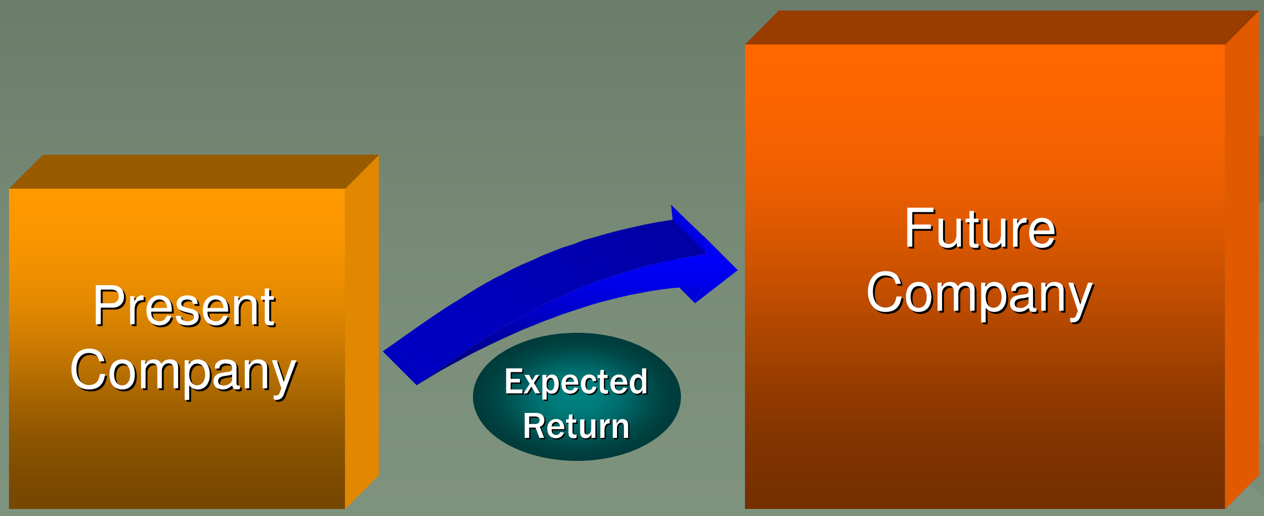


Building Unified Financial Visions

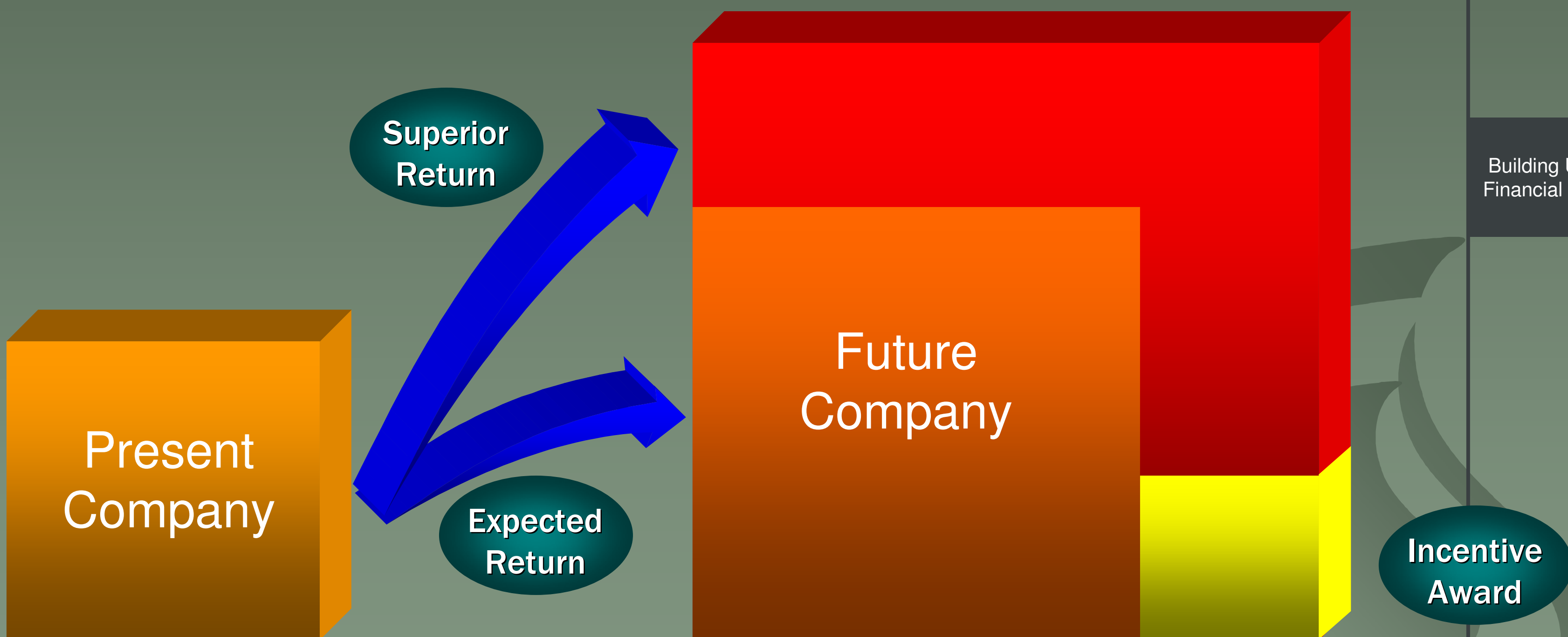
Increasing productivity and profitability

- Identify core drivers of business growth (key performance indicators)
- Establish the value to be earned by shareholders if the drivers are reached
- Determine how much value to be shared with employees
- *The easy part*—determine how to get the employees to achieve the results

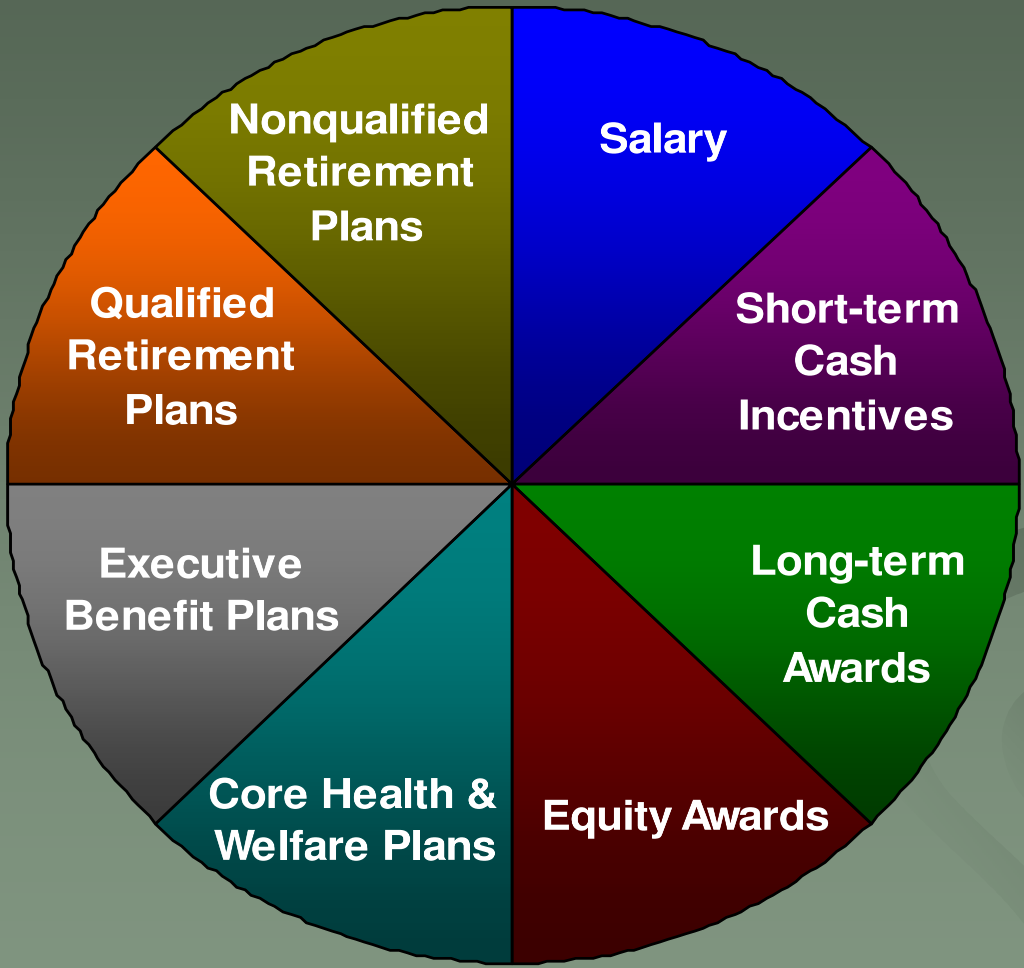
Creating value added results

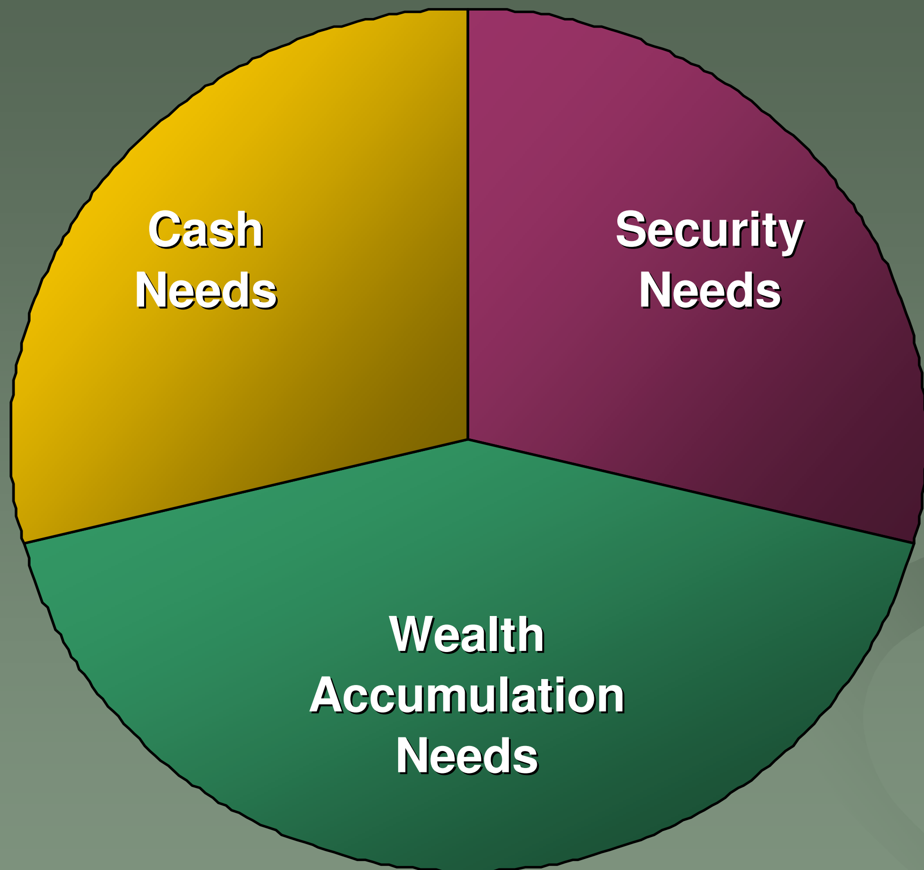


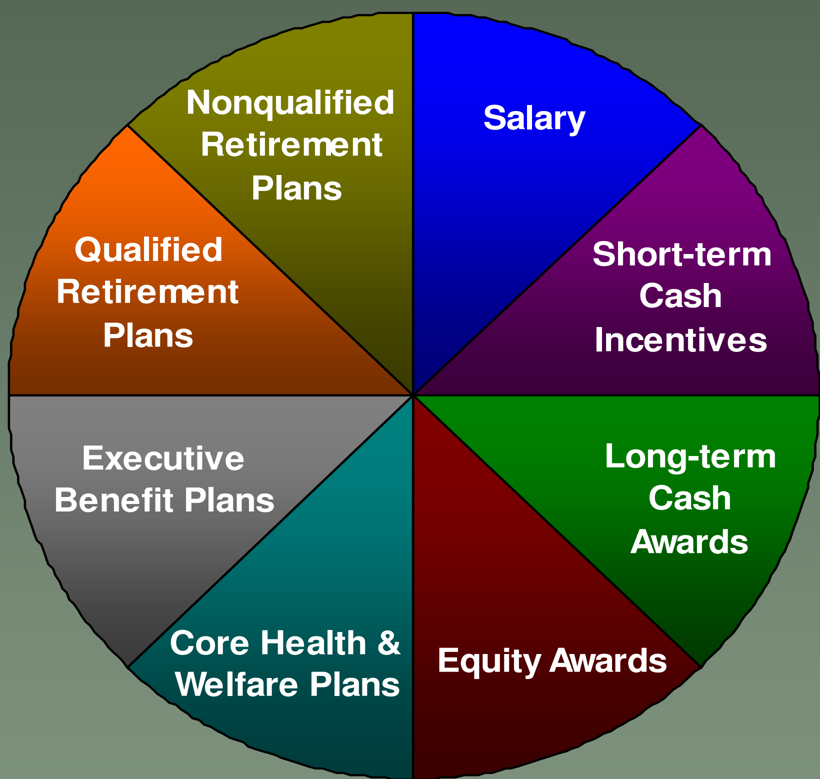
Creating value added results

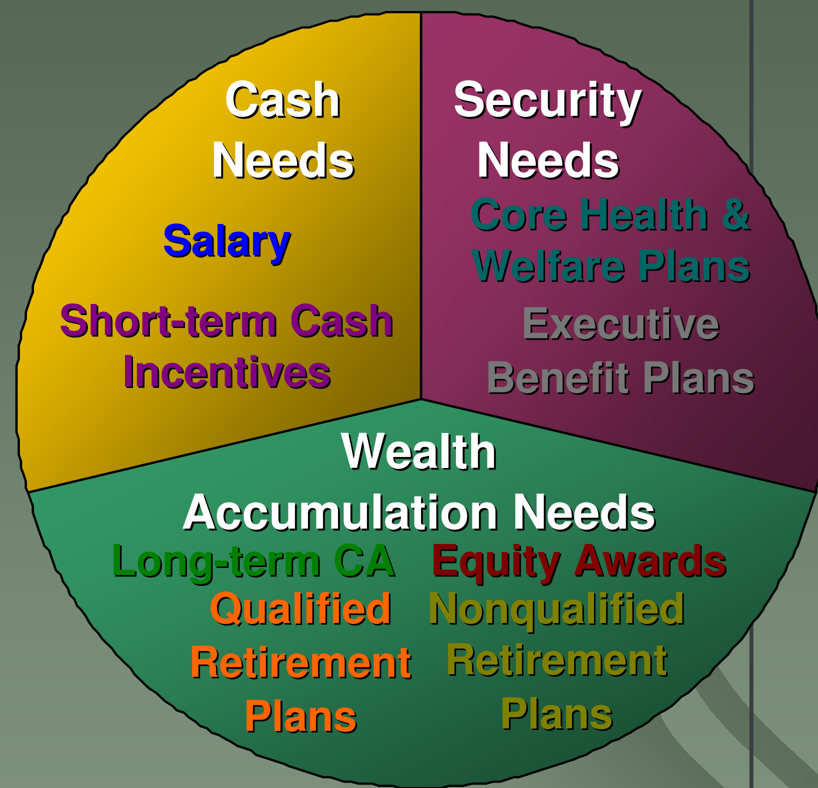


Building Unified Financial Visions


Salary
Short-term Cash Incentives
Long-term Cash Awards
Equity Awards
Core Health & Welfare Plans
Executive Benefit Plans
Qualified Retirement Plans
Nonqualified Retirement Plans


Cash
Needs
Security
Needs
Wealth
Accumulation
Needs



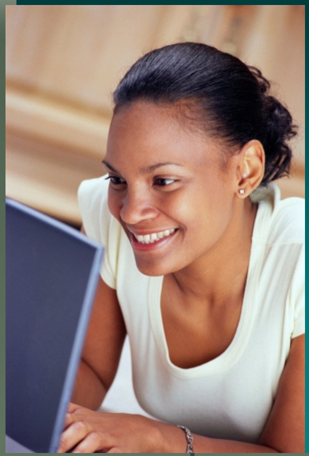


ng Unified
ial Visions

Deferred Compensation Plans—A Very Brief History

- 1950s—simple voluntary deferral plans
- 1970s—employer paid SERPs to supplement defined benefit pensions
- 1980s—trend back to deferral plans in line with movement to 401(k) plans
- 2000s—trend towards "hybrid" plans that focus on employee rewards, strategic alignment and retention
- Overall—strong movement from Fortune 500 down to small businesses
- 2004-2009—codification via IRC section 409A

What's made Deferred Comp so popular?



- Avoidance of current taxation on employee deferrals and company contributions/credits
- Legal means of offsetting regulatory limits of qualified plans
- Flexible features
- Strong retention characteristics (SERP)
- Barely disclosed in SEC reporting (previously)

Building Unified Financial Visions

What have been the problems?

- IRS interest in taxing participants under constructive receipt and economic benefit doctrines
- Vague lines of interpretation regarding plan security
- Aggressive plans pushing the limits (haircut provisions, last minute changes, distributions prior to insolvency)
- Delayed tax deduction (may be acute in smaller companies)

What's happened recently?

- Section 409A defined and clarified:
  - How deferrals may avoid inclusion in income of participants
  - Terms and limitations on extending or reducing payment periods
  - Conditions under which plans may be terminated
  - Definitions of hardship and disability
  - Conditions under which distributions may be accelerated

What's happened recently?

- Section 409A requires document amendment (in most cases)
  - The IRS has thrice extended compliance deadlines (pending final regulations)
  - Current deadline—12/31/08
  - Nonetheless, plans must operate in good faith with the primary characteristics of the legislation

So where are we now?

- Commonplace
- Commoditized
- Somewhat more complicated, but greater certainty
- Multiple vendors offering “turnkey” programs

Building Unified Financial Visions

Problem

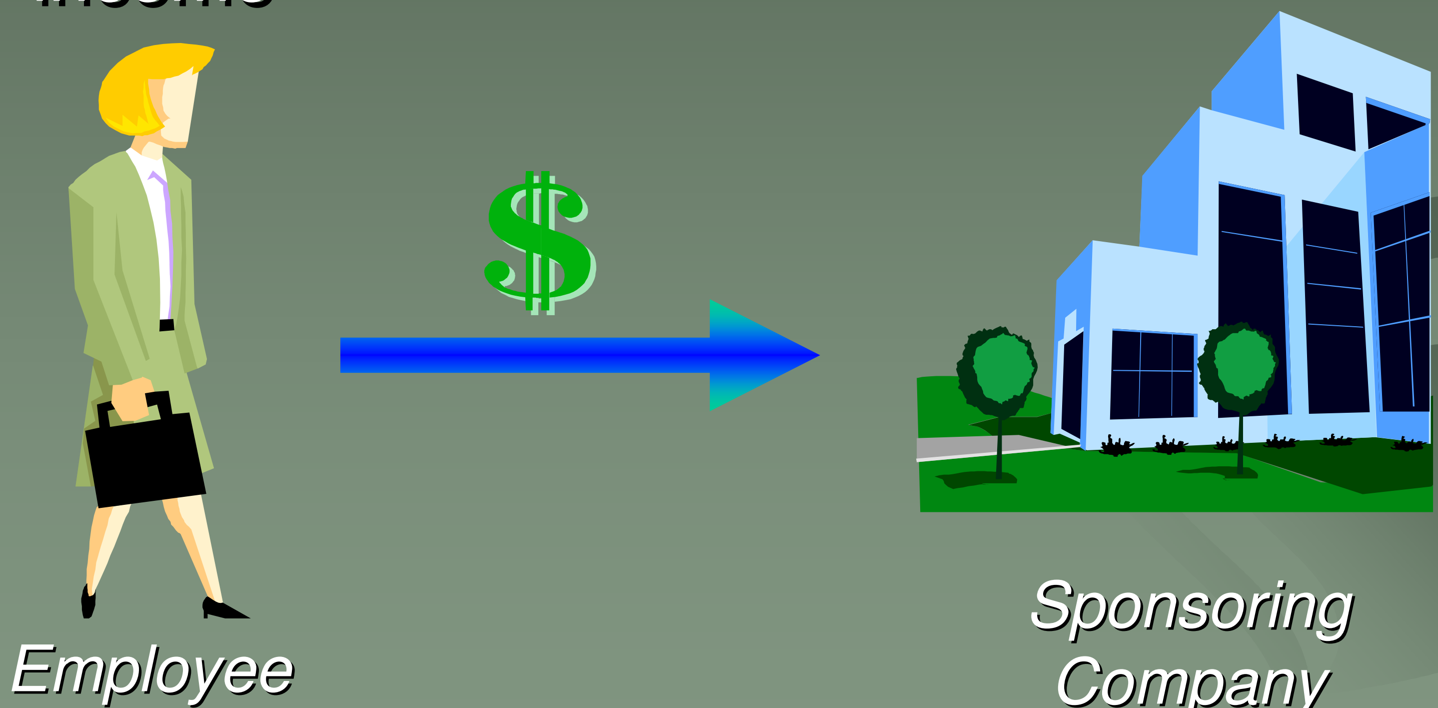
None of the turnkey or traditional plans in the market drive productivity and profitability!

Example 1:
Traditional deferral plan

- “Convenience plan”
- Voluntary deferral in excess of allowable 401(k) contribution
- Possibly a slight employer match

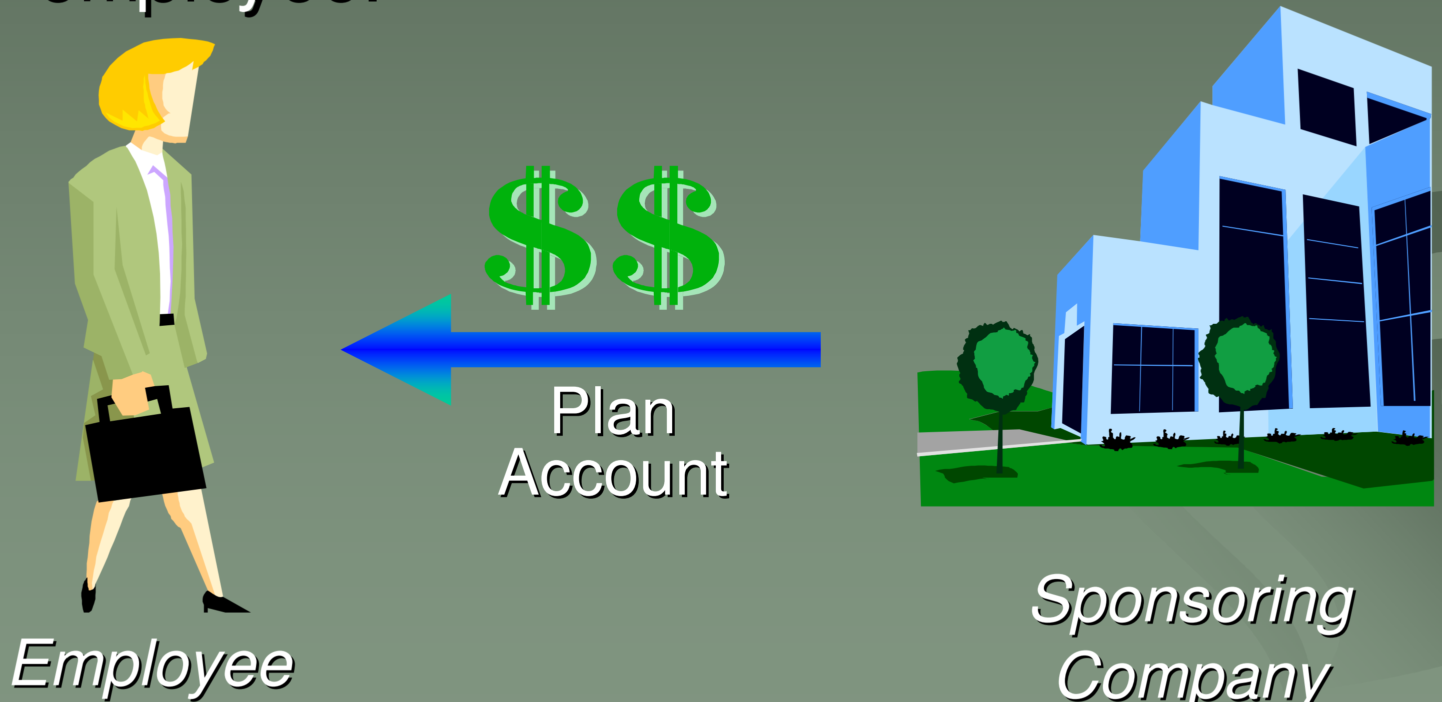
Step One

- Employee enters into agreement (year to year) to defer a percentage of income



Step Two

- When the employee leaves, the Company pays the amount owed to the employee.



Traditional deferral plan

- Where is the retention value?
  - Very little
- Where is the focus on improving productivity?
  - None
- How does the plan increase profits?
  - It doesn't

Building Unified Financial Visions

Example 2: Traditional SERP

- Supplemental Executive Retirement Plan
- Like a defined benefit pension but for a small group of executives
- A pension benefit is “defined” at a given age (e.g., 65)
- The benefit is expressed as a percentage of final salary or total compensation (e.g., 50% for 15 years)

Building Unified Financial Visions

Traditional SERP

- Where is the retention value?
  - Some
- Where is the focus on improving productivity?
  - None
- How does the plan increase profits?
  - It doesn't

Building Unified Financial Visions

Traditional SERP vs. Deferral Plan

- Typically no employee contribution to a SERP
- SERP is "age and salary" valued
- SERP expense is accrued over working period (according to one of two accounting formulas)
- Deferral plan is defined contribution (employee's account = employer's liability)

Why have a deferral plan or SERP that does not make a contribution to winning the talent wars, enhancing productivity or increasing profits?

Said differently:

Should we have a deferral plan or SERP if it can help us win the talent wars, enhance productivity and improve profits?

Poll #2

QUICKPOLL

How frequently have you seen either a traditional deferred compensation plan or a SERP implemented by your clients?

Please select one:

- ○ **Never**
- ○ **Less than 10% of my clients**
- ○ **10 to 50% of my clients**
- ○ **Over 50% of my clients**

QUICKPOLL

How frequently have you seen either a traditional deferred compensation plan or a SERP implemented by your clients?

Poll Results (single answer required):

Never	0%
Less than 10% of my clients	71%
10 to 50% of my clients	29%
Over 50% of my clients	0%

Two Possibilities

- Strategic Deferred Compensation
- Balanced Rewards Plan

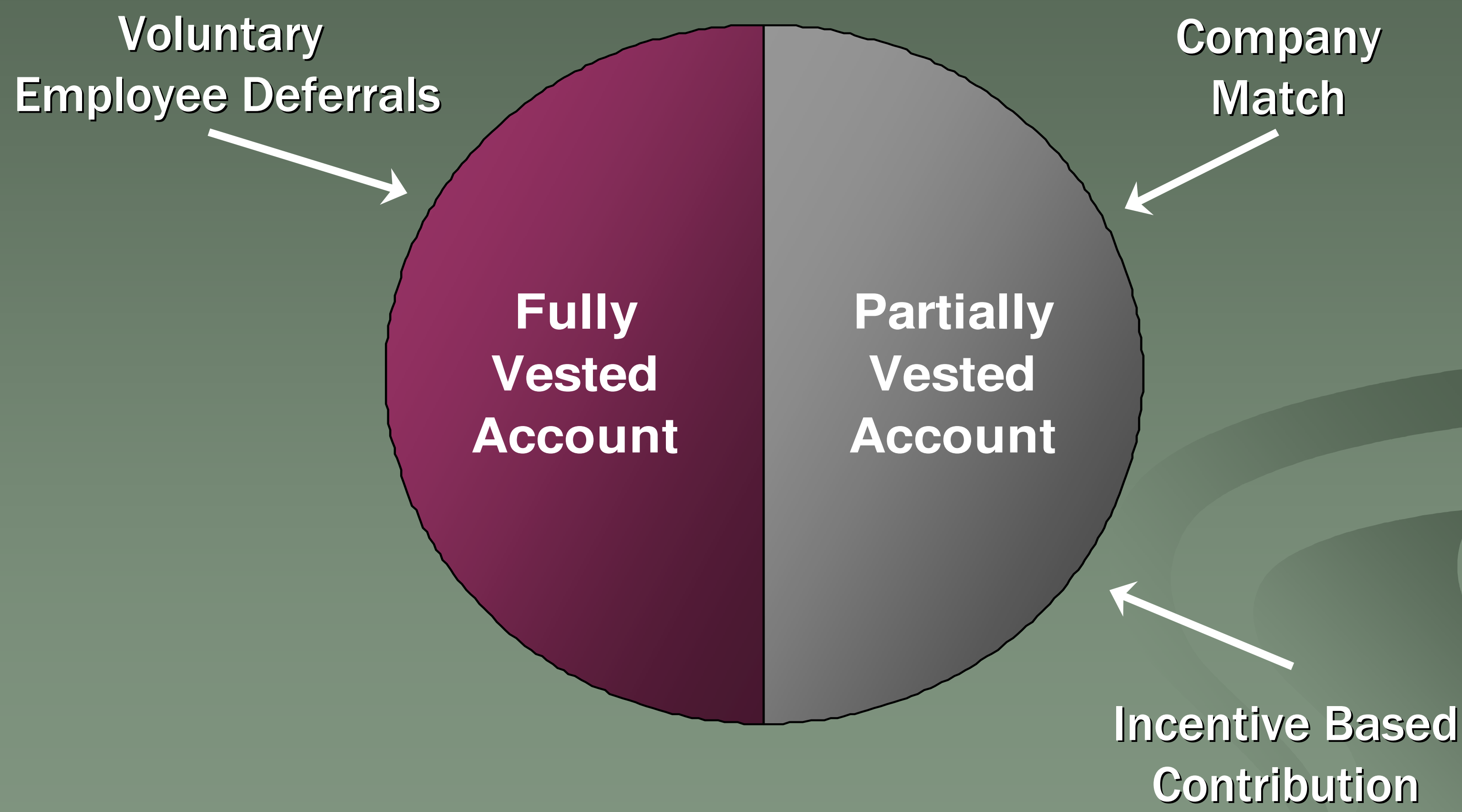
Building Unified
Financial Visions

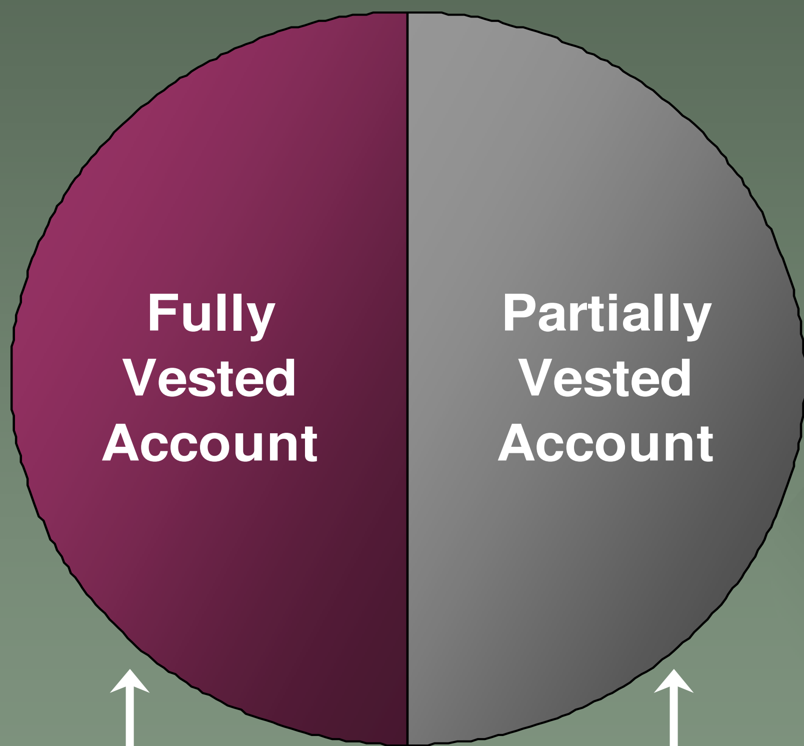
Strategic Deferred Compensation
Characteristics

Combination of—

- employee elective deferrals
- company contributions or matches
- incentive matches
- creative vesting schedules

Building Unified Financial Visions

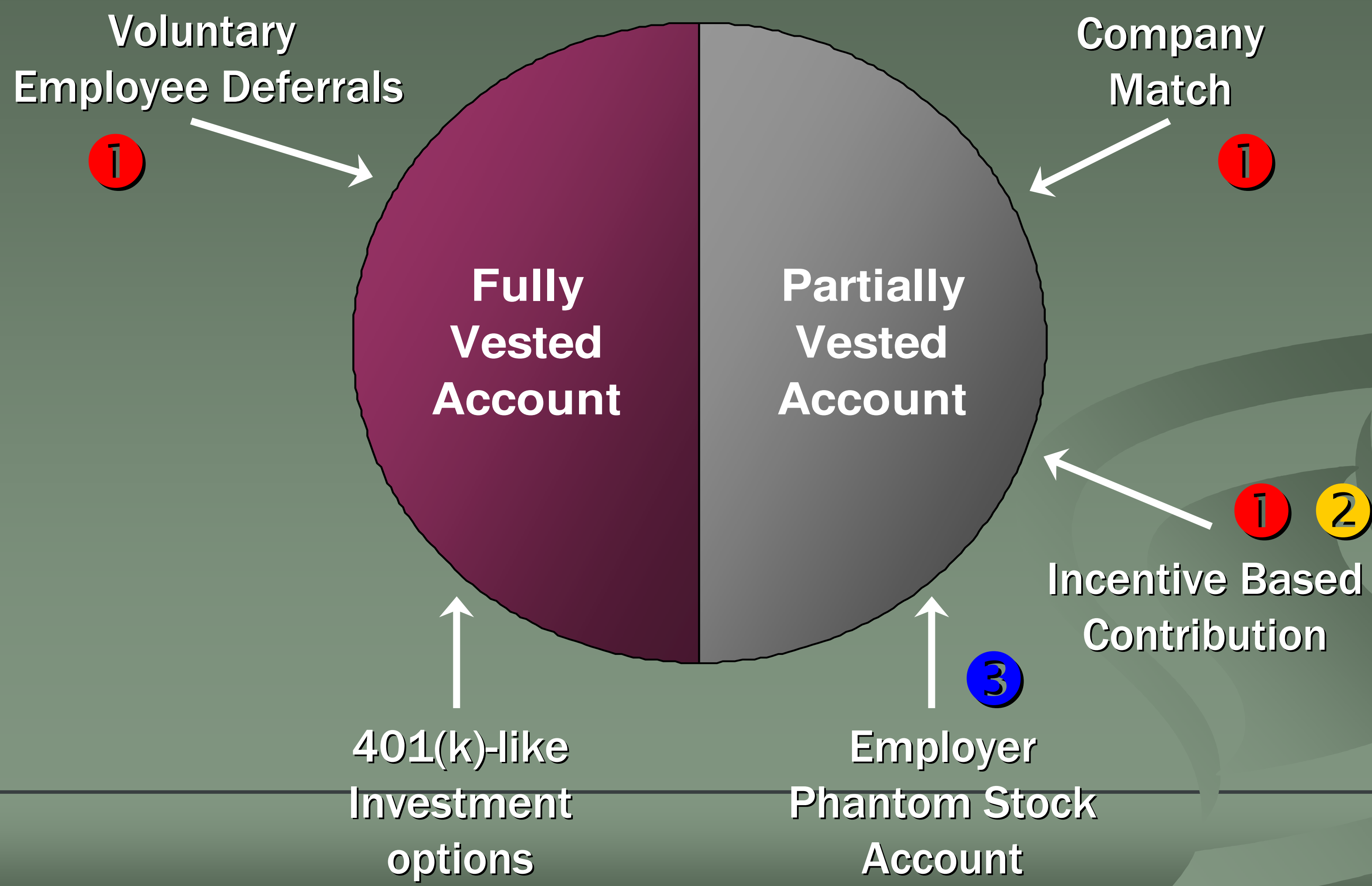

Voluntary
Employee Deferrals
Company
Match
Fully
Vested
Account
Partially
Vested
Account
Incentive Based
Contribution



401(k)-like Investment options

Employer Phantom Stock Account

1. Win the Talent Wars
2. Enhance Productivity
3. Improve Profits



Example: John

- John elects to defer $15,000 from salary
- Company matches 15%
- Company promises an end-of-year contribution based on improvements in sales/net income matrix
- Company account tied to employer phantom stock value (multiple of earnings)

Building Unified Financial Visions

Net Income %	Revenue Growth 10%	Revenue Growth 12%	Revenue Growth 14%
15.0%	150,000 1,500,000 10.0%	250,000 2,200,000 11.4%	400,000 3,100,000 12.9%
17.5%	225,000 2,150,000 10.5%	350,000 2,950,000 11.9%	525,000 3,600,000 14.6%
20.0%	350,000 2,825,000 12.4%	550,000 3,450,000 15.9%	750,000 4,500,000 16.7%

Year	(1) Deferral Amount	(2) Deferral Account	(3) Company Match (15%)	(4) Match Account Value	(5) Incentive Contribution	(6) Incentive Plan Value	(7) Total Plan Value	(8) Forfeitures
1	15,000	16,200	2,250	2,430	14,000	14,000	32,630	16,430
2	15,600	34,344	2,340	5,152	0	15,400	54,896	20,552
3	16,224	54,613	2,434	8,192	21,000	40,040	102,845	48,232
4	16,873	77,205	2,531	11,581	8,000	52,844	141,630	51,540
5	17,548	102,333	2,632	15,350	9,000	68,028	185,712	66,703
6	18,250	130,230	2,737	19,534	0	74,831	224,596	75,493
7	18,980	161,146	2,847	24,172	35,000	120,814	306,133	115,989
8	19,739	195,356	2,961	29,303	15,000	149,396	374,056	142,959
9	20,529	233,156	3,079	34,973	6,000	170,935	439,064	164,727
10	21,350	274,866	3,202	41,230	0	188,029	504,124	183,407
11	22,204	320,835	3,331	48,125	0	206,832	575,792	203,966
12	23,092	371,441	3,464	55,716	28,000	258,315	685,472	219,822
13	24,015	427,093	3,602	64,064	11,000	296,246	787,403	216,186
14	24,976	488,234	3,746	73,235	0	325,871	887,341	219,508
15	25,975	555,346	3,896	83,302	7,000	366,158	1,004,807	224,730

Strategic Deferred Compensation *Characteristics*

Combination of—

- – employee elective deferrals
- – company contributions or matches
- – incentive matches
- – creative vesting schedules

Balanced Rewards Plan
Characteristics

Combination of—

- 50-60% traditional SERP plan
- Target incentive credits to employee accounts
- Possible self-direction of account

$ Value
of Traditional
SERP

$ Value
Of BRP

"Guaranteed"

"Guaranteed"

Building Unified
Financial Visions

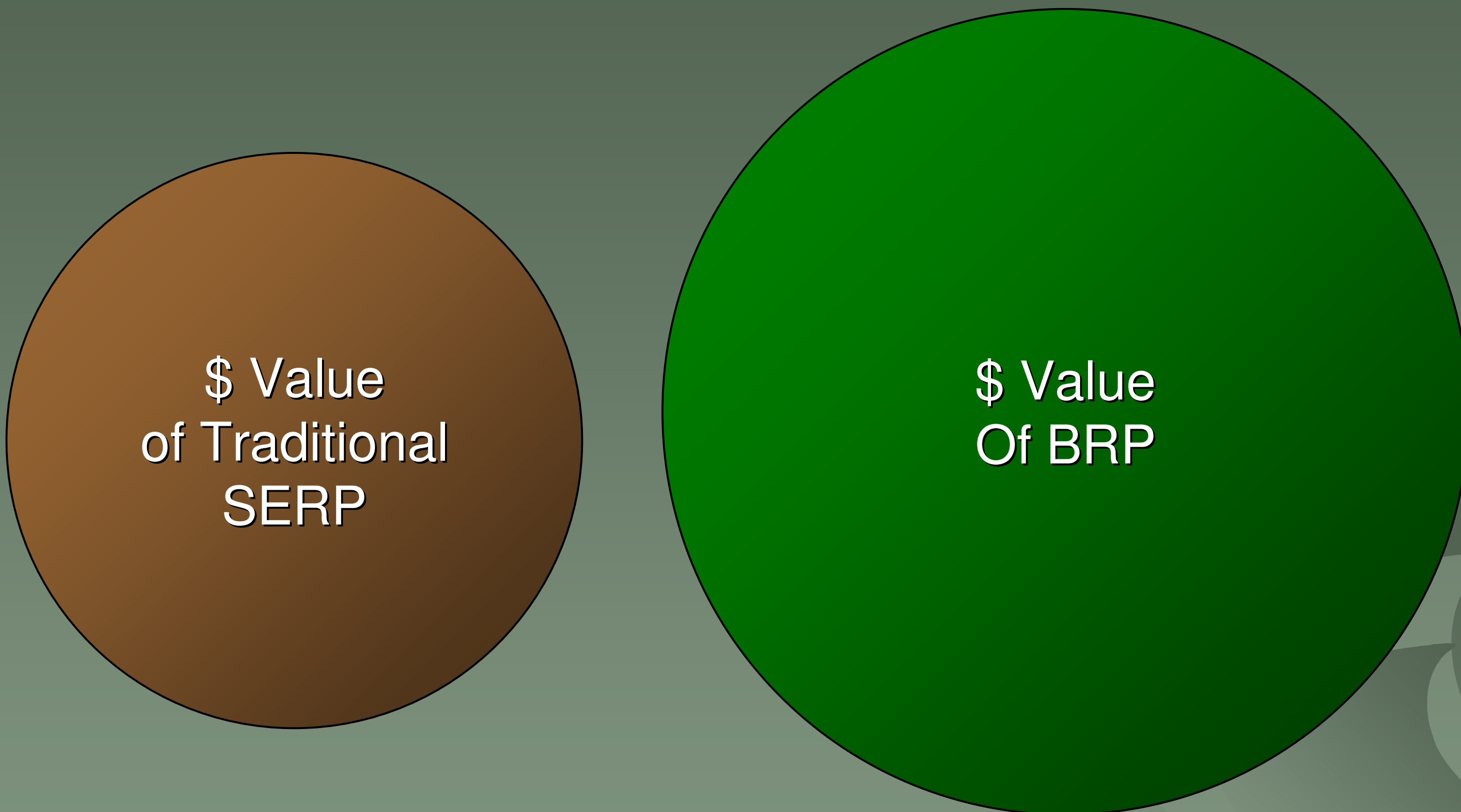
$ Value
of Traditional
SERP

$ Value
Of BRP

"Guaranteed"

Performance Tier 1

Building Unified
Financial Visions



“Guaranteed”

Performance Tier 2

Example: John

- John is provided a retirement benefit equal to 50% of a traditional SERP (25% of salary for 15 years at 65)
- The company will double the credit if the annual budgeted net income is achieved
- The company will triple the credit if the year-end net income is 120% of budget
- John is given an option to self-direct the account (rather than earn a fixed crediting rate)

Building Unified Financial Visions

Traditional SERP		Minimum BRP	Tier 1 Performance Every Year	Tier 2 Performance Every Year
$80,000		$40,000	$80,000	$120,000

With Employee Investment Options (9%)

Traditional SERP		Minimum BRP	Tier 1 Performance Every Year	Tier 2 Performance Every Year
$80,000		$52,000	$105,000	$160,000

Building Unified Financial Visions

Balanced Rewards Plan
Characteristics

Combination of—

- 50-60% traditional SERP plan
- Target incentive credits to employee accounts
- Possible self-direction of account

So who should have a DCP?

- Companies prepared to handle or outsource the administrative responsibilities
- Companies who view the plan as something more than a "convenience" for employees
- Companies large enough to manage and benefit from the financial operation of the plan
- Generally, plan should have deferrals or company contributions of $100,000 (or more)

Building Unified Financial Visions

What about "S" Corporations?

- SERP still viable
- Additional tax analysis required to justify deferral plan
- Owners should not defer

Building Unified Financial Visions

Poll # 3

QUICKPOLL

Based on your understanding of these two approaches, how likely are you to recommend one or both to your clients

Please select one:

- Very likely, I might call them today
- Maybe, I need to learn more
- Wouldn't work for any of my clients

QUICKPOLL

Based on your understanding of these two approaches, how likely are you to recommend one or both to your clients

Poll Results (single answer required):

Very likely, I might call them today	0%
Maybe, I need to learn more	100%
Wouldn't work for any of my clients	0%

For qualified companies, it may be a competitive disadvantage to not have a DCP (and a real competitive advantage to have one)

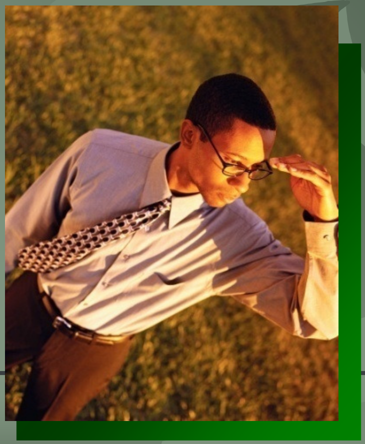
A great plan…

- Will make it hard for top employees to leave
- Will focus employees on the achievement of key company goals
- Will produce a positive economic return for the company

Building Unified Financial Visions

How does a great plan produce a positive economic return for the company?

Motivational components of the plan produce an otherwise unachieved result—creating new economic value to share (self-financing)



What about plan funding?

- Financing approach of the plan can produce a positive economic return.
- This is accomplished through successful use of investments and/or corporate owned life insurance.
- Proper understanding of tax mechanics is essential.
- Typical plan should be producing positive financial impact within 2-4 years of inception.

Financial Concept

	Deferrals	Tax Cost
Deferrals	$20,000	($8,000)
Earnings	$15,000	$0
Payment	$35,000	$14,000
Gain		$6,000

Building Unified Financial Visions

If you have a plan…

- Is the plan evaluated with an eye towards executive retention?
- Has the financing/funding arrangement been contrasted with viable options to insure optimal financial results?
- Does the communication of plan values reinforce corporate strategy and promote employee value proposition?
- Is the plan up-to-date with all legal requirements?
- Does the plan have a purpose that is aligned with corporate strategy?

Building Unified Financial Visions

Conclusions

- For qualified companies, no better time to capitalize on the flexibility and financial viability of a well-designed DCP
- New plans should only be adopted if they fulfill a strategic and economic objective
- “Convenience” plans should be reviewed and updated to create strategic and economic alignment

Next CPE Course:

"How Does My Client Get Sustained Performance From his Key People?"

To be held on:

Tuesday, August 18th, 2009

Building Unified Financial Visions

Next Online Seminar:

"How Do I Create a Competitive Advantage with My Compensation Programs?"

To be held:

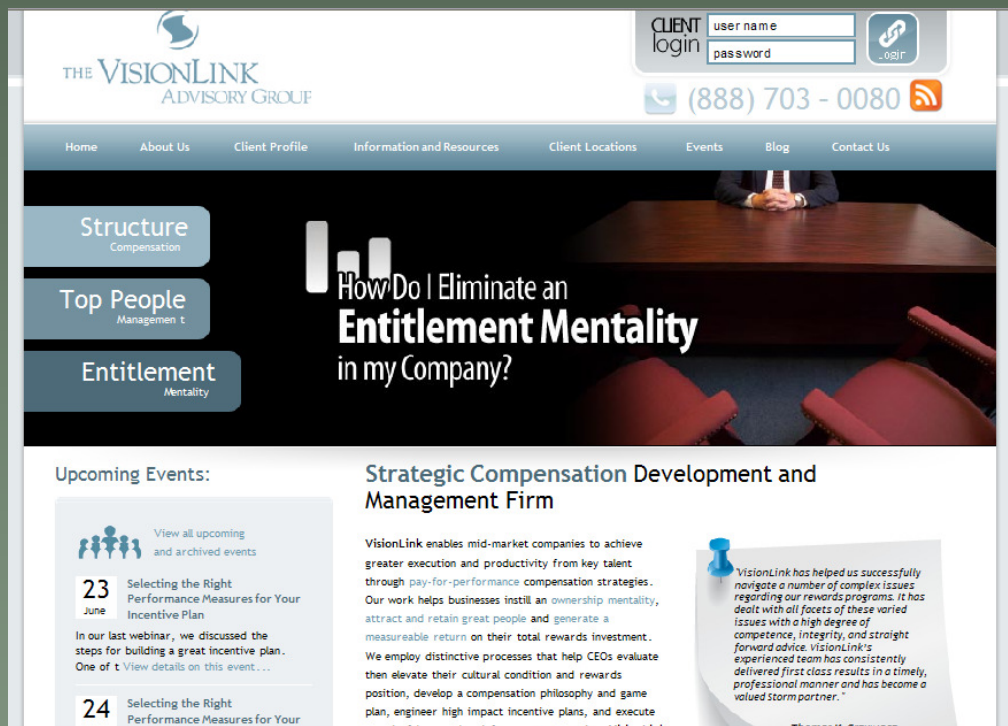
Next Tuesday, July 28th, 2009

Visit our website to register

Building Unified Financial Visions

Check out our NEW website:

www.VLadvisors.com



You can also subscribe to our **new blog**

Building Unified Financial Visions

Questions?

Building Unified Financial Visions

Thank you for attending

Please complete our survey form immediately following our presentation.

This will be counted as a monitoring event.

You may request a copy of the slides and also a CD of today's presentation

Building Unified Financial Visions

Thank You!

Ken Gibson

Senior Vice-President

(949) 265-5703

kgibson@vladvisors.com

Building Unified Financial Visions

THE VISIONLINK ADVISORY GROUP