

RESTRICTED EXECUTIVE BONUS ARRANGEMENT

Restricted Executive Bonus Arrangement

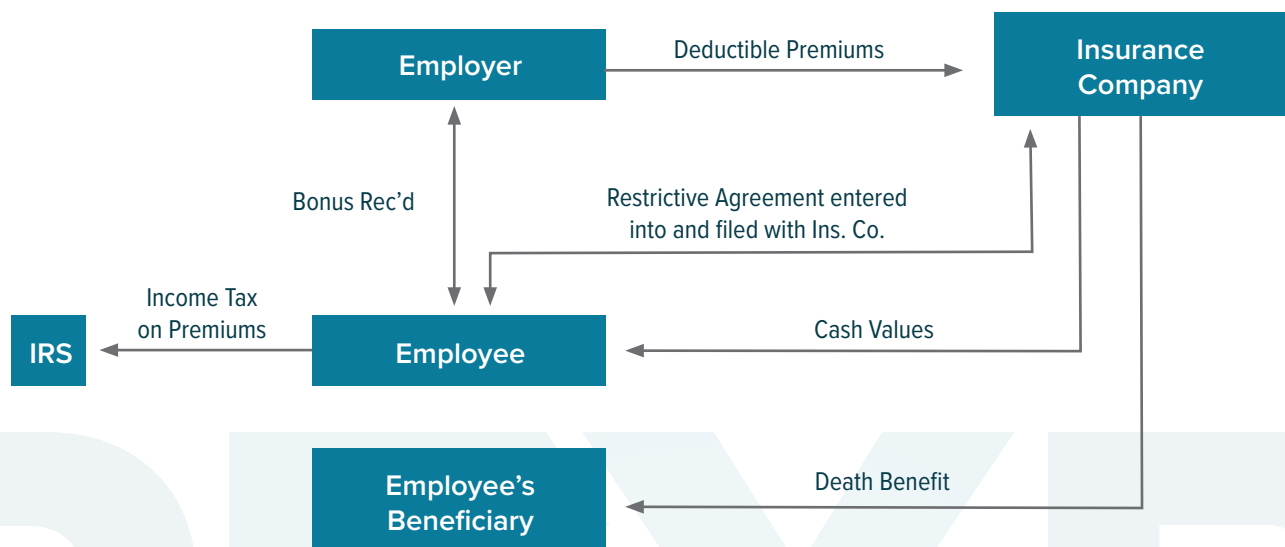
Under a restricted executive bonus arrangement (REBA), the Employer uses tax-deductible bonuses to assist the Executive in purchasing a permanent life insurance policy on his or her own life. The Executive owns the policy and names the beneficiary. Through an endorsement to the policy, the Employer is able to limit the Executive's access to the cash value.

The Employer and Employee enter into a supplemental employment agreement spelling out the terms and conditions of the restrictions designed to motivate the employee to stay with the employer for an agreed upon period of time. Typically, an endorsement is filed with the insurance company, restricting the executive's rights in the policy for the agreed term.

Examples of policy rights that might be restricted include surrendering the policy for its cash value, partial withdrawals of cash value, borrowing cash values, assigning the policy as collateral, or changing ownership of the policy. Though the employer controls access to the cash value by the executive, values can never revert to the employer under the restrictive agreement, or the current year tax deduction could be jeopardized under Internal Revenue Section 264 that prohibits an employee from deducting premiums when it benefits from the policy.

The Restricted Executive Bonus Arrangement can, if desired, be structured to pay all the individual income taxes generated by the bonus, resulting in a zero net cost to the Executive. The employer can pick and choose who is to be covered under this arrangement.

How It Works:



While this communication may be used to promote concepts discussed in the publication, it is intended to provide general information and is provided with the understanding that Pinnacle Executive Benefits is not rendering legal, accounting, or tax advice. It may not be used to avoid penalties under the Internal Revenue Code. On all matters pertaining to legal, tax or accounting obligations and requirements, the appropriate counsel or other advisors should be consulted.

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Continued

ADVANTAGES

For the Employer

- Premiums are tax deductible
- The plan provides a fringe benefit to the employee
- It provides a “golden handcuff” fringe benefit for select employees
- Benefits may vary between employees
- The plan is relatively easy to establish and administer
- No minimum or maximum number of lives must be covered

For the Employee

- The cost of the plan is paid for by the employer
- Generally, the employee is owner of the policy and designates a personal beneficiary
- The potential cash values of the policy may be accessed by the employee to supplement retirement income or to cover unexpected expenses after the restrictive endorsement is removed.
- The employee is able to take the policy if he/she leaves after restriction period
- The death benefit is income tax-free to the beneficiary

OTHER CONSIDERATIONS

- The premium and any bonus used to pay the tax bill is fully reportable as taxable income to the employee
- The bonus made by the employer must be considered reasonable additional compensation for the employee’s position in order to be deductible under Section 162 of the Internal Revenue Code
- The employer may not be named as owner or beneficiary nor have any rights to the policy cash value in order for the premium to be tax deductible to the employer
- As owner of the policy, the death proceeds will be includible in the employee’s estate (If this is an issue, there is a way to exclude it from the employee’s estate by having an irrevocable trust as owner/beneficiary, but that will tie up the cash value in the trust)
- Employer’s attorney will need to draw up the employment agreement (Insurance companies generally provide specimen wording for restrictive policy endorsement)
- The arrangement, if properly constructed, should not be required to comply with Internal Revenue Code Section 409A and its regulations. However, the employer and employee should consult with their legal counsel regarding the design of the specific arrangement and the possible consequences under Section 409A

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