



Agent and Advisor Guide to Advanced Markets Concepts



Executive Bonus

Executive bonus is the simplest of the executive benefit plans. In an effort to recruit, reward and/or retain top talent, the employer agrees to pay the premiums on a life insurance policy owned by the executive. This amount is includible in the executive's compensation and is generally deductible to the employer (it would not be deductible to the extent that his or her compensation is not "reasonable" per IRC 162).

This policy is under the complete control of the executive and the employer has no interest in the policy. The executive can change the beneficiary, take a withdrawal from the policy, take a loan against the policy, collaterally assign the policy, and may consider transferring the policy to an irrevocable trust (ILIT) for estate planning purposes. If the policy is transferred

to an ILIT, the transfer will have gift tax implications, three year inclusion implications, and transfer for value implications. All implications can be adequately handled with proper planning (eg. the executive can make cash gifts to the ILIT using his/her annual exclusions, the ILIT is structured as a "grantor trust", and the ILIT trustee purchases the policy from the executive).

The executive bonus arrangement is a "fuzzy" handcuff in that the executive can terminate employment and does not forfeit any rights or benefits in the policy. If a slightly stronger handcuff is desired see "Restricted Executive Bonus" or "Golden Executive Bonus Arrangement" (GEBA). If a complete handcuff is desired see "Employer Loans" or "Employer Endorsement".

Pros

Simple to understand and administer

Valuable benefit for Executive

Helps recruit, reward, retain

Generally deductible to Employer

Cons

Still is not much of a handcuff – Executive is free to leave and take policy

Is classified as a welfare benefit plan for ERISA purposes

Entire premium amount is included in Executive's – as executive bonus without restriction

The preceding summary is intended to be a general discussion of the topic presented, and is based on our current understanding of applicable tax laws, regulations and rulings. In actual practice, the transaction discussed may be more complex and will require the attention and expertise of professional advisors. In no way should this summary be construed to constitute tax or legal advice. **For agent use only.**