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WALL STREET JOURNAL ARTICLE TALKS ABOUT TRANSFERRING NON-QUALIFIED SERP BENEFITS TO QUALIFIED PLANS

In an article on August 4, 2008 entitled "Companies Tap Pension Plans to Fund Executive Benefits", the *WSJ* addressed a compensation approach that is garnering the increased interest of many large companies. Supposedly, supplemental retirement benefits to certain executive officers can be transferred to a qualified pension plan. The article casts the technique as a "dubious use of tax laws" and asserts that it weakens a company's qualified pension plans. The article also claims the approach has contributed to the loss of promised retirement benefits to many rank-and-file employees in underfunded pension plans. The transferred benefits are called "QSERPs." This is of interest to ENDSIGHT because many ECS credit union clients have SERP arrangements in place for their executives.

There could be significant advantages to credit union executives in shifting supplemental retirement benefits from a non-qualified to a qualified pension plan. Moreover, where a credit union has an overfunded qualified pension plan, the excess pension assets might be used to fund the credit union's non-qualified retirement benefit obligations to its senior executives. In addition, while non-qualified benefits cannot be funded and must be paid out of the credit union's general assets, which must remain subject to general creditor claims, qualified retirement benefits generally must be funded by current contributions to a qualified trust, which is a separate legal entity from the credit union and not subject to the claims of general creditors. Thus, by shifting some or all of their promised supplemental retirement benefits to a qualified pension plan, the supplemental retirement benefits generally become more secure. The shift of supplemental retirement benefits to a qualified plan can also provide favorable tax advantages to the executives. Unlike distributions from a non-qualified arrangement, amounts distributed from a qualified plan can be rolled over to an IRA or another tax-favored retirement plan and the limitations of IRC 457 do not apply. Thus, the executives would have a lot more flexibility to extend the deferral period and benefit payment periods.

The QSERP is based on the IRS nondiscrimination testing rules of 1994. Some of these testing alternatives may allow for greater benefits to certain highly compensated employees. A pension plan actuary can determine the amount of additional benefits that can be provided by running a number of tests taking into account the plan terms and the plan sponsor's particular demographics.

Inherent Problems

There are a number of potential issues with the use of the QSERP approach. First, it involves replacing existing non-qualified supplemental retirement obligations with new benefit

accruals under a qualified plan. In many cases, the existing non-qualified arrangement would be subject to the new rules imposed by Code Section 409A. It is not clear whether the technique works after full implementation of 409A on January 1, 2009. Section 409A provides that the substitution of a newly created obligation for an existing non-qualified deferred compensation obligation generally be treated as a payment of the existing obligation, which would likely violate the 409A requirements and result in adverse tax consequences, including current income tax recognition and an additional tax of 20% plus interest.

At this point, it is difficult to speculate on the regulatory reaction to a technique that flies in the face of the intent of 409A and similar legislation. Obviously, the extent of the use of the technique will be a factor and Congress is already considering at least two potential pieces of legislation that may further restrict the amount of compensation that can be deferred under a non-qualified arrangement: (1) the proposed \$1 million annual cap, and (2) the current taxation of offshore deferred compensation. ENDSIGHT will monitor developments.

ECS CEO TODD LANE INTERVIEWED BY CREDIT UNION JOURNAL

Demographic evidence sees the leadership of credit unions changing over the next several years. Todd Lane, CEO of Executive Compensation Solutions says, "We think it's important that credit union boards begin planning for that change." He points out that, "...about 3,000 credit union CEOs will be reaching retirement age in the next five years."

In the August 11 issue of *Credit Union Journal*, Lane says, "That is why succession planning needs to be part of 2009 strategic planning discussions. Boards need to be planning ways for the credit union to quickly and effectively address a potential change. I think too many credit unions wait until the CEO announces he or she is retiring and that is not strategic."

To help assure that credit unions can attract and retain top leadership talent, Lane suggests structuring a meaningful, reasonable, and affordable approach to providing long-term compensation incentives, retention programs, and supplemental retirement benefits. "Strategically, this is the right thing to do. Not thinking about continuity issues strategically creates unnecessary risk for a credit union."

Lane stressed that, "There will be no consistency in leadership and direction without an effective plan to attract, retain, and reward the leadership group. Continuity issues are every bit as important as growth and ALM strategies."

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