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Retaining Key Employees

• You’re not alone!
• How do you retain your best and brightest?
• How do you develop future leaders and owners?
Long Term Incentive Plans (LTIP)
Stock Appreciation Rights (SAR)
Deferred Compensation Plan

• Attract, retain and reward top, key talent
• Complete flexibility in design (customize to meet goals / needs)
• **FAR Considerations**
• In addition to compensation and cash bonuses (not a take away)
• First and foremost reward for key employees for their contributions
• Recognition of substantial contributions to the operations and financial success of the organization
• Provide additional financial security as an inducement to remain employed with the corporation
Example Simplistic Model
Discussion points

• Build in a vesting schedule (example 3 or 5 year rolling vesting)
• Some window of time identified to realize vested portion of benefit (i.e. year 4 or 6)
• But if separation, potential to leave an amount on the table
• Individuals continue to be a participant until account is distributed or forfeited in accordance with the plan
• Deferred value meaningful value to be effective (hard to define, based on individual circumstances)
Characteristics of and requirements for a deferred compensation plan

• Pre-determined criteria for participation (optional)
• Predominately a performance based plan (handling of annual change between participants can vary to design)
• Can have various levels of participation (A, B units, etc.)
• Complete flexibility in design
  • Funding Formula (stock value, annual profitability)
  • Vesting Terms
  • Payout Terms
Characteristics of and requirements for a deferred compensation plan

- Obligation accrued on balance sheet, impact financials and ratios
  - Impacts financials, cash if funded, accrued liability, net profit, and equity
  - Impacts ratios, working capital, debt to equity, profitability and others
  - Obligation will have short term and long term components
  - Can pro-rate and net present value obligation as earned
- Tax Considerations
  - Not deductible to Company or included in employee income until earned and paid for federal and state income tax
  - Special FICA / Medicare treatment when earned and not subject to substantial risk of forfeiture
Characteristics of and requirements for a deferred compensation plan

- Funding of obligation (optional but recommended)
- Consideration of use of Rabbi Trust
  - Allows participant “limited” input over investment of funds (careful, need to avoid constructive receipt)
  - Level of protection from creditor claims in ordinary course of business (not company bankruptcy)
- Subject to 409A regulations, tax code with detailed requirements, deferral elections, distributions, etc.
- Thorough preparation of documents to protect Company
Characteristics of and requirements for a deferred compensation plan

- Attorney will draft documents
- Top Hat filings
- Recorded in board minutes and parameters defined
- Often clause that employee death or permanent disability will provide for immediate vesting and payment to employee or estate
- Often life insurance used for funding in case of death
Overhead Rate Considerations

• Effect of Deferred Compensation on your firm’s overhead rate.
INCENTIVE FUNDING – FINANCIAL FOUNDATION

- **Total Incentives $ (no upper limit)**
- **Inverted Curve**
- **Pools are funding simultaneously**
  - Cash Bonus
  - Deferred Compensation
    - 401K, Profit Sharing
  - Financial Foundation $  
  - Support Growth – Equity, Working Capital, Banking, Bonding, investment in infrastructure, etc. (No incentive)  

**Profit $**  
**Incentive $**
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**Profit $**

**Incentive $**