Nonqualified Deferred Compensation
Business Opportunity

A nonqualified deferred compensation plan is an agreement between an employer and an employee, under which the employer promises to pay the employee compensation at a future date.

This compensation is taxed to the key employee when the compensation is paid to the key employee in the future. The employer is entitled to a compensation deduction when the key employee is provided the compensation, assuming overall compensation is deemed to be reasonable.

The employer should plan for this future benefit obligation, which is most commonly accomplished through the business purchasing a permanent life insurance policy insuring the key employee. The employer may not deduct the premiums paid for this policy. As the policy owner, the employer controls the policy, including its cash value. The employer can leverage the policy's cash value and/or death benefit to recover the costs incurred under the arrangement.

Client Profile

Possible Objectives:

- Discriminatory benefit for key employees
- Flexibility in plan design
- Potential to provide supplemental retirement income for the owner-employee or non-owner key employee
- Future deductible expense for the business
- Income tax advantages and cost recovery for the business if permanent life insurance is used as the informal funding method

Entity Types

- If the benefit is for a **non-owner key employee**: C corporations, professional corporations, S corporations, partnerships, and LLCs (regardless of tax status)
- If the benefit is for an **owner-employee**: C corporations, professional corporations, and LLCs taxed as C corporations

Relevant Factors:

- Supplements a qualified plan
- Selective benefit for certain key employees
- Helps the employer recruit, retain, and reward key employees
- Must satisfy the requirements of Internal Revenue Code §101(j) and 409A

Notes: