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A New Thought on Key Executive Benefits

By Allan Mosher

Much has been written about retaining key employees. Human Resource firms have studies and analysis that establish that companies invest in human resources. Employees are won and lost over competitive advantages.

It is often a struggle to find that balance between the expense of benefits and the value they bring in attracting and retaining key talent. Companies recognize that employees are vital to the future of the corporation but, how do they effectively engage their loyalty?

What makes Company A more enticing than Company B? Is it group benefits, vacation, bonus or, work environment? There is no doubt all four play a key role in attracting and retaining key employees but, does the benefit portion particularly, the pension component, warrant the expense?

When an employee chooses a Public Corporation or Government employment over a private corporation the pension plan plays a key role in their decision. There has been plenty of discussion surrounding pension plans – the cost, the risk and the liability. It is very difficult for a Private Corporation to compete with a Defined Benefit or even a well funded Defined Contribution Plan.

But what if it was possible to offer key employees a Supplemental Pension that does not expose them to market risk? A Supplemental Pension with funding mitigation, no requirement for pension integration, deferred vesting options, tax deductible, and easy to administer.

There is an answer. A Managed SERP Programme (www.rcf.ca) utilizing a Retirement Compensation Arrangement (RCA). The *Income Tax Act* only allows for "pension shortfalls" to be funded and secured by an RCA as defined under subsection 248(1). Contributions are 100% tax deductible to the employer and, not taxable to the employee until benefits commence.

Any key employee is eligible to participate. Income levels are not a determinant. Entitlements are based on a compensation formulae following CRA Guidelines. Unless the SERP is integrated with a Registered Pension Plan, the maximum formulae should not be used, nor should employees have the option to elect a bonus over SERP benefits.

Minimum SERP Benefits

- Provides 50% of Pension Target with Employees' Registered Pension Plan providing the remainder.
- Based on a formulae of 1% times years of service times final five year average earnings. Indexed at 2% with a 2/3 spousal benefit.
- Member must still be employed by the Company at age 65 or 60 to receive benefits.
- Normal Retirement Benefits commence at age 65.
- Early retirement option at Age 60 but reduced by 0.5% x year of service.
- In the event of disability, vested benefits accrue to that date.
- In the event of death prior to retirement, spouse will receive 2/3rds of earned benefits at 1% x years of service x final and/or best (for cyclical companies) 5 year average salary.
- Variations can be made relative to vesting, mid & late term hire credits, increased formulae to 2% (inclusive of any benefits from Company sponsored Registered Pension Plan) and, earnings increased to include 50% of average bonuses, following Generally Accepted Guidelines.

Advantages to SERP Sponsor

Funding is flexible, with contributions made in years company is profitable.

Deferred vesting options provide a retention strategy. Company decides when key employees are vested to receive supplemental income based on years of service with company.

Unlike other retirement alternatives, it does not involve investment decisions. Assets are transferred to the Participating Pool of a major insurance company through individual contracts for each SERP member. Guarantees secure projected benefits.

Having a Managed SERP Programme in place can also make a business more "saleable". It may not make a company worth more but, potential buyers know a funded SERP combined with a vesting agreement means that key employees they will rely on for future profits are tied to the company. Also, funding mitigation will allow them to fund future SERP members at a much reduced cost.

Benefits for Key Employees

They receive a tax deferred benefit. Retirement security is on the minds of all Canadians after the market performance of the past 12 years.

The tax deferred benefit is welcomed by key executives as they are normally at a stage in their life where a tax deferred and secure benefit is far more beneficial than a taxable benefit that requires management.

In the event of disability, benefits can be accrued to that date to financially aide the employee.

Spousal benefits are included.

They know that their performance is valued which provides incentive to stay with company.

An employer who can offer retirement security will win the battle in attracting and retaining key talent.

Owner Participation

Owner Employees (non-employee shareholders are excluded) can also participate in a Managed SERP Programme. However, they are also aware of their Registered Pension Benefits (RPPs), they will normally integrate benefits with the SERP using a 2% per year of service benefit.

By utilizing their Employee status to supplement their personal pension benefit, owners remove money from the company tax free (following CRA guidelines with no caps like RRSPs), have a creditor proof asset and enjoy a flexible retirement benefit with estate advantages. These benefits also reduce the risk profile of an owner, very important in today's environment.

Allowable contributions for SERPs secured and funded with RCAs can be substantial for high earning Owner Employees. This often results in a Terminal Funding liability that can reduce net cost for Purchasers.

A Managed SERP is one of the few retention strategies that can benefit both Owner Employees and key people.

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