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REBAs Provide Employers with a Deductible Executive Benefit Plan with Handcuffs

In today's business environment, executives are sometimes reluctant to participate in benefit programs where their employer's obligation is nothing more than an unsecured promise. They have legitimate concerns about the effect that bankruptcy, buyouts, and management changes could have on future benefits.

Would your business clients be willing to address these concerns if it could provide a supplemental benefit arrangement to a selective group of key executives as long as the arrangement is deductible and binds the executive to the company?

Example of REBA

Joel Johnson, age 55, is the dynamic and charismatic CEO of Micro Technologies, Inc., a leading provider of surgical lasers in the medical industry. For the last 10 years, he has shaped the company by producing cutting edge equipment, controlling costs, and developing marketing strategies. Not only does he bring business acumen to the table, but he is also a true leader who motivates and rallies the staff.

Recently he came to the board of directors to discuss the possibility of early retirement. The board realizes his departure could jeopardize the company's future. Transition planning has been put into effect and leaders to replace Joel are being trained, but his departure is too quick. The company needs more time to train successor management. And they need to have access to Joel's creativity and solutions during this period. Here's how a REBA would work to help solve this problem.

Micro Technologies, Inc. agrees to pay a $100,000 annual premium on an insurance policy to be personally owned by Joel. The Company will double bonus Joel $138,888.89 (assuming a tax bracket of 28%) for 15 years so Joel will have no out-of-pocket costs. The policy on Joel's life will be structured with an increasing (option B) death benefit and funded sufficiently to encourage cash value growth.

In return for this zero-cost death benefit protection, Joel will execute a policy endorsement that restricts his right to access cash values for the earlier of 15 years or his release by Micro Technologies, Inc. Joel's employment agreement is amended to require he remain an active CEO of the company for a period of five years and then serve on the board of directors for another ten years. If Joel leaves Micro Technologies, Inc. before the end of his employment agreement, the death benefit remains in place, but he cannot withdraw, borrow, or surrender cash value, or use the policy as loan collateral until age 70.

REBA Benefits Both Employer and Executive

It is a win-win situation! Micro Technologies, Inc. has ensured Joel's active leadership at the helm of the company for a five-year transition period. In addition, they have kept his expertise tied to the company as a director for another ten years. All this at a minimal annual cost!

As for Joel, he is the owner of a valuable policy. Not only do his heirs have the benefit of death proceeds, which are generally income tax free under I.R.C. § 101(a) should something happen to Joel, but once Joel meets the term of the employment agreement, he has unrestricted access to the policy cash value. A REBA must be structured carefully to achieve the desired results. Legal and tax counsel should be consulted prior to establishing the arrangement.

How Can DBS Help?

A REBA must be structured carefully to achieve the desired results. Legal and tax counsel should be consulted prior to establishing the arrangement. For more in-depth information on how a REBA might help your business owners retain the talents of their key executives contact DBS advanced case design resource, Terri Getman, JD*, CLU, ChFC, RICP, AEP (Distinguished).

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