ADVANCED PLANNING

Business Strategies

Executive Bonus Arrangement

EXECUTIVE BENEFITS

THE CHALLENGE

Your employees make important contributions to your business. Some key employees may have unique skills and abilities that are critical to the continued success of your business. Do you worry that they will be lured away by a competing company? Are you concerned that their current benefit package may not be enough to keep them working for your company? Or is there an employee at a competing firm whom you would like to have working for you?

Most businesses, whether large or small, are concerned about attracting and retaining the key employees who help make them successful. As a business owner, your challenge is to create benefit programs and incentives that will motivate key employees and make your company an attractive place to work.

THE SOLUTION

One solution to attracting and retaining quality employees may be an **executive bonus arrangement**. This arrangement allows you to recognize and reward a key employee while helping to provide financial security for the employee and his or her family. It can also serve as a recruiting tool if competing companies don't offer similar benefits.

THERE IS AN OPPORTUNITY FOR YOU TO CUSTOM DESIGN A PLAN TO FIT THE UNIQUE NEEDS OF EACH KEY EMPLOYEE, RATHER THAN TRYING TO FIND A "ONE-SIZE-FITS-ALL" INCENTIVE.

An executive bonus arrangement is a method of purchasing life or disability income insurance[1] as an additional employee benefit. It may also be used to purchase annuities that can provide supplemental retirement benefits over and above those provided by a qualified retirement plan.

You may find the executive bonus arrangement particularly attractive because you can pick and choose those key employees to be covered, while your business gets a tax deduction for the bonuses. There is an opportunity for you to custom design a plan to fit the unique needs of each key employee, rather than trying to find a "one-size-fits-all" incentive. For example, one employee's major concern may be retirement income while another may need additional life insurance to provide for his or her family. A younger, single employee may want disability insurance. You have the flexibility to create separate arrangements that will meet each individual's needs.

[1] The availability of disability income insurance varies by carrier and state.

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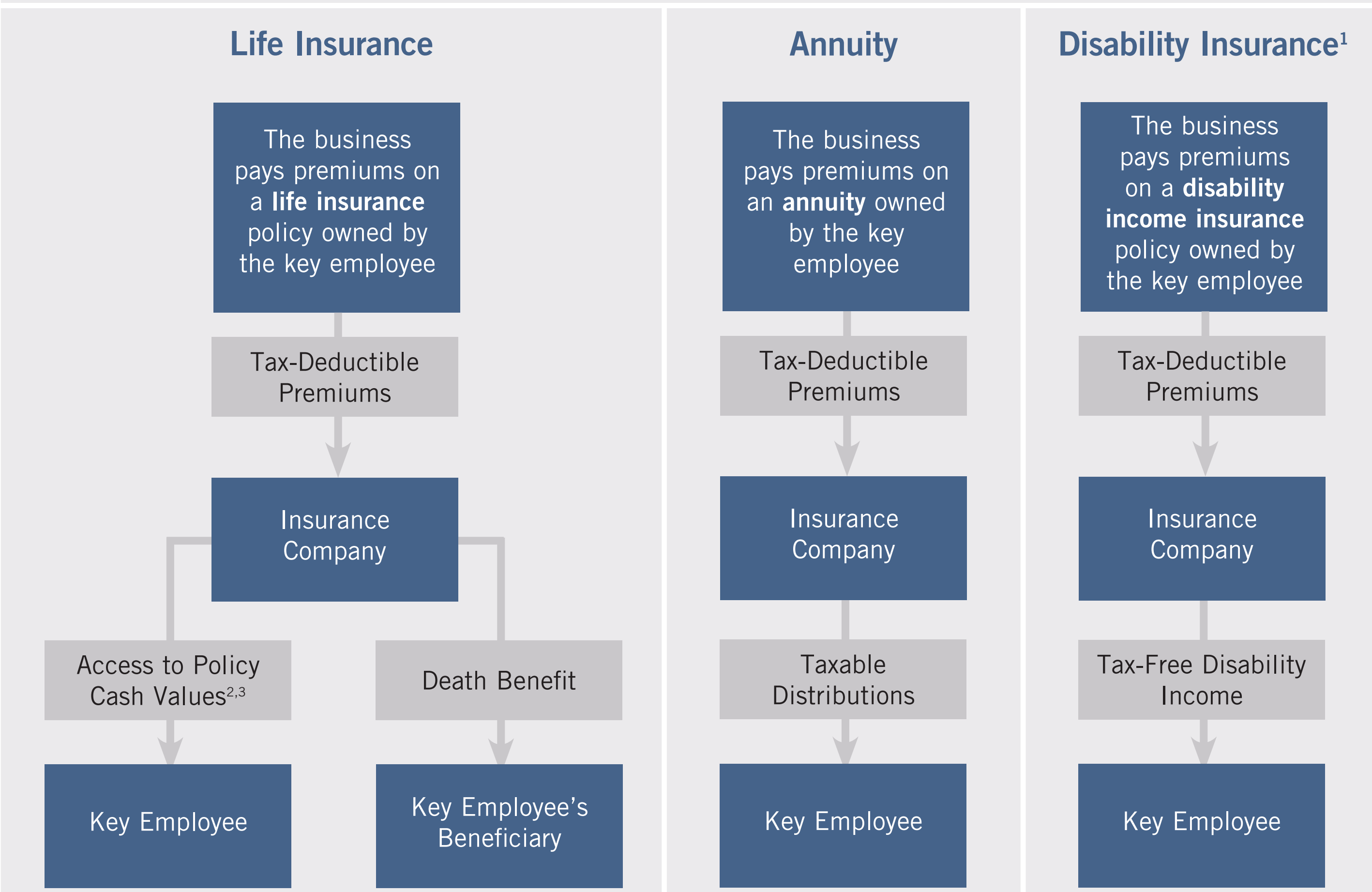
HOW IT WORKS—THE ARRANGEMENT IS SIMPLE

- Your key employee purchases and owns an annuity, life, or disability income insurance policy and names a personal beneficiary.
- Your business agrees to pay the premiums, either directly to the insurance company or as a cash bonus to the employee.
- **If life insurance is provided:** When the employee dies, the policy proceeds are paid to the named beneficiary, usually a family member. Or, when the employee retires, policy cash values can be used to supplement his or her retirement income.[2]
- **If an annuity is provided:** When the employee retires, annuity values can be used to supplement his or her retirement income.
- **If disability income insurance[1] is provided:** If the employee becomes disabled (as defined in the policy), monthly benefits are paid to the employee to help meet financial obligations during the period of disability.



[2] Loans are charged interest; they are usually not taxable. Withdrawals are generally taxable to the extent they exceed basis in the policy. Loans that remain unpaid when the policy lapses or is surrendered while the insured is alive will be taxed immediately to the extent of gain in the policy. For policies that are Modified Endowment Contracts (MECs), distributions (including loans) are taxable to the extent of income in the policy; an additional 10% federal income-tax penalty may apply. Consult your tax advisor for advice about your own situation.

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TAX CONSIDERATIONS

The bonus, whether paid in cash or premium payments, is considered compensation and is generally tax-deductible subject to the limits under Section 162 of the Internal Revenue Code (IRC). The bonus is subject to payroll taxes and withholding and must be reported on the employee's Form W-2.

The employee must pay income tax on the bonus. However, your business may provide an additional bonus to the employee to make up for the income-tax payments. This is called a "Double Bonus" and provides enough cash to cover both the insurance or annuity premiums and the employee's income tax on the bonus. This approach effectively eliminates any out-of-pocket expense for the key employee.

EXECUTIVE BONUS WITH LIFE INSURANCE

ADVANTAGES TO YOUR EMPLOYEE

If the employee lives to retirement:

- Since the employee owns the policy, he or she may continue the policy after retirement without evidence of insurability or additional cost to your business.
- The policy cash values may be used to supplement retirement income from the employee's qualified retirement plan funds.[2,3]
- With the employee's unrestricted access to the policy's cash values, he or she can take policy loans or withdrawals against those values for unexpected events.[2]

If the employee dies before retirement:

- The death benefit is paid to the employee's beneficiary and is generally income tax-free.[4]
- The employee's beneficiary can elect to receive the death benefit as a lump sum or can choose one of several annuity options that will provide regular income for a specified period or for life.

ADVANTAGES TO YOUR BUSINESS

- The executive bonus arrangement is easy to establish. No Internal Revenue Service approval is required, and administration costs are very low.
- Premium payments are tax-deductible as compensation. The employee pays income tax on the premium payments or cash bonus.
- You may choose which key employees to include in the executive bonus arrangement. There is no requirement that all company employees be included.

[3] A policy's illustrated cash value consists of both guaranteed and nonguaranteed values. Nonguaranteed values may include dividends or earnings that are not guaranteed and will change. Please see your financial professional for more information.

[4] Death benefit proceeds are generally income tax-free as provided in Internal Revenue Code Section 101(a). There are some exceptions to this general rule, including certain changes in ownership, and payments of additional earnings on the death benefit that accrued subsequent to the death of the insured are generally subject to federal income tax.

WHY THE RIGHT CHOICE IS PRUDENTIAL

The company you purchase your insurance and financial products and services from is just as important as the products themselves.

When you buy your products from The Prudential Insurance Company of America or one of its affiliates, you can be assured that you are with a company that is dedicated to helping you and your business achieve your financial security goals. Your financial professional can work with you and your professional tax and legal advisors to help ensure continued success for your business.