Morgan Stanley

# Nonqualified Deferred Compensation Plans

Bolster your benefits program with a powerful vehicle to help attract and retain key employees. Nonqualified Deferred Compensation Plans offer a valuable and flexible wealth planning vehicle for executives and other highly compensated key employees. Whether exploring a new plan or evaluating an existing one, there are best practices and important considerations to keep in mind.

## Participant Eligibility

While Nonqualified Deferred Compensation Plans are typically offered to highly compensated executives, employers have a great deal of flexibility when deciding which employees to include. It is important to define your goals and ensure that the participants selected can drive desired performance and behavior for your company.

**KEY QUESTIONS:**

Do key employees face limits when contributing to your 401(k)?

Are there key populations that you want to recruit, retain and/or reward?

What are the objectives of the plan and what behaviors do we want to drive?

Considering your goals, who should be included in the plan?

## Deferral Sources

Typically, participants can defer traditional sources of income such as salary, commissions, annual incentives and bonuses. However, other sources such as long-term incentive plans, company match and company contributions with vesting can be tied to performance criteria, offering a powerful incentive.

**KEY QUESTIONS:**

Are plan goals and desired performance being realized?

Are vesting schedules being properly used?

How can voluntary and company contributions be maximized?

How is the company match being allocated?

Is company match being optimized for key employees?

## Distribution Options

With highly flexible distribution options, Nonqualified Deferred Compensation Plans offer executives an important wealth planning vehicle.

Participants can choose to take distributions when they retire, separate from service or while they are still employed. They can also customize their distributions with installments to help them meet specific financial goals such as college funding.

**KEY QUESTIONS:**

Can distributions be elected by plan year?

Does the plan allow for installments?

Does the plan allow distributions to be taken while still employed by the company?

Is there a retirement or qualifying definition for installments, and how does that affect the plan and participation?

## Investment Management

While investment choices offered in a Nonqualified Deferred Compensation Plan can mirror those in your 401(k) plan, some investments may not be appropriate due to the possibility of a lump sum distribution and shorter time horizons that are typical for Nonqualified Deferred Compensation Plans. Because of this, it is a good practice to consider investments specifically for your plan. As with a 401(k) plan, investments should be evaluated and monitored for performance and expenses.

**KEY QUESTIONS:**

How do your funds perform?

Are the expense ratios in your funds in line with industry standards?

If target date or lifestyle funds are offered, are they appropriate for the plan's design and population?

Do your participants have the necessary information and assistance to evaluate funds to make good investment choices?

## Education and Communication

Nonqualified Deferred Compensation Plans have many considerations for participants. From the mechanics of how they work, to understanding how they can be used as a valuable wealth management tool, your executives need education that addresses all aspects of participation and planning.

**KEY QUESTIONS:**

What financial education programs are currently available at your company?

How do you currently communicate with your executive population?

What are the financial educational needs of your executives?

What are the wealth planning needs of your executives?

## Informal Funding Strategies

Ongoing evaluation of your informal funding strategy is crucial. Items that should be considered include the corporate cost of the plan, deferral and distribution rates, cash flow and earning impacts, asset and liability management and security.

**KEY QUESTIONS:**

What is your company's short- and long-term tax rate?

What is the cost of capital?

What are your plan's deferral and distribution levels?

Does your company have P&L sensitivity and/or exposure?

What are your funding target levels?

What is the overall administration and funding expenses?

Investments in target-date funds are subject to the risks associated with their underlying funds. The year in the fund name refers to the approximate year (the target date) when an investor in the fund would retire and leave the workforce. The fund will gradually shift its emphasis from more aggressive investments to more conservative ones based on its target date. An investment in a target date fund is not guaranteed at any time, including or after the target date. These funds are based on an estimated retirement age of approximately 65. Should you choose to retire significantly earlier or later, you may want to consider a fund with an asset allocation more appropriate to your particular situation.

**Investors should carefully consider the investment objectives, risks, charges and expenses of a mutual fund before investing. The prospectus contains this and other information about the mutual fund. To obtain a prospectus, contact your Financial Advisor or visit the mutual fund company's website. Please read the prospectus carefully before investing.**

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