

Executive Benefits: When Is Enough, Enough?

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A DIVISION OF
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Agenda

- Welcome
- Overview of executive benefits
- Overview of compensation
- Key concepts for developing compensation
- Next steps
- Q&A



Executive Benefits: The Basics

- Benefit plans are designed to attract, retain and reward senior executives
- Pay for performance and longevity
- The ability to provide supplemental retirement benefits to key executives with minimal impact on the Credit Union's earnings
- NCUA guidelines/benchmarks on "fair and reasonable" and "safety and soundness"

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Executive Benefit Plans

- Deferred Compensation
 - 457(b), 457(f), and 409A
- Welfare Benefit
 - Split Dollar
- Section 162 Bonus
 - Deferred Compensation and Welfare Benefit

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Compensation Package

- Systematic approach to providing monetary value to employees in exchange for work performed
- Achieves several purposes assisting in recruitment, job performance, and job satisfaction

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Compensation Components

1. Base salary – competitive to market and considers experience, skills, success
2. Bonus/incentives – engage and focus
3. Benefits
4. Perquisites

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Common Misconceptions

- My CEO has been here a long time and wouldn't leave
- My CEO is happy here and wouldn't leave
- My CEO's salary and benefits are already excessive – it's more than my own retirement package
- There isn't anywhere else for my CEO to go
- My CEO is well-taken care of

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Consequences

Paying Too Little

Risks starving the credit union of critical managerial talent

Paying Too Much

Wastes assets and risks embarrassing the board and sowing discord among employees and with members

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How do we know if a benefit is too little or too much?

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Three Key Concepts

A successful compensation package incorporates these key concepts:

1. Fair and reasonable compensation
2. Shortfall analysis
3. Compensation philosophy

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Fair and Reasonable

Federal Credit Union Act

Board provides for hiring and compensation
of officers and employees

12 U.S.C. § 1760(c)(12)

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Fair and Reasonable

Reasonableness

- Federal Credit Union's size and financial condition
- Employee's duties

NCUA Reg. §701.19(a)

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Fair and Reasonable

Examiner's Guide

- Generally hands off
- Unless not safe and sound

NCUA Examiner's Guide, p. 7-22.

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Fair and Reasonable

Unsafe and Unsound

Compensation arrangements that significantly exceed compensation paid to persons with similar responsibilities and duties in other insured credit unions of similar size, in similar locations, and under similar circumstances, including financial health and profitability.

Examiner's Guide at 7-22 to 7-23

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Fair and Reasonable

Similarity

- Responsibilities / duties
- Credit union size
- Location
- Circumstances

NCUA Examiner's Guide, p. 7-22.

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Shortfall Analysis

- Projection of what benefits might be payable during retirement years
- Evaluate actual vs. projected percentage of retirement income
- If percentage of salary falls short, need to look at non-qualified executive benefit plans

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SHORTFALL ANALYSIS SUMMARY


Hypothetical Illustration for Sample Credit Union

Values are based on current assumptions. Actual results may vary

COMPENSATION		EXISTING BENEFIT PLANS				RETIREMENT			SHORTFALL	
Current Salary (\$)	Final Salary (\$)	Employer Social Security (\$)	Employer 401(k) (\$)	Total Existing Benefits (\$)	Total %	Goal Total %	Total Annual Benefit (\$)	Shortfall %	Split-Dollar Annual Shortfall Amount (\$)	457(f) Alternative Lump Sum Distribution (\$)
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
200,000	436,575	26,412	101,828	128,040	29.33%	65.00%	283,774	35.67%	\$155,733	\$1,992,954


Sample Executive, Age 50, Current Age 50, Retirement Age 65, 20 Retirement Benefit Years

- The report is based on values provided by the credit union as of 1/1/2016.
- (2) Final Salary: Future compensation is based on a 5% annual infator.
- (3) Employer Social Security: The full estimated monthly benefit according to the online social security quick calculator is \$4,402, * 12 months/year = \$52,624, divided by 2 to get the employer portion only = \$26,412.
- (4) Employer 401(k): 12/1/15 prior balance = \$500,000; monthly contributions projected as 4% of salary; 5% interest; 2031 based on 1 month from 1/1/31 to 1/1/31; Annual Benefit = $-Pmt((1+5\%)^{12}-1)/5\%$ monthly rate, 20 payout years * 12 months, \$1,300,559 retirement balance, \$0 fv, begin of month payments * 12 months = \$101,628
- (5) Total Existing Benefits = (3) + (4)
- (6) Total % = (5) / (2)
- (8) Total Annual Benefit = (2) * (7)
- (9) Shortfall % = (7) - (6)
- (10) Split-Dollar Annual Shortfall Amount = (8) - (5)
- (11) 457(f) Alternative Lump Sum Distribution = Present Value of 20 Years of (10), Discounted @ 5%



Compensation Philosophy

Is compensation an expense or an investment?



Compensation Philosophy

- Mission statement for your compensation program
- Benchmarks the competitive market and sets target percentiles for high performers, those meeting expectations, and new hires
- Strategic roadmap and consistency
- Due diligence

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Resources

- Industry surveys
- Best practices
- Compensation consultant
- Executive benefits consultant

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Pulling It All Together

- Did you educate the board and executives?
- Have you performed due diligence?
- Have you documented the process and results?

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When Is Enough, Enough?

- The answer is different for each credit union and each executive
- Compensation needs to be regularly reviewed
- Salary and benefit discussions can be difficult and awkward – use education, data, and transparency
- Consultants help maintain objectivity
- Benefit administration provider ensures performance and compliance

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Questions?

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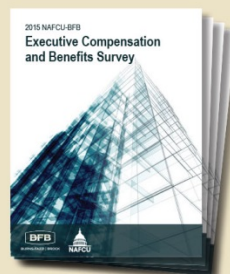
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