



Controlled Executive Bonus Plan

Typical questions about the plan:

Q: Is it legal?

A: Yes (IRC Sec. 162 and Reg. Section 1.61-22(b)(5)).

Q: Is IRS approval required to use it?

A: No.

Q: Is discrimination acceptable as to which non-shareholder executives are included?

A: Yes, just one executive can be selected. (The benefit can also be used selectively with key independent contractors associated with the firm.)

Q: What range of years is typically designated for the repayment feature?

A: Any range desired. For example: five years, 10 years, even retirement, or an event like reaching a revenue or sales goal.

Q: What is the source of funds for repayment?

A: Plan values. If they are insufficient, the executive covers the shortfall. That is the point of the program -- to induce retention of a valuable executive's services.

Q: What if the executive dies or becomes disabled during the repayment period?

A: The repayment is waived.

Q: Is the benefit and potential recovery covered in legal documents?

A: Yes, and they must be approved by the participants' legal and tax advisers and signed by the employer and the executive.

Q: Can an executive refuse to participate?

A: Yes; however, a refusal to participate may be an indication that the executive is considering leaving the firm. Contingency plans can be made accordingly.

Q: What about executives who own a small amount of stock -- can they be included?

A: Yes.

Q: Is the benefit appropriate for a sole shareholder-executive or several shareholder-executives with significant ownership interests?

A: Yes, but in most of these cases, the benefit should not include the cost recovery feature as there is typically no reason to penalize these executives in this way.

Q: Does the benefit work for members of an Advisory Board (like a Board of Directors)?

A: Yes, but the benefit generally would not include the cost recovery feature.

Q. What business entities can utilize the benefit?

A. C Corporation, S Corporation, Limited Liability Company, Partnership, and Tax Exempt Organization.

Q: Are there any special considerations for tax exempt organization?

A: Yes. Due to its tax exempt status, the employer's funding is not deductible, but it is recoverable on a tax free basis from a terminating executive. With these organizations, there is also an issue of *excess benefit transactions* that should be analyzed to determine that overall benefits, along with other compensation and benefits, are not excessive. Executives of such organizations are entitled to receive special benefits, and so as long as the plan provides a reasonable level, it should be relatively easy to validate its use. The fact that funding is recoverable should help in this evaluation.

Tax exempt hospitals, in particular, need to be careful when considering this benefit for doctors who are independent contractors so as not to run afoul of the Medicare-Medicaid Anti-KickBack and Stark II rules. Such rules do not generally apply to doctors who are employees of a hospital.

Q: Can this plan be used for officers and directors of public corporations?

A: Yes. While Sarbanes-Oxley's prohibition against loans to such individuals applies to Loan Regime Split Dollar, a Controlled Executive Bonus Plan should be acceptable.

Important Notice

The information in this Blog is presented for educational purposes only. In all cases, the approval of the participants' legal and tax advisers must be secured regarding the implementation or modification of any planning technique as well as the applicability and consequences of new cases, rulings, or legislation upon existing or impending plans.

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