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Navigating the Executive Benefits Landscape
with The Todd Organization

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Deferred Compensation Grows in Importance with Rising Tax Rates

With higher personal tax rates now in effect for 2013, corporate sponsors have a crucial opportunity to let their key employees know about the tax savings and other benefits that non-qualified deferred compensation plans provide.

Deferred compensation plans help key employees accumulate savings for retirement and other needs. The plans usually postpone and reduce overall taxes as executives draw upon these funds when retired or otherwise in a lower tax bracket.

Corporate sponsors, working with plan providers, can demonstrate to plan participants that deferred compensation is a valuable tool that has been provided to help meet the challenges key employees face. For many such employees, those challenges just became more problematic with the federal income tax increase.

Among the near-term steps that plan sponsors can take are the following.

- ***Review the plan to know when deferral decisions can be made or changed.*** Many executives have already been asking about this information. The corporate sponsor can provide an important service by publicizing the upcoming deferral deadline dates.
- ***Assess how executives are being impacted by the tax rate changes, and communicate potential opportunities to offset the increased tax impact with greater use of deferred compensation.*** While each executive's situation is different, it is helpful and illustrative to offer a few general examples of how deferred compensation plans can reduce their tax burden. We offer such examples below and encourage you to share them.
- ***Encourage executives to check retirement goals and needs annually.*** This should be a regular practice, with opportunities provided to executives to make such assessments. Executives should also be encouraged to evaluate where funds are invested and how they are performing.

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Deferral Strategies with Higher Tax Rates

Below are the 2013 tax rates for executives who are married and file joint tax returns.

Tax Rate	Income -- Married Filing Jointly
25%	$72,500-$146,399
28%	$146,400-$223,050
33%	$223,050-$398,350
35%	$398,350-$450,000
39.6%	$450,000 and up

A highly effective deferral strategy is to set aside all income above a certain tax rate into deferred compensation plans.

- For example, if a married joint filer with income in excess of $450,000 defers enough compensation so that their taxable income is reduced to less than $398,350, they will avoid the highest marginal tax brackets of 39.6% and 35%. Their highest marginal bracket will instead be 33%.
- If a married joint filer with income in excess of $250,000 defers enough compensation so that their taxable income is reduced to less than $223,050, their highest marginal tax bracket will be 28%, which applies to income from $146,400-$223,050.

Regardless of tax filing status, though, many executives earning more than $125,000 annually find it advantageous to make contributions to deferred compensation plans.

A summary of the higher federal tax rates is also provided below.

Summary of Higher 2013 Tax Rates

The key tax rate changes impacting executives since January 1, 2013 are the following.

- The top federal income tax rate has increased to 39.6% from 35%. For single filers the 39.6% tax rate applies to income that exceeds $400,000 and for joint filers income that exceeds $450,000.
- The tax rate on capital gains and qualified dividends for the above earners increased from 15% to 20%.

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- There also is an additional 3.8% tax on dividends and capital gains that applies to individual filers earning more than $200,000 and joint filers earning more than $250,000. This is a provision of the Affordable Care Act, often referred to as Obama Care.
- Under the Affordable Care Act, the Medicare tax rate on compensation income for high-income taxpayers increased from 1.45% to 2.35%. This also applies to wages above $200,000 for single filers and $250,000 for joint filers.

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