Life

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Executive Retention+

A whitepaper and overview of a life insurance strategy designed to help strengthen employee loyalty and support long-term business goals.

Why this matters now

Business owners are a growing segment of the high-net-worth marketplace.[1] Their needs are multi-faceted: protect their company, ensure a smooth succession, and reward and retain their best employees.

When job satisfaction drops, the risk of turnover rises. Today:



Only 50% of workers feel committed to staying with their current employer in the short- or long-term. [2]



20% of workers are actively seeking a new position [2]



The rest are "in the middle"—open to new opportunities but not actively looking. [2]

It's this middle group—key employees who could be swayed by the right offer—that can keep business owners up at night. And for these top performers, compensation matters to many:

91% of employees rank salary among their top five reasons to stay.[3]

Top-performing employees are crucial to a company's success. Losing them can have significant financial and operational consequences.

Traditional executive benefit arrangements, such as nonqualified deferred compensation, are still viable but have faced increased regulation, scrutiny and cost over the last two decades.[4] Executive bonus plans are simpler to administer, but they provide limited control and no cost recovery.

Executive Retention+
can be the ideal tool for business owners seeking to protect their company while ensuring their key employees are rewarded for their efforts.

The overlap of business owner concerns and employee expectations provide an opportunity for a new, flexible solution—one that can:

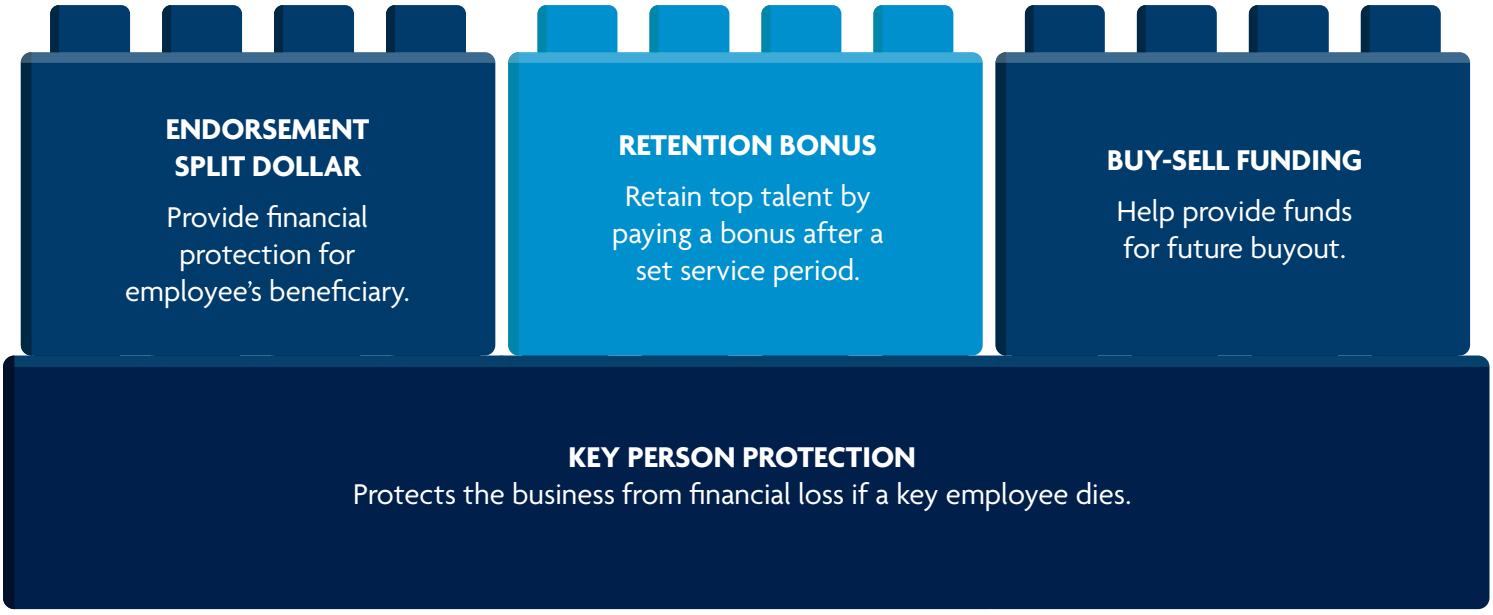
- Avoid the cost and complexity of traditional deferred compensation plans.
- Retain the simplicity of bonus arrangements.
- Give business owners control to customize benefits for their key people.

Another alternative?

An Executive Retention+ arrangement may offer that solution. It ties key employees to the business with a tangible benefit while sidestepping regulatory and cost challenges of traditional Employee Retirement Income Security Act (ERISA) plans.[5]

Setting up the arangement

Let's build the arrangement, block by block. Start with the base: key person protection. Then add any needed blocks — endorsment split dollar, retention bonus, buy-sell funding — to fit your clients' goals. It's all built around a single employer-owned permanent life insurance policy, whose death benefit and cash value support each component.



Key person protection

Goal: Protect the business from financial loss if a key employee dies.

The business owns, pays for, and is the beneficiary of a permanent life insurance policy[6] on the key employee. If that employee passes away, the policy provides funds that company can use to cover costs and recruit a replacement.

Coverage for a key person is typically based on a multiple of earnings or a discounted business value approach. **An added advantage:** The policy's cash value appears as a balance sheet asset, with cost recovery through death benefit proceeds.[7]





Endorsement split dollar

Goal: Cost recovery for the business and help provide financial protection for the employee's beneficiary.

In an endorsement split dollar arrangement, the employer continues to own the policy and pays the premium. The employee is insured but can now designate a beneficiary for a portion of the death benefit. The employer retains rights to the policy's cash value and to recover at least premiums paid, while the employee is taxed only on the economic benefit of their share.[8] For the employee, the after-tax cost of this financial protection is often less than if the employee was to personally purchase the same amount of term life insurance.

If the insured passes away during the agreement, both the employer and the employee's beneficiary receive their respective portions of the death benefit, generally income-tax free. This approach provides valuable death benefit protection for the employee's beneficiary while still reimbursing the company for its investment.

Retention bonus

Goal: Incentivize the employee to stay with the company long term

The business purchases a life insurance policy on its key employee. The business is the owner, payer, and beneficiary. The employer agrees to pay the key employee a lump-sum bonus after a set service period—of 10–25 years.[10] This is the period when the split dollar agreement (if any) is generally terminated. The payment can then be made from company funds, by accessing the policy's cash value, or by transferring the policy itself to the employee. The bonus may be a fixed dollar amount or a multiple of final salary, and it is *only* paid if the service requirement is met.



At payout, the employer receives a tax deduction, and the employee reports the bonus as income. This mirrors the tax treatment of a traditional deferred compensation plan.[10] [11] If the policy itself is transferred, the employee can access its cash values and name their own beneficiary. [12] Keep in mind any gain in a transferred contract will be taxable to the employer. Lastly, the employer may choose to structure the policy as paid-up before the service period ends, creating the most flexibility in deciding how to meet the lump sum obligation.

A key compliance point: the lump sum must be paid within 2½ months after the close of the tax year in which the employee qualifies. This ensures the arrangement avoids treatment under Internal Revenue Code (IRC) Section 409A deferred



Buy-sell funding

Goal: Support business succession by helping enable key employees to purchase the company.

Some business owners envision a key employee as their successor. But these employees often don't have the cash to buy the company outright. By the time a retention bonus is paid—or a policy ownership is transferred—the employee may now have funds available to use as a down payment toward a buyout.

Additional amounts can be financed through an installment note, with the policy's death benefit offering protection if the buyer passes away before completing payments.

A properly drafted buy-sell agreement is essential to help with a smooth and legally sound transfer. When aligned with Executive Retention+, it can provide both the business and key employees with a clear succession pathway.

An example of the Executive Retention+ in action

A business owner of a privately held company wants to keep her top executive for the long term. She implements an Executive Retention+ arrangement with a 15-year service period ending December 31, 2040.

Here's how it plays out:



During the service period

- The company owns a permanent life insurance policy insuring the top executive.
- Through an endorsement split dollar arrangement, the executive's beneficiary gets a portion of the death benefit, while the company retains the rest for cost recovery.
- The executive pays income tax each year on the value of his death benefit coverage.



At the end of 15 years

- If the executive is still with the company, the business owner awards him a lump sum bonus. This bonus can be paid by transferring ownership of the policy to the executive.
- By paying the bonus within 2½ months after year-end, the arrangement avoids IRC §409A deferred compensation rules.
- The company gets a tax deduction for the bonus; the executive reports it as taxable income.[14]



After the transfer

- The executive now owns the policy outright. The executive can:
  - Keep the death benefit protection for their beneficiary.
  - Access the cash value for a multitude of personal needs, including generally tax-advantaged retirement income and education funding.[15]
- If the cash value of the policy doesn't fully meet the lump sum agreement, the company can use other company assets to make up the difference.[16]
- The business owner may choose to issue another bonus (aka "double bonus") to help cover the executive's taxes.

What if the executive leaves early?

If the executive doesn't complete the service period, the company keeps full ownership of the policy—no bonus is paid.

A perfect prospect

Business owners who...

- Seek to provide key employees both **death benefit protection and retirement.**
- Desire **tax-advantaged reimbursement** for loss of a key employee.
- Are comfortable providing an executive a **robust future bonus** after conclusion of a predetermined service period.
- Have a need for **agreed lump sum to be applied towards a future buyout** by a key employee.
- Wish to **avoid the complication** of more established arrangements by aiming to **retain control** of the life insurance policy as a **corporate asset**.

Conclusion

Executive Retention+ can offer a cost-effective, flexible approach to executive benefits and business succession. By letting business owners select what best fits their goals, the strategy creates a compelling way to retain and reward key employees.

When structured properly, it combines the advantages of traditional agreements with a straightforward, customizable incentive that business owners and employees can easily understand.

For financial professionals, Executive Retention+ can be a practical addition to the executive benefit toolkit—one that can help strengthen client relationships and support long-term business success.

Help business owners keep their best employees with Executive Retention+

[1] Cerulli, U.S. High-Net-Worth and Ultra-High-Net-Worth Markets 2024 The Great Wealth Transfer: Capturing Money in Motion, 45% of advisors' clients are business owners or high net worth executives. pg. 139.

[2] LIMRA 2025 BEAT Study: Benefits and Employee Attitude Tracker, Kim Landry, Figure 22, pg. 32.

[3] Ibid, Figure 26, pg. 36.

[4] If a nonqualified deferred compensation plan violates Internal Revenue Code (IRC) Section 409A, the deferred amounts are treated as income to the service provider in the year they cease to be subject to a substantial risk of forfeiture. This means the employee may have to pay income tax on compensation they haven't received yet. A 20% penalty tax is applied to the portion of the deferred compensation that is includible in income due to the violation. The service provider is also subject to an increased interest rate on the late payment of the income tax due on the deferred compensation. This interest is calculated at the underpayment rate plus 1%. While the penalties primarily fall on the service provider, the employer may also face penalties for failing to properly withhold and report taxes related to the deferred compensation.

[5] Employee Retirement Income Security Act (ERISA) of 1974. To ensure compliance, a Top Hat letter should be filed with the Department of Labor when the plan is established. By limiting this benefit to this select group of management or highly compensated employees, the employer can avoid excess exposure to ERISA guidelines. When ascertaining the eligible group, generally not more than 10%-15% of the total number of employees should be included in the plan.

[6] To ensure that the death proceeds of an employer-owned policy can retain its tax-free treatment, it is essential to comply with the requirements of IRC Section 101(j). for business owned policies. A carrier will often require a Notice and Consent Form and sometimes other documentation authenticating the authority of the business owner to make decisions regarding the life insurance contract.

[7] The insurance premiums are a non-deductible expense by the employer.

[8] The measure of the value of life insurance protection provided under endorsement split dollar plans utilizes Table 2001 rates.

[9] This plan is designed to qualify as an exception to the definition of deferred compensation under IRC Section 409A regulation 1.409A-(b)(4). Failure to pay the bonus before the end of this period may result in significant income tax consequences, penalties and interest.

[10] It is important for employers and executives to seek advice from their tax and legal advisors whenever a split dollar plan is terminated. In addition to potential income tax issues to the parties, transfer of a policy may raise transfer-for-value issues under IRC Section 101.

[11] Any formal agreement in advance to forgive the future bonus will subject this arrangement to deferred compensation treatment under 409A.

[12] It is critical that the arrangement be funded adequately and contain enough cash to meet the lump sum obligation. A clearly drafted bonus agreement will avoid potential uncertainty over expected benefits.

[13] To qualify for the exception, the payment must be required to be made and must be made on or prior to the 15th day of the 3rd month following the end of the employer's tax year in which the right to the payment vests. In other words, no longer subject to what employee benefit practitioners refer to as a substantial risk of forfeiture. Note: If no payment date is specified, the exception still qualifies if the payment is made during the period.

The short-term deferral rule is often referred to as an exemption to Section 409A, but it is distinguishable from the special exemptions because a severance payment that meets the requirements of the short-term deferral rule does not constitute deferred compensation under Section 409A.

[14] 26 U.S. Code §162(a)(1) There shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered.

[15] Distributions are generally treated first as tax free recovery of basis and then as taxable income, assuming the policy is not a Modified Endowment Contract (MEC). However, different rules apply in the first fifteen policy years, when distributions accompanied by benefit reductions may be taxable prior to basis recovery. Non-MEC loans are generally not subject to tax but may be taxable when the policy lapses, is surrendered, exchanged or otherwise terminated. In the case of a MEC, loans and withdrawals are taxable to the extent of policy gain and an additional 10% tax may apply if taken prior to age 59½. Always confirm the status of a particular loan or withdrawal with a qualified tax advisor. Cash value accumulation may not be guaranteed depending on the type of product selected. Investments in variable life insurance are subject to market risk, including loss of principal.

[16] If the policy value does not align with the value of the promised bonus, the employer is still obligated to provide the agreed upon bonus. Other employer funds may be used to make up for the difference. Alternatively, if agreed to in advance, the entire lump sum promise can be met by the employer using outside funds. In this scenario the policy can be held onto as a balance sheet asset and any future death proceeds remaining tax-free to the business.

Neither Midland National nor its agents give tax advice. Please advise your customers to consult with and rely on a qualified legal or tax advisor before entering into or paying additional premiums with respect to such arrangements.

As independent financial professionals, it is up to you to choose whether any of the sales concepts contained in these materials might be appropriate for use with your particular sales strategy and clients. Please note that Midland National does not require you to use any of these sales concepts; they are resources that can be used at your option for your own individualized sales presentations if appropriate for the particular client and circumstances.

Under an endorsement split dollar arrangement, the employee enters into an agreement with their employer. Midland National is not a party to this agreement and Midland National's only obligation is to administer the policy it issues consistent with the policy's terms and conditions.

Under an endorsement split dollar arrangement, the value of the life insurance afforded the employee is taxable to the employee. The employer should provide the employee with tax reporting based on requirements specified in the tax code. The parties to the endorsement split dollar arrangement should seek their own independent legal and tax advice as to whether and how to enter into an endorsement split dollar arrangement based on the employer's and employee's unique circumstances.

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