Why a SERP Still Makes Sense

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Recruiting, retaining and motivating vital employees is a constant concern for companies regardless of the economic and regulatory climate. In the area of human resources, hiring and retaining quality employees has always been a top priority. The challenge remains as to how to reward key players in a way that aligns with the company's long-term strategic goals.

There are a multitude of reward and retention strategies available and the company must weigh the options carefully. Many companies fall into the trap that their pay and benefit strategies must link incentives to multiple metrics. While complex programs look good on paper, they are often not implemented and communicated properly. Overly complicated strategies tend to blur the ultimate objectives and either fail or produce unintended harmful results.

> ***"Fools ignore complexity. Pragmatists suffer it. Some can avoid it. Geniuses remove it."*** **-- Alan Perlis, Famous Computer Scientist**

Sometimes simplicity makes sense. One retention and reward plan that companies have used for many years is simple in its design and simple to understand, the Supplemental Executive Retirement Plan (SERP).

What is a Supplemental Executive Retirement Plan (SERP)?

A supplemental executive retirement plan is a deferred compensation agreement between the company and the key executive whereby the company agrees to provide supplemental retirement income to the executive and his family if certain pre-agreed eligibility and vesting conditions are met by the executive. A typical example of a plan would provide the executive a retirement benefit from all employer provided retirement benefit plans equal to 70% of the executives high three year average compensation payable for ten to fifteen years after retirement. The total retirement benefits from traditional sources, such as a 401k plan and social security, typically fall short of the 70% compensation level. The SERP, in this example, is used to fill in that shortfall, or gap. At retirement, the company determines the level of benefits paid from all other retirement benefit plans and any shortfall will be paid as supplemental income by the company to the key executive based upon the terms of the agreement.

SERPs are relatively easy to implement and require no IRS approval or involved administration. The company can select the executives it wants to reward with supplemental benefits, as long as the executive belongs to a select group of management or highly compensated employees. When the supplemental income benefits are paid to the key employee, the company gets a tax deduction. The retentive qualities of SERPs are simple, yet effective; the company can design any type of vesting schedule so if the executive leaves the company prior to retirement, he may get a portion of his benefit or nothing at all. Also, there is no third-party protection of an executive's benefits if the company fails, incenting the executive to maintain and protect the financial health of the company at his retirement and beyond (through his retirement payment stream).

Why a SERP Still Makes Sense *(Cont.)*

The retirement of baby boomers is creating a void that needs to be filled by younger talent. Due to higher taxes and increasing restrictions on qualified retirement plans, meaningful retirement income has become a top priority for emerging executives. A properly designed SERP answers this need and can be an essential component in any recruiting and retention strategy. A disadvantage to a SERP plan is that the company must accrue a liability and can only deduct expenses related to the plan when the benefits are paid. While simple in concept, they can be customized to provide different metrics and benefit levels consistent with the plan sponsor's objectives without added complexity or promotion of risky behavior.

Retaining good people is just as difficult as it has ever been. Replacing a key executive is significantly expensive, but the intangible costs associated with lost leadership and delays in achieving a company's strategic goals, is immeasurable. The traditional SERP provides a simple, clean plan with known, achievable goals and is proven to be a successful recruiting and retention vehicle.

About the Author

John has almost thirty years of experience in the executive benefits area. From 1997 through 2004 he was the President and Chief Executive Officer of a nationally recognized executive benefit organization. John then co-founded GW Financial, a company that assists corporations, banks and individuals in establishing and implementing retirement programs and insurance investments. Having completed hundreds of corporate engagements and board presentations, he is uniquely prepared to deal with the specific nuances that accompany each client engagement. John is a registered representative with M Holdings Securities, Inc. He is a current member of AALU. John is a member of various state banking associations and The Financial Managers Society.

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