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Short-Term & Long-Term Incentive Plans

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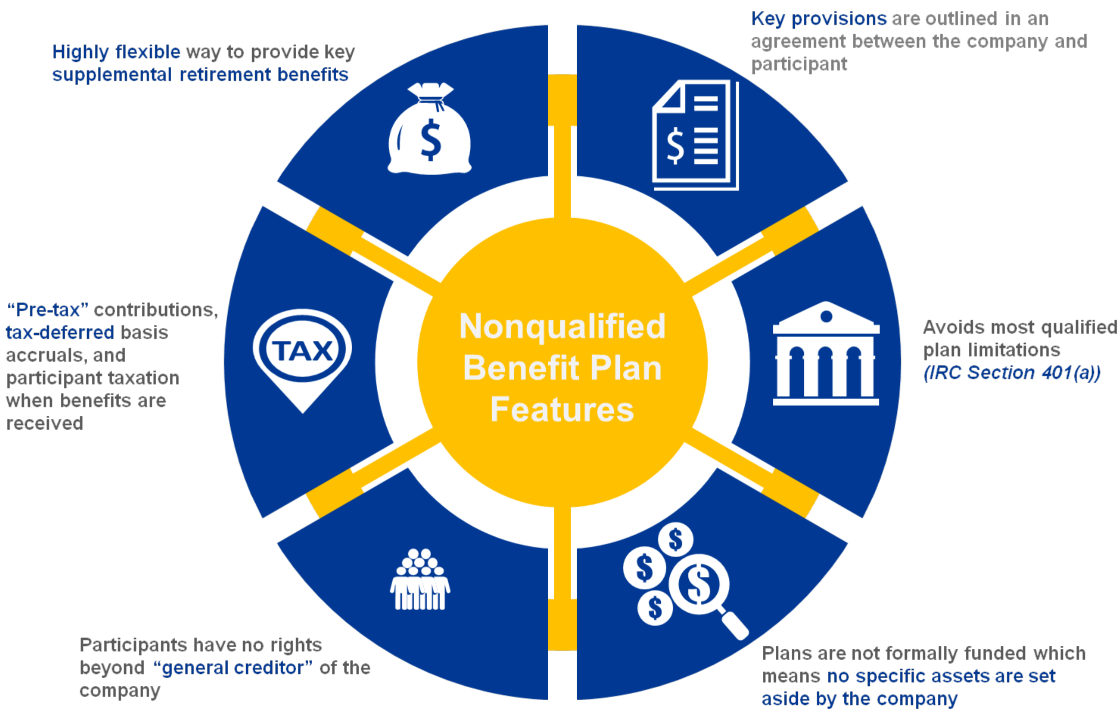
The "Why" for Nonqualified Benefit Plans

Nonqualified benefit plans are implemented to recruit, retain and reward key employees. Properly implemented plans motivate and reward employees to work towards common company goals while retaining employees with a long-term outlook. These plans enable companies to provide appropriate retirement benefits with a more targeted and efficient use of benefit dollars. There are a few different plans to consider when looking at a nonqualified retention plan. These include: Short-Term Incentive Plan (STIP), Long-Term Incentive Plan (LTIP), Supplemental Executive Retirement Plan (SERP), Voluntary Deferral Plan and a Split Dollar Plan. Specifically, we will be focusing on ***Short-Term and Long-Term Incentive Plans*** providing an overview of each plan, advantages and a sample design structure.



Short-Term and Long-Term Incentive Plans

The best way for these plans to recruit, retain and reward your employees is implementing both an STIP and LTIP. The two plans complement each other and can be very effective if designed properly. STIPs should be used to motivate key employees to execute the company goal's and make good operating decisions to maximize performance over the course of the year. LTIPs are developed to achieve long-term growth and increase the value of the organization over a long period of time. These plans are not governed by the Employee Retirement Income Security Act of 1974 (ERISA). They are simply bonus plans for key employees.

Objectives of Incentive Plans

- Offer a reward for exceeding set goals
- Provide a market-competitive cash compensation opportunity
- Assist in recruiting and retaining key employees critical to the company's success
- Support and reward the achievement of the company and individual results
- Build a strong, performance-based culture across the company

Short-Term Incentive Plan

The objective of an STIP is to reward key employees for their individual contribution for achieving the company's short-term business strategies and goals set by the compensation committee to increase the company's profitability. This plan is similar to a cash incentive plan. STIP metrics are determined by a compensation committee and can be measured both financially, such as revenue growth or maximizing profit or non-financially, with goals that align with the company strategy, such as meeting safety or quality assurance hurdles or the development of a new product.

Employer Benefits of STIPs:

- Provides greatest "pay for performance" flexibility
- Each contribution has its own vesting schedule (i.e. 5 year rolling vesting)
- Plan costs are offset indirectly through increasing profitability

Employee Benefits of STIPs:

- Participant is rewarded based on a percentage of base pay (i.e. 5% to 25%) being contributed on a pre-tax basis
- Contributions grow on a tax-deferred basis tied to a fixed or variable rate index (selected by the employer)
- Distributions at the end of each vesting cycle provide employee a meaningful payout while employed making the benefit more relevant than a retirement-based benefit

A Short-Term Incentive Plan rewards key employees for their individual contribution for achieving the company's short-term business strategies and goals.

EBN EXECUTIVE BENEFITS NETWORK insights

Sample Case Study: Short-Term Incentive Plan for Future Leaders

Scenario:

- CEO and Board have identified several key individuals to be future leaders of the bank
- Bank is in a competitive urban marketplace, where retention is a challenge and recruiting key talent is equally as hard
- Company pays competitive salary and cash bonuses, but has no long-term retention plans in place for this group
- Traditional deferred compensation programs have little power for this group due to the number of years they have to wait to receive the funds

Assumptions:

Annual Employer Contribution:
$10,000 (10% of pay)

Cost of Living Adjustment:
3%

Annual Interest Crediting Rate:
4.5%

Vesting Schedule:
4-year rolling vesting

Benefit Payout:
Lump Sum

End of Plan Year	1	2	3	4	5	6	7	8	9	10
1	$10,000	$10,450	$10,920	$11,412						
2		$10,300	$10,764	$11,248	$11,754					
3			$10,609	$11,086	$11,585	$12,107				
4				$10,927	$11,419	$11,933	$12,470			
5					$11,255	$11,762	$12,291	$12,844		
6						$11,593	$12,114	$12,660	$13,229	
7							$11,941	$12,478	$13,039	$13,626
8								$12,299	$12,852	$13,431
9									$12,668	$13,238
10										$13,048
Payout Amount	**$0**	**$0**	**$0**	**$11,412**	**$11,754**	**$12,107**	**$12,470**	**$12,844**	**$13,229**	**$13,626**
Unvested Balance	**$10,000**	**$20,750**	**$32,293**	**$33,262**	**$34,259**	**$35,287**	**$36,346**	**$37,436**	**$38,559**	**$39,716**

Employer Contribution

Benefit paid out first of the year after 4-year vesting

Serves as a Golden Handcuff

Long-Term Incentive Plan

Similar to an STIP, the purpose of an LTIP is to reward and retain key employees providing to the company's achievement in their goals and objectives. LTIPs are focused on the company's long-term goals and accomplishments. Typically, LTIPs are a mix of equity (ie. stock options, performance shares, etc.) and a cash component. This plan allows the key employee help achieve the performance goals of the company in order to earn more for themselves in either compensation or stock in the future.

LTIP's are beneficial for those key employees who are loyal to the company in hopes that they will stay for years. The drawback of an LTIP is that if the benefit is so far out, it appears to be unreachable to that key employee. They may find another opportunity that has a more immediate compensation payout.

Employer **Benefits of LTIPs**:

- Contributions are pre-tax and all account values grow on a tax-deferred basis
- Vesting reduces costs on short-term participation
- Plan costs are offset indirectly through increased profitability
- Provides greatest "pay for performance" flexibility
- Employer can determine an annual interest crediting rate to be added to the account values

Employee **Benefits of LTIPs**:

- Employer provides personal wealth accumulation
- Executives are financially rewarded for contributing to company's success
- Provided with a meaningful supplemental retirement benefit

Long-Term Incentive Plans allow key employees help achieve performance goals of the company in order earn more for themselves.

Sample Case Study: Long-Term Incentive Plan for Future Leaders

Scenario:

- CEO and Board have identified several key individuals to be future leaders of the bank
- Company is in a competitive urban marketplace, where retention is a challenge and recruiting key talent is equally as hard
- Company pays competitive salary and cash bonuses, but has no long-term retention plans in place for this group
- Company wants to provide their future leaders an extra retirement benefit

Assumptions:

Annual Employer Contribution:
$10,000 (10% of pay)

Vesting Schedule:
0% Years 1-5; 10% per year after

Cost of Living Adjustment:
3%

Benefit Payout:
Paid out in 10 equal annual installments

Annual Interest Crediting Rate:
4%

Employer Contribution

	Projected Salary	10% Employer Contribution	Annual Benefit Accrual	Benefit Payment	Projected Account Balance	Vested Account Balance	Unvested Account Balance
1	$100,000	$10,000	($10,000)	$0	**$10,000**	**$0**	**$10,000**
2	103,000	10,300	(10,707)	0	**20,707**	**0**	**20,707**
3	106,090	10,609	(11,453)	0	**32,160**	**0**	**32,160**
4	109,273	10,927	(12,238)	0	**44,398**	**0**	**44,398**
5	112,551	11,255	(13,064)	0	**57,462**	**0**	**57,462**
6	115,927	11,593	(13,934)	0	**71,395**	**7,140**	**64,256**
7	119,405	11,941	(14,849)	0	**86,245**	**17,249**	**68,996**
8	122,987	12,299	(15,812)	0	**102,057**	**30,617**	**71,440**
9	126,677	12,668	(16,826)	0	**118,883**	**47,553**	**71,330**
10	130,477	13,048	(17,891)	0	**136,774**	**68,387**	**68,387**
11	134,392	13,439	(19,012)	0	**155,785**	**93,471**	**62,314**
12	138,423	13,842	(20,189)	0	**175,975**	**123,182**	**52,792**
13	142,576	14,258	(21,427)	0	**197,402**	**157,921**	**39,480**
14	146,853	14,685	(22,728)	0	**220,130**	**198,117**	**22,013**
15	151,259	15,126	(24,094)	0	**244,224**	**244,224**	**0**
16	155,797	15,580	(25,530)	0	**269,754**	**269,754**	**0**
17	160,471	16,047	(27,037)	0	**296,791**	**296,791**	**0**
18	165,285	16,528	(28,620)	0	**325,411**	**325,411**	**0**
19	170,243	17,024	(30,282)	0	**355,693**	**355,693**	**0**
20	175,351	0	(13,690)	(39,613)	**329,770**	**329,770**	**0**
21	180,611	0	(12,487)	(43,215)	**299,043**	**299,043**	**0**
22	186,029	0	(11,236)	(43,215)	**267,064**	**267,064**	**0**
23	191,610	0	(9,933)	(43,215)	**233,782**	**233,782**	**0**
24	197,359	0	(8,577)	(43,215)	**199,144**	**199,144**	**0**
25	203,279	0	(7,166)	(43,215)	**163,095**	**163,095**	**0**
26	209,378	0	(5,697)	(43,215)	**125,577**	**125,577**	**0**
27	215,659	0	(4,168)	(43,215)	**86,531**	**86,531**	**0**
28	222,129	0	(2,578)	(43,215)	**45,894**	**45,894**	**0**
29	228,793	0	(922)	(43,215)	**3,601**	**3,601**	**0**
30	235,657	0	(0)	(3,601)	**0**	**0**	**0**
		$251,169	**($432,147)**	**($432,147)**			

Employee Benefit

Retention Component

Conclusion

In order to implement one of these plans, the company has to determine its overall goals and objectives. This will help determine if both an STIP and LTIP would work for their company, or if only one would be necessary. In order to determine which may be best, consider the following:

- What are competitors offering?
- What are the ages and generations of your key employees?
- What attracts your employees to the company?
- What are your key employees future goals with the company?
- Do your key employees appear loyal and satisfied with the company?

As mentioned, STIPs and LTIPs compliment one another by providing a 'reachable' incentive coupled with a longer term incentive.

About Executive Benefits Network (EBN):

As the leading industry advisor, EBN specializes in the customized design, administration, and informal financing of Nonqualified Executive Compensation and Benefit Plans (Deferred Compensation Plans), as well as the procurement of Bank Owned Life Insurance (BOLI) programs to attract, retain, and reward key executive talent. We emphasize the importance of education and build long-lasting relationships with clients in all 50 states, and we have access to the highest rated insurance companies in the nation. Lastly, we believe that no two companies are alike in their needs; therefore, customization of executive benefit and compensation plans is paramount to a successful program.

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