

Executive bonus plans

Allianz Life Insurance Company of North America



An executive bonus plan can help you reward and motivate your key employees, while providing a tax deduction for your business.

Bonus plan basics

Section 162(a)(1) of the Internal Revenue Code allows businesses a tax deduction for salaries or other compensation as “reasonable allowances for personal services actually performed.”

Certain executive bonuses are included in this definition of “reasonable compensation,” which is why they’re sometimes called Section 162 executive bonus plans.

Such bonuses are generally deductible by an employer according to the same rules as other forms of cash compensation – although, no deduction is generally allowed for compensation in excess of \$1 million.

Options for structuring a bonus plan

Many businesses choose to pay their bonuses in cash, but you might consider offering your key people other choices. One option could involve using part – or all – of their bonus to purchase needed life insurance. Here’s how it works:

Under the executive bonus plan, the employee purchases (and owns) a cash value life insurance policy. The employer then uses the bonus to pay the entire policy premium directly to the insurance company.

The premium payment is reported as “other compensation” on the employee’s W-2 statement. (This compensation is subject to Social Security (FICA) taxes, as well as Federal Unemployment (FUTA) tax.) Because the bonus is reported as compensation, you can deduct it as a business expense under Section 162(a)(1).

Why not just buy a life insurance policy?

Life insurance premiums are not tax-deductible to the employer if an individual life insurance policy is purchased. (Life insurance premium is a tax-deductible business expense only when group term life insurance is purchased for all qualified employees.)

By contrast, when your employee uses a bonus to buy a life insurance policy, as explained above, the premium can be tax-deductible for your business, since it’s considered compensation.

The benefits of Section 162 plans

Executive bonus plans benefit your employees by helping them feel valued and appreciated. If the executive bonus is used to purchase life insurance for your employee, it can also offer many other tangible benefits, by:

- Providing needed coverage at little or no cost to the employee
- Offering an income-tax-free death benefit for their beneficiaries
- Becoming a potential source of retirement income

But executive bonus plans can also benefit you. In addition to the tax advantages described above, an executive bonus plan can help your business attract and keep top talent. And remember that, as a business owner, you can set up an executive bonus plan for yourself, too – so you can enjoy the same tangible benefits as your employees.

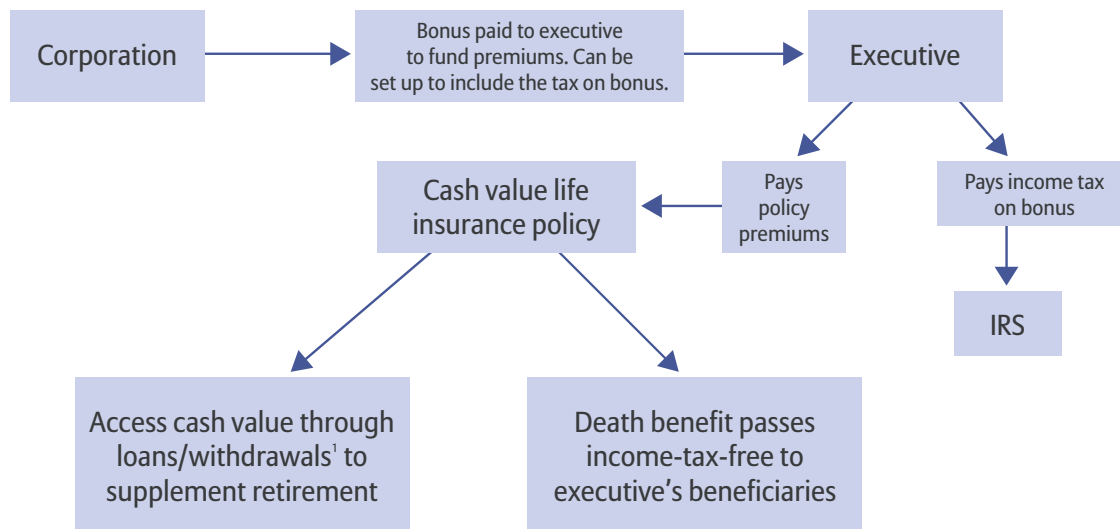
Ready to set up an executive bonus plan?

Executive bonus plans are straightforward to set up. There are no government reporting costs, and a written agreement is usually not required because the executive owns the policy, and the employer has no rights or benefits in the policy.

Executive bonus plans are also flexible. You can decide who will receive this benefit, and in what amount. You can tie the bonus to company performance or to individual goals, and you can start or discontinue an executive bonus plan at any time. The bonus paid to the executive can also be set up to include the tax incurred on the bonus.

However, you should consult with an attorney and an accountant before you set up any new employee plan, including an executive bonus plan.

Executive bonus plans, at a glance



Life insurance provides a death benefit – and so much more. Look beyond the death benefit and see how your insurance can be “bigger than life.”

Call your financial professional today to learn more about how life insurance can be an important part of your business plan.

Allianz. Financial solutions from A – Z.®

¹ Policy loans will reduce available cash values and death benefits and may cause the policy to lapse, or affect guarantees against lapse. Additional premium payments may be required to keep the policy in force. In the event of a lapse, outstanding policy loans in excess of unrecovered cost basis will be subject to ordinary income tax.

Please note that loans and withdrawals may be subject to regular income tax and, if taken prior to age 59½, a 10% federal tax penalty may apply.

This piece is designed to provide general information on the subjects covered. Pursuant to IRS Circular 230, it is not, however, intended to provide specific legal or tax advice and cannot be used to avoid tax penalties or to promote, market, or recommend any tax plan or arrangement. Please note that Allianz Life Insurance Company of North America, its affiliated companies, and their representatives do not give legal or tax advice. You are encouraged to consult your tax advisor or attorney.

Guarantees are backed by the financial strength and claims-paying ability of Allianz Life Insurance Company of North America.

Products are issued by Allianz Life Insurance Company of North America, 5701 Golden Hills Drive, Minneapolis, MN 55416-1297. 800.950.1962 www.allianzlife.com