



Executive Bonus Plans

Funding insurance policies with a company bonus

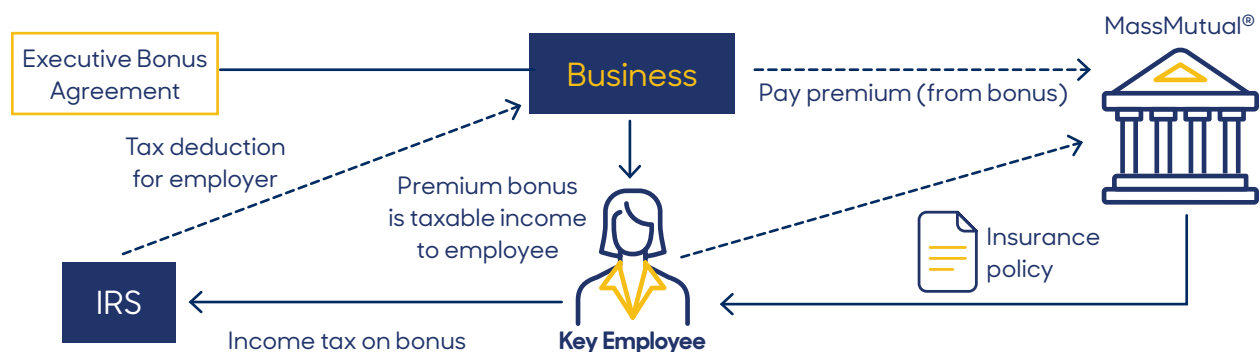
An executive bonus plan allows employers to offer a valuable insurance benefit to key employees to provide an incentive for them to remain with the company. Executive bonus plans are attractive because:

- The employer can be selective as to which employees to include in the plan.
- The employer receives a tax deduction when making bonus payments to pay insurance premiums on policies that benefit their key employees.
- Life insurance coverage, as well as disability income insurance, are perceived as valuable benefits by employees because these policies provide income protection for their families in the event of premature death or a disability.
- An Executive Bonus Plan requires minimal administration and cost, unlike a qualified or nonqualified retirement plan.
- The employee owns the insurance policy outright and names the beneficiary of the policy.
- The policy is also portable when the employee leaves the company.
- **The employer can use an executive bonus plan as an incentive to keep key people from leaving during a period in which the business owners are trying sell the business or merge with another company.**

Tax-Deductible Compensation. The bonus, whether paid by the employer in cash to the employee, or as a premium payment direct to the insurance company, is considered compensation that is generally tax-deductible to the company, subject to the limits under IRC Section 162. The bonus is subject to payroll taxes and withholding and must be reported on the employee’s Form W-2.

Double Bonus Option. The employee must pay income tax on the bonus. However, the company may provide an additional bonus to the key employee to account for the income tax due. Such an arrangement is referred to as a double bonus plan and is included as a feature when the employer wants to minimize the out-of-pocket costs to the employee.

HOW AN EXECUTIVE BONUS PLAN WORKS



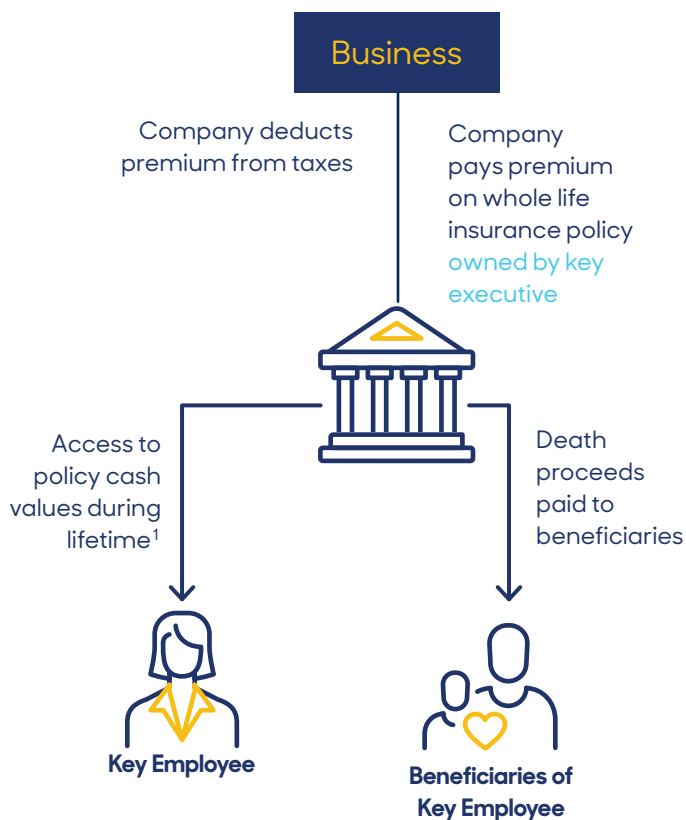


Insurance

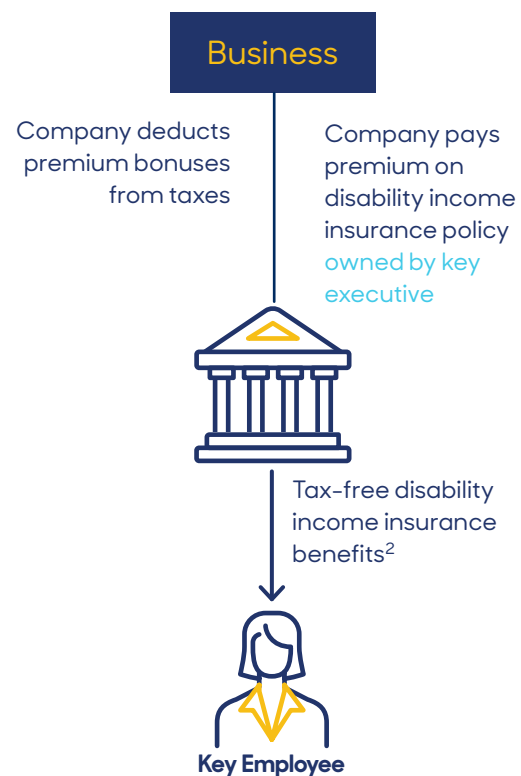
Tax-advantaged Benefits. Executive Bonus Plans are established by companies as an executive incentive benefit for key executives to cover a life insurance need, and/or a disability income need. In both cases, the bonus of the premium by the company to the executive on a life insurance policy and/or a disability income insurance policy, are tax deductible to the employer, and offer tax-advantaged policy benefits to the executive.

- **Life Insurance Benefit.** If the employee dies during the working years, the net death proceeds of the life insurance policy are paid to the beneficiaries named on the executive's policy. Otherwise, when the employee retires, the policy cash values can be used at retirement by the employee to supplement retirement income, with any net death benefit transferring to beneficiaries at death.¹
- **Disability Income Insurance Benefit.** If the employee becomes disabled (as defined by the policy), monthly disability benefits are paid to the employee from the insurance company to help the employee meet financial obligations during the period of disability (limited to the terms of the policy).

LIFE INSURANCE



DISABILITY INCOME INSURANCE



¹ Distributions under the life insurance policy (including cash dividends and partial/full surrenders) are not subject to taxation up to the amount paid (cost basis). If the policy is a Modified Endowment Contract, policy loans and/or distributions are taxable to the extent of gain and are subject to a 10% tax penalty. Access to a whole life insurance policy's cash values through borrowing or partial surrenders will reduce the policy's cash value and death benefit, increase the chance the policy will lapse, and may result in a tax liability if the policy terminates before the death of the insured.

² Disability income insurance payments are generally tax-free when after-tax dollars are used to pay the premiums.



Life Insurance

Life Insurance Case Example. Assume Jonathan is owner of Tiger Corporation. Jonathan wants to offer an executive bonus plan to his key employee, Don Perry, in which he funds annual premiums on a whole life insurance policy on Don's life. Don is owner of the policy and designates his wife as beneficiary of the policy. Jonathan's advisor illustrates a MassMutual WL10 because of the cash accumulation it offers as a retirement supplement. Distributions can be taken from the policy cash values on a tax-advantaged basis to supplement income at retirement.¹ During the working years, Don will have valuable life insurance coverage. The below example includes policy details and the net cost to the company (after deduction savings) of offering an Executive Bonus program:

Male, Age 30, Non-Tobacco, Ultra Preferred Risk
Whole Life 10 Pay Life Insurance Annual Premium: \$53,490
Initial Death Benefit: \$1M

EMPLOYER COST OF OFFERING WHOLE LIFE POLICY					EMPLOYEE BENEFITS FROM WHOLE LIFE POLICY		
YR	Annual double bonus by employer ³	Cumulative bonuses paid by employer	Cumulative tax deduction for employer @30% tax ⁴	Cumulative net out of pocket cost to employer	Annual premium paid	Total cash value end year	Total death benefit end year
1	\$71,320	\$71,320	\$21,396	\$49,924	\$53,490	\$19,730	\$1,005,137
10	\$71,320	\$713,200	\$213,960	\$499,240	\$53,490	\$580,820	\$1,276,472
11	—	\$713,200	\$213,960	\$499,240	—	\$612,965	\$1,323,928
25	—	\$713,200	\$213,960	\$499,240	—	\$1,288,912	\$2,185,855

At age 65 (year 35), Don can potentially distribute \$162,734 per year through his age 85 as tax-free supplemental retirement income by taking distributions up to cost basis in the policy (cumulative premiums paid), followed by taking tax-free policy loans thereafter.¹ The tax equivalent amount of \$162,734 based on a 25% tax rate is \$216,978.

Potential Distributions
 Years 35-55
 (Age 65-85)
 \$162,734/year

³ Assumes a double bonus and that Don has an effective income tax rate of 25% for purposes of calculating the double bonus amount.

⁴ It is assumed that the company is a pass-through entity and that its effective tax rate is 30%. The information provided is not written or intended as specific tax or legal advice. MassMutual, its subsidiaries, employees and representatives are not authorized to give tax or legal advice. Individuals are encouraged to seek advice from their own tax or legal counsel. Individuals involved in the estate planning process should work with an estate planning team, including their own personal legal or tax counsel.



Disability Income Insurance

The above example is a supplemental life insurance illustration and is not valid unless accompanied by or preceded by a Whole Life 10 Pay basic illustration. Refer to the Basic Illustration for guaranteed elements and other important information. Click here for the Basic Illustration: [Illustration 1](#) [Illustration 2](#)

These illustrated amounts are not guaranteed. They include dividends, which are neither estimates nor guarantees, that have been applied to purchase paid-up additions based on the 2022 dividend schedule. The dividend schedule is reviewed annually, and it is likely that dividends in future years will be lower or higher depending on the Company's actual experience. For this reason, we strongly recommend that you look at a lower dividend schedule illustration. Refer to the Basic Illustrations for guaranteed elements, assumptions, explanations, and other important information.

Disability Income Insurance Case Example. Assume Jonathan also offers a Disability Income Insurance policy as a benefit to Don Perry. Below are the details of the Disability Income Insurance policy and the net cost of the Executive Bonus program to the company:

Male, Age 30, Non-Nicotine, Occ Class 5P, Current Income/Salary: \$131,244
Disability Income Insurance Annual Premium: \$2,479.51
Annual Disability Benefit: \$84,000 with 3% COLA⁵

YR	EMPLOYER COST				EMPLOYEE BENEFITS
	Annual Bonus by employer	Cumulative bonuses paid by employer	Cumulative tax deduction for employer @30% Tax Rate ⁴	Cumulative net out of pocket cost to employer	Annual Disability Income Benefit Being Purchased ⁵
1	\$2,479.51	\$2,479.51	\$743.85	\$1,735.66	\$84,000
10	\$2,479.51	\$24,795.10	\$7,438.53	\$17,356.60	\$84,000

This presentation is not valid unless accompanied by a Radius Choice® Disability Income Insurance Illustration Summary. Refer to the Illustration Summary for monthly benefit, premium, specific policy details and other important information. This presentation is for informational purposes only. Actual numbers may vary based on factors such as your actual tax liability, our underwriting evaluation and any actual disability benefits you may receive from other sources. Click here for the Radius Choice® Disability Income Insurance Illustration [Illustration](#).

⁵ The disability benefit is a monthly benefit. The benefit is shown as annual for illustrative purposes only. COLA is a cost of living adjustment rider that helps benefits keep pace with inflation in the event of a disability lasting longer than 12 months. After you have been disabled for 12 months (or the waiting period, if it is longer), your benefit will be increased at an annually compounded rate of 3%, in this example. The policy duration period assumed is to age 65. Note that although the disability income benefit being purchased is \$84,000/ year, this example assumes a 12 month waiting/elimination period. Therefore, if a qualifying disability occurs in year 1, the waiting period would need to be satisfied before the benefit begins.



Disability Income Insurance

WITHOUT DISABILITY INCOME INSURANCE. If no disability income insurance is purchased as part of an executive bonus plan, and Don becomes disabled, he would need to use his brokerage account as a source of income while disabled. Assuming he becomes disabled in year 15 (age 44) and he remains disabled for 5 years, he would need to withdraw \$105,000 per year from his account, assuming a 20% effective tax rate, to net \$84,000 per year, the amount he needs to cover expenses. Assuming the brokerage account grows at 6% per year, by year 35 (age 64), he has **\$490,201** in his brokerage account.

WITH DISABILITY INCOME INSURANCE. On the other hand, if he had the disability insurance offered through an executive bonus plan sponsored by his employer, Don would have **\$1,666,277** in his brokerage account. The disability income insurance policy protected Don's brokerage account by over **\$1.1M**.

The Amount of Asset Protection the Disability Income Insurance Policy Offers Assumes disability occurs in year 15 and lasts for 5 years

YR	DISABLED – WITHOUT DISABILITY INSURANCE					DISABLED – WITH DISABILITY INSURANCE			
	Brokerage Account @6% End Year	Premium Savings @ 6% End Year	Balance of Total Accounts End Year	Taxable Income @ 20% Tax	Net Income During Disability @3%	Brokerage Account @6% End Year	Premium Cost @6% End Year ⁶	Balance of Total Accounts End Year	Potential Income from Disability Insurance ⁷
1	\$265,000	\$2,628	\$267,628	—	—	\$265,000	(\$2,628)	\$262,372	—
10	\$447,712	\$34,643	\$482,355	—	—	\$447,712	(\$34,643)	\$413,069	—
15	\$487,840	\$58,547	\$546,387	\$105,000	\$84,000	\$599,140	(\$58,547)	\$540,593	\$84,000
16	\$402,471	\$62,060	\$464,531	\$108,150	\$86,520	\$635,088	(\$62,060)	\$573,028	\$86,520
17	\$308,541	\$65,784	\$374,325	\$111,395	\$89,116	\$673,193	(\$65,784)	\$607,409	\$89,116
18	\$205,433	\$69,731	\$275,164	\$114,736	\$91,789	\$713,585	(\$69,731)	\$643,854	\$91,789
19	\$92,490	\$73,915	\$166,405	\$118,178	\$94,543	\$756,400	(\$73,915)	\$682,485	\$94,543
35	\$234,957	\$255,244	\$490,201	—	—	\$1,921,522	(\$255,244)	\$1,666,277	—

Disability Insurance protects over **\$1.1M** of Don's assets

⁶ This column reflects the annual premium payable to maintain the disability insurance policy. Premium payments are waived during disability.

⁷ This column represents the potential Disability Income benefit during a period of disability, assuming the disability occurs in year 15 for 5 years. Assumes the disability benefit includes a 3% cost-of-living-adjustment (COLA) rider. This example assumes that after being disabled for 12 months (or the elimination period if it is longer), Don's benefit will be increased at an annually compounded rate of 3%.



Insurance

COMBINED BENEFITS FOR EMPLOYER AND EMPLOYEE. The below chart demonstrates the cumulative bonuses made to Don over time by Tiger Corporation, to fund the life and disability income insurance policies as an incentive benefit. The chart combines the cumulative tax deduction received by the employer, and the benefits that both insurance policies offer Don.

Combined Life Insurance & Disability Income Insurance Values							
BENEFITS TO EMPLOYER				BENEFITS TO EMPLOYEE			
YR	Age	Cumulative bonuses paid by employer	Cumulative tax deduction for employer @30% tax ⁴	Life Insurance Death Benefit to Employee	Life Insurance Net Cash Value	Life Insurance Annual Distributions (Age 65-85) ¹	Annual Disability Income Benefit being purchased ⁸
1	31	\$73,800	\$22,140	\$1,005,137	\$19,730	–	\$84,000
10	40	\$737,995	\$221,339	\$1,276,472	\$580,820	–	\$84,000
20	50	\$750,393	\$225,118	\$1,831,990	\$990,942	–	\$84,000
30	60	\$775,188	\$232,556	\$2,606,542	\$1,671,576	–	\$84,000
34	65	\$787,585	\$236,276	\$2,867,953	\$1,991,363	\$162,734	\$84,000

For more information on how an executive bonus plan can be included in a Qualified Sick Pay plan, [click here](#).

⁸ This column represents the Disability Income (DI) benefit being purchased. This example assumes the waiting or elimination period has been satisfied. Because it is assumed that the waiting period (before benefits begin) is 12 months in this example, if disability were to occur in year 1, the actual disability income benefit payable in year 1 would be \$0. Once the waiting period is satisfied, benefits would begin, assuming the disability is ongoing.

Notes:

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