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The Resurging Interest in Bank Supplemental Executive Retirement Plans

By: *Glenn Blackwood* | APRIL 6TH, 2017

The roller coaster ride in banking over the last eight to 10 years took another unexpected turn in November with the election results. The financial sector gained new life, bank stocks soared and community banks began to see the prospect of regulatory relief becoming a reality. Interest in de novo banks has been picking up, and the likelihood of interest rate increases and decent loan demand appear to bode well for banks.

With that as a backdrop, **the need to retain key members of a bank's management team has re-emerged**. Loan demand is good, profits are rising, optimism regarding regulatory relief is growing and the need to stabilize the management team of the bank is on the front burner as the talent grab has begun to heat up. Comprehensive compensation plans that serve to retain, reward and appropriately retire management teams are back in the spotlight.

During the financial crisis, many banks maintained salaries, as well as short and long-term incentive plans. Qualified benefit plans were continued, though often temporarily curtailed. But one key element of retention and reward, non-qualified plans, were either terminated, frozen or not introduced at all. Supplemental Executive Retirement Plans, or SERPs, are some of the most common non-qualified plans. Since the financial crisis, SERPs have lately seen a resurgence due to their multi-faceted benefit to both the bank and executive.

Objectives of a SERP

1. **Retirement:** Since inception, SERPs were designed to allow the company to provide supplemental benefits to executives whose contributions to traditional qualified plans such as 401ks and profit sharing plans were limited by the Internal Revenue Service or ERISA (The Employment Retirement Income Security Act). For example, the general employee base may be able to retire with 75 to 80 percent of final salary based on income from Social Security and qualified plans while the executive team was retiring at 35 to 45 percent from the same sources. In essence, those executives were discriminated against due to the ERISA and IRS caps. SERPs bridged the gap and allowed for the bank to provide commensurate benefits to key executives.

2. **Retention:** SERPs are non-qualified plans. They do not have the restrictions of qualified plans regarding

vesting terms. As a result, the bank can structure the terms in the SERP however they desire from a vesting perspective. For example, assume an executive is to receive $60,000 per year for 15 years in a SERP. If in year five, the executive gets an offer from another bank, depending on the plan vesting, the executive may be walking away from all, or a large portion, of their SERP benefit. That's $900,000 in post-retirement income at risk. This deterrent becomes a "golden handcuff."

3. **Reward:** Banks can use SERPs whose value are determined based on performance measures. There may be a return on equity or return on assets threshold needed to get a minimum percentage of final salary from the SERP. That percentage would grow based on performance measures established in the plan.

4. **Recruiting:** SERPs provide the bank a plan that attracts talent. If the target executive is working at an institution that does not provide SERPs, the plan becomes an added attraction to joining your organization.

Other Items of Consideration

Unfunded, unsecured promise to pay: It is important to note that non-qualified plans such as SERPs are balance sheet obligations of the company and must be accrued for under generally accepted accounting principles (GAAP). The plan is an unfunded promise to pay by the bank. As a result, if the bank were to fail, the executive would lose his or her benefit. The SERP benefit is often matched up with bank-owned life insurance (BOLI) to provide income to offset the SERP accrual. This is not a formal funding of the plan, but a cost offset.

Top-hat guidelines: Executives participating in a non-qualified plan must qualify under top-hat guidelines as provided under the Department of Labor. These guidelines are murky, and consider position in the organization, compensation, negotiating ability (with the bank) and number of participants as a percentage of full-time equivalents. If there is any concern about who can participate, it is best to have legal counsel review prior to implementation.

In summary, SERPs are back in favor. The practical need for equitable retirement benefits, as well as the ability to retain, reward and recruit all have been catalysts in the resurgence of SERPs in the banking marketplace.

Glenn Blackwood, a principal at Equias Alliance, has more than 20 years of experience in the BOLI/nonqualified benefits industry. He has assisted hundreds of banks with the design and implementation of programs to recruit, retain and reward key officers and directors.