Retaining Your Key Executives

A Look at Retirement Packages and Experiences

By Bob James, CCE, CCM, CHE

During our search and consulting assignments we are often asked to advise the club on compensation packages, either to formulate an attractive package for a new manager or to evaluate whether their current manager's compensation is keeping up with the market. In either case, clubs should regularly evaluate their salary and benefits packages to ensure they can continue to *attract* and *retain* a highly skilled staff, at both the line and management levels.

Clubs that are fortunate to have long-tenured management are especially at risk of falling behind market standards for compensation and benefits. Even regular salary bumps of 3% to 5% may not be keeping up with the market, which is being driven by a shortage of talent in the greater hospitality industry. There is also the issue of fairness and equity that motivates enlightened club boards to revisit their offerings. In this article we share what we regularly see regarding retirement benefits as an important element of the total compensation package, particularly for tenured management.

This article is written from first and secondhand experiences and nothing in this article should be construed as legal or accounting advice. We appreciate club auditor's advice from Dan Condon, senior partner at Condon O'Meara, McGinty & Donnelly LLP: "Due to certain tax and regulatory issues, managers and their clubs would be well advised to consult with an experienced employee benefits attorney familiar with 501(c)(7) organizations when contemplating entering into any deferred compensation plan, including 457(b), 457(f) and supplemental executive retirement plans."

Retirement Plans

It's been slightly more than 30 years since 401(k) plans first became available to nonprofit organizations such as 501(c)(7) clubs. Previously, many clubs offered a defined benefit plan to their employees that rewarded long-tenured staff, providing for their retirement as was the standard for many businesses. To receive 60% of your salary as an annual retirement benefit was not unusual in the general business world, although private clubs often targeted somewhat less. Once 401(k)s arrived on the scene for nonprofit organizations in 1989, many clubs froze and ultimately terminated their defined benefit plans and substituted a 401(k) plan. However, the amount that a highly paid employee with or without employer contribution may contribute is limited. Consequently, some clubs also offer 457(b) or 457(f) or other deferred compensation plans to senior management to enable them to set aside higher amounts than the regulatory limits on 401(k) plans allow. These plans may have been funded by additional compensation or simply by the manager deferring part of their regular compensation. As many soon-to-retire managers have found out, there are several ways to defer compensation into tax deferred vehicles such as 401(k) accounts and 457(b) and 457(f) plans; but these are generally used to defer income over time and not as catch-up funding mechanism for large lumpsum deposits, like purchasing an annuity.

Golden Handcuffs vs. Leaving a Club Before Retirement Age

If a manager leaves a club before retirement age and is not going to another 501(c)(7), 457s may become a taxable source of income as they have to be hosted by a qualifying organization. For example, a 457(f) plan is only available to nonprofit organizations. If you must withdraw from the plan your choices are limited to taking a onetime lump sum or spread distribution out over five years. This type of plan may be useful if the manager has several years before retirement, but probably not much use on the eve of retirement as there are similar maximum annual contributions and catch-up limitations as 401(k)s.

Unfortunately, there are situations where, because of lack of planning or understanding of the tax codes, managers have been faced with lump sum distributions that they could not roll over into another tax deferred account. When those amounts are substantial, they will bump the employee's tax rate up, resulting in an extraordinarily high tax on the distribution and often hard feelings towards the club. This is something that both parties may not have been aware of but may have been avoided by proper planning!

Supplemental Executive Retirement Plan

Even the best of plans may fall behind the market over time and because of statutory limits on some plans, the benefits for senior management may actually fall behind those for the rank and file as a percentage of annual income. In many cases initial employment agreements promised the executive the same rights and benefits as afforded all staff. Might this be construed as the same percentage of salary as the staff receive or for management that initially had benefits under a defined plan? Might it be fair that they continue to accrue equal benefits from a replacement plan, after the defined benefit plan was terminated and distributed? These are arguments that we've heard raised and know that some clubs have used a Supplemental Executive Retirement Plan (SERP) to address the shortfalls.

If the club is looking to augment the executive's retirement benefits, a SERP might be a solution. SEPRs are nonqualified plans that can be set up to supplement the executive's income for a specific or indefinite number of years and within

high percentage limits of the employee's compensation. It is an enforceable contract with the club that protects the executive from some future board being able to modify or cancel the contract, which makes it an attractive plan to the employee. It need not be funded, but then auditors might consider it an unfunded liability whose present value needs to be reported on the financial statements.

Other Considerations

There are also several other options such as Simplified Employee Pension, certain permanent insurance policies, Roth 401(k)s, and others. Each plan has specific advantages and disadvantages depending upon the club's tax status, benefit options and goals of the retirement program. To determine which is right for the club and manager, considerations generally include:

- Plan eligibility requirement
- Asset ownership
- Rollover options
- Distribution options
- Risk of forfeiture from bankruptcy
- Vesting schedules

Also important to consider are the three usual events that trigger distribution:

- Disability
- Retirement
- Death of the Employee

Both the club and employee will also want to consider what benefits might still be available if the employee chooses to leave the club's employment early or is terminated before retirement. Some plans simply end in these latter two cases.

Transitioning to Retirement

To ensure a smooth transition for the club and to demonstrate appreciation, many clubs offer a continuance of pay and benefits to their retiring executive for some period after their actual retirement date. This may be particularly important to managers with personal or family medical issues who rely upon the club's health insurance plan and are not yet old enough to qualify for Medicare. Often this extension of wages and benefits is only a few months but sometimes longer.

A tenured GM we know with strong board support negotiated an agreement to retire within a couple of years, taking a cut in his annual compensation, but with the club agreeing to continue his employment on a limited (consulting) basis for several years after his actual retirement, with full benefits for that period. It is important to note that to stay on a club's medical program and continue to receive other insurance-related benefits, the "retired" employee must remain an employee of the club in some capacity, providing some measure of value, otherwise the medical coverage may be at risk. If your club is planning a large capital project, centennial celebration, tournament, history book or some other important future event whereby the club would want the manager to remain involved after retirement, that might be a reason why you would create some phase out or transition into retirement.

Other Common Retirement Benefits

It is very common that retiring managers are honored by some celebrations of their service; the club throws them a party, gives them an expensive trip or gold watch, and sends them on their way with best wishes. Occasionally, the club will collect contributions from the membership towards the manager's retirement if the manager is particularly well loved or the club's retirement program is subpar. This may be done through the business but rather a passing of the hat by the members themselves to avoid potential tax implication. This is a wonderful tribute but becoming less common. Often the club offers an honorary membership to their long tenured retiring manager. If so, it is a nice perk, but be aware that the value may be construed as taxable income each year to the manager if the club reports it or happens to be audited. An alternative may be to offer club privileges without a membership per se, but that may be less secure over time as boards and policies change.

These are a few of the scenarios clubs and retired and tenured GMs have personally shared with us over the years, mixed in with what we understand to be regulatory considerations. It is never too early to evaluate your retirement and benefit plans as costs will continue to escalate and options may grow limited. To get started, a targeted survey of compensation and benefits for comparable clubs is the most effective and reliable means to compare your package against the market and to generate ideas as to retirement benefits you might consider. Ultimately, a review and update will provide confidence to the board that the club is doing what is appropriate for your key staff and ensure their continued loyalty.

One final point, *make sure everything is put in writing*. Misunderstandings can be financially and emotionally devastating! CD

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