

UPDATING EXECUTIVE SERPS

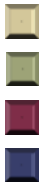
An Opportunity Under 409A Transition Rules for Funding and Securing SERPs

Today's Presenters



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The Evolution of Nonqualified Plans

How Nonqualified Plans Evolved

Over the last 20 years, corporate America implemented nonqualified (NQ) retirement plans to restore and supplement qualified plans due to government imposed contribution limitations.

Qualified Plan Limitations (\$000's)

QUALIFIED PLANS	1987	1992	1997	2002	2007
Defined Contribution Limit:	\$30	\$30	\$30	\$40	\$45
Defined Benefit Limit:	90	112	125	160	180
Compensation Limit:	200	229	160	200	225



The Evolution of Nonqualified Plans

How Nonqualified Plans Evolved *(continued)*

- Retirement Age: 65
- Total Service at Retirement: 25 Years
- DB Plan Formula: 2% x years of service (max. 25 years) x final average compensation
- Restoration Plan: 2% x years of service (max. 25 years) x final average compensation (without regard to qualified plan limitation) less qualified plan benefit
- SERP – 70% of final average compensation less restoration plan benefit less qualified plan benefit

ASSUMPTIONS

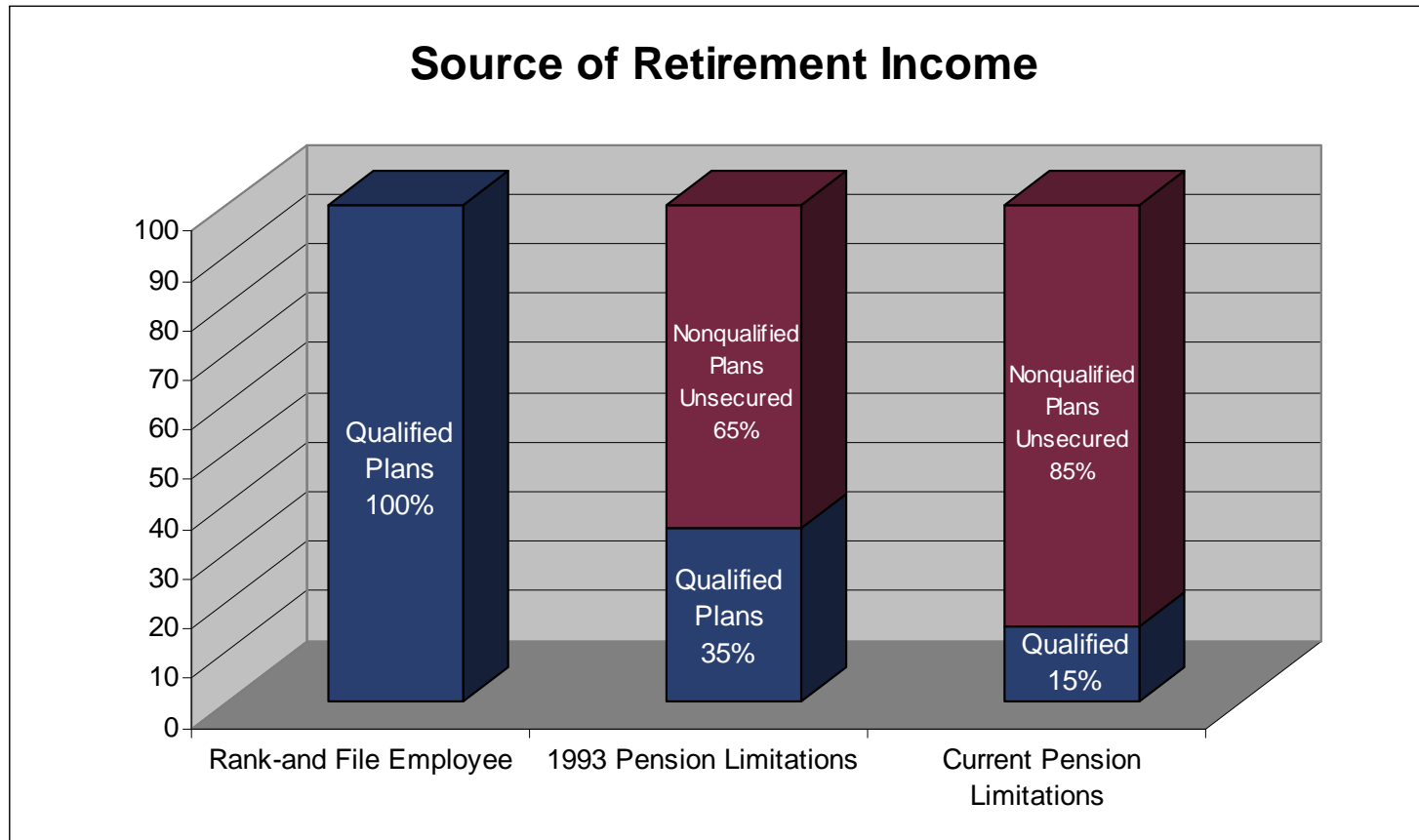
Example of Limits on Sample Client

Participant	Final Average Salary	Pension	SERP/Restoration Plan	SERP as % of Total DB Benefit
Executives				
Executive 1	\$2,000,000	\$112,500	\$1,287,500	92%
Executive 2	1,000,000	112,500	587,500	84
Executive 3	500,000	112,500	237,500	68
Executive 4	250,000	112,500	62,500	36
Rank and File				
Employee 1	100,000	50,000	0	0
Employee 2	75,000	37,500	0	0



The Evolution of Nonqualified Plans

How Nonqualified Plans Evolved *(continued)*



Note: Average Executive (male, age 50, salary \$185,000)

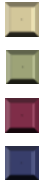


The Evolution of Nonqualified Plans

How Nonqualified Plans Evolved *(continued)*

The original premise of NQ plans was to:

1. Restore benefits and contributions
2. Defer taxation until retirement when tax rates would *presumably* be lower

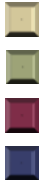


The Evolution of Nonqualified Plans

How Nonqualified Plans Evolved *(continued)*

Companies implemented variations of the following NQ plans:

- Defined Benefits Excess/Restoration Plans
- Deferred Compensation Plans
- 401(k) Excess Plans
- Split Dollar and SERP Swap Plans
- Executive Retiree Medical Funding Plans

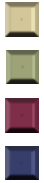


The Evolution of Nonqualified Plans

How Nonqualified Plans Evolved *(continued)*

Because these plans are unsecured, many companies chose to fund through general corporate assets or Rabbi Trusts.

In addition, many plans provided 401(k) mirror investments and companies chose to hedge investment risk with mirror funding.



The Evolution of Nonqualified Plans

How Nonqualified Plans Evolved *(continued)*

Defined benefit pension plans became a staple of corporate benefit planning. However, DB plans (and DB SERPs) began to lose favor because:

- The popularity of 401(k) plans pushed the world towards DC plans
- The volatility and financial strain of the DB approach

Consequently, many qualified plans were updated to cash balance and/or other modified DC approaches.

Nonqualified DB SERPs have not been updated per this trend.



The Evolution of Nonqualified Plans

Recent Regulatory Action

NQ plans began to attract IRS/Congressional attention because the plans:

- Were initially very limited in terms of participation, benefits, and funding
- Evolved into broad based plans with significant benefits, funding, and executive exposure to corporate risk

The NQ market became very sophisticated and progressively transferred greater control/security to executives, through:

- Hair cut provisions
- Executive discretion over distributions
- Financial triggers
- Self-directed brokerage accounts
- Offshore funding to protect against solvency risk

Such improvements to security and executive control focused more regulatory attention on NQ plans

- Enron, WorldCom, and perceived executive compensation abuses attracted greater visibility to NQ retirement plans and led directly to new regulations and legislation



The Evolution of Nonqualified Plans

Congressional, IRS, SEC, and FASB Reactions

In response to the increased versatility of NQ plans and the perceived need for intensified corporate governance, there has been a series of limitations either made or proposed:

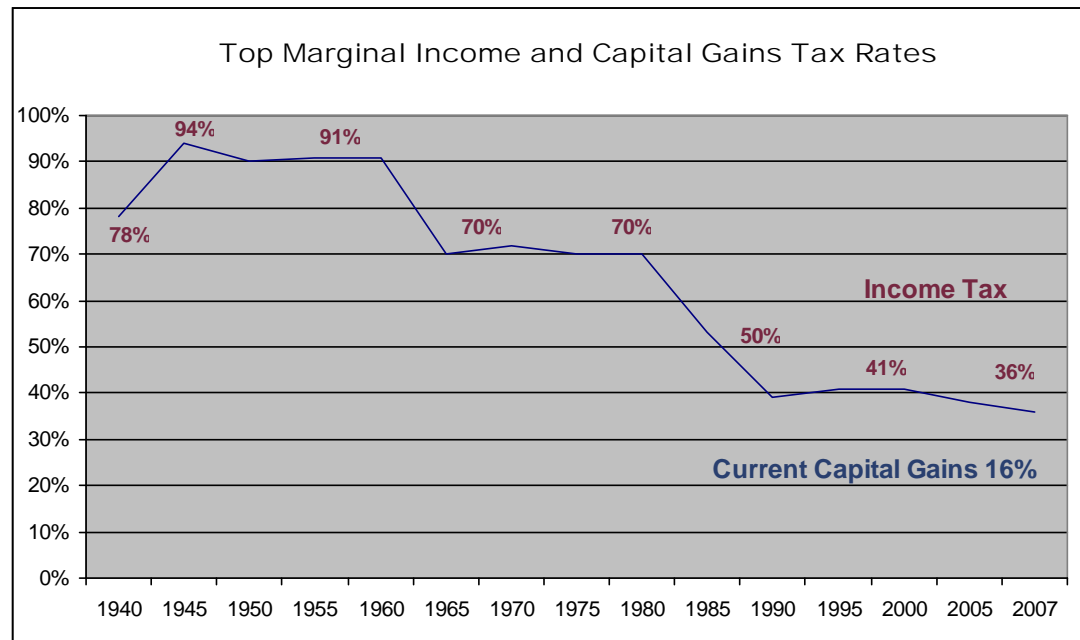
<u>Sarbanes-Oxley</u> <ul style="list-style-type: none">• No personal loans to officers• No offshore Rabbi Trusts	<u>Split Dollar Regulation</u> <ul style="list-style-type: none">• Eliminated collateral assignment• Redefined restrictive Split Dollar taxation/methodology
<u>American Jobs Creation Act: 409A</u> <ul style="list-style-type: none">• Reduced flexibility on deferral elections• No "hair cut" provisions (accelerated distributions)• Delayed payouts for key executives• Limiting financial triggers	<u>FASB/EITF Ratifications</u> <ul style="list-style-type: none">• Endorsement Split Dollar• COLI accounting• Stock Option expensing
<u>Pension Protection Act</u> <ul style="list-style-type: none">• Penalties on nonqualified funding• COLI best practices	<u>SEC</u> <ul style="list-style-type: none">• Increased disclosure requirements
	<u>Pending Legislation</u> <ul style="list-style-type: none">• New caps on NQ annual deferrals/accruals• Expansion of 162(m) limitations



The Evolution of Nonqualified Plans

The Changing Tax Environment

- ❑ A premise of most NQ plans was to defer taxation until tax rates would presumably be lower.
- ❑ Consequently, executives have assumed an over-concentration of tax rate deferral risk (assuming that current tax rates are lower than post retirement tax rates).
- ❑ Combined marginal income and capital gains tax rates are at an all-time low; if rates increase, it will likely be inefficient to currently defer into a higher future tax bracket.





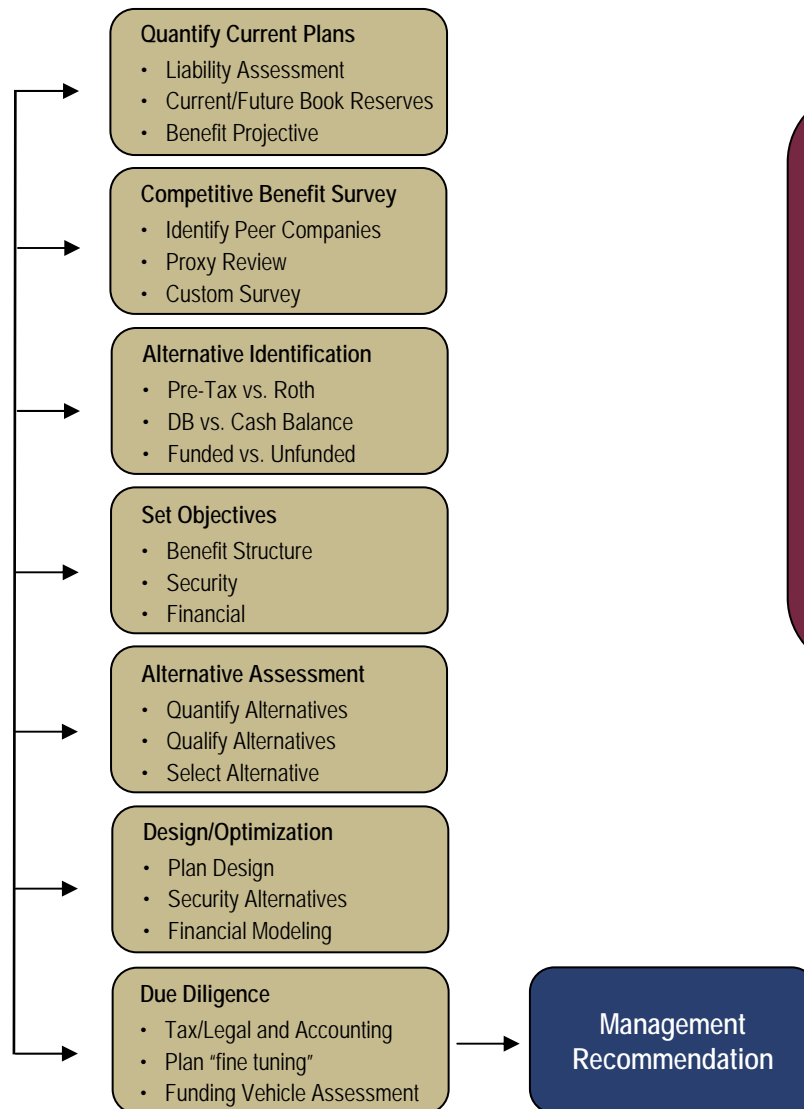
The Evolution of Nonqualified Plans

Corporate Reactions to New Environment

- Amending plans to comply with 409A (e.g., eliminating hair cut provisions, distribution discretion)
- Modifying proxy disclosure
- Eliminating and/or phasing out executive Split Dollar plans
- Eliminating qualified DB plans and analyzing what to do with nonqualified DB SERPs
- Reducing contributions to and/or eliminating Rabbi Trusts
- Analyzing methods to reduce and diversify executive tax rate deferral risk
- Implementing alternative deferred compensation plan options
- Updating DB SERPs with conversion to DC approaches and/or after-tax Executive Roth Plan options



The Evolution of Nonqualified Plans



Analytical Process

A proper analytical process can result in:

- ✓ Efficient use of company staff resources
- ✓ Proper risk assessment
- ✓ Appropriate objectives
- ✓ Selection of program that meets company and executive goals and objectives





Executive Roth Plan Details

Overview

- The Executive Roth Plan (ERP) is an after-tax funding arrangement companies are utilizing to settle existing defined benefit SERPs.

- Assets accumulating within the Executive Roth account:
 - ◆ Are bankruptcy remote
 - ◆ Have no contribution limits
 - ◆ Have no age restrictions
 - ◆ Have no early withdrawal penalties
 - ◆ Are not subject to 409A or new funding restrictions



Executive Roth Plan Details

Overview (continued)

- The Executive Roth Plan (like a qualified Roth plan) provides a hedge against increasing tax rates by:
 - ◆ Taxing the “principal” contributions now, under low current income tax rates
 - ◆ Providing tax-deferred investment earnings
 - ◆ Enabling non-taxable benefit distributions
 - ◆ And, unlike a Roth plan, providing a mechanism to restore current tax payments, keeping those dollars working in the plan

- The ERP targets the present value of the SERP at retirement

- The ERP provides a full array of capital market investment options for the company or executive to invest plan assets



Executive Roth Plan Details

Plan Details

- The company amends their existing DB SERP to schedule settlement of the plan on an annual basis over remaining working service.
- Each year, the Accumulated Benefit Obligation (ABO) will be settled on a present value basis through contributions to the Executive Roth Plan.
- Annually, company accruals will be adjusted/reversed to mirror new, reduced ABO.
- The discount rate utilized will define how favorable the settlement will be to the executive and the company. For instance, a rate lower than what was utilized for FAS87 calculations will increase the participant benefits and reduce the company's recovery of P&L accruals.
- If the company desires to retain a "hook" on participant benefits, a high discount rate and future performance-based discretionary bonuses can be utilized to adjust settlement amounts.



Executive Roth Plan Details

Plan Details *(continued)*

- Company contributions to the ERP are currently taxed to the participant and tax deductible to the company.
- To provide tax-favored accumulation and distributions, ERP balances are invested in institutional variable life insurance contracts.
- Based upon overall financial objectives (e.g. asset allocation, risk constraints, duration, liquidity), participants designate ERP investment allocations.
- Participants should designate ERP asset allocation based upon overall NQ after-tax efficiency.



Executive Roth Plan Details

Tax Restoration Feature

- At the Company's discretion, after-tax contributions to the trust can be supplemented by a tax-restoration account structured internally through the funding contract.
- This account is funded through an internal contract loan with the following features:
 - ◆ Policy loans are automatically deployed in participant-directed contract investment accounts
 - ◆ The loan charge is LIBOR + 1.5% or the Moody's Seasoned Corporate Bond rate
 - ◆ At the participant's direction, the account can be invested in any appropriate investment in the contract to generate a long-term positive investment spread above the loan rate
 - ◆ The loan is non-recourse with no required prepayment period except through policy proceeds at surrender or death and no prepayment penalty

Executive Roth Plan Details

S&P vs. Contract Loan Rate

Year	S&P 500 Index Fund Average Annual Return*	ALR Indexed Average Annual Interest**	S&P Annual Spread Over Loan Rate
1982	20.97%	14.95%	6.02%
1983	21.29%	11.95%	9.34%
1984	6.21%	13.45%	-7.24%
1985	31.23%	10.92%	20.31%
1986	18.06%	9.00%	9.06%
1987	4.71%	8.84%	-4.13%
1988	16.22%	10.18%	6.04%
1989	31.36%	9.72%	21.64%
1990	-3.32%	9.84%	-13.16%
1991	30.22%	8.60%	21.62%
1992	7.42%	6.11%	1.31%
1993	9.89%	5.49%	4.40%
1994	1.18%	7.33%	-6.15%
1995	37.45%	7.90%	29.55%
1996	22.88%	7.71%	15.17%
1997	33.19%	7.56%	25.63%
1998	28.62%	6.88%	21.74%
1999	21.07%	7.46%	13.61%
2000	-9.60%	7.99%	-17.59%
2001	-12.02%	5.86%	-17.88%
2002	-22.15%	3.64%	-25.79%
2003	28.50%	2.96%	25.54%
2004	10.74%	3.51%	7.23%
2005	4.77%	5.65%	-0.88%
2006	15.64%	6.03%	9.61%

Observation
There are years where there is a negative spread between the loan rate and the S&P 500.

This chart represents recent history of the relationship between the ALR Indexed Interest Rate and the performance of an S&P 500 Index Fund. Historical performance may not be used to predict future performance.

*Source: Vanguard 500 Index Fund; fund is available by prospectus only.

**ALR Interest Indexed to LIBOR + 1.5% (prime minus 1 prior to 1990) capped by Moody's.

Website Sources:

http://www.federalreserve.gov/releases/h15/data/Monthly/H15_AAA_NA.txt

http://mortgage-x.com/general/indexes/fnma_libor_history.asp

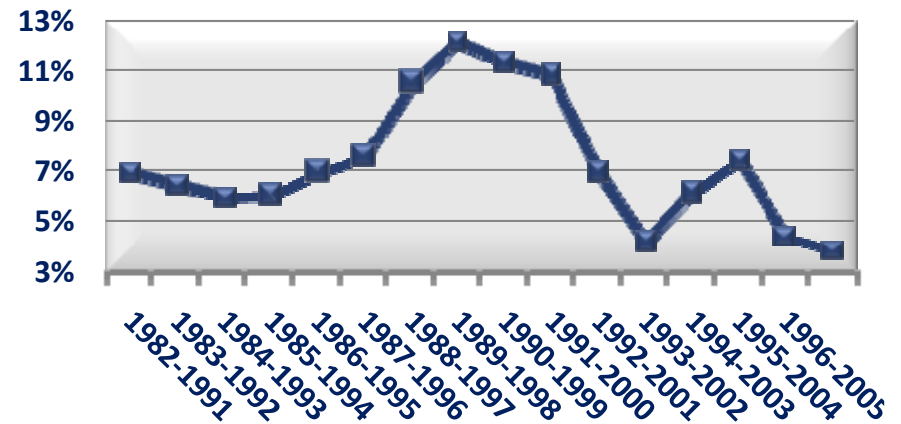


Executive Roth Plan Details

Recent History of 10-Year Average Performance of S&P 500 Index Fund Against ALR Indexed Interest	
Time Period	% Spread
Years 1982 thru 1991	6.95%
Years 1983 thru 1992	6.48%
Years 1984 thru 1993	5.98%
Years 1985 thru 1994	6.09%
Years 1986 thru 1995	7.02%
Years 1987 thru 1996	7.63%
Years 1988 thru 1997	10.61%
Years 1989 thru 1998	12.18%
Years 1990 thru 1999	11.37%
Years 1991 thru 2000	10.93%
Years 1992 thru 2001	6.98%
Years 1993 thru 2002	4.27%
Years 1994 thru 2003	6.38%
Years 1995 thru 2004	7.72%
Years 1996 thru 2005	4.68%
Years 1997 thru 2006	4.12%

This chart represents recent history of the relationship between the ALR Indexed Interest Rate and the performance of an S&P 500 Index Fund. Historical performance may not be used to predict future performance.

Historic Positive Spread: S&P Minus Annual Loan Rate



Observation
However, when looking at long-term performance, there has consistently been a positive spread.



Executive Roth Plan Details

Sample Transaction: Assumptions

SERP Formula	60% of Final Average Salary payable for 15 years certain
Executive Roth Plan Formula	Target insurance values to annually settle SERP ABO. Policy cash values are invested to provide non-taxable withdrawals and loans equal to the after-tax equivalent SERP payments. After-tax equivalence assumed at 35% retirement tax rate.
Sample Executive	Age: 53 Current Salary: \$515,967 Retirement age: 65 Projected SERP: \$476,584 per year (4% salary increase each year) Present Value of After-tax SERP at 65: \$3,376,180 (5% discount rate)
Currently Accrued SERP	\$1,735,300 Assumes reversal over remaining service. May be possible to reverse over a shorter term.
FAS87 Discount Rate	5%
Corporate Tax Rate	40%
Executive Tax Rate	Current 35% increasing to 40% after 2010
Insurance Policy Investment Return	7% net of asset management fees
Premium Payment Period	Remaining working service. Premium changes can be used to readjust funding for asset/liability matching due to changes in actuarial assumptions or investment performance.
Insurance Contract	Lincoln Variable Universal Life with Alternative Loan Rider

Executive Roth Plan Details

Executive Perspective

Age	Baseline PAYG SERP			Executive Roth Plan				
	SERP Payment	Taxes Paid	Net Benefits	SERP Settlement Bonus	Tax Paid	Net ERP Contribution	Net Death Proceeds	Net Proceeds
53	-	-	-	295,058	(103,270)	(191,788)	-	-
54	-	-	-	295,058	(103,270)	(191,788)	-	-
55	-	-	-	295,058	(103,270)	(191,788)	-	-
56	-	-	-	295,058	(118,023)	(177,035)	-	-
57	-	-	-	295,058	(118,023)	(177,035)	-	-
58	-	-	-	295,058	(118,023)	(177,035)	-	-
59	-	-	-	295,058	(118,023)	(177,035)	-	-
60	-	-	-	295,058	(118,023)	(177,035)	-	-
61	-	-	-	295,058	(118,023)	(177,035)	-	-
62	-	-	-	295,058	(118,023)	(177,035)	-	-
63	-	-	-	295,058	(118,023)	(177,035)	-	-
64	-	-	-	295,058	(118,023)	(177,035)	-	-
65	476,584	(190,634)	285,950	-	-	-	-	309,780
66	476,584	(190,634)	285,950	-	-	-	-	309,780
67	476,584	(190,634)	285,950	-	-	-	-	309,780
68	476,584	(190,634)	285,950	-	-	-	-	309,780
69	476,584	(190,634)	285,590	-	-	-	-	309,780
70	476,584	(190,634)	285,590	-	-	-	-	309,780
71	476,584	(190,634)	285,590	-	-	-	-	309,780
72	476,584	(190,634)	285,590	-	-	-	-	309,780
73	476,584	(190,634)	285,590	-	-	-	-	309,780
74	476,584	(190,634)	285,590	-	-	-	-	309,780
75	476,584	(190,634)	285,590	-	-	-	-	309,780
76	476,584	(190,634)	285,590	-	-	-	-	309,780
77	476,584	(190,634)	285,590	-	-	-	-	309,780
78	476,584	(190,634)	285,590	-	-	-	-	309,780
79	476,584	(190,634)	285,590	-	-	-	-	309,780
80	-	-	-	-	-	-	4,794,229	4,794,229
Total			\$4,289,250					\$9,440,229

Executive Roth Plan Details

Corporate Cash Flow Comparison

	Basic PAYG SERP			Executive Roth Plan		
	SERP Payment	Tax Savings	Net Outlay	SERP Settlement Bonus	Tax Savings	Net Outlay
53	-	-	-	(295,058)	118,023	(177,035)
54	-	-	-	(295,058)	118,023	(177,035)
55	-	-	-	(295,058)	118,023	(177,035)
56	-	-	-	(295,058)	118,023	(177,035)
57	-	-	-	(295,058)	118,023	(177,035)
58	-	-	-	(295,058)	118,023	(177,035)
59	-	-	-	(295,058)	118,023	(177,035)
60	-	-	-	(295,058)	118,023	(177,035)
61	-	-	-	(295,058)	118,023	(177,035)
62	-	-	-	(295,058)	118,023	(177,035)
63	-	-	-	(295,058)	118,023	(177,035)
64	-	-	-	(295,058)	118,023	(177,035)
65	(476,584)	190,634	(285,950)	-	-	-
66	(476,584)	190,634	(285,950)	-	-	-
67	(476,584)	190,634	(285,950)	-	-	-
68	(476,584)	190,634	(285,950)	-	-	-
69	(476,584)	190,634	(285,950)	-	-	-
70	(476,584)	190,634	(285,950)	-	-	-
71	(476,584)	190,634	(285,950)	-	-	-
72	(476,584)	190,634	(285,950)	-	-	-
73	(476,584)	190,634	(285,950)	-	-	-
74	(476,584)	190,634	(285,950)	-	-	-
75	(476,584)	190,634	(285,950)	-	-	-
76	(476,584)	190,634	(285,950)	-	-	-
77	(476,584)	190,634	(285,950)	-	-	-
78	(476,584)	190,634	(285,950)	-	-	-
79	(476,584)	190,634	(285,950)	-	-	-
80	-	-	-	-	-	-
Total	(7,148,760)	2,859,510	(4,289,250)	(3,540,696)	1,416,278	(2,124,420)
NPV@ 6% Gross			(2,139,171)			(1,700,723)
NPV@ 5% Gross			(2,394,273)			(1,762,206)

PRESENT VALUE ANALYSIS

Executive Roth Plan Details

Corporate P&L Comparison

Age	Baseline PAYG SERP					Executive Roth Plan				
	FAS87 Service Cost	Interest Cost	Total Accrual	Deferred Tax Savings	Net P&L Impact	SERP Settlement Bonus	Tax Savings	SERP Reversal	Reversal: SERP Def. Tax	Net P&L Impact
Prior			1,735,000	(694,000)	1,041,000					1,041,000
53	124,353	92,968	217,321	(86,928)	130,393	295,058	(118,023)	(144,583)	57,833	90,285
54	124,353	103,834	228,187	(91,275)	136,912	295,058	(118,023)	(144,583)	57,833	90,285
55	124,353	115,243	239,596	(95,838)	143,758	295,058	(118,023)	(144,583)	57,833	90,285
56	124,353	127,223	251,576	(100,630)	150,946	295,058	(118,023)	(144,583)	57,833	90,285
57	124,353	139,802	264,155	(105,662)	158,493	295,058	(118,023)	(144,583)	57,833	90,285
58	124,353	153,099	277,363	(110,945)	166,418	295,058	(118,023)	(144,583)	57,833	90,285
59	124,353	166,878	291,231	(116,492)	174,738	295,058	(118,023)	(144,583)	57,833	90,285
60	124,353	181,439	305,792	(122,317)	183,475	295,058	(118,023)	(144,583)	57,833	90,285
61	124,353	196,729	321,082	(128,433)	192,649	295,058	(118,023)	(144,583)	57,833	90,285
62	124,353	212,783	337,136	(134,854)	202,282	295,058	(118,023)	(144,583)	57,833	90,285
63	124,353	229,640	353,993	(141,597)	212,396	295,058	(118,023)	(144,583)	57,833	90,285
64	124,353	247,339	371,692	(148,677)	223,015	295,058	(118,023)	(144,583)	57,833	90,285
65		235,877	235,877	(94,351)	141,526	-	-	-	-	0
66		223,842	223,842	(89,537)	134,305	-	-	-	-	0
67		211,204	211,204	(84,482)	126,723	-	-	-	-	0
68		197,935	197,935	(79,174)	118,761	-	-	-	-	0
69		184,003	184,003	(73,601)	110,402	-	-	-	-	0
70		169,374	169,374	(67,750)	101,624	-	-	-	-	0
71		154,013	154,013	(61,605)	92,408	-	-	-	-	0
72		137,855	137,855	(55,154)	82,731	-	-	-	-	0
73		120,950	120,950	(48,380)	72,570	-	-	-	-	0
74		103,168	103,168	(41,267)	61,901	-	-	-	-	0
75		84,497	84,497	(33,799)	50,698	-	-	-	-	0
76		64,893	64,893	(25,957)	38,936	-	-	-	-	0
77		44,308	44,308	(17,723)	26,585	-	-	-	-	0
78		22,694	22,694	(9,078)	13,617	-	-	-	-	0
79		-	-	-	-	-	-	-	-	0
80		-	-	-	-	-	-	-	-	0
Total	1,492,236	5,719,514	7,148,750	(2,859,500)	\$4,289,250	3,540,696	(1,416,276)	(1,735,000)	694,000	\$2,124,420



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