



SPLIT-DOLLAR ARRANGEMENT: ENDORSEMENT METHOD USING LIFE INSURANCE



Program Highlights & Fact Finder

A Valuable Benefit for Employers and Key Executives

The endorsement method for a split-dollar life insurance arrangement is a strategy that can serve a dual purpose. It can provide employers with a valuable fringe benefit that will appeal to talented executives in the employer's field. If set up correctly, this benefit will also help ensure the executives' longevity with the company.

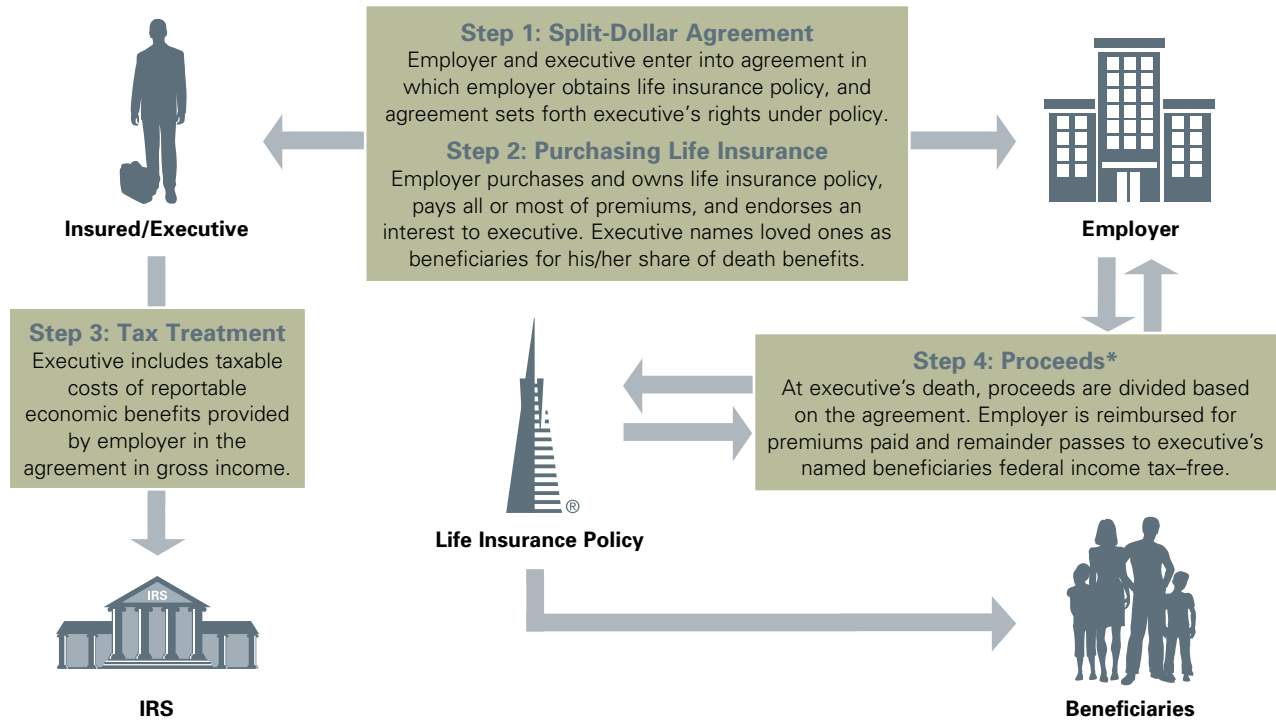
The benefit provided via the split-dollar endorsement method is attractive to executives because the life insurance offered can provide security and liquidity for their family members in the event of the executive's death. Many executives delay purchasing adequate insurance due to a need to use cash flow for other purposes. As a result, having the policy purchased by the company allows the insurance coverage to be obtained at a low cost to the executive and frees his or her assets to be invested in alternative ways.

A split-dollar endorsement arrangement also offers a method of using life insurance to retain the employer's key executives by helping them finance a policy to protect the financial needs of the executive and his or her family.

The split-dollar arrangement is an agreement between two parties—usually an employer and executive—to purchase life insurance. Using the endorsement method, the employer would purchase the policy and hold ownership of the policy. The employer would also make the premium payments due on the policy.

Typically, the split-dollar agreement would provide the executive with current life insurance protection; however, the exact division of the policy proceeds would be split between the parties as established in the agreement.

Split-Dollar Nonequity Endorsement Method



*If the split-dollar arrangement will terminate at some point during the executive's life and the policy will be rolled out to him/her, this arrangement would likely be subject to IRC § 409A tax treatment as a form of deferred compensation.

Here's How it Works

Step 1. Entering Into the Split-Dollar Agreement

- The employer and executive enter into a contractual agreement in which the employer agrees to pay all or most of the premiums and obtains a life insurance policy insuring the executive's life while the employer retains ownership of the policy.
- The agreement provides that, at the executive's death, the proceeds are split. There are several ways in which the proceeds can be split, including, for the employer, a return of premiums paid only, return of cash value only, or a return of the greater of the premiums paid or the cash value. If cash value exceeding the premiums paid is credited to the executive, then this type of agreement is called "equity split dollar." When the executive has an interest only in the death benefit and no interest in the cash value of the policy, then the arrangement is referred to as "nonequity split dollar."
- By reserving ownership of the policy, the employer is able to retain control of the policy and access to its cash value. The employer endorses a benefit under the policy over to the executive. Typically, the agreement would give the executive the right to name a personal beneficiary for the employee's share of the death benefits.
- In order to prevent the death benefits from being included in the employer's gross income for tax purposes, there are certain exceptions for which the agreement must qualify. It must also satisfy pre-issue notice and consent requirements, and the employer must follow additional annual recordkeeping and reporting obligations under IRC §§ 101(j) and 6039I.

Step #2: Premiums and Taxes

- The owner of the policy is deemed to provide a taxable economic benefit to the other party. The economic benefit may be the value of the life insurance protection (nonequity split dollar) or may include other benefits (equity split dollar).
- The executive reports the value of the economic benefits received as gross income, reduced by any amounts paid by the employee as reimbursement of economic benefit costs. The economic benefit is usually determined based upon IRS Table 2001, or an insurer's alternative term rates may be used if they meet the requirements of split-dollar regulations.
- Economic benefit costs paid by the executive to the employer are gross income to the employer.
- Premium payments made by the employer are generally not deductible by the employer.

Step #3: Accessing the Benefits

- If the arrangement is terminated due to the executive's death, then the policy proceeds are divided as specified in the agreement.
- If the employee is still alive and the employer wishes to terminate the arrangement, the employer can remove the endorsement on the policy and either continue with the policy or surrender it for its cash value.
- Alternatively, the employer may wish to pass the policy on to the executive—such as in the form of a bonus retirement benefit. In this case, the employer would roll out the policy to the executive. The executive can either purchase the policy from the employer or pay tax on the fair market value of the policy, with the employer likely receiving an income tax deduction. Once the policy has been rolled out to the executive, he or she no longer needs to report the economic benefit amounts.



What Are the Advantages?

With the Split-Dollar Life Insurance Endorsement Method, both employer and key executive benefit. Here's how:

The Employer...

- Distinguishes its compensation package to attract and retain key talent
- Provides selected employees with attractive benefits
- Retains control over the policy including all policy rights, access to cash value, and nonforfeiture privileges
- Is repaid for premiums loaned to pay for the policy at the termination of the agreement
- Is not subject to burdensome approval, testing, and discrimination requirements since the split-dollar plan is not a qualified retirement plan

The Executive...

- May be able to obtain the policy at the time the agreement is terminated by purchasing it at a fair market value, or through a transfer of ownership via a bonus or similar compensation
- May benefit from accumulated cash value, which can be accessed later for retirement needs
- Is able to obtain death benefit protection for his or her named beneficiaries
- Can use cash flow that would have been used to pay premiums for other needs
- Can likely obtain life insurance protection at a lower current out-of-pocket cost than for a personally purchased policy



Employers can help prevent a loss of their talent, executives are able to prepare for retirement and estate planning by a less costly means, and beneficiaries obtain a federal income tax-free death benefit.

Who Can Benefit from the Split-Dollar Endorsement Method?

- Employers who want to strengthen relationships with key executives
- Executives who want to provide financial security for their families in a cost-effective manner
- Employers who want to offer benefits in excess of those offered by their qualified retirement plans

What Is Being Achieved?

Using the endorsement method for a split-dollar arrangement allows for the funding of life insurance where there is a clear need for the added security and financial enhancement that life insurance provides. Using this arrangement, employers can help prevent a loss of their talent, executives are able to prepare for retirement and estate planning by a less costly means, and beneficiaries obtain a federal income tax-free death benefit.



Individually Designed Proposal

By completing the attached Fact Finder, a Transamerica life insurance professional can develop a customized proposal illustrating a split-dollar arrangement using the endorsement method.

Split-Dollar Arrangement: Endorsement Method Fact Finder

Executive

Executive Name _____ Date of Birth _____ Gender: M F
Address _____ State _____
Spouse Name _____ Date of Birth _____ Gender: M F
Retirement Age _____ Annual Retirement Income Goal _____ Payable to Age _____
Risk Status: Insured S NS Risk Classification: Select Preferred Standard
Table Rating _____ Flat Extra/Amount _____
Risk Status: Spouse S NS Risk Classification: Select Preferred Standard
Table Rating _____ Flat Extra/Amount _____
Officer of Corporation? Y N Shareholder of Corporation? Y N Percentage of Corporate Ownership _____ %
Executive Premium Share: PS58 ART Other _____
Bonus: Y N Single Double

Employer

Employer Name _____ Status: C Corp S Corp Partnership, LLC
Address _____ State _____ Number of Employees _____
Federal Tax Bracket _____ % State Tax Bracket _____ %
Premium Payment Mode _____ Solve? _____ or Amount? _____
Years of Out-of-Pocket Premium Payments _____ Rollout Year _____

Illustration

Type of Illustration: Fixed Universal Life Variable Universal Life
Product to Illustrate _____
Policy Assumptions: Current _____ Guaranteed _____ Illustrated (VUL) _____
Desired: Death Benefit \$ _____ or minimum so as not to create a MEC _____
Death Benefit Option: Level Increasing with cash value Increasing switching to Level
Plus-Premium _____
Annual Insurance Premium \$ _____
Years to pay premium _____ or to age _____
Maximize income from policy at insured's age _____ for _____ number of years
If premium is not known, indicate desired cash flow from policy beginning in year _____, and ending in year _____.
Policy cash value at 100 equal to:
Endowment at initial face _____ or keep in force until age 100 _____
or cash value equal to \$ _____

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