

SPLIT DOLLAR INSURANCE

What is it?

Split Dollar Insurance doesn't refer to a particular type of policy, but to a method of paying for the policy. In a split dollar arrangement, an employer and an executive agree to "split" both the cost (premiums) and benefits (cash-value and death benefits) of a permanent life insurance policy.

How does it work?

Three elements of a permanent insurance policy which can be split are:

1. Ownership

- Endorsement Method -- the employer owns the policy, but a written endorsement is added which splits the ownership between the employer and the executive.
- Collateral Assignment -- the executive owns the policy and assigns certain interests in the policy to the employer as collateral for payments made by the employer as outlined in the split dollar agreement.

2. Beneficiary

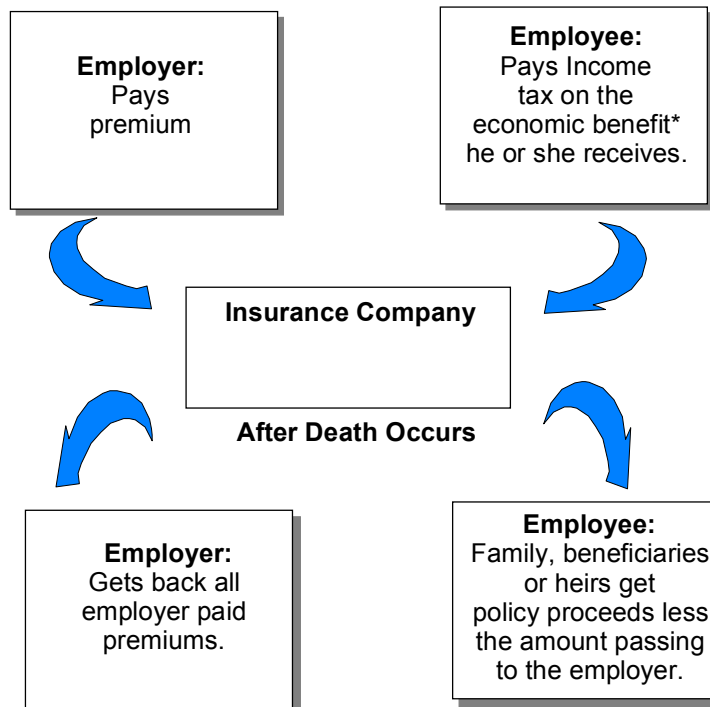
- Employer Share -- the employer receives back the cash value of the policy or total premiums paid, whichever is greater, on a tax-free basis.
- Executive Share -- the executive's beneficiary receives the balance of the policy proceeds (for example, face amount less cash values paid back to employer, on a tax-free basis).

3. Premium Payor

- Classic Approach -- the employer pays the portion of the premium equal to the increase in cash value. The executive pays the balance.
- Employer Pays All -- the employer pays the entire premium and the executive pays income tax on the economic value of the death benefit.
- Executive Bonus Plan -- the employer pays the executive a bonus which is deductible to the employer and taxable to the executive. The employer also pays the balance of the premium to the insurance company. The executive pays the economic benefit portion of the premium from proceeds of the bonus, and pays taxes on the bonus. Some plans pay a bonus to cover the tax due.

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Split Dollar Insurance Diagram *Endorsement Method*



Notes: This diagram illustrates a very basic variety of Split Dollar plan which can be modified to meet the needs of both employer and employee.

The IRS has taken the position that life insurance policies owned by the employer in an employment related Split Dollar arrangement are treated as transfers to the benefited party. If the life insurance policy is owned by the employee the premium paid by the employer is treated as a series of loans. Notice 2002-8

*Economic benefits measured using Table 2001

What are the benefits?

Split Dollar Insurance can be used in the following ways:

- Fringe benefit for executives
- Estate planning when the estate is large
- Key Employee Replacement Insurance
- Group Term Replacement coverage
- In tandem with a 457(f) Plan