



## **Split Dollar in the 21st Century**

by  
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What follows is an important update to a previously issued Concept Library article outlining the features of the split dollar arrangements that survived the final split dollar regulations issued in September 2003 along with the location of InsMark illustrations for each one. This will be a valuable resource for you as all the concepts examined have application for shareholder employees of C corporations and non-owner key executives of any business entity.

**a) Endorsement Split Dollar** is an arrangement in which the policy owner is an employer and a portion of the policy death benefit is assigned to the insured executive's family.

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**b) Endorsement Split Dollar with Optional Transfer** is a powerful planning technique particularly for sole and majority shareholders. With this plan, the employer owns the policy but has the *option* to transfer the policy to the insured executive at a future point. While this tends to limit the use of this plan for non-shareholder key executives due to the uncertainty of the transfer, it still leaves substantial use of this strategy for sole and majority shareholders. (Owners need no contractual certainty.) This plan also allows great flexibility in determining the best tax environment in which to make the transfer. A spike in income taxes by the employer coupled with an unexpected dip in the executive's tax bracket could make for perfect transfer timing.

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**c) Endorsement Split Dollar with Salary Continuation** is an arrangement in which the policy owner is an employer and policy values are loaned or withdrawn by the employer to fund the after tax cost of a taxable retirement income payment to the participating executive.

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**d) Limited Collateral Assignment Split Dollar** is an arrangement in which the policy owner is typically a trust that assigns all cash values to the sponsoring employer.

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**e) Private Limited Collateral Assignment Split Dollar** is an arrangement in which the policy owner is typically a trust that assigns all cash values to the sponsoring parent or grandparent.

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**Note:** We recommend that you do not have the executive pay any portion of the policy premium in any form of employer-owned Endorsement Split Dollar or Limited Collateral Assignment Split Dollar since, under the final split dollar regulations issued in September 2003, such payments represent income to the employer. Instead, design your plans so the economic benefit is imputed to the executive. In any of the employer-sponsored split dollar illustration modules in the InsMark Illustration System, you can zero out the executive's out-of-pocket income tax costs on the imputed income by selecting a gross-up bonus. This should not be an issue with grantor-trust-owned plans as income tax consequences on transactions between the trust and grantor are ignored. (IRC Secs. 671 & 675, IRS Reg. 1.671-2(c), Rev. Rul. 85-13.)

To review Split Dollar illustrations for the concepts described in **a)** through **e)**, click here and review the Split Dollar section: <http://insmark.com/ProductCenter/InsMarkIllustrationSystem/output.html>.

**f) Loan-Based Split Dollar** is a high-powered arrangement involving employer-sponsored loans that fund executive-owned life insurance ("EXOLI"). In the InsMark design, the loans are illustrated bearing interest at the Applicable Federal Rate ("AFR") established under IRC Sections 7872 and 1274(d). This overall strategy produces substantial cash value equity for the insured participant and is a powerful replacement for employer-sponsored equity split dollar plans that were eliminated by the final split dollar regulations. (Due to provisions of Sarbanes-Oxley involving prohibition of loans to executives, this arrangement cannot be used for executives of publicly-owned companies.)

Licensees of Version 2.1 (and higher) of the InsMark Loan-Based Split Dollar System can generate illustrations of this variation using the module named Loan-Based Split Dollar. Documents for this variation are included in Version 19.0 (and higher) of InsMark's Documents On A Disk™ System and Documents On The Net System®.

**g) Loan-Based Private Split Dollar** is designed for use by wealthy parents and irrevocable trusts formed on behalf of their children. Utilizing a grantor trust as policy owner (see IRC Sections 671, 675, IRS Reg. 1.671-2(c), and Rev. Rul. 85-13), this System features loans from the grantor that allow virtually unlimited funding of irrevocable trusts. Loan-Based Private Split Dollar is one of the most efficient, parent-funded, trust-owned, wealth preservation strategies available.

Licensees of Version 2.1 (and higher) of the InsMark Loan-Based Split Dollar System can generate illustrations of this variation using the module named Loan-Based Private Split Dollar. Documents for this variation are included in Version 19.0 (and higher) of InsMark's Documents On A Disk™ System and Documents On The Net System®.

To review Loan-Based Split Dollar and Loan-Based Private Split Dollar illustrations described in **f)** and **g)**, click here: <http://insmark.com/ProductCenter/LBSD/index.html>.

**h) Leveraged Deferred Compensation** uses split dollar principles that fund executive-owned life insurance (“EXOLI”). The structure is similar to Loan-Based Split Dollar except the employer’s cost of loans is funded via a compensation reduction by the insured participant thus trading current taxable compensation for tax free retirement income (via policy loans). The concept provides an irresistible executive benefit that typically produces a powerful credit to earnings for the employer. (Due to provisions of Sarbanes-Oxley involving prohibition of loans to executives, this arrangement cannot be used for executives of publicly-owned companies.) A variation of this concept called Leveraged 401(k) Look-A-Like is also available.

Licensees of Version 5.0 (and higher) of the InsMark Leveraged Compensation System can generate illustrations of either variation. Specimen documents are in Version 19.0 (and higher) of InsMark’s Documents On A Disk™ System and Documents On The Net System® in the Employer-Sponsored Split Dollar Plans section. (Use the specimen documents for Leveraged Deferred Compensation with either variation.)

**i) Leveraged Executive Bonus** uses split dollar principles that fund executive-owned life insurance (“EXOLI”) where the employer bonuses a key executive an amount equal to the premium on a personally-owned policy and loans the executive the funds to pay the tax on the bonus. Loan interest can be illustrated as paid by the executive or offset by a further bonus from the employer. (Due to provisions of Sarbanes-Oxley involving prohibition of loans to executives, this arrangement cannot be used for executives of publicly-owned companies.)

Licensees of Version 5.0 (and higher) of the InsMark Leveraged Compensation System can generate illustrations for this variation. Specimen documents are in Version 19.0 (and higher) of InsMark’s Documents On A Disk™ System and Documents On The Net System® in the Executive Bonus Plans section. Use the specimen document entitled “Leveraged Executive Bonus (With Loan Regime Collateral Assignment Split Dollar to Pay Tax on Bonus)”.

To review specific illustrations for the concepts discussed in **h)** and **i)**, click here: <http://insmark.com/ProductCenter/LCS/index.html>.

**System Resources:** If you would like to have more information or to order a System, please contact an InsMark Account Executive at 1-888-InsMark (467-6275). Institutional inquiries should be made to David A. Grant, Sr. V.P. - Sales at 1-925-543-0513 or [dag@insmark.com](mailto:dag@insmark.com).

**Important Notice:** The information in this article is for education purposes only. The approval of a client’s legal and tax counsel must be secured before implementing any form of split dollar.

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