

# **Deferred Equity Split Dollar**

## **The Plan Description**

Of all the strategies used by employers to provide unique fringe benefits for their valuable executives, this variation is one of the most efficient. With this plan, the employer pays all (or substantially all) the premium due on a cash value life insurance policy on the life of a valued executive.

The policy is owned by the employer and, through use of a policy endorsement, the executive is given rights to name beneficiaries for a portion of the death benefit. Any remaining death benefits are paid to the employer. During the initial phase of this plan, the policy cash values are the property of the employer and are carried as assets on its books.

By way of a "conditional assignment" agreement executed at the inception of the plan, the employer agrees it will transfer its interest in the plan to the executive at a specified future date, e.g. after a specific term of years or, perhaps, at retirement. If the employee does not meet the conditions agreed upon, no transfer takes place.

When the employer's interest is transferred, the employer has taxable income to the extent its cash value exceeds its cost basis and an income tax deduction equal to the policy cash value less the executive's cumulative premium share, if any. (Reg. 1.83-6(b).) At the point of transfer, the executive has taxable income equal to the policy cash value less his/her cumulative premium share, if any. (IRC Sec. 83 and PLR 8310027.) The source of the funds for the executive's resulting income tax is generally one or more of the following: 1) withdrawal or loan on the policy; 2) bonus from the employer; or 3) out-of-pocket cash.

After the transfer, the executive has unfettered access to plan cash values through the policy's loan and withdrawal provisions, and this source of continuing cash flow is often used to supplement the executive's retirement income.

Split dollar plans have yearly income tax ramifications. The IRS has issued rulings specifying that, unless an offsetting payment is made, an executive covered with a split dollar arrangement is in receipt of a taxable economic benefit to the extent relief is provided from paying premiums personally. Income tax calculations are not, however, derived from the premium paid by the employer. Instead, they are based on the premium relief the executive has experienced -- measured by certain term insurance rates available from the issuing insurance company or, at the taxpayer's option, from a special term-type rate table published by the government. Either method usually creates an advantageous spread between the actual policy premium and the cost of the plan to the executive.

Low cost benefits for the executive, combined with an impressive array of cash value for the employer during the plan's initial phase and the executive thereafter, constitute a program that may be financially irresistible to both employer and executive. This is particularly evident in the accompanying presentation.

Note: IRS Notice 2002-8 issued in January 2002 should have no adverse impact on this plan.

# Deferred Equity Split Dollar Using Variable Universal Life (VUL)

## Illustration of Values of The Policy Used in the Plan

Values Page: 1  
Date: 08/01/2002

Presented By: [Licensed user's name appears here]

For: Robert Haynes  
Hudson Mills, Inc.

Male Age 45	Employer's Tax Bracket 34.00%	VUL Interest Rate 10.00%	Initial Payment 50,000	Initial Death Benefit 1,250,000
-------------------	-------------------------------------	--------------------------------	------------------------------	---------------------------------------

Year	(1) Net Payment	(2) Pre-Tax Partial Withdrawal	(3) Year End Accum Value*	(4) Year End Cash Value*	(5) Death Benefit
1	50,000	0	50,826	33,326	1,250,000
2	50,000	0	106,107	71,107	1,250,000
3	50,000	0	166,005	128,755	1,250,000
4	50,000	0	230,926	193,676	1,250,000
5	50,000	0	301,324	264,074	1,250,000
6	0	92,426	217,087	184,317	1,157,549
7	0	0	231,532	200,832	1,157,549
8	0	0	246,900	218,614	1,157,549
9	0	0	263,242	237,716	1,157,549
10	0	0	280,615	258,193	1,157,549
11	0	0	299,099	280,126	1,157,549
12	0	0	318,771	303,593	1,157,549
13	0	0	339,702	328,664	1,157,549
14	0	0	361,997	355,443	1,157,549
15	0	0	385,765	385,765	1,157,549
20	0	0	531,306	531,306	1,157,549
25	0	0	740,815	740,815	1,157,549
30	0	0	1,067,337	1,067,337	1,157,549
35	0	0	1,587,639	1,587,639	1,667,021
40	0	0	2,347,018	2,347,018	2,464,369
	250,000	92,426			

### 40 Year Summary

Cum. Payments	250,000
Cum. Pre-Tax Withdrawals	92,426
Cash Value	2,347,018
Death Benefit	2,464,369

\*This is an example of an InsMark "supplemental" illustration for variable universal life insurance. In a real presentation, this footnote will refer to an accompanying "basic" illustration from a specific life insurance company and a prospectus.

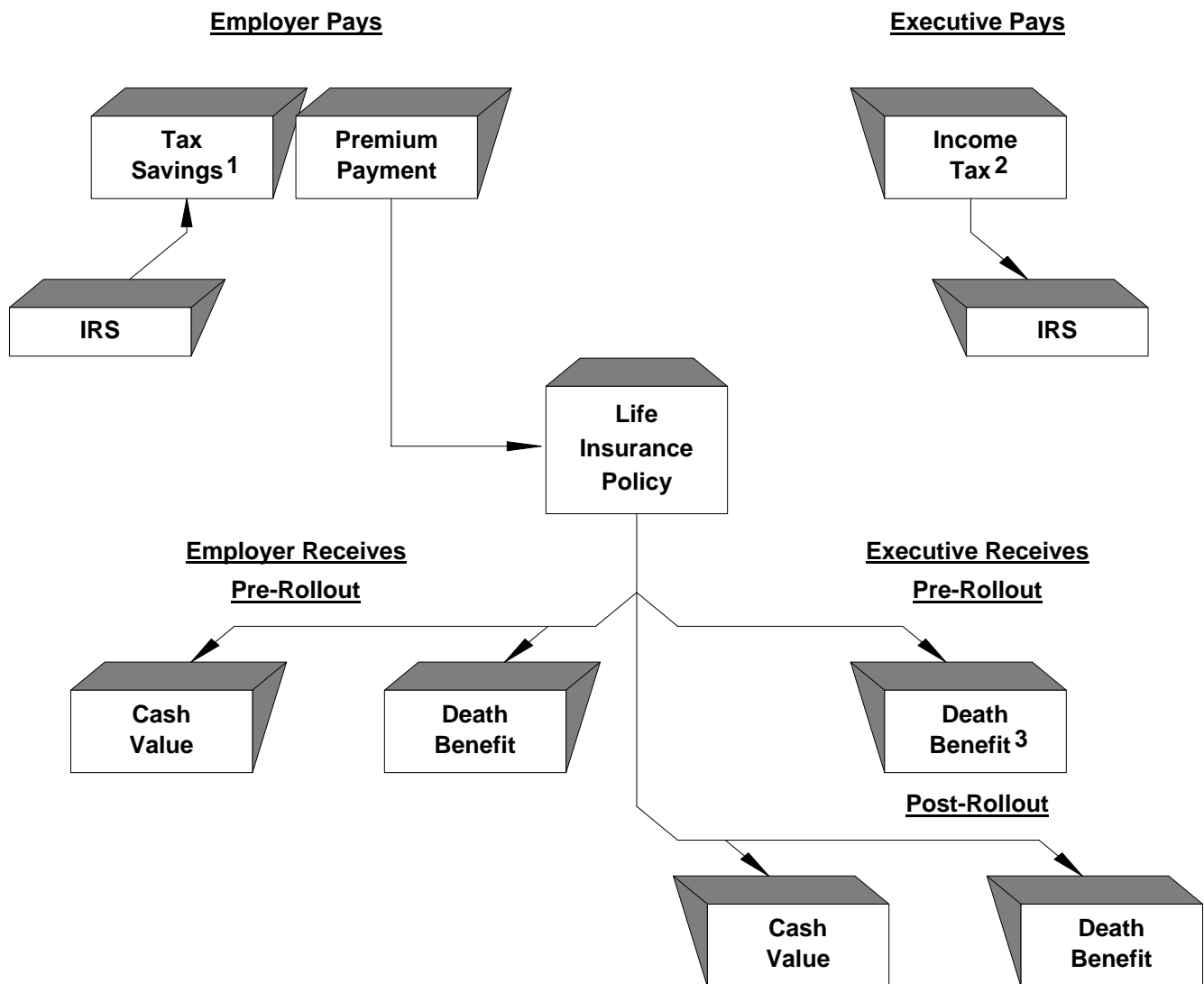
# Deferred Equity Split Dollar Using Variable Universal Life (VUL)

## Who Pays What - Who Receives What

Presented By: [Licensed user's name appears here]  
Date: 08/01/2002

For: Robert Haynes  
Hudson Mills, Inc.

### Flow Chart Analysis



(1) See Employer's Analysis page for details.  
(2) See Executive's Analysis page for details.

(3) Equal to remaining balance after employer's portion is deducted.

## Details of the Tax Consequences of the Rollout

Detail Page: 1  
Date: 08/01/2002

Presented By: [Licensed user's name appears here]

For: Robert Haynes  
Hudson Mills, Inc.

Male Age	Employer's Tax Bracket	Executive's Tax Bracket	Year of Sec. 83 Rollout
45	34.00%	35.00%	6

### Rollout Details:

Cash value in year of rollout: \$264,074  
Employer's cumulative premiums: \$250,000  
Executive's cumulative premiums: \$0  
Timing of rollout: beginning of year 6

### Employer's Rollout Tax Consequences:

The employer must recognize gain to the extent that the cash value exceeds the employer's premium payments; however, the employer is entitled to a deduction equal to the total cash value less the executive's cumulative premium share, if any. (Reg. 1.83-6(b).)

Therefore, for this case:

1. The employer has a taxable gain of the difference between \$264,074 (policy cash value) and \$250,000 (employer's cumulative premium share) which equals \$14,074 in taxable gain.  $\$14,074 \times 34.00\%$  (the employer's tax bracket) = \$4,785 of income tax due.
2. In addition, the employer has an income tax deduction of the difference between \$264,074 (policy cash value) and \$0 (executive's cumulative premium share) which equals \$264,074.  $\$264,074 \times 34.00\% = \$89,785$  of income tax savings.
3. \$89,785 of income tax savings less \$4,785 of income tax due = \$85,000 of net income tax savings to the employer at rollout.

### Executive's Rollout Tax Consequences:

The executive must recognize gain to the extent that the cash value transferred from the employer exceeds his/her cumulative premium payments. (IRC Sec. 83 and PLR 8310027.)

Therefore, for this case:

1. The executive has a taxable gain of the difference between \$264,074 (policy cash value) and \$0 (executive's cumulative premium share) which equals \$264,074 in taxable gain.
2.  $\$264,074 \times 35.00\% = \$92,426$  of income tax due.

Note: Any premium payment or policy activity (loans, withdrawals, etc.) in the year of rollout is presumed to occur after the rollout takes place.

## Summary of Costs and Benefits

### Deferred Equity Split Dollar Using Variable Universal Life (VUL)

Summary Page: 1  
Date: 08/01/2002

Presented By: [Licensed user's name appears here]

For: Robert Haynes  
Hudson Mills, Inc.

	Male Age 45	Form of Transaction (Endorsement)	Employer's Tax Bracket 34.00%	Executive's Tax Bracket 35.00%	VUL Interest Rate 10.00%	Year of Sec. 83 Rollout 6			
	Employer					Executive			
Year	(1) Net Payment	(2) Cumulative Net Payments	(3) Share of Policy Accum Value*	(4) Share of Policy Cash Value*	(5) Share of Policy Death Benefit	(6) Net Payment	(7) After Tax Withdrawal Applied to Rollout	(8) Share of Policy Cash Value*	(9) Share of Policy Death Benefit
1	50,000	50,000	50,826	33,326	50,000	643	0	0	1,200,000
2	50,000	100,000	106,107	71,107	100,000	672	0	0	1,150,000
3	50,000	150,000	166,005	128,755	150,000	705	0	0	1,100,000
4	50,000	200,000	230,926	193,676	200,000	728	0	0	1,050,000
5	50,000	250,000	301,324	264,074	264,074	735	0	0	985,926
6	-85,000	165,000	0	0	0	0	92,426	184,317	1,157,549
7	0	165,000	0	0	0	0	0	200,832	1,157,549
8	0	165,000	0	0	0	0	0	218,614	1,157,549
9	0	165,000	0	0	0	0	0	237,716	1,157,549
10	0	165,000	0	0	0	0	0	258,193	1,157,549
11	0	165,000	0	0	0	0	0	280,126	1,157,549
12	0	165,000	0	0	0	0	0	303,593	1,157,549
13	0	165,000	0	0	0	0	0	328,664	1,157,549
14	0	165,000	0	0	0	0	0	355,443	1,157,549
15	0	165,000	0	0	0	0	0	385,765	1,157,549
20	0	165,000	0	0	0	0	0	531,306	1,157,549
25	0	165,000	0	0	0	0	0	740,815	1,157,549
30	0	165,000	0	0	0	0	0	1,067,337	1,157,549
35	0	165,000	0	0	0	0	0	1,587,639	1,667,021
40	0	165,000	0	0	0	0	0	2,347,018	2,464,369
	165,000					3,483	92,426		

Split dollar arrangement presumed terminated in year 6.

40 Year Summary

\*This is an example of an InsMark "supplemental" illustration for variable universal life insurance. In a real presentation, this footnote will refer to an accompanying "basic" illustration from a specific life insurance company and a prospectus.

Employer's Cum. A/T Costs	165,000
Employer's Cash Value	0
Employer's Death Benefit	0
Executive's Cum. A/T Costs	3,483
Executive's A/T Withdrawal Applied to Rollout	92,426
Executive's Cash Value	2,347,018
Executive's Death Benefit	2,464,369

# Employer's Analysis

## Deferred Equity Split Dollar Using Variable Universal Life (VUL)

Employer's Analysis Page: 1  
Date: 08/01/2002

Presented By: [Licensed user's name appears here]

For: Robert Haynes  
Hudson Mills, Inc.

Male Age 45	Form of Transaction (Endorsement)	Employer's Tax Bracket 34.00%	VUL Interest Rate 10.00%	Year of Sec. 83 Rollout 6
-------------------	---	-------------------------------------	--------------------------------	---------------------------------

Year	(1) Split Dollar Premium Share	(2) Cum. Split Dollar Premium Share	(3) Income Tax Savings from Rollout**	(4) Net Payment (1)-(3)	(5) Cumulative Net Payments
1	50,000	50,000	0	50,000	50,000
2	50,000	100,000	0	50,000	100,000
3	50,000	150,000	0	50,000	150,000
4	50,000	200,000	0	50,000	200,000
5	50,000	250,000	0	50,000	250,000
6	0	0	85,000	-85,000	165,000
7	0	0	0	0	165,000
8	0	0	0	0	165,000
9	0	0	0	0	165,000
10	0	0	0	0	165,000
11	0	0	0	0	165,000
12	0	0	0	0	165,000
13	0	0	0	0	165,000
14	0	0	0	0	165,000
15	0	0	0	0	165,000
20	0	0	0	0	165,000
25	0	0	0	0	165,000
30	0	0	0	0	165,000
35	0	0	0	0	165,000
40	0	0	0	0	165,000
	250,000			165,000	

\*This is an example of an InsMark "supplemental" illustration for variable universal life insurance. In a real presentation, this footnote will refer to an accompanying "basic" illustration from a specific life insurance company and a prospectus.

\*\*The split dollar plan is scheduled to be terminated at the beginning of year 6 via a Section 83 rollout. This produces taxable income to the employer to the extent its cash value exceeds its cost basis and an income tax deduction equal to the policy cash value less the executive's cumulative premium share, if any. (Reg. 1.83-6(b).)

# Executive's Analysis

## Deferred Equity Split Dollar Using Variable Universal Life (VUL)

Executive's Analysis Page: 1  
Date: 08/01/2002

Presented By: [Licensed user's name appears here]

For: Robert Haynes  
Hudson Mills, Inc.

	Male Age 45	Form of Transaction (Endorsement)	Executive's Tax Bracket 35.00%	VUL Interest Rate 10.00%	Year of Sec. 83 Rollout 6		
Year	(1) Split Dollar Premium Share	(2) Additional Taxable Value of Benefit*	(3) Income from Section 83 Rollout**	(4) Taxable Income (2)+(3)	(5) Income Tax Due on Col (4)	(6) After Tax Partial Withdrawal	(7) Net Payment (1)+(5)-(6)
1	0	1,836	0	1,836	643	0	643
2	0	1,921	0	1,921	672	0	672
3	0	2,013	0	2,013	705	0	705
4	0	2,079	0	2,079	728	0	728
5	0	2,100	0	2,100	735	0	735
6	0	0	264,074	264,074	92,426	92,426	0
7	0	0	0	0	0	0	0
8	0	0	0	0	0	0	0
9	0	0	0	0	0	0	0
10	0	0	0	0	0	0	0
11	0	0	0	0	0	0	0
12	0	0	0	0	0	0	0
13	0	0	0	0	0	0	0
14	0	0	0	0	0	0	0
15	0	0	0	0	0	0	0
20	0	0	0	0	0	0	0
25	0	0	0	0	0	0	0
30	0	0	0	0	0	0	0
35	0	0	0	0	0	0	0
40	0	0	0	0	0	0	0
	0	9,949	264,074	274,023	95,909	92,426	3,483

\*Assuming column (1) offsets the economic benefit.

\*\*The split dollar plan is scheduled to be terminated at the beginning of year 6 via a Section 83 rollout. This produces taxable income to the executive equal to the policy cash value less the executive's cumulative premium share, if any. (IRC Sec. 83 and PLR 8310027.)

This is an example of an InsMark "supplemental" illustration for variable universal life insurance. In a real presentation, this footnote will refer to an accompanying "basic" illustration from a specific life insurance company and a prospectus.

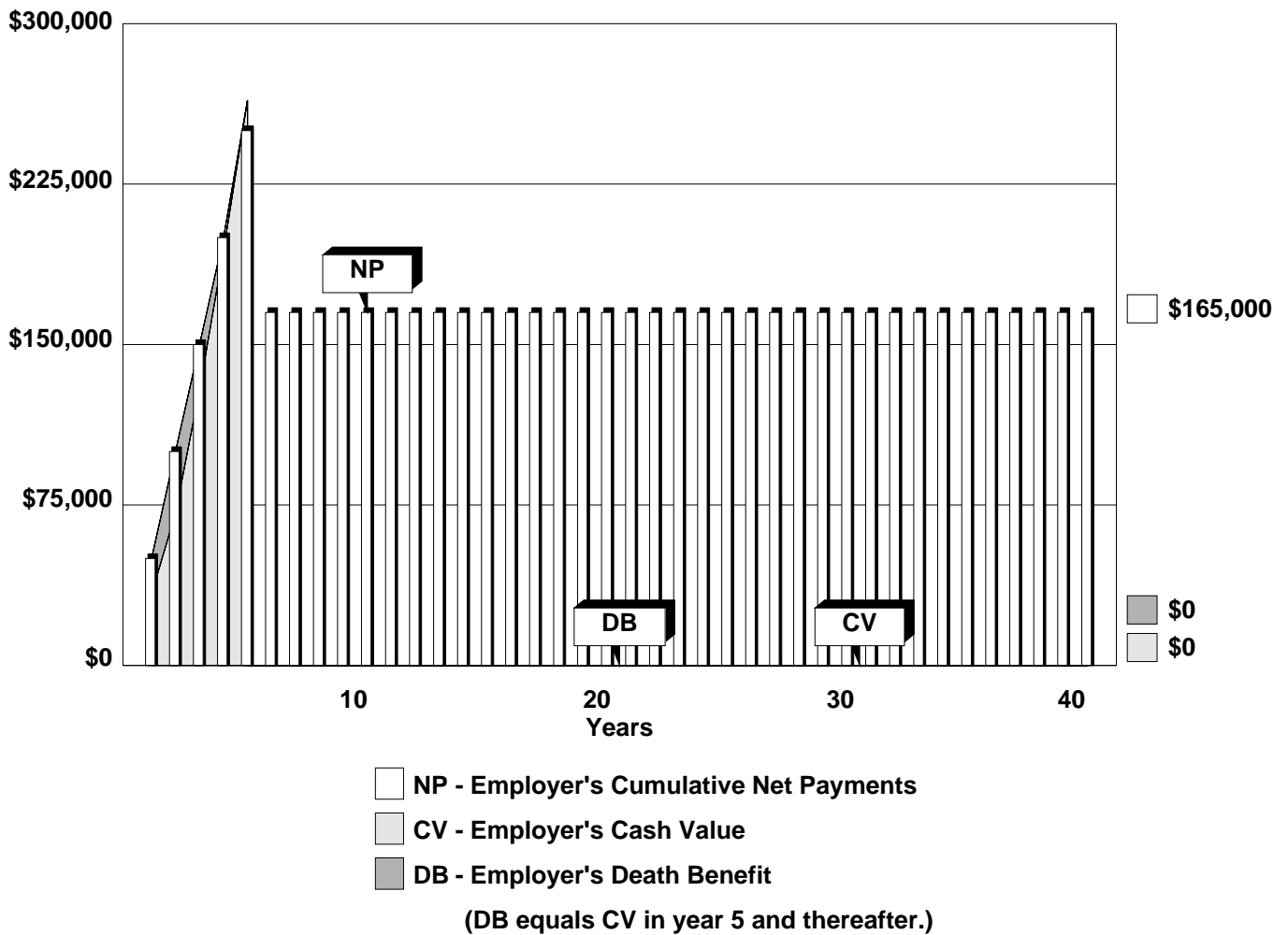
Column (2) is the imputed economic benefit in compliance with IRS Notice 2002-8. (Table 2001 rates utilized.)

# Deferred Equity Split Dollar Using Variable Universal Life (VUL)

Presented By: [Licensed user's name appears here]  
Date: 08/01/2002

For: Robert Haynes  
Hudson Mills, Inc.

## Employer's 40 Year Graphic Analysis



# Deferred Equity Split Dollar Using Variable Universal Life (VUL)

Presented By: [Licensed user's name appears here]  
Date: 08/01/2002

For: Robert Haynes  
Hudson Mills, Inc.

## Executive's 40 Year Graphic Analysis

