CBS | BROKERAGE
OUR GOAL IS YOUR LEGACY EST. 2008 SHAKOPEE, MINNESOTA

Advanced Sales - Loan Regime Split Dollar

Providing Golden Handcuffs Using Loan Regime Split Dollar

What is Loan Regime Split Dollar?

Loan regime split dollar is a life insurance policy in which the premium payment(s) and the death benefit are split between a business and a key employee. In a loan regime split dollar situation, the business loans premium(s) to the key employee to purchase the life insurance policy. Most plans are set up so that the business pays all of the premium(s) through a loan to the key employee. There is an option for the employee to contribute premium(s), Which is rare. The employee must recognize the loan interest every year on the loan balance and pay the tax on the imputed income when the business forgives the loan interest. The loan interest rate the key employee must recognize are the IRS's Applicable Federal Rates (AFR rates).

Candidates

- C corporation owners, professional corporations, non-profits, and highly paid non-owner executives.

Non-Candidates

- Owners of pass-through entities.

Purpose: Executive Benefit

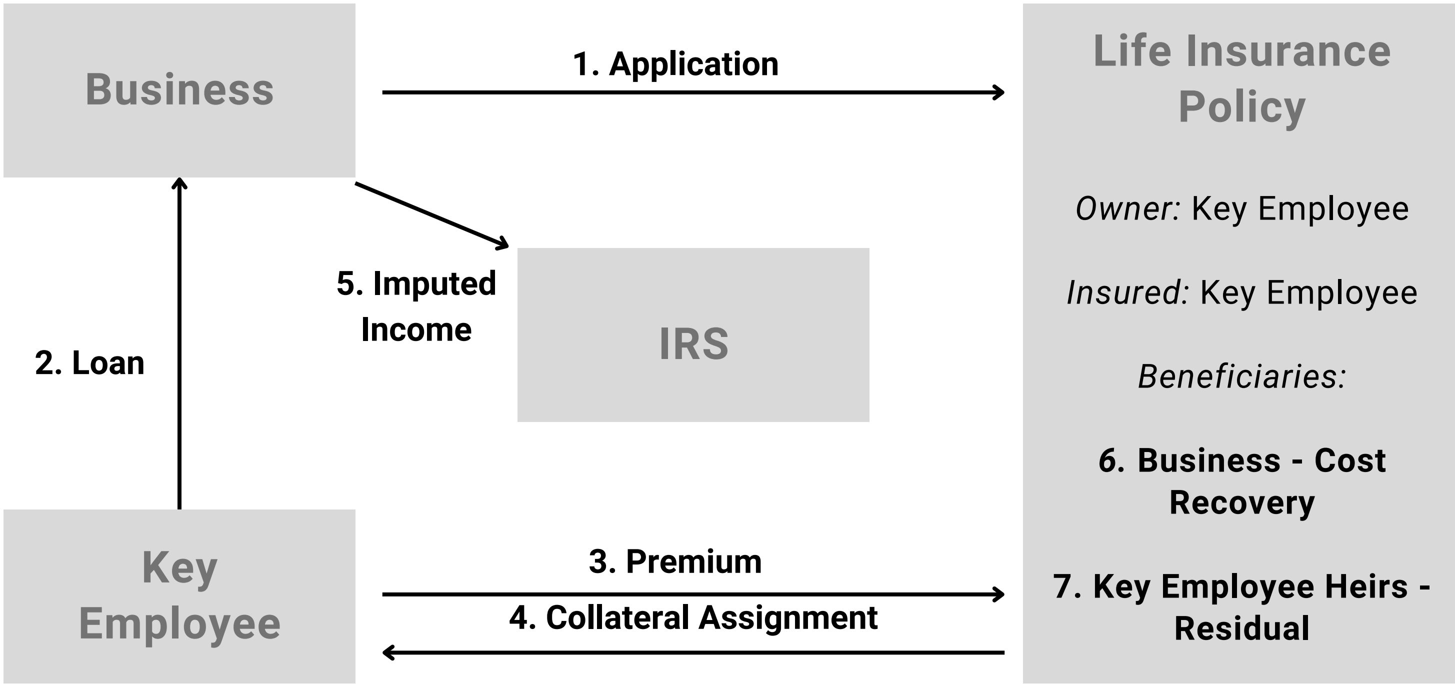
- Provides a strong golden handcuff on a business owner or key employee. Provides low cost insurance for the key employer while they are working.

Opportunity Under the New Tax Law

- A new tax legislation was signed into law by President Trump in December2017. C corporations' tax brackets fell from 35% to 21%. Pass-through entities can receive a 20% discount on their "qualified business income" if they qualify for the new Section 199A deduction. However, these tax cuts are set to expire on December 31, 2025 and under current law, most of the tax cuts will revert back to 2017 rules (indexed for inflation). C corporations may go back to higher tax brackets and S corporations may no longer be able to take advantage of the Section 199A deduction.

- So what does this mean? The business has extra cash to provide golden handcuffs on their key employees. The business can set up split dollar arrangements on their key employees while they are in a lower tax bracket and take the tax deductions after December 31, 2025 when they are expected to be in a higher tax bracket.

How Does Loan Regime Split Dollar Work?



Typical Endorsement Split Dollar Sale

1. The key person applies for life insurance on their life.

2. The business loans money to the key employee for premium payment(s).

3. The business pays premium(s) to the life insurance company on behalf of the key employee with the loaned funds.

4. The key employee executes a collateral assignment against the policy, giving the business an interest in the policy's cash value and death benefit, in order to provide cost recovery of the loaned premium(s).

5. The employee must recognize the loan interest forgiven as imputed income or pay the loan interest to the business (this is rare). The loan rates are subject to the IRS's Applicable Federal Rates (AFR Rates).

6. The death benefit is split between the employer and employee. If the key employee dies while working, the business would receive the greater of the cash surrender value or the premium(s) paid (cost recovery).

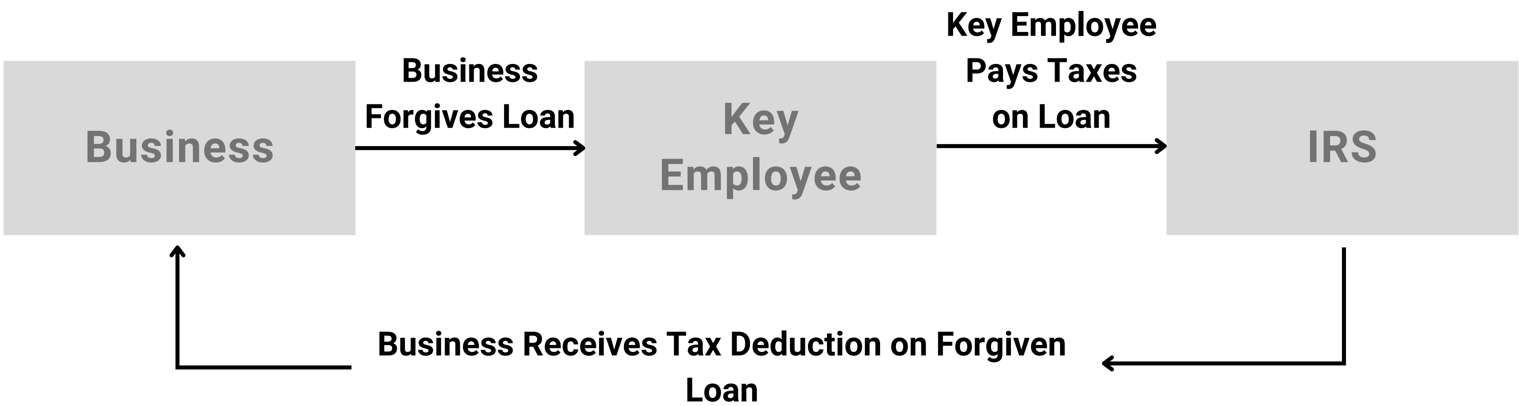
7. The key employee's heir(s) would receive the residual death benefit after the portion of the death benefit pays the loan back to the business.

The Exit Strategy

When the business forgives the loan to the key employee, the business can deduct the forgiveness of the loan as compensation and the key employee would have to recognize the loan forgiveness as ordinary income. Below are two ways to mitigate the taxes to the key employee:

- When the business forgives the loan, it could bonus the taxes to the employee through a Section 162 executive bonus (increases the tax deduction to the business).

- When the business forgives the loan, the key employee could take a withdrawal from the life insurance policy to pay the taxes due.



Conclusion

Loan regime split dollar provides an incentive to the client to stay with the business. If the key employee leaves the business prior to the exit strategy set forth in the split dollar agreement, the executive would have to repay the loan back to the business.

For More Information Contact CBS Brokerage at 763.450.1870