

# Split dollar plans funded with life insurance

Hypothetical case study

## Problem

Your business-owner clients face the challenge of retaining and rewarding employees. Certain employees could be critical to the life of their business and keeping them committed is essential.

## A Solution

Split dollar plans can be used to encourage employee retention. A split dollar plan is an arrangement in which life insurance premiums, death benefit, and cash values are split between the employer and an employee. This strategy can help reduce turnover by rewarding key employees with an exclusive benefit that offers protection during employment for their families, and later, a potential supplement to retirement income.

A split dollar plan can offer a number of benefits for both the employer and the employee.

### For the employer

- No discrimination tests or criteria. The employer can freely choose which key employee receives the benefit.
- No IRS pre-approval required<sup>1</sup>
- Flexible plan design and exit options
- Alternative to offering equity in the company
- Ability to recoup costs at retirement, termination, or death

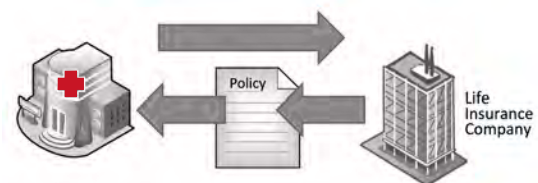
### For the employee

- Generally tax-free death benefit
- Opportunity to obtain life insurance benefit for minimal expense
- May be designed so the employee owns the policy and potential cash value during retirement
- An alternative to partial interest in the company

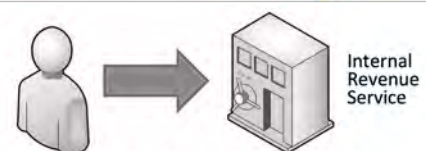
## Hypothetical Case Study

Your client is the founder of a prominent ear, nose and throat clinic based in a rapidly growing community. Two years ago, two of your client's physicians left to start their own clinic in a new up-and-coming suburb. Since then, a top specialist has joined your client's clinic and your client is close to recruiting a second. In an effort to prevent losing quality physicians in the future, your client works with an attorney to implement a split dollar agreement using the Economic Benefit regime design.

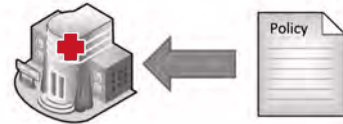
1. The clinic purchases and owns a Builder Plus IUL® 3 Indexed Universal Life policy on each of the new physicians. The clinic is paying the full premium for the policies.



2. Annually, the physicians pay tax on the value of the economic benefit received, minus any amount actually paid by the employee.



3. The plan is structured so that if a physician leaves the clinic, the clinic is repaid back the amount of premiums it has paid into the policy from the policy's cash surrender value and the policy is terminated.



4. If the physician dies, a portion of the death benefit equal to the clinic's interest is paid to the clinic. Any remaining death benefit is paid to the physician's beneficiaries.



5. If the physician stays with the clinic until retirement, a portion of any policy's cash surrender value equal to the clinic's interest is paid to the clinic. If the policy's cash value is insufficient to cover the employer costs, the clinic may retain a portion of the death benefit as a beneficiary. The policy and any remaining cash value is transferred to the physician. The transfer of ownership is a taxable event for the physician.



<p><b>Monthly Premium</b> \$4,000 paid by clinic</p>	<p><b>Death Benefit</b></p> <table> <tr> <td>Day 1</td> <td>\$664,245</td> </tr> <tr> <td>Age 65</td> <td>\$2,902,510</td> </tr> </table>	Day 1	\$664,245	Age 65	\$2,902,510	<p><b>At Retirement (Age 65)</b></p> <table> <tr> <td>Cash Value age 65</td> <td>\$2,379,106</td> </tr> <tr> <td>Clinic's Interest</td> <td>- \$552,000</td> </tr> <tr> <td>Cash Value age 66</td> <td>\$1,972,837</td> </tr> </table>	Cash Value age 65	\$2,379,106	Clinic's Interest	- \$552,000	Cash Value age 66	\$1,972,837
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Male, Age 42 • Preferred NT • Builder Plus IUL 3 • Return of Premium DB • \$4,000 Monthly Premium to Age 65  
 Illustrated at 5.97% • Fixed Participating Loan<sup>2</sup> at Age 65 • Builder Plus IUL 3 was chosen in this example for its potential long-term cash value accumulation. North American offers several indexed universal life insurance products. The information presented is hypothetical and not intended to project or predict future results. Illustrations are not complete unless all pages are included.

## Case design tips

<p>Be sure the specified amount is enough to meet the client's pre-retirement life insurance death benefit needs.</p>	<p>A minimum death benefit solve with Return of Premium<sup>3</sup> death benefit option can help control policy charges which can reduce the cash value of the policy.</p>	<p>Return of Premium Death Benefit option<sup>3</sup> can help ensure the death benefit covers the company's interest in the policy.</p>
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Be sure to discuss with clients that performance is not guaranteed and depending on funding, life insurance may not guarantee avoiding the loss of premium.

## Next steps

1. Make a list of clients that own businesses or hold leadership positions within their organization.
2. Reach out to them to see if they have a plan in place to retain key employees.
3. Share how a split-dollar plan could be used to fund a life insurance policy, offering an exclusive way to help reward and retain top employees.

Neither North American nor its agents give tax advice. Please advise your customers to consult with and rely on a qualified legal or tax advisor before entering into or paying additional premiums with respect to such arrangements.

1. To ensure the death benefit proceeds of any employer-owned policy retains its tax-favored treatment, it is essential to comply with the notice and consent requirements of IRC Section 101(j).
  2. In some situations loans and withdrawals may be subject to federal taxes. North American does not give tax or legal advice. Clients should be instructed to consult with and rely on their own tax advisor or attorney for advice on their specific situation. Income and growth on accumulated cash values is generally taxable only upon withdrawal. Adverse tax consequences may result if withdrawals exceed premiums paid into the policy. Withdrawals or surrenders made during a Surrender Charge period will be subject to withdrawal charges, processing fees, or surrender charges, and may reduce the ultimate death benefit and cash value. Surrender charges vary by product, issue age, sex, underwriting class, and policy year.
  3. Return of Death Benefit option is subject to eligibility requirements.
- Under an economic split-dollar arrangement, your client enters into an agreement with their employer. North American Company is not a party to this agreement and North American Company's only obligation is to administer the policy it issues consistent with the policy's terms and conditions.
- Under an economic split-dollar arrangement, the value of the life insurance afforded the employee is taxable to the employee. The employer should provide the employee with tax reporting based on requirements specified in the tax code. The parties to the economic split-dollar arrangement should seek their own independent legal and tax advice as to whether and how to enter into an economic split-dollar arrangement based on the employer's and employee's unique circumstances.

Indexed universal life insurance products are not an investment in the "market" or in the applicable index and are subject to all policy fees and charges normally associated with most universal life insurance. Builder Plus IUL 3 (policy form series LS191), or state variation including all applicable endorsements and riders, is issued by North American Company for Life and Health Insurance, West Des Moines, Iowa. Product, features, endorsements, riders, or issue ages may not be available in all jurisdictions. Limitations or restrictions may apply.



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