An educational guide for business owners

Guardian®

Employee retention — easy and affordable

Discover the benefits of a Split Dollar Plan

Your key employees are vital to your success... but do you need a way to help ensure their loyalty?

If you're like many successful business owners today, you don't want to lose your top performers to the competition. But do you also struggle with how to offer those key employees a benefit that's affordable for your business, yet compelling enough to make them want to stay on board for the long term?

A Split Dollar Plan is a business-sponsored benefit that rewards top performers and provides cost recovery for the company. In a Split Dollar Plan, the employer and the employee "split" the main components of a life insurance policy: the premium, the death benefit, and the cash value. A Split Dollar Plan is comprised of two specific elements: 1. A life insurance policy; and 2. A legal agreement drafted by the client's attorney. The legal agreement spells out how the employer and employee will split the main components of the life insurance policy. It also addresses all the rights and obligations of the parties.

You can offer this flexible executive benefit strategy to only those employees you choose — and you can design the plan to meet your needs.

Two primary types of Split Dollar Plans

In a Loan Regime Split Dollar Arrangement, the employee owns the policy that funds the plan, and the employer loans the employee money to pay the premium at the Applicable Federal Rate (AFR). The specific AFR that may be used for the loan is dependent upon whether the loan is structured as a demand or term loan — and if it is the latter, the length of the term. Your business will receive a portion of the cash value and death benefit equal to the loan, until it is repaid. At the time of rollout (when the plan ends), the loan can be forgiven or potentially repaid from policy cash values. A third option for the rollout is to secure repayment from other resources.

In an Economic Benefit Split Dollar Arrangement, your business applies for and owns the life insurance policy that funds the plan. The policy is issued with ownership and beneficiary designations that note how the death benefit will be split between your business and the executive's beneficiaries. The business owns 100% of the cash value of the life insurance policy. You have the option to pay the executive a separate bonus to cover the tax cost liability of receiving this economic benefit so that the executive will have no out-of-pocket expense for this arrangement.

What is a Split Dollar Agreement?

In a Split Dollar Agreement, the business owner and employee document how they will "split" the main components of the life insurance policy that helps to fund the Split Dollar Arrangement — the premium, the death benefit, and the cash value — and how the policy proceeds will be divided upon termination of the arrangement, which ordinarily occurs at the employee's death or retirement.

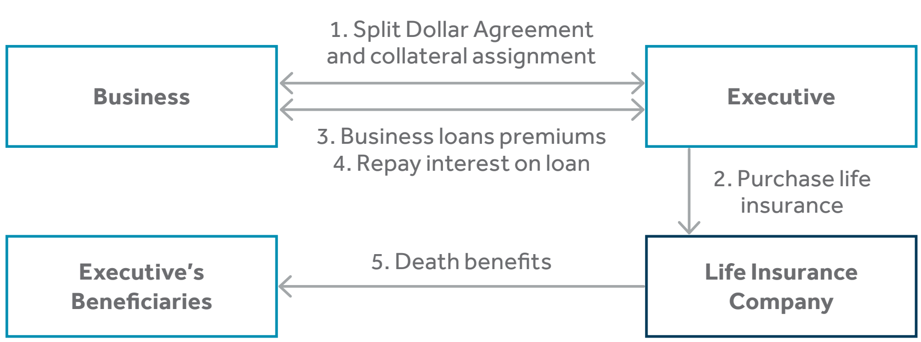
How it works

When funded with life insurance

Loan Regime Split Dollar Arrangement

In our first hypothetical case, Elaine Carpenter owns a mid-size test-preparation firm that helps students prepare for college entrance exams. There is more turnover in her staff than she would like, and she wants to find ways to encourage her best teachers to stay. Steve Brown is one of those teachers — he has been with her for seven years, and she'd like him to stay with her company until his retirement. She'd like a plan that she could offer just to Steve, and if that goes well, she'd then think about opening it up to other promising teachers in the future.

Elaine decides to implement a Loan Regime Split Dollar Plan. Steve will get a $1M Guardian 10-pay policy on his life, and Elaine will loan him the premium amount. At retirement, Elaine will "bonus" the policy to Steve, and he will withdraw money from the policy to pay the taxes on the bonus. There is still enough money in the policy after paying the taxes to provide about $27.7K of retirement income for 20 years.



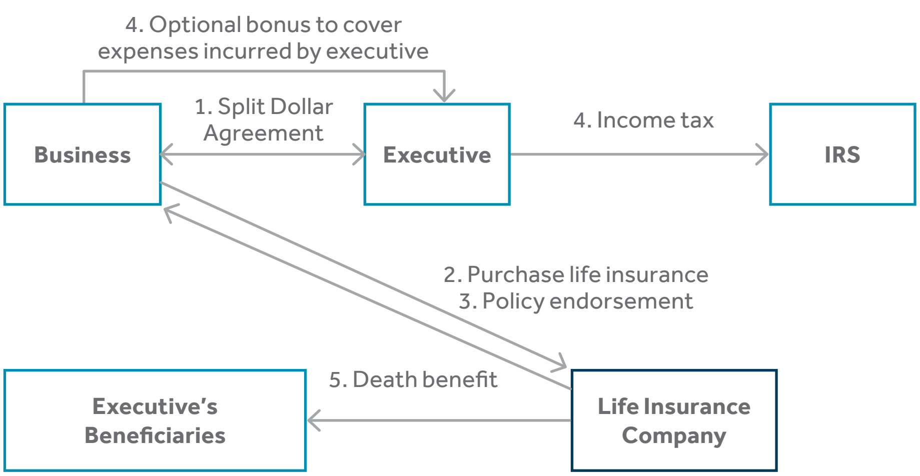
How it works

When funded with life insurance

Economic Benefit Split Dollar Arrangement

In our second hypothetical case, Richard Patterson is the owner of a real estate business. His top agent, Sarah Hanover, is a widow who has been with the business a number of years. Sarah would like more life insurance to protect her children, but hasn't been able to buy as much as she'd like because of cost concerns. Richard decides to reward Sarah with an Economic Benefit Split Dollar Arrangement.

With Sarah's permission, Richard's company applies for and purchases a $1.5M life insurance policy on her life. He endorses $1M of the death benefit over to Sarah, who pays taxes on the economic benefit costs as measured by Table 2001-10.[1] This greatly reduces her out-of-pocket costs. At retirement, Richard could decide to "bonus" the policy to Sarah, who could use the cash value to pay the taxes on the transfer. That way, Sarah could continue to enjoy the death benefit protection for her family in retirement.[2]



How much insurance coverage would be needed?

The amount of the whole life policy that funds your Split Dollar Plan should be enough to:

- protect your business and your employee's beneficiaries in the event that the key employee should die; and
- enable, for your business, cost recovery of cumulative premiums through the life insurance death benefit proceeds.

Consider your exit strategy

A Split Dollar Arrangement can be a cost-effective approach for the purchase of large amounts of life insurance. However, it makes financial sense for all parties to plan for an exit strategy (other than the death of the insured) during the plan design phase — so that proper planning can take place with respect to how the employee/insured can ultimately either pay the tax on the transaction, or repay your business for its interest in the policy.

An executive benefit strategy

Advantages for you and your top performers

The Split Dollar Plan offers advantages for both the employer and the employee.

Loan Regime Split Dollar Arrangement

Advantages for your business:	Advantages for the employee:
It's flexible: You can choose which employee(s) will participate in the Split Dollar Plan — and can offer each participant a different Split Dollar Agreement and different life insurance policy.	**It provides protection they need:** Participating employees will receive valuable life insurance protection with little out-of-pocket expense during their working years.
It's cost-effective: Your business can recover the premiums loaned from the cash value[3] or the death benefit, through the collateral assignment of the policy. You can elect to recover costs on some employees, but not others.	**It's valuable:** The executive may have the right to a portion of the policy cash value during his or her lifetime. The executive can use the cash value to supplement retirement income or for any other purpose.[5]
It's easy to administer: There's less administration and paperwork with a Split Dollar Plan than with many other executive benefit programs.	**It can be portable:** When retiring or leaving the company, the executive can retain the insurance policy, after paying off the loan, and then pay future premiums from his or her own resources.
It's an "asset": Your business's portion of the cash value may be shown as an asset on your corporate books.	
It's tax-efficient: There are no adverse tax consequences[4] from the buildup of cash value inside the policy, even if the cash value exceeds the cumulative premiums paid.	
It can particularly benefit C-Corporations: The current maximum corporate income tax rate is 21%, while the current maximum personal income tax rate is 37%. As an owner-employee, you could use Loan Regime Split Dollar to pay for an insurance premium using dollars from the corporation, which is taxed at a lower rate than an individual.	

Economic Benefit Split Dollar Arrangement

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It's flexible: You can choose which employee(s) will participate in the Split Dollar Plan — and can offer each participant a different Split Dollar Agreement and different life insurance policy.	**It provides protection they need:** Participating employees will receive valuable life insurance protection with little out-of-pocket expense during their working years.
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Which plan may be right for you?

When it comes to deciding which Split Dollar Plan may be the right choice, you may be asking yourself which approach works better or which one is more cost effective. While it's natural to ask these questions, before you can select the plan you feel is right for your business, you and your financial professional should consider what your goals are.

Here's a chart that summarizes some of the main features sought after by business owners who implement Split Dollar Plans — and the structure of which Split Dollar Arrangement may be appropriate for each goal:

Goal	Loan Regime	Economic Benefit Regime
Employee portability	X	
Control by the business		X
Employee contribution to premiums	X	
Employee equity	X	
Lower taxes for younger employees		X
Lower taxes for older employees	X	

Why a Split Dollar Plan may be right for you

A Split Dollar Plan can help to ensure the profitability of your business for the long term, since it can help you provide your top performers (including yourself) with a valuable benefit whose value they will appreciate. This type of plan could be the executive benefit solution you've been looking for if you:

- are looking for a way to retain or reward selected executives or employees — to help ensure they'll stay with your business for the long term
- have key employees who need permanent life insurance to protect their family
- are willing to provide an executive benefit to help your top performers obtain this valuable protection, and you would like your business to have the option to retain control over the life insurance
- view cost recovery for providing this benefit to be an important consideration
- are interested in exploring whether your business's cash flow can be leveraged to assist in the payment of premiums for your own life insurance needs

Protect a valuable business asset — while watching out for your bottom line

Learn more about how to implement an effective, yet cost-efficient strategy that can help you ensure the loyalty of those employees who are important to your success. Your Guardian Financial Professional can help you choose a strategy that can help you provide your top performers with the kind of rewards they both expect and deserve. Contact your Guardian Financial Professional to start developing your strategy today.

[1] Table 2001-10 is a table promulgated by the IRS and used to determine the economic benefit provided by receiving death proceeds, based on the insured's age. It provides a rate per $1,000 of death benefit from ages 0-99 that represents the value of the death benefit.

[2] Care should be taken not to create a promise, formal or informal, to give the policy to the executive at retirement. Doing so could inadvertently create a Non-Qualified Deferred Compensation Plan, which would then be subject to IRC 409A.

[3] Some whole life policies do not have cash values in the first two years of the policy and don't pay a dividend until the policy's third year. Talk to your financial representative and refer to your individual whole life policy illustration for more information.

[4] Guardian, its subsidiaries, agents, and employees do not provide tax, legal, or accounting advice. Consult your tax, legal, or accounting professional regarding your individual situation.

[5] Supplemental income from a whole life policy comes from loans and withdrawals. Normally, cash values accumulate over the long term. Policy benefits are reduced by any outstanding loan or loan interest and/or withdrawals. Dividends, if any, are affected by policy loans and loan interest. Withdrawals above the cost basis may result in taxable ordinary income. If the policy lapses, or is surrendered, any outstanding loans considered gain in the policy may be subject to ordinary income.

All scenarios and names mentioned herein are purely fictional and have been created solely for educational purposes. Any resemblance to existing situations, persons or fictional characters is coincidental. The information presented should not be used as the basis for any specific insurance/investment advice.

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