



Dynamic Duo: Key Person and Split Dollar

Do you have business clients with the desire to both:

- ◆ Subsidize the purchase of a key executive's personal life insurance, and
- ◆ Protect the business against the loss it may suffer from the death of a key executive?

If so, you may want to suggest an endorsement split dollar arrangement.

Facts: An employer desires to help a 45-year-old key executive purchase \$1,000,000 of life insurance coverage. The company has a need for key person coverage of \$500,000. The employer has also indicated that the business would like to recover the premium it advances. All of these objectives can be accomplished by using a single permanent policy subject to a split dollar agreement.¹ Here is how the concept works.

Solution: The employer purchases, and is owner of, a \$1,500,000 *Option C* death benefit PruLife® Universal Plus life insurance policy on the life of the key executive.

The employer and the executive enter into an endorsement split dollar agreement. The split dollar agreement is structured as a non-equity arrangement where the executive has no rights to any cash values. Through the policy beneficiary endorsement, the face amount of the policy is split so that the executive is given the right to designate the beneficiary of \$1,000,000 of the policy death benefit and the employer designates the business as the beneficiary of the remaining death benefit, which is equal to \$500,000 plus return of premiums.

Premiums are paid according to the terms of the split dollar agreement. The executive is taxed annually on the value of any economic benefits received. Under a non-equity endorsement split dollar arrangement, the executive is taxed on the cost of current life insurance protection less the amount the executive has contributed.²

During the executives' employment, he/she receives valuable life insurance protection with minimal or no out-of-pocket expense.

Meanwhile, the business has key person coverage that will help protect against losses it may suffer as a result of the key executive's death.

At the key executive's retirement, the split dollar agreement is generally terminated. The business then has full control over the policy cash value and death benefit. At that point, the business has a variety of options. It can:

- ◆ Keep the policy intact and recover plan costs from life insurance policy proceeds at the death of the executive, or
- ◆ Access policy cash values through withdrawals and or/loans to take reimbursement sooner.³

Where the executive has a continuing need for life insurance protection during the retirement years, he/she can negotiate with the employer to buy the policy. Or, the business can bonus the policy to the executive as compensation for a job well done. Once the employee owns the policy, he/she can choose to access the policy cash values for retirement income needs.³

Where inclusion in the estate is an issue, an irrevocable life insurance trust (ILIT) can be established and the executive can gift the policy to the trust. This transfer is subject to the gift tax rules.

So, where there are two strong needs for insurance and design flexibility is key, this dynamic pairing may be just the solution.

Product Choice: PruLife® Universal Plus is the appropriate product for this split dollar arrangement. The product includes:

- ◆ Three death benefit options, including Option C – return-of-premiums plus interest
- ◆ Extended maturity beyond age 100
- ◆ Competitive compensation structure, unreduced by age or risk impairment, including 24-month rolling commissionable target premiums (except in NY)

PruLife® Universal Plus has the flexibility you need to meet your client's split dollar objectives.

CHART IS ATTACHED.

¹ The Sarbanes- Oxley Act makes it a crime for publicly-traded companies to, directly or indirectly, enter into a loan with certain directors and officers. It is unclear whether the Act applies to split dollar arrangements. Clients should consult with their own tax or legal adviser for the most recent developments.

² The current life insurance protection is calculated using either the rules in Notice 2002-8 or the rules in other IRS guidance, as applicable.

³ Withdrawals and loans will reduce policy values and death benefit; may affect any guarantee against lapse; and may have tax consequences.

PruLife® Universal Plus is issued by Pruco Life Insurance Company except in New York where it is issued by The Prudential Insurance Company of America. Both are Prudential Financial companies located in Newark, NJ. All guarantees are based on the claims-paying ability of the issuer.

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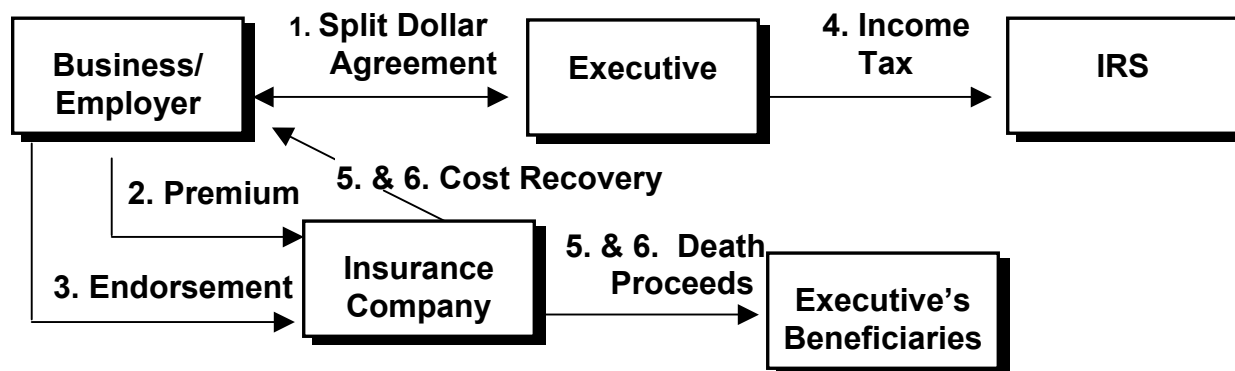
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Structure of Key Person & Split Dollar Combination



1. The employer and executive enter into a non-equity endorsement split dollar agreement detailing the structure as well as the benefits and responsibilities of each party.
2. The employer purchases a life insurance policy insuring the key executive's life. The business is the owner of the policy. Policy premiums are paid in accordance with the written split dollar agreement.
3. Through the policy beneficiary endorsement, the face amount of the policy is split with the business receiving the amount needed for key person coverage and with the balance of the death benefit passing to the executive's named beneficiaries.
4. The executive is taxed on the value of any economic benefit received less the amount the executive contributed.⁴
5. **Pre-retirement:** If the executive should die during employment the business recovers its share of the key person coverage from the death proceeds and the executive's beneficiaries receive the balance of the proceeds, as provided in the split dollar agreement.
6. **Post-retirement:** At the key executive's retirement, the split dollar agreement is generally terminated and the business regains control of the policy cash value and death benefits. The employer may keep the policy intact and recover plan costs at the death of the executive, or may choose to access cash value to reimburse the business.⁵ Alternatively, the business may bonus or sell the policy to the executive.

⁴ The current life insurance protection is calculated using either the rules in Notice 2002-8 or the rules in other IRS guidance, as applicable. This statement is true if the split dollar arrangement is structured as a non-equity endorsement plan; if the split dollar arrangement is structured as an equity endorsement plan, then as part of the economic benefit, the executive is also taxed on the policy cash value to the extent he/she is deemed to have current access and the value of any other economic benefits.

⁵ Life insurance policy cash values are accessed through withdrawals and/or policy loans. Loans are at interest. Loans and/or withdrawals cause a reduction in cash values and death benefits, may affect any guarantee against lapse and may have tax consequences.