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**About our firm:**  
Tempewick Wealth Management is a wealth and insurance firm with professionals specializing in estate and investment planning, business succession and wealth transfer.

# TEMPEWICK

WEALTH MANAGEMENT



## Economic Benefit Regime Private Split Dollar

Recently, a small number of life insurance carriers announced that they're increasing their cost of insurance (COI) rates for in-force policies. This move has prompted concern within the industry and among clients and their advisors, about the drivers of the increases and expectations going forward.

### What is Private Split Dollar?

Private Split Dollar is an advanced life insurance strategy that combines and Irrevocable Life Insurance Trust (ILIT), a life insurance policy and a split dollar agreement to reduce gift taxes and potentially increase an inheritance.

### How Does The Strategy Work?

In an Economic Benefit Private Split Dollar arrangement, a life insurance policy is owned by an ILIT. The Grantor of the trust provides funds to pay the premiums on the policy, but reserves the right to be repaid the greater of the premiums paid or the policy cash values.

### Advantages over a Traditional ILIT

In a typical ILIT, gifts are made by the Grantor to the trust to fund life insurance premiums. These gifts may be subjected to gift tax to the extent that they exceed the annual exclusion available to the Grantor. With an Economic Benefit Private Split Dollar arrangement, gift taxes may be reduced or completely eliminated, depending on the arrangement's structure.

### Planning Steps

- ❖ An ILIT is drafted with an attorney's assistance.
- ❖ The Trustee of the ILIT purchases a life insurance policy insuring the Grantor's life.
- ❖ The Grantor and the Trustee enter into a Split Dollar agreement in which the Grantor provides the trust with funds necessary to pay the policy premiums.
- ❖ Trust commits to repaying the Grantor the greater of the premium paid or policy cash values at later date.
- ❖ The trust collaterally assigns the policy and its cash value to the Grantor as security for the premiums advanced. The Grantor's estate will receive the greater of premiums paid or policy cash value upon death, with the trust as beneficiary of the residual death benefit.

Insurance carriers realize that it isn't in the best interest of anyone to increase COI rates or other policy charges. Carriers will continue to invest in policy management systems and tools to help give clients and advisors a clear understanding and clear expectations of in-force policies.

### Economic Benefit

The IRS has determined that in the Split Dollar Transaction arrangement described above, the non-owner of the policy is providing the policy owners an economic benefit.

## Non-Contributory vs. Contributory Plans

There are two typical premium payment structures.

- ❖ The Grantor will pay the entire premium. The gift he or she is deemed to make to the trust is equal to the economic benefit value of the trust's insurance protection.
- ❖ The trust will pay that portion of the premium equal to the economic benefit value, and the Grantor will pay the balance of the premium.

## What Happens At Death?

At death, the estate of the Grantor receives a portion of the policy death benefits equal to the greater of the total premiums paid or the cash value. The balance is paid to the trust for distribution to the trust's beneficiaries.

## Lifetime Exit Strategy ("Rollout")

Private Split Dollar arrangements can also end at a designated time during the Grantor's life. In a rollout, the Grantor gives up his or her interest for full consideration. The trust then takes full control of the policy.

In order to fund the rollout, the trust must have assets other than the life insurance policy from which to buy out the Grantor's interest. If the trust lacks sufficient assets for this purpose, the Grantor may make additional gifts to the trust.

## Estate Planning Benefits

- ❖ Gift taxes, if any, are limited at the economic benefit value rather than subjecting the full premiums to gift taxation.
- ❖ The Grantor retains control of his or her funds by being able to modify or discontinue future premiums in the event of changing circumstances and by the recovery of policy cash values personally or for his or her estate.
- ❖ The policy owner trust receives cash proceeds at death that are income and estate tax –free to fund the Grantor's estate planning objectives and legacies.

## Considerations

- ❖ If the Grantor is repaid at death from the policy death benefits, the proceeds are includible in the Grantor's estate for estate tax purposes.
- ❖ The economic benefit rates are age based and increase annually.
- ❖ It is important for tax purposes that Split Dollar arrangements be well documented and administered.

Please contact Tempewick Wealth Management if you wish to have a more in-depth discussion regarding Private Split Dollar arrangements.

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The Five Star Wealth Manager award, administered by Crescendo Business Services, LLC (dba Five Star Professional), is based on 10 objective criteria: 1. Credentialed as a registered investment adviser or a registered investment adviser representative. 2. Active as a credentialed professional in the financial services industry for a minimum of 5 years. 3. Favorable regulatory and complaint history review\*; 4. Fulfilled their firm review based on internal standards; 5. Accepting new clients. 6. one-year client retention rate 7. Five-year client retention rate 8. Non-institutional discretionary and/or non-discretionary client assets administered; 9. Number of client households served; 10. Education and professional designations. Wealth managers do not pay a fee to be considered or awarded. Once awarded, wealth managers may purchase additional profile ad space or promotional products. The award methodology does not evaluate the quality of services provided and is not indicative of the winner's future performance. 4,143 New Jersey wealth managers were considered for the award; 626 (16 percent of candidates) were named Five Star Wealth Managers.

Split-Dollar Insurance is not an insurance policy; it is a method of paying for insurance coverage. A split-dollar plan is an arrangement between two parties that involves "splitting" the premium payments, cash values, ownership of the policy, and death benefits. These arrangements are subject to Split Dollar Final Regulations that apply for purposes of federal income, employment and gift taxes. The final regulations provide that the tax treatment of split-dollar life insurance arrangements will be determined under one of two sets of rules, depending on who owns the policy. Transfers to an ILIT are irrevocable and the client may not possess any incidents of ownership in the life insurance policy owned by the ILIT. Trusts should be drafted by an attorney familiar with such matters in order to take into account income, gift and estate tax laws (including generation skipping transfer tax). Failure to do so could result in adverse tax treatment of trust proceeds.