

Using a Business to Fund Life Insurance

For owners, owner-employees, and non-owner employees, personal insurance may be funded through the business a number of different ways. Cash value life insurance, in particular, is frequently employed due to the fact that it can provide long-term insurance protection for one’s family and estate planning needs, as well as act as a tax-efficient source of retirement accumulation funds. In situations where the business retains ownership of the policy, cash values can provide liquidity for certain business needs, while insurance protection guards against unforeseen events, such as loss of a key employee.

	C Corporation	S Corporation	Partnership/LLC*
W-2 Bonus Compensation/ Restricted Bonus Arrangement	<ul style="list-style-type: none"> • Taxable to employee/owner-employee. • Assuming compensation is reasonable, payment is deductible to Company. • Payment may be made directly into policy subject to restrictive endorsement, acting as “handcuff” on key employee. 	<ul style="list-style-type: none"> • Taxable to employee/owner-employee. • Assuming compensation is reasonable, payment is deductible to Company. • Payment may be made directly into policy subject to restrictive endorsement, acting as “handcuff” on key employee. 	<ul style="list-style-type: none"> • Taxable to employee/owner-employee. • Assuming compensation is reasonable, payment is deductible to Company. • Payment may be made directly into policy subject to restrictive endorsement, acting as “handcuff” on key employee.
Cash Dividend/ Distributions to Owners or Owner-Employees	<ul style="list-style-type: none"> • Dividends are taxable at 15% (currently) to shareholder to the extent of earnings and profits (E&P). • May be subject to 20% rate if AGI is in top (39.6%) bracket. • May also be subject to Medicare Surtax of 3.8% if AGI exceeds \$200K/\$250K single/joint filer. • Dividends are not deductible to Company. 	<ul style="list-style-type: none"> • Distributions must be pro-rata based on ownership. • Not subject to FICA taxes, assuming compensation otherwise paid is commensurate with services performed on behalf of Company. • Distributions reduce basis, with distributions in excess of basis subject to capital gains. • Distributions from AAA (if former C corp) - not taxable but reduces shareholder’s basis. • Distributions from E&P (if former C corp) does not reduce basis but is taxable to shareholder. 	<ul style="list-style-type: none"> • Distributions do not need to be pro-rata. • Return of Basis – partner’s basis is reduced by distribution. • Capital Gain – distributions in cash that exceed partner’s basis are subject to capital gain.

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Loan Split Dollar Insurance	<ul style="list-style-type: none"> • Company lends premiums to employee/owner-employee in exchange for a promissory note. • Interest rate should be at the applicable federal rate, and is taxable as income to Company. 	<ul style="list-style-type: none"> • Generally same as C Corp. 	<ul style="list-style-type: none"> • Generally same as C Corp.
Economic Benefit Split Dollar Insurance	<ul style="list-style-type: none"> • Company pays premiums and owns the cash value. • Company may own the policy and endorse proceeds in excess of cash value to beneficiary of insured. • Conversely, insured may own policy so long as no rights to anything other than death benefit protection possessed. • Insured recognizes value of economic benefit of insurance protection as either compensation income or distribution, depending on ownership in the Company. 	<ul style="list-style-type: none"> • Generally same as C Corp, subject to S Corp rules governing taxation of deemed distributions of economic benefit. 	<ul style="list-style-type: none"> • Generally same as C Corp, subject to partnership rules governing taxation of deemed distributions of economic benefit.
Deferred Compensation Programs for Key Employees	<ul style="list-style-type: none"> • Company makes unsecured promise to pay stipulated benefit to employee in the future, generally subject to forfeiture if employee leaves Company within certain timeframe. • Benefit typically taxable to employee when paid, at which point it becomes deductible to Company. • Cash value life insurance frequently employed as informal accumulation vehicle to provide key employee insurance, as well as tax efficient source of promised payments. 	<ul style="list-style-type: none"> • Generally same as C Corp. 	<ul style="list-style-type: none"> • Generally same as C Corp.

* Assuming LLC taxed as partnership.



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