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# The Feldmans

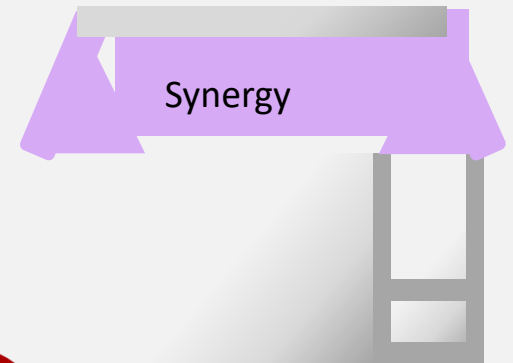
Generation 2

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# Agenda

- Feldman Family: Generation 2
  - Issues/Needs
  - Solutions
- Maya
  - Issues/Needs
  - Solutions
- Other Members of the Executive Team
  - Issues/Needs
  - Solutions





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# Continuing Education

IMPORTANT – Watch for the survey questions!  
They are necessary for CE credit.



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Abel  
Sr. Sales  
Director

5%



Patti  
COO

5%



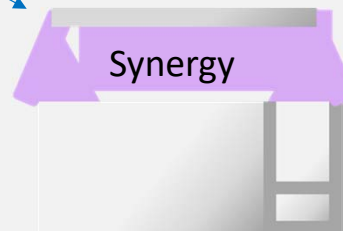
Sheldon  
Innovation  
Strategist

5%



Keegan  
Playboy

5%





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# Issues

- Estate Planning – Do each of them have plans in place in case of death or disability?
- Retirement Planning – Abel, Patti and Sheldon have concerns about funding their plans.
- Business Succession Planning – What happens to their equity if they die or become disabled?





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# Succession Planning

## Generation 2

# Questions:

- Who will buy?
  - The company?
  - All shareholders pro-rata?
  - Only employee/shareholders?
- When will they buy?
  - Death?
  - Disability?
  - Retirement?
  - Proceeding?





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# Questions:

- At what price?
  - Willing buyer/Willing seller
  - Special requirements to fix business value for estate tax purposes (IRC §2703):
    - Bona fide business arrangement;
    - Not a device to transfer property to family for less than full and adequate consideration;
    - Terms are comparable to arms' length transaction
    - Discounted valuation?







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# Questions:

- How will they pay?
  - Installment sale
  - Insurance
    - Executive bonus arrangements
    - Split Dollar Arrangements
  - Insurance LLC
    - Holds life insurance contracts for cross-purchase
    - Need special provisions in operating agreement





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## Polling Question

IRC §2703 requires that a buy-sell agreement between family members must be:

- a. Bona fide business arrangement
- b. Not a device to transfer property to family for less than full and adequate consideration
- c. Comparable to arms' length transaction
- d. All of the above
- e. None of the above



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# Maya

# Maya

- VP Strategic Operations
- Company's most valuable employee
- Being heavily recruited
- Special Needs son, Riley (age 17)
- Wants to be rewarded for growth of the Company, but does not want stock





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## Questions:

- What type of needs does Riley have?
  - Guardianship?
  - Needs based benefits?
- Special needs trust?
  - Within an RLT vs. Stand Alone?
  - Funding the SNT
  - Retirement plan assets?
    - SECURE Act special rules
  - Life insurance?





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# Executive Benefits



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# Tie Non-family Key Employees to the Business

- Employment Agreements
- Equity plans (Restricted Stock, stock options)
- “Synthetic Equity” (Phantom Stock, Stock Appreciation Rights)





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# Phantom Stock/Equity

- Right to receive cash at a specified date in the future based upon the performance of company equity over a specified period of time
- Structure can take a number of forms
- May provide vesting schedule







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# Phantom Stock/Equity

- Deferred compensation plan subject to the provisions of §409A
  - Failing to meet requirements has serious adverse tax consequences:
  - All vested accrued benefits become immediately taxable.
  - The taxable amount is also subject to a 20% penalty and interest charges.





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# Phantom Stock/Equity

## When does it pay?

- Separation from service
- Death
- Disability (defined in §409A)
- Change in control of company (defined in §409A)
- Unforeseeable emergency
- At a specified time or pursuant to a fixed schedule.





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# Phantom Stock/Equity: Taxation

- Executive normally taxed at ordinary income rates (and company gets a deduction) when paid.

*Anna receives 1,000 shares of phantom stock which will pay a benefit only upon a change of control of the company.*





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## Uses of Phantom Equity

- Owners do not want to dilute ownership
- Owners only want to pay a benefit to participants upon a change of control or specified events
- Can be used to recruit, retain or reward executives
- Amount of benefit linked to company *value*
- Can be used in various types of entities



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# Phantom Equity

## ***Pros***

- No dilution of owners
- Minimal effect on corporate cash flow
- Only pays out upon occurrence of events
- Tax deferral for executive/deduction for company
- Available to many types of entities

## ***Challenges***

- Company deduction deferred
- No voting rights or rights to dividends
- May not be meaningful to the executive
- Deferred compensation plan subject to §409A



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# Equity Appreciation Rights

Right to receive cash on or after a specified date in the future based upon the difference in the value of X units of equity on the grant date and the value of the same number of units on the exercise date

*Rob receives a grant of appreciation rights in 100 shares when the stock is worth \$5 per share. At exercise, the stock is worth \$10 per share. His benefit is \$5 per share*





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# Equity Appreciation Rights

Participant will be taxed at ordinary income rates, generally at the time that the benefit is paid.

*Rob exercises his appreciation rights as to 1000 shares in 2018. He will include \$5,000 in his income (\$5 per share appreciation x 1000 shares) and be taxed at ordinary income rates.*





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# Uses of Appreciation Rights

- When the owners do not want to be diluted
- To recruit, retain or reward
- To provide an incentive tied to the company's success on a go forward basis
- Flexibility to add conditions to exercise:
  - Vesting schedule
  - Achieving financial benchmarks
  - Both





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# Appreciation Rights

## ***Pros***

- No dilution
- Benefit tied to company's success
- Flexible
- Simple to understand and administer
- No tax until exercise

## ***Cons***

- Executive does not have the rights of a stockholder
- Deduction deferred until exercise



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# Split Dollar Life Insurance Solutions

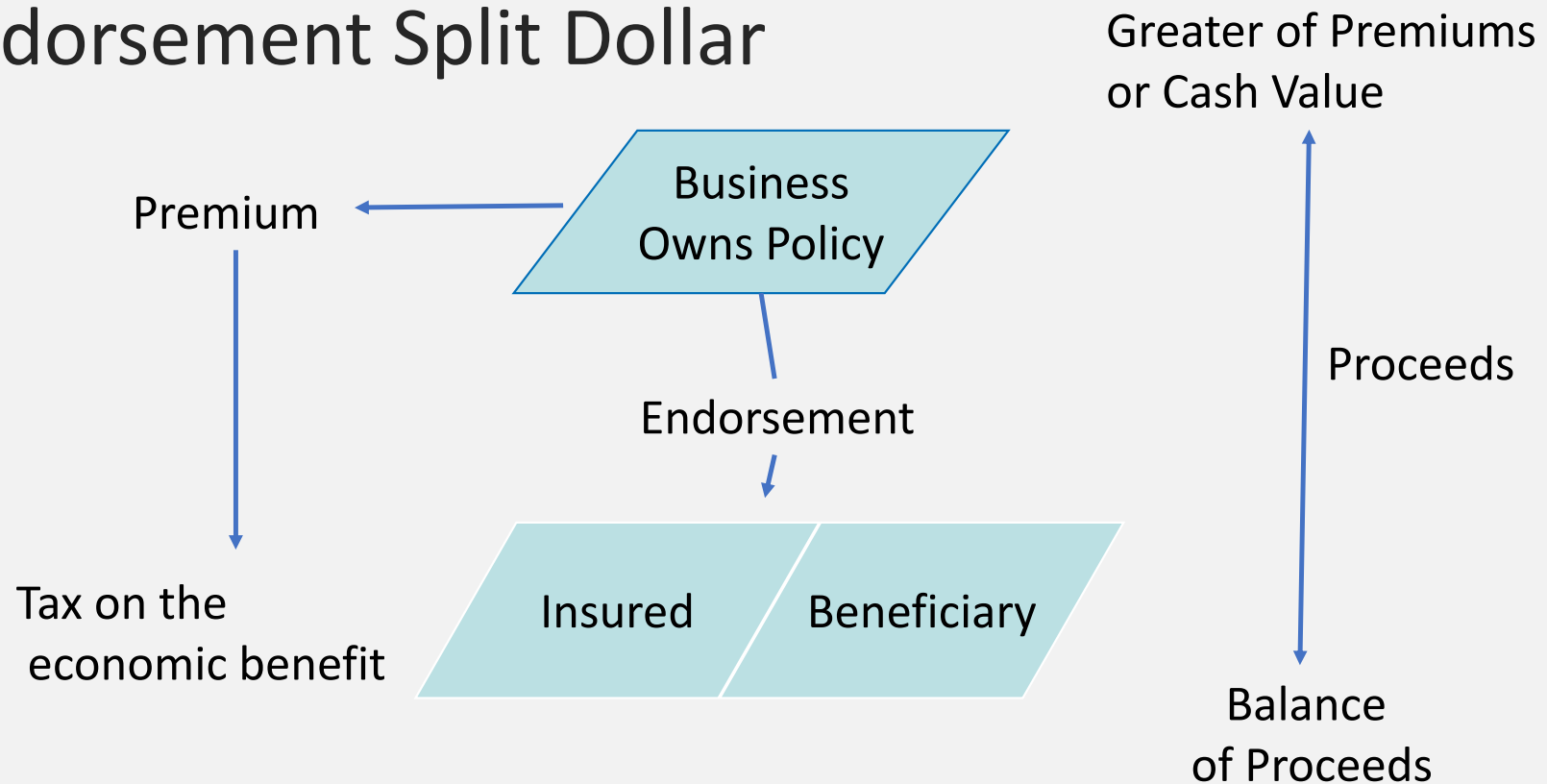
- Business and key employee or owner share the costs and benefits of a life insurance policy
- Endorsement Split Dollar Plans
  - Taxation under Economic Benefit Rules
- Collateral Assignment Split Dollar Arrangements
  - General Rule: Taxed under the Loan Regime
  - Exception



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# Employer Owned: Endorsement Split Dollar

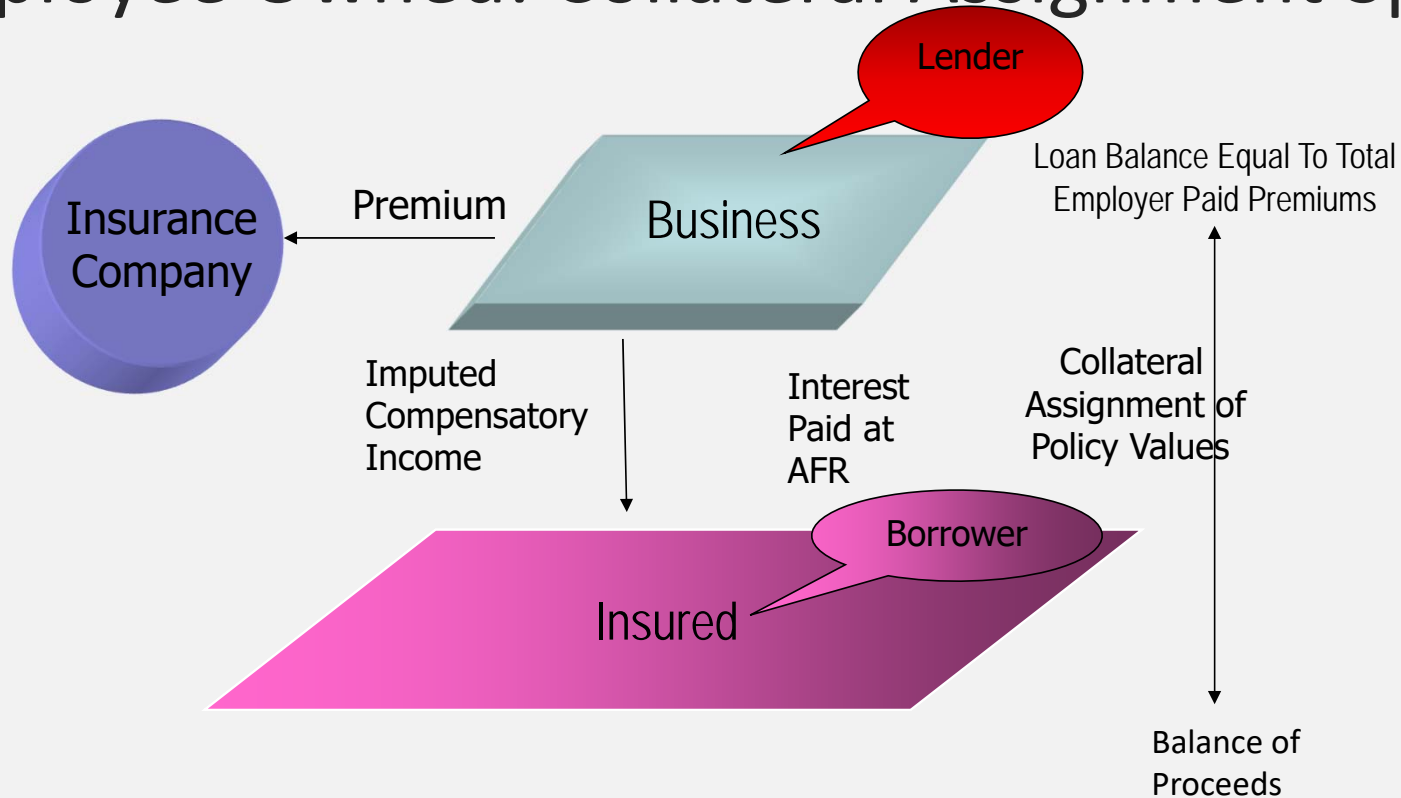




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# Employee Owned: Collateral Assignment Split Dollar





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# Collateral Assignment Split Dollar

- Employer loans premium payments to employee to pay policy premiums
- Loan to be repaid when employee separates from service or dies
- Loans may be demand loans (payable on demand) or term loans (for a term of years)
  - Must bear interest at the appropriate Applicable Federal Rate or income will be imputed
    - Demand loans = Blended Rate
    - Term Loans = Long-Term, Mid-Term or Short-Term rate



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# Collateral Assignment at Termination of Employment

- Employee pays back loan
  - Agreement terminates
  - Employee keeps policy
- Employer forgives the loan
  - Employee taxed on the amount of the loan forgiveness
- Employee dies
  - Under Split Dollar Agreement, Employer is paid from policy proceeds
  - Remaining proceeds to beneficiary income tax free





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# Split Dollar

## ***Pros***

- Significant amounts of life insurance at a minimal out of pocket cost for the employee
- Possible source of supplemental retirement income
- Selective benefit
- Few ERISA requirements
- Minimal administration

## ***Cons***

- Economic benefit may become prohibitively expensive at older ages
- No deduction for business' share of the premium payment
- Perception that split dollar taxation rules are complicated



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## Polling Question

Which of the following gives the executive benefits on a go-forward basis only?

- a. Phantom Stock
- b. Stock Appreciation Rights
- c. Both of the above
- d. Neither of the above





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# Remainder of Executive Team





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## Questions:

- Remainder of executive team ages 37, 48, 61
- Is there a plan that will appeal to all of these executives and future recruits?





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# What is a SERP?

- 100% employer paid type of non-qualified plan to provide benefits to a select group of employees
- Select group of management or highly compensated personnel = Top Hat
- May be defined benefit or defined contribution
- Avoids most ERISA requirements
- Subject to 409A





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Which plans can be informally financed  
with life insurance?



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# Why Use Life Insurance to Informally Finance?

## ***Pros***

- Tax deferred cash accumulation
- Tax-free access to policy values via withdrawals and loans
- Company receives tax-free death proceeds
- Cost recovery from proceeds

## ***Cons***

- High early policy charges
- Difficult to use policy values for older participants
- Premium payments are not deductible



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## SERP Dollar –Two Benefits in One

- Split dollar plan provides a pre-retirement death benefit which is received income tax free
- The cash values of the same business owned life insurance policy can be used to informally fund the SERP





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## Polling Question

Which executive benefit plans may be informally financed using life insurance?

- a. Phantom Stock
- b. Stock Appreciation Rights
- c. SERPs
- d. All of the above
- e. None of the above



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## Questions:

- What about Doris?
- Can she be part of the top hat group?
- Are there other options that might work better for her?







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# Questions and Answers



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## Tune In Next Week!

When Andrew Rinn of Ameritas is going to dig deeper on a few great planning ideas that will work for generation three of the Feldmans!

- Creating estate equalization
- Solving the Maria dilemma
- Crafting a business transfer to Hunter



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# The Feldmans

Generation 2

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