

Financing Options At-A-Glance

This chart summarizes some of the financing options available to fund a large life insurance need.

	Private Split Dollar	Private Financing	Premium Financing	Dual Loan Planning
Lender	Mom/Dad	Mom/Dad	Bank	Mom/Dad and Bank
Description	Mom/Dad pays annual term costs or Table 2001 rates ¹ and Trust pays the difference	Intra-family Loan Transaction ²	Approved third-party lender (AI Credit, or other bank) provides loan for purchasing life insurance	Combining different loan arrangements to minimize loan interest cost (Private vs. Premium)
Loan Interest Rate or Annual Cost of Financing	Economic benefit cost	Applicable Federal Rate (AFR): short-term (0–3 years), mid-term (3–9 years) or long-term (9+ years)	LIBOR + spread (typically)	Rates linked to each type of loan arrangement
Gift Tax Impact	Minimizes gift taxes because loans are NOT gifts	Minimizes gift taxes because loans are NOT gifts	Minimizes gift taxes because loans are NOT gifts	Minimizes gift taxes because loans are NOT gifts
How It Works	Mom/Dad as lender provides liquidity to pay large premiums on needed policy	Mom/Dad as lender provides liquidity to pay large premiums	Lender provides liquidity to pay large premiums on needed policy	Provides liquidity while potentially minimizing loan interest costs
Benefits	Minimizes gift tax costs	Minimizes gift tax costs	No need to liquidate taxable assets to fund liquidity needed for premiums	Minimizes gift taxes and reduces the need to liquidate taxable assets to fund premiums
Collateral	Policy	Not required but may be advisable	Policy and/or other liquid assets	Collateral requirements of commercial lender
Potential Generation-Skipping Transfer Tax (GSTT) Impact	GSTT exemption should be allocated to gift of economic benefit amount	GSTT exemption should be allocated to gifts of interest	GSTT exemption should be allocated to gifts of interest	GSTT exemption allocated to gifts of interest

1. Instead of loan interest which is based on the cumulative loan principal balance, the economic benefit cost (which is based on the death benefit amount and age) is used. This can be quite low at the younger ages, especially when a survivorship policy is used. However, the economic benefit rates increase over time as the insured ages. It may make sense to consider Private Split Dollar (PSD) arrangement initially and switch to a Privately Financed Plan when the economic benefit rates get too high.
2. Arms length transaction between family members and/or trust. Interest will be based on Applicable Federal Rates (AFR) published monthly by government.

Trusts should be drafted by an attorney familiar with such matters to take into account income, gift, and estate taxes, including generation-skipping transfer taxes. Failure to do so may result in adverse tax consequences.

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