**Internal Revenue Service**

Department of the Treasury
Washington, DC 20224

Number: **200825011**
Release Date: 6/20/2008

Index Number: 2501.00-00, 2042.00-00

Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:PSI:B04 – PLR-136339-07
Date: FEBRUARY 05, 2008

Re:

Legend

A =
B =
Child 1 =
Child 2 =
Child 3 =
Trust =

Date 1 =
Date 2 =
Policy =
Agreement =

Dear :

This is in response to your letter dated January 29, 2008, and prior correspondence, submitted by your authorized representatives in which you requested rulings concerning the federal estate and gift tax consequences of the ownership by a trust of a life insurance policy subject to a split-dollar life insurance agreement.

On Date 1, A and B, husband and wife ("Grantors"), established an irrevocable trust, Trust, for the benefit of their descendants. The initial trustee of Trust is the Grantors' child, Child 3. The Grantors are prohibited from serving as trustees. Under the terms of Trust, the trustee initially is to hold the trust property as three separate trusts, one trust for the primary benefit of each of the Grantors' three children Child 1,

Child 2, and Child 3 (each denoted as a "Beneficiary"). Prior to the death of the last to die of A and B, the trustee has discretion to distribute such amounts of income and corpus to any descendant of A and B, as the trustee deems desirable; provided, however, that a person who is serving as a trustee cannot distribute any amounts to himself or herself other than amounts subject to a withdrawal power. After the death of the last to die of A and B, the trustee has discretion to distribute income and corpus to the Beneficiary and that Beneficiary's descendants, in such amounts as are necessary to provide for the Beneficiary's or the Beneficiary's descendants', health, support, maintenance, and education. Each trust established for a Beneficiary who is a child of the Grantors, is to terminate on the Beneficiary's death, at which time the trust corpus is to be distributed pursuant to the exercise of a testamentary limited power of appointment granted to each Beneficiary.

On Date 2, Trust purchased and paid the initial premiums on Policy, a second-to die life insurance policy on the lives of A and B. Trust was designated owner and beneficiary of the policies.

It is proposed that A, B, and the trustee will enter into a split-dollar arrangement. Under the arrangement, the parities will execute a split-dollar agreement ("Agreement") and a collateral assignment. Under the Agreement, A and B will contribute 100% of the annual premium amounts to Trust and Trust will make the premium payment to the insurance company. Upon the death of the survivor of A and B, the survivor's estate is entitled to receive the greater of the cash surrender value of the policy prior to termination or an amount equal to all premiums paid by A and B. Trust is designated as the beneficiary of the balance of the insurance proceeds. Trust is also designated as the owner of Policy. Trust retains all ownership rights, but may only pledge or assign the Policy for the sole purpose of securing a loan from the insurer or third party for the purpose of repaying A and B. All other incidents of ownership reside in the trustee.

Prior to the death of the survivor of A and B, the Agreement may be terminated at will: (i) by A and B acting jointly, or by the survivor between them; or (ii) by the trustee of Trust. In addition, the Agreement will also terminate upon the personal bankruptcy of A and B, the failure of A and B to pay premiums and the trustee's surrender or cancellation of Policy. If the Agreement terminates during the lifetimes of A and B, or the lifetime of the survivor, then within 60 days of termination, Trust is required to repay A and B, or the survivor, an amount equal to the greater of the cash surrender value of the policy, or the premiums paid by A and B to the extent the cash surrender value of the policy is not sufficient to pay this amount.

To secure A's and B's and their respective estates' interest in Policy and its proceeds, the trustee proposes to execute a Collateral Assignment pursuant to which the trustee will assign Policy to A and B. However, under the terms of the Collateral

Assignment, the trustee specifically retains all rights of ownership in the Policy subject to the right of A and B, or the estate of the survivor to receive repayment on termination of the Agreement.

You have asked that we rule as follows:

1. A and B are the deemed owners of Policy under section 1.61-22(c)(1)(ii)(A)(2) of the Income Tax Regulations.

2. Pursuant to section 1.61-22(d), a taxable gift occurs upon each payment of premium by A and B.

3. The value of the annual gifts made by A and B is equal to the cost of current life insurance protection provided to Trust.

4. The insurance proceeds payable to Trust will not be includible under § 2042 of the Internal Revenue Code in the gross estate of the survivor of A and B.

Ruling Requests 1-3

Section 1.61-22(b)(1) provides that a split-dollar life insurance arrangement is any arrangement between an owner and a non-owner of a life insurance contract that satisfies the following criteria—(i) either party to the arrangement pays, directly or indirectly, all or any portion of the premiums on the life insurance contract, including a payment by means of a loan to the other party that is secured by the life insurance contract; (ii) at least one of the parties to the arrangement paying premiums is entitled to recover (either conditionally or unconditionally) all or any portion of those premiums and such recovery is to be made from, or is secured by, the proceeds of the life insurance contract; and (iii) the arrangement is not part of a group-term life insurance plan described in section 79.

Section 1.61-22(b)(3)(ii)(B) provides that section 1.61-22(d) through (g) applies (and section 1.7872-15, addressing split-dollar loans does not apply) to any split-dollar life insurance arrangement where the arrangement is entered into between a donor and a donee (for example, a life insurance trust) and the donor is the owner of the life insurance contract (or is treated as the owner of the contract under 1.61-22(c)(1)(ii)(A)(2)).

Section 1.61-22(c)(1) provides, in general, that with respect to a life insurance contract, the person named as the policy owner of such contract generally is the owner of such contract.

Section 1.61-22(c)(1)(ii)(A)(2) provides that a donor is treated as the owner of a life insurance contract under a split-dollar life insurance arrangement that is entered into between a donor and a donee (for example, a life insurance trust) if, at all times, the only economic benefit that will be provided under the arrangement is current life insurance protection as described in section 1.61-22(d)(3).

Section 1.61-22(d)(1) provides in part, that in the case of a split-dollar life insurance arrangement subject to the rules under section 1.61-22(d) through (g), economic benefits are treated as being provided to the non-owner of the life insurance contract. The non-owner (and the owner for gift and employment tax purposes) must take into account the full value of all economic benefits described in section 1.61-22(d)(2), reduced by the consideration paid directly or indirectly by the non-owner to the owner for those economic benefits. Depending on the relationship between the owner and the non-owner, the economic benefits may constitute a payment of compensation, a distribution under section 301, a contribution of capital, a gift, or a transfer having a different tax character.

Section 1.61-22(d)(2) provides generally that the value of the economic benefits provided to a non-owner for a taxable year under the arrangement equals: (i) the cost of current life insurance protection provided to the non-owner determined under section 1.61-22(d)(3); (ii) the amount of policy cash value to which the non-owner has current access within the meaning of section 1.61-22(d)(4)(ii) (to the extent such amount was not actually taken into account for a prior taxable year); and (iii) the value of any economic benefits not described above provided to a non-owner (to the extent not actually taken into account for a prior taxable year).

Section 1.61-22(d)(3)(i) provides, in part, that the amount of current life insurance protection provided to the non-owner for a taxable year (or any portion thereof in the case of the first year or the last year of the arrangement) equals the excess of the death benefit of the life insurance contract (including paid-up additions thereto) over the total amount payable to the owner (including any outstanding policy loans that offset amounts otherwise payable to the owner) under the split-dollar life insurance arrangement, less the portion of the policy cash value actually taken into account under section 1.61-22(d)(1) or paid for by the non-owner under section 1.61-22(d)(1) for the current taxable year or any prior taxable year.

Section 1.61-22(d)(3)(ii) provides that the cost of current life insurance protection provided to the non-owner for any year (or any portion thereof in the case of the first year or the last year of the arrangement) equals the amount of current life insurance projection provided to the non-owner (determined under section 1.61-22(d)(3)(i)) multiplied by the life insurance premium factor designated or permitted in guidance published in the Internal Revenue Bulletin.

Section 1.61-22(d)(4)(ii) provides in part, that for purposes of section 1.61-22(d), a non-owner has current access to that portion of the policy cash value to which, under the arrangement, the non-owner has a current or future right; and that currently is directly or indirectly accessible by the non-owner, inaccessible to the owner, or inaccessible to the owner's general creditors.

In the present case, under section 1.61-22(c)(1)(ii)(A)(2), A and B will be treated as the owners of Policy, because under the terms of the Agreement, the only economic benefit that will be provided under the split-dollar arrangement is current life insurance protection. Because Trust will not provide any consideration towards the purchase of the life insurance, the amount of the annual gift by A and B is the full cost of current life insurance protection provided to Trust.

We express no opinion concerning the federal gift tax consequences between A and B of the arrangement regarding the second-to-die policy.

Ruling Request 4

Section 2042(1) provides that the value of a decedent's gross estate shall include the proceeds of insurance policies on the decedent's life receivable by the decedent's estate.

Section 2042(2) provides that the value of a decedent's gross estate shall include the proceeds of all life insurance policies on the decedent's life receivable by beneficiaries other than the executor of the decedent's estate, to the extent that the decedent possessed at his death any incidents of ownership exercisable either alone or in conjunction with any other person. An incident of ownership includes a reversionary interest arising by the express terms of the instrument or by operation of law only if the value of such reversionary interest exceeds 5 percent of the value of the policy immediately before the death of the decedent.

Section 20.2042-1(c)(2) of the Estate Tax Regulations provides that "incidents of ownership" is not limited in its meaning to ownership of a policy in the technical legal sense. Generally, the term has reference to the right of the insured or his estate to the economic benefits of the policy. Thus, it includes power to change the beneficiary, to surrender or cancel the policy, to assign the policy, to revoke an assignment, to pledge the policy for a loan, or to obtain from the insurer a loan against the surrender value of the policy.

In the present case, under Agreement and the Collateral Assignment, neither A nor B will hold any incidents of ownership in Policy. As noted above, all incidents of

ownership in the policies are vested in the trustee of Trust. Accordingly, we conclude that the proceeds of the policy payable to Trust will not be included in the gross estate of the second to die of A and B under section 2042(2). The portion of the proceeds payable to the estate of the survivor of A and B will be includible under section 2042(1). See, e.g., Rev. Rul. 79-129, 1979-1 C.B. 306.

Except as specifically set forth above, we express no opinion concerning the federal tax consequences of the foregoing transactions under any other provisions of the Code or regulations.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Under a power of attorney on file with this office, we are sending a copy of this letter to your authorized representative.

Sincerely,

George Masnik
Chief, Branch 4
Office of Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosures (2)
Copy of this letter
Copy for § 6110 purposes

cc: