Internal Revenue Service

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Person To Contact:
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Refer Reply To:
CC:PSI:4
PLR-118835-99

Date: SEPTEMBER 30, 2008

Re:

Legend

Settlor A =
Settlor B =
Trust =

Agreement =

Date =
Trustees =

Dear :

This is in response to your request for a ruling on behalf of Settlor A and Settlor B concerning the gift and estate tax consequences of a private split-dollar insurance arrangement.

The facts, as submitted, indicate that Settlor A and Settlor B who are married, created an irrevocable trust (Trust) on Date. Trustees were named as trustees of the

trust. Under the terms of Trust, the trustee is required to distribute trust income annually to a class of beneficiaries consisting of the Settlors' living issue (but excluding their children). Each member of the class has a noncumulative power to withdraw their share of any contributions to the trust. The trustee also has the discretion to distribute corpus to a member of the class to provide for the beneficiary's health, education, support, and maintenance. If a member of the class dies survived by issue, the surviving issue become members of the class. Trust will terminate on the later of the death of the last surviving Settlor, or when the number of class members equals 40. In no event may any trust established under the Trust instrument extend beyond the applicable rule against perpetuities. Upon termination, the corpus will be divided into as many equal shares as there are then living children of the Settlors and deceased children of the Settlors who have left issue then surviving.

Each share created on account of a living or deceased child of the Settlors shall be further divided into as many equal shares as there are then living children of the said child and deceased grandchildren who have left issue then surviving. Each share created for a grandchild that is age 35 at termination will be distributed outright. If a grandchild is not age 35, then the share will continue in trust for the grandchild. If a deceased grandchild is survived by issue, then the grandchild's share is to be distributed outright, per stirpes.

The terms of the Trust specifically preclude either Settlor from acting as trustee. Further, the Settlors have retained no powers or authority over the Trust, Trust property, or the administration of the Trust.

The Trust has purchased a second-to-die life insurance policy on the lives of Settlor A and Settlor B and proposes to entered into a split-dollar life insurance agreement (Agreement) with Settlors. Under the agreement, the Trust will continue to own the policy and will pay during the joint lives of the Settlors an amount equal to the insurance company's current published premium rate for annually renewable term insurance generally available for standard risks. After the death of the first Settlor, the Trust will pay an amount equal to the lesser of: (1) the applicable amount provided in Notice 2001-10, 2001-1 C.B. 549**,** or subsequent IRS guidance; or (2) the insurer's current published premium rate for annually renewable term insurance generally available for standard risks. The Settlors will pay the balance of the premiums.

Under the Agreement, the Trust will collaterally assign the following rights to the Settlors: (1) if the Agreement terminates on the death of the survivor of Settlor A and Settlor B, then upon the death of the survivor, the right of the survivor's estate to receive the greater of the cash surrender value of the policy or the cumulative premiums paid by the Settlors; and (2) if the Agreement terminates during the lifetime of Settlor A and Settlor B, or the lifetime of the survivor, then within 60 days of termination, the right to receive from Trust an amount equal to the greater of the cash surrender value of the policy, or the premiums paid by Settlor A and Settlor B, to the extent Trust has other

assets. Under the Agreement, all incidents of ownership over the policy (including the sole right to surrender or cancel the policy, and the sole right to borrow or withdraw against the policy) are vested in the Trustees of Trust.

You have asked that we rule as follows:

1. The payment by Settlor A and B of the premiums pursuant to the Agreement will not result in a gift or a deemed gift to the Trust by Settlor A and B under §§ 2501 and 2511.

2. The insurance proceeds payable to the Trust will not be includible under § 2042 in the gross estate of either Settlor A or B.

ISSUE 1

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 section 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. Under the terms of the Agreement, Trust will pay the portion of the premium equal to the cost of current life insurance protection and Settlor A and B will pay the balance of the premium. Settlor A and/or B (or the estate of the survivor) will be entitled to receive an amount equal to the greater of the policy cash surrender value or premiums paid on early termination or at the death of the survivor. We conclude that the payment of the premiums by Settlors A and B, pursuant to the terms of the Agreement, will not result in a gift by Settlor A and B under section 2511, provided that the amounts paid by the Trust for the life insurance benefit that the Trust receives under the Agreement is at least equal to the amount prescribed under Notice 2001-10

We also conclude that, if some or all of the cash surrender value is used (either directly, or indirectly through loans) to fund the Trust's obligation to pay premiums, Settlor A and B will be treated as making a gift at that time.

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

Ruling Request 2

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 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 Settlor A nor B will hold any incidents of ownership in Policy. As noted above, all incidents of ownership in the policies, including the power to change the beneficiary, the power to surrender or cancel the policy, the power to assign the policy or to revoke an assignment, and the power to pledge the policy for a loan or to obtain from the insurer are vested in the Trustee of Trust. Accordingly, we conclude that the proceeds of the policy payable to the 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.

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

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.

Sincerely,

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

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