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By **Robert W. Finnegan**

Designing a Generational Split-Dollar Plan

Careful planning, implementation and administration are needed

Much has been written[1] about generational split-dollar (GSD).[2] Let's take a fresh look at the 2016 *Morrissette v. Commissioner*,[3] 2021 *Morrisette v. Comm'r*[4] and *Levine v. Comm'r* cases[5] in light of recent developments, including the Internal Revenue Service's reported aggressive examination of GSD plans. I'll review important aspects of these cases and offer a number of important GSD plan and policy design considerations.

GSD is a funding strategy in which a senior generation (G1), rather than the insured second generation (G2), funds trust-owned life insurance. Here's how the typical GSD plan operates:

- Parent (G1) creates an irrevocable dynasty trust that's also a grantor trust for income tax purposes with respect to G1 for the benefit of grandchildren and subsequent generations (G3+).
- The trust purchases a substantial life insurance policy on the child's life and/or the child's spouse (G2).
- Unlike the typical plan in which G2 is the premium payer, G1 makes substantial upfront advances or loans to the trust to fully fund the policy pursuant to a split-dollar agreement and holds a split-dollar receivable based on the premiums advanced or lent to the trust.
- The split-dollar agreement provides that G1 will be repaid at G2's death.
- During G1's lifetime or on their death, G1 transfers the receivable to a second trust. Because the receivable won't be repaid until the G2's death (actuarially, a long time in the future), it's valued at a substantially lower amount than its face value.

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Morrissette, *Levine* and, to a lesser extent, *Estate of Cahill*,[6] provide a roadmap for implementing a GSD plan. It's important to note at the outset, however, that the law in this area continues to develop, and the IRS continues aggressively to examine, audit and, in some cases, litigate these plans.

I'll explore GSD planning factors that will help lead to a favorable outcome and suggest ways to minimize plan risks and manage client expectations.

Morrissette

In 2006, Clara Morrissette's revocable trust advanced a total of $30 million[7] to dynasty trusts pursuant to economic benefit regime split-dollar plans to purchase life insurance on the lives of her three sons to fund a buy-sell agreement.[8] Clara established one dynasty trust for each son for the benefit of grandchildren and future generations. Each son's dynasty trust purchased insurance on his brothers, and Clara's revocable trust held receivables equal to the combined $30 million premium advances. Each year, from 2006 to 2009, the dynasty trusts paid a portion of the respective 1-year term cost of its share of the death benefit based on the Table 2001 rates, and Clara reported the balance of the 1-year term cost as a gift. Clara died in 2009. The estate valued her receivables at $7.5 million, 25% of their face value. Pursuant to IRC Sections 2036, 2038 or 2703, the IRS asserted that the entire $30 million was a gift at inception of the policy and issued a deficiency notice to the estate equal to $13.8 million in gift taxes and $2.76 million in penalties.

In the 2016 *Morrissette* Tax Court gift tax case, the court granted partial summary judgment in

favor of the estate, holding that the GSD agreements were, in fact, economic benefit regime split-dollar agreements and that the only benefit conferred on the dynasty trusts were the 1-year term costs. In reaching its holding, the court noted two critical facts. First, the agreements adhered to the economic benefit regime rules and exactly followed an example in the IRS' preamble to the final split-dollar regulations. Second, the agreements served a valid non-tax reason, providing for the continuation of the business in the event of the sons' deaths. It's important to note that the IRS didn't acquiesce to the Tax Court's ruling, and as a gift tax case, the Tax Court didn't address the valuation of the receivable in Clara's estate.

In the 2021 *Morrissette* estate tax case, a Tax Court memorandum decision, the court ruled favorably that only the date-of-death fair market value (FMV) of the receivable was includible in her estate.[9] First, the court ruled that the GSD agreement qualified for the bona fide sale exception to Sections 2036 and 2038. The court determined that: (1) the GSD plan had a valid business purpose; and (2) Clara's rights to full repayment of the receivable during her lifetime constituted adequate and full consideration. Second, the court determined that Section 2703 didn't apply because the GSD plan met the three requirements of the subsection (b) exception. Finally, distinguishing adequate and full consideration at inception of the plan, the court went on to determine the FMV of the receivable at Clara's death.

The court rejected the estate's valuation equal to 25% of the receivable's face value, holding that a prearranged plan existed to terminate the GSD plan shortly after Clara's death. First, when Clara implemented the GSD plan, her revocable trust was amended to allow it to distribute the receivable to the dynasty trust. This amendment evidenced a prearranged plan to terminate the GSD plan. Second, when one of Clara's sons (G2) indicated an interest in surrendering the policies, his counsel advised him (in an email!) to wait three years until the statute of limitations expired. Third, the mutual consent of Clara's revocable trust and each dynasty trust was required to terminate the split-dollar agreements. In *Cahill*, the court had held that G1's right to terminate a split-dollar agreement with the mutual consent of the trustee was a property right for purposes of Section 2036(a)(2) and 2038.[10] Fourth, each son's respective receivable was transferred to his dynasty trust, extinguishing the split-dollar agreement and giving him full control of the policies in his trust insuring his brothers. This combination of "bad facts" led the court to shorten the discount period to just over three years rather than base the valuation on the insureds' mortality over time. (See "Valuing the Split-Dollar Receivable," p. 28.)

Although the 2021 *Morrissette* case had a negative outcome for the family, it was a victory for GSD planning in three important respects. First, the court ruled that, if properly structured, none of Sections 2036, 2038 or 2703 will cause estate inclusion of the face value of the receivable. Second, it established a valuation methodology followed by the IRS, the *Morrissette* estate and, ultimately, the *Levine* estate. Third, perhaps most importantly, it identified a number of design and administrative pitfalls to avoid.

SPOTLIGHT

Taking A Break
Cigarette Girl by Pauline Palmer sold for $7,620 at Freeman's | Hindman A Lasting Legacy: The Estate of Michael Mennello auction on Feb. 21, 2024 in Palm Beach, Fla. Considered Chicago's best known female artist, Palmer taught art in Chicago public schools. Her marriage to Albert Palmer, a wealthy physician, allowed her to focus on her art fulltime.

Levine

In *Levine*, the full Tax Court took up the estate tax consequences of Marion Levine's receivable from a GSD plan entered into with an irrevocable insurance trust holding life insurance on Marion's daughter and son-in-law.[11] Both the G1 and G2 generations of the Levine family were heavily invested in real estate, and the GSD plan was created to help address the family's significant estate liquidity and basis management needs. The IRS again argued that the full value of the receivable should be included under Sections 2036, 2038 or 2703. The Tax Court again rejected the IRS' position, ruling that Marion held no rights or interests in the policy, that her only property interest was the receivable and that she held the complete and undivided interest in the receivable. Because her only property interest was the receivable, there was no transfer of an interest in the policy so that none of Sections 2036, 2038 or 2703 could apply. The court emphasized the independence of the trustee and highlighted Marion's attorney's careful planning and implementation of the plan.

This brings into focus a critical distinction between the *Morrissette* and *Levine* cases. In *Morrissette*, the mutual consent of Clara's revocable trust and the dynasty trust gave her revocable trust an interest in the policy. In effect, the court determined that Clara had transferred her interest in the policy while retaining the receivable, bringing the plan within the purview of Sections 2036, 2038 or 2703. Although the *Morrissette* GSD plan met the bona fide sale exception to Sections 2036 and 2038 and the Section 2703(b) exception, it's best to avoid these potential pitfalls altogether.

Valuing the Split-Dollar Receivable

Methodology used

Here's the general valuation methodology the Internal Revenue Service, the *Morrissette* court and the *Levine* court used:[1]

- Based on a current mortality table adjusted to reflect the insured's (G2) health at the time of the transfer, for each year the amount G1 would likely be repaid is calculated by multiplying G1's receivable by the probability that G2 dies in that given year.[2]
- This is repeated each year so that the receivable is repaid over the term of the mortality table in a series of small actuarially determined payments.
- The fair market value of the receivable is equal to the present value of that stream of payments based on the appropriate discount interest rate.

Endnotes

1. *See* Espen Robak, *LISI Estate Planning Newsletter* #2444 (Aug. 9, 2016).
2. Valuation Basic Table 2015, published by the Society of Actuaries, provides mortality rates to age 115.

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Not the Final Word

The IRS doesn't like the discounting of split-dollar receivables, and the *Morrissette* and *Levine* decisions are unlikely to be the final word.[12] Sources report that the IRS is closely examining every GSD discount transaction disclosed on an estate or gift tax return whether that transaction was pursuant to an economic benefit regime or loan regime plan.[13] An examination is a fact-finding exercise that may lead to an audit and, depending on what the IRS finds, to litigation. Litigation could also be based on future IRS guidance and/or updated regulations. Some of the GSD plan factors the IRS is examining include:

1. What's the size of the discount? The larger the discount, the greater the risk of proceeding to audit.
2. Do the parties intend to terminate the GSD plan and/or the policy prior to its maturity, that is, prior to the death of the insured? This may include examining the "as sold" illustrations. A policy with high early cash values may indicate the intent to surrender the policy shortly after it's transferred. A policy that isn't issued and funded based on an illustration that's expected to remain in force for the life of the insured may raise a red flag.
3. Is there a well-established long-term need for the coverage, and does the as-sold illustration reflect that? (See below.) Although coverage that's only funded to age 95 based on current assumptions may reflect the client's comfort with the funding amount, the IRS may try to twist that to argue there was no long-term intention to maintain coverage.
4. How strong are the guaranteed elements of the policy? The IRS is reportedly arguing that, if the policy isn't fully guaranteed, there's a gift at inception equal to the full premium advances or loans because there was no intent to maintain the coverage until death. With loan regime GSD plans, the IRS is likely taking the position that the loan doesn't qualify as a split-dollar loan because a reasonable person arguably wouldn't expect repayment of the loan.[14]

Regarding economic benefit regime GSD plans, the *Morrissette* and *Levine* decisions represent current law. In the 2016 *Morrissette* case, the IRS made the gift at inception argument based on Treasury Regulations Section 1.61-22(d)(2)(iii). Paragraph (d)(2) provides that:

> the value of the economic benefits under an economic benefit regime split-dollar plan equals (i) the one year term cost, (ii) any cash value the trust has access to, and *(iii) the value of any economic benefits not described in paragraph (d)(2)(i) or (ii) of this section provided to the non-owner* [the trust]. (Emphasis added.)

In the 2016 *Morrissette* case, the Tax Court soundly rejected the IRS' gift at inception argument, concluding that the only economic benefit conferred on the trust was the 1-year term cost and that the receivable provided Clara's revocable trust with

adequate and full consideration.[15] In *Levine*, the full Tax Court opined that the IRS would have to rewrite the split-dollar regulations to support the gift at inception position, stating:

> If there is a weakness in this transaction, it lies in the calculation of the value of the gift between Levine and the Insurance Trust—the difference between the value that her Revocable Trust gave to the Insurance Trust and what it got in return. But the gift-tax case is not this estate-tax case.
>
> And the problem there is traceable to the valuation rule in the regulations. No one has suggested that this rule is compelled by the Code and, if it isn't, the solution lies with the regulation writers and not the courts.[16]

Shoehorning a new gift at inception theory into the split-dollar regulations directly contradicts the 2016 *Morrissette* summary judgment ruling, and it could be argued that the IRS is expanding the regulations without following the required procedures, including notice, preliminary publication and comment periods. Modifying the regulations would take years and, in staking out an aggressive examination/auditing posture, the IRS may be looking for a way to shortcut the regulation writing process.

Dealing With Uncertainty

The IRS will be looking to capitalize on any flaw in a GSD plan. Its aggressive examination posture emphasizes the need to adhere to the split-dollar regulations. Nevertheless, there will be plenty of bad facts cases, and the law in this area can be expected to evolve and develop. You may be getting a sense of déjà vu because the current state of GSD planning is similar to the path treaded with family limited partnerships. For many GSD plans, it will be years before the receivable is transferred, and we don't know what the valuation rules will be at that time. How to proceed in light of this uncertainty? Here are some considerations:

First, advise clients of the risk of examinations, audits and litigation and that the IRS (through future guidance or updated regulations) or Congress (through legislation) may try to limit or eliminate discounts.

Second, because a receivable won't be transferred for years, your client can decide based on the law at that time whether to take a valuation discount and the size of any discount.

Third, relying on the *Morrissette* and *Levine* decisions, it may be possible to negotiate a favorable settlement.[17] Closely adhering to the guidance provided by the regulations and these cases can help ensure a favorable outcome.

Finally, I believe that the IRS' gift at inception position—that the policy must be fully guaranteed for a GSD plan to be valid—is unsupportable. The lion's share of indexed universal life (UL) and fixed UL policies sold today don't offer fully guaranteed coverage.[18] Furthermore, in the last few years, there have been fewer fully guaranteed UL policies available and, based on reasonable performance assumptions, they're more expensive than comparable non-guarantee products.[19]

> Designing the GSD plan under the loan regime rather than the economic benefit regime offers meaningful advantages

The IRS' guaranteed values only position is further undercut by the fact that all policies have the option to pay additional premiums if necessary to maintain coverage. When there's an established need for permanent insurance, in many if not most cases, a client will provide additional funding to shore up an underperforming policy. In pricing coverage, actuaries rely on current mortality, expense and interest assumptions. For fully guaranteed coverage, guarantees are undermined if premiums aren't paid on time. The real guarantee is that actual performance will vary from that illustrated. Guarantees aside, the life insurance industry is one of the most highly regulated,

conservatively invested and well-managed industries committed to meeting its long-term promises. Every day, clients and advisors select the type of insurance and its funding that best suits the clients' needs based on a myriad of non-tax factors. To focus on one small segment of the insurance market, fully guaranteed policies, seems disingenuous and destined to fail.

Loan Regime GSD Plan

Disregarding the IRS' loan regime gift at inception position, designing the GSD plan under the loan regime rather than the economic benefit regime offers meaningful advantages. Based on current higher applicable federal rates (AFRs), although the loan regime discount will likely be smaller than under the economic benefit regime, there's no provision in the loan regime regulations comparable to the catchall Treas. Regs. Section 1.61-22(d)(2)(iii) discussed above. In addition, the loan regime regulations authorize four beneficial design features: (1) lifetime loans, potentially locking in favorable AFRs for decades; (2) the ability to accrue and capitalize interest; (3) unlike economic benefit plans, a split-dollar loan with accrued interest doesn't trigger gifts or require that the trust have funds to pay loan interest; and (4) the receivable needn't be transferred to a dynasty trust but can be transferred to anyone including the insured (provided the receivable is secured by a restricted collateral assignment). Importantly, the loan regime regulations dictate that both parties must sign a representation stating that a reasonable person would expect that all payments under the loan will be made and file a copy of that representation with their respective income tax return for each year an additional loan is made.[20]

Designing a Successful GSD Plan

Here are some planning pointers that can help guide the design, implementation and administration of a successful GSD plan:

Trustees and trusts. The trustee should unilaterally control all policy and GSD plan decisions, including the right to terminate the GSD agreement. That is, at all times, the trust holds all interests in and all incidents of ownership in the policy.[21] The trust secures G1's premium advances or loans with a restricted collateral assignment of the policy. This restricted assignment provides G1 with a mere security interest equal to the receivable. G1 can't hold any powers to modify or terminate the GSD plan unilaterally or participate in any decision to do so. At no point should G1 hold any interest in the policy (other than the bare security interest) or incidents of ownership in the policy either pursuant to the trust or under the assignment. The restricted collateral assignment is also important if G2 will ultimately hold the receivable secured by a policy on their own life.

The trustee should be truly independent, that is, shouldn't be a "related or subordinate party."

G2, the insured, shouldn't be a trustee or co-trustee because: (1) G2 isn't an independent trustee, and (2) the policy proceeds could be included in G2's estate because G2 holds incidents of ownership in a policy insuring G2's life.[22]

The trustee should be truly independent, that is, the trustee shouldn't be a "related or subordinate party."[23] Institutional trustees are viewed favorably. That being said, in *Levine*, the trustee was a family friend and longtime employee. Although the court didn't view this as unfavorable because the trustee was bound by fiduciary duties to the trust beneficiaries, it's skating a bit too close to the line.

In *Cahill*, G1's son was the decedent's attorney-in-fact, the trustee of G1's revocable trust and, on G1's death, executor of G1's estate.[24] On behalf of G1, the son created the irrevocable life insurance trust (ILIT) for the benefit of himself and his issue, managed all aspects of the implementation of the GSD plan and, as executor of G1's estate, valued the receivable. The son's cousin and business partner was the trustee of the ILIT. Although the case was ultimately settled, clearly, the son's involvement in and control of all aspects of the plan were problematic.

The client should execute the dynasty trust before applying for the insurance. Acting through

the independent trustee, the trust should apply for the policy. On approval and initial funding, the policy should be issued directly to the trust. Once issued, the split-dollar agreement can be implemented, including the restricted collateral assignment to secure premium advances or loans.

Advisors. G1 and the trust should each have separate independent legal and tax attorneys, and the attorneys should carefully document negotiations. Additional security (see below) and the size of the discount (see below) could be items that the parties negotiate and document.

Furthermore, clients should engage highly qualified legal, tax and insurance advisors who understand and have successfully implemented GSD plans. It may be advisable to partner with an advisor who specializes in GSD planning. Frequently, highly competent advisors with GSD plan expertise may be willing to act as an advisor's back office or otherwise guide and support the transaction. The client's attorney may want to hire co-counsel so that communications with co-counsel will be protected by the attorney-client privilege. Finally, bring in qualified advisors as early as possible to help clients make critical and better informed opinions.

Valuation. A qualified valuation of the receivable from a professional appraiser is essential. A conservative valuation discount is advisable, for example, in the 30%-to-60% range, with the understanding that the higher the discount, the greater the likelihood that an IRS examination leads to an audit. In *Morrissette*, *Levine* and *Cahill*, the litigated discounts were 75%, 65% and 98% respectively. Interestingly, in *Levine*, the IRS and the estate agreed to a 65% discount prior to the hearing, but that should be considered a fluke. The size of the discount should be discussed confidentially between the client and their legal counsel.

In implementing a GSD plan, clients should consider that discounts could be smaller than expected or may not be available at all. Because a receivable won't be transferred for years, your client can base their decision on the law at that time regarding whether to take a valuation discount and the size of any discount. All parties should understand that with or without discounts, split dollar is an extremely effective strategy for funding large life insurance policies. In the worst case, when there's no discount, GSD plans still make sense.

Document that a permanent policy is purchased for legitimate non-tax planning purposes.

Policy design. Document that a permanent policy is purchased for legitimate non-tax planning purposes. Citing *Amlie v. Comm'r*, the 2016 *Morrissette* case provided, "planning for future liquidity constitutes a valid business purpose under section 2703(b)(1)."[25] Other legitimate non-tax reasons include protecting a family business and/or investments by providing liquidity to retain them through the generations, repaying debt, leaving a legacy for grandchildren and future generations and diversifying investments through policy death benefits.

Document a clear intention to maintain the policy to maturity. In the 2021 *Morrissette* case, there was evidence of a prearranged plan to surrender policies early when, responding to a request from G2 to surrender the policy, the client's attorney sent an email advising G2 to wait until the statute of limitations ran.

The policy should be designed and funded to ensure coverage for G2's lifetime. For example, based on the Valuation Basic Table 2015 mortality table, for a 60-year-old preferred risk at issue: (1) there's a 22% (male) or 33% (female) probability that the insured will be alive at age 95, and (2) there's a 2% (male) or 3% (female) probability that the insured will be alive at age 105. In that case, funding to age 105 should demonstrate the intention to maintain the policy for the insured's lifetime and undercut the IRS' "guaranteed values only" position, while funding to age 95 may not. Insureds whose policy is rated at issue should warrant funding coverage for a shorter duration.

Illustrating (and documenting) policy performance that's worse than the carrier's current assumptions and estimating the premiums necessary in future years to maintain coverage for the insured's lifetime can support the intention to keep the coverage and the GSD plan in place. Document planning for additional premiums in case the policy underperforms or the insured lives longer.

Selecting a fully guaranteed fixed UL policy with little or no cash value can address this "issue." Fully guaranteed variable UL policies are available. Although there's a meaningful reduction in cash value growth due to the guarantees, the product does offer additional upside performance potential when compared to a guaranteed fixed UL policy. Whole life offers fully guaranteed base coverage; however, total death benefit in most years will exceed the guaranteed death benefit because it's supported by policy dividends.[26] A protection-type UL product balances guarantees (that typically extend to the insured's life expectancy) with suppressed cash values. If the IRS' guaranteed values-only position becomes law, in the economic benefit regime context, protection products should still be eligible for a meaningful discount.

A policy with a high early cash value may indicate an intent to surrender the policy and should generally be avoided. Nevertheless, the totality of circumstances should determine whether the GSD plan is valid, and the type of policy selected is just one factor to be considered. Even a non-modified endowment contract (MEC) that minimizes death benefit and develops strong cash values may be a legitimate choice because it best meets the client's needs.

Finally, the policy should be designed to avoid classification as a MEC,[27] because the assignment of a MEC may be treated as a taxable distribution to the extent of gain in the contract as it accrues.[28]

Additional security. As an alternative to using a fully guaranteed policy, a trust funded with

additional assets or a personal guarantee may neutralize the IRS' gift at inception argument.[29] In the loan regime setting, additional security, including a larger loan, helps ensure that the plan meets the loan regime requirement that a reasonable person would expect repayment of the loan.[30]

Protective gift tax return. It's advisable to file a protective gift tax return on transfer of the receivable during G1's lifetime. Provided that the return adequately discloses the material elements of the transaction, the 3-year gift tax statute of limitations will start to run. Although this may trigger an examination/audit, the exposure to audit is open-ended if a protective gift tax return isn't filed.

Avoiding Unfavorable Outcomes

Although the IRS is currently examining virtually all GSD plans on the transfer of the receivable, GSD remains an attractive life insurance funding vehicle, with or without discounting of G1's receivable. The unilateral control of the policy and the plan by an independent trustee is essential. *Levine* emphasizes the importance of careful planning and design, clear communication with the family, thorough execution and meticulous administration. Demonstrating that G1 retained sufficient assets to maintain Marion's lifestyle was an important factor in that case. If there's one overarching recommendation that can help deflect an attack by the IRS, it's to adhere to the regulations and the guidance offered by the case law, as well as to carefully and thoroughly document every stage of the GSD plan—from first considering the plan through implementation and its ongoing administration.

Endnotes

1. Short excerpts in this article were originally published by the author in *Estate Planning* magazine, 44 *ETPL* 3 (August 2017), 46 *ETPL* 14 (January 2019) and 46 *ETPL* 20 (June 2019).
2. Generational split-dollar (GSD) is also referred to as "inter-generational split-dollar."
3. *Estate of Clara M. Morrissette v. Comm'r,* 146 T.C. No. 11 (April 13, 2016).
4. *Estate of Clara M. Morrissette v. Comm'r,* T.C. Memo. 2021-60 (May 13, 2021).
5. *Estate of Marion Levine v. Comm'r,* 158 T.C. No. 2 (Feb. 28, 2022).
6. *Estate of Cahill v. Comm'r*, T.C. Memo. 2018-84 (June 18, 2018).
7. Clara Morrissette advanced $29.9 million to the trusts, rounded here for the sake of simplicity to $30 million.
8. The final split-dollar regulations are applicable to agreements entered into after Sept. 17, 2003.
9. *Estate of Morrissette, supra* note 4.
10. *Ibid.,* at pps. 33, 68 and 69.
11. *Estate of Levine, supra* note 5.
12. To refer to the value of G1's receivable as being "discounted" is a misnomer. An appraisal by a professional valuation firm determines the receivable's fair market value (FMV). The term "discount" is merely used herein as a matter of convenience to describe the receivable's FMV.
13. Remember that both the *Morrissette* and *Levine* cases involved economic benefit regime plans, and at this time, we don't have any decisions on loan regime GSD plans.
14. Provided that the loan isn't otherwise a loan for federal tax purposes. Treasury Regulations Section 1.7872-15(a)(2)(B).
15. Discussing the court's reliance on the IRS' preamble to the split-dollar regulations, the 2016 *Morrissette* opinion stated, "Therefore, the Commissioner is entitled to at least the lowest deference in interpreting his own regulations and their statutes."
16. *Estate of Levine, supra* note 5, at p. 41.
17. Once the Internal Revenue Service initiates an audit or examination, there's likely no possibility to settle until the appeals level of IRS agency review, which may be prior to any required litigation once a Notice of Deficiency is issued.
18. According to the Life Insurance Marketing and Research Association (LIMRA) U.S. Individual Life Insurance Sales Survey (Years 2018–2022):
    - Just over 4% of $15.6 billion of indexed universal life (UL) premiums funded lifetime guarantee policies.
    - Just over 33% of $5.5 billion of fixed UL premiums funded lifetime guarantee policies.
    - Combining these two market segments, just under 12% of $21 billion of premiums funded lifetime guarantee policies.
19. The market has reflected this: The LIMRA study indicates that the percentage of lifetime guarantee fixed UL premiums has dropped precipitously from 40.2% in 2018 to 21.2% in 2022, and the combined percentage of lifetime guarantee indexed and fixed UL premiums have dropped from 15.9% in 2018 to 6.6% in 2022. *See ibid.*
20. Treas. Regs. Section 1.7872-15(d)(2).
21. *See* Treas. Regs. Section 20.2042-1(c).
22. Internal Revenue Code Section 2042. In *Morrissette,* incidents of ownership weren't an issue because each dynasty trust only held policies insuring the brothers of the trustee, not the trustee.
23. IRC Section 672(c).

24. *Estate of Cahill, supra* note 6. *Estate of Richard F. Cahill v. Comm'r,* Joint Stipulation of Settled Issues, U.S. Tax Court, Docket 10451-16 (Aug. 16, 2018).
25. *Amlie v. Comm'r*, T.C. Memo. 2006-76 provided:

    Respondent argues that the 1995 [agreement] cannot meet the requirement of section 2703(b)(1) because the agreement's subject, decedent's FABG stock, was not an actively managed business interest but merely an investment asset. We rejected such an argument in Estate of Bischoff v. Commissioner, 69 T.C. 32, 40-41 (1977), and find it equally unpersuasive here. … In addition, planning for future liquidity needs of decedent's estate, which was also one of the objectives underlying the 1995 [agreement], constitutes a business purpose under section 2703(b)(1). See 136 Cong. Rec. 30,539 (1990).
26. For example, based on an illustration from a prominent whole life carrier, for a preferred risk female age 60 with 100% base guaranteed whole coverage and using dividends to purchase paid-up additional insurance, at life expectancy, 53.4% of the total death benefit is non-guaranteed.
27. IRC Section 7702A was implemented to discourage the purchase of single premium and "short-pay" life insurance policies. If a life insurance policy fails the 7-pay test of Section 7702A(b), it's classified as a modified endowment contract (MEC). Any distribution from a MEC is taxable to the extent that there's gain in the contract (policy cash value in excess of cost basis). This reverses the usual rule of the tax-free surrender of cash value to the extent of basis and tax-deferred policy loans. A 10% penalty may also apply. IRC Section 72.
28. Sections 72(e)(4)(A)(ii) and (e)(10). Although it's not clear that this IRC section is directed at a split-dollar assignment, best practice suggests assuming that it applies and avoiding MEC contracts.
29. The use of personal guarantees may raise issues beyond the scope of this article.
30. Treas. Regs. Section 1.7872-15(a)(2)(B).

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