

## U.S. Tax Court Rules on a Case of Intergenerational Split Dollar: Estate of Levine

On February 28, 2022, the United States Tax Court ruled in favor of the taxpayer in Estate of Levine v. Commissioner concerning the estate tax consequences of a split-dollar life insurance arrangement. This same Court ruled against the taxpayer in the 2021 case Estate of Morrisette v. Commissioner. The two cases illustrate that when it comes to this complicated estate planning strategy, facts can make all the difference.

### Background

Intergenerational split dollar usually involves the wealthiest and oldest members in a family (often aged 80 or above) funding life insurance policies on the lives of their adult children. The insurance is controlled by a split dollar agreement, which in turn is subject to certain highly restrictive terms affecting the value of the right to repayment of the split dollar premiums. Part of the legal controversy is due to the likelihood that the oldest generation will never recover their premiums: the agreements are structured to repay the premiums at the *children's* death, to or for the benefit of the family's grandchildren. But what would a disinterested party on the open market really pay for the right to receive a certain sum at an uncertain date, decades in the future? In all likelihood, only a fraction of the sum of the premiums, effectively shrinking the value of the oldest generation's estates.

### The Outcome

Before she died, Marion Levine created an estate plan to protect her estate from estate tax. The plan included a GRAT, a QPRT, and several other trusts she created for the benefit of her family. Among these were a revocable grantor trust and an irrevocable insurance trust that owned life insurance policies on the lives of her daughter and son-in-law. She gave the irrevocable insurance trust \$6.5 million to pay the premiums and the insurance trust gave her a receivable for the greater of premiums paid or the policies' cash value, thus creating split dollar arrangements.

The Court found that the life insurance policies weren't included in Levine's estate because they were always owned by the irrevocable insurance trust. It also found that the \$6.5 million receivable, though also includible in her estate, could be valued at a discount because she couldn't call it on demand: she needed to wait either until the deaths of both her daughter and son-in-law or the time when the trust cancelled the insurance policies, which she retained no power to do. The Tax Court rejected the IRS's argument that Levine could have terminated the split dollar arrangements at any time because her longtime accountant was both her attorney-

in-fact (i.e. held general power of attorney on her behalf) and trustee of the life insurance trust. The Court held instead that the individual's fiduciary duty to the trust beneficiaries effectively prevented him from cancelling the insurance policies, which under the agreement would have left the beneficiaries with nothing.

## **Conclusion**

Here, the Court concluded, in contrast to the *Morrisette* facts, that a third party exclusively held the right, both factually and substantively, to decide whether to surrender the trust owned policies. As a result, the IRS was prohibited from including the cash surrender value of the policies in the estate of the decedent because she did not substantively control the policies. Given the position of the Court, the estate was able to take a substantial discount when valuing the split dollar receivable.

## **A Final Note**

Prudential does not market or otherwise endorse intergenerational split dollar arrangements but may participate as a product provider on an exception basis. If you are approached with an intergenerational split dollar case opportunity, do not hesitate to contact Prudential's Individual Life Advanced Planning team. We look forward to being of assistance, and can be reached at 800-800-2738, Option 4.

This material is being provided for informational or educational purposes only and does not take into account the investment objectives or financial situation of any clients or prospective clients. The information is not intended as investment advice and is not a recommendation about managing or investing a client's retirement savings. Clients seeking information regarding their particular investment needs should contact a financial professional.

We do not provide tax, accounting, or legal advice. Clients should consult their own independent advisors as to any tax, accounting, or legal statements made herein.

Life insurance is issued by The Prudential Insurance Company of America, Newark, NJ, and its affiliates.

© 2022 Prudential Financial, Inc. and its related entities. Prudential, the Prudential logo, and the Rock symbol are service marks of Prudential Financial, Inc. and its related entities, registered in many jurisdictions worldwide.