

IRS tax rules on split dollar policies disappoint industry

Copyright. InsuranceTimes™ © 2003 by M&S Communications, Inc. All rights reserved. September 30, 2003

The Internal Revenue Service has dashed the hopes of the insurance industry with new rules that alter the tax scheme on split dollar life insurance.

The rules, which have been under review for more than a year by IRS and Treasury department officials, mean that a person with an interest in a split dollar policy will be taxed annually, regardless of whether he or she has accessed the cash value.

The rules, which go into effect beginning Sept. 17, were opposed by the life insurance industry which has found sales of these policies complicated by the Sarbanes-Oxley restrictions on corporate loans to executives and lack of clarification whether such split dollar arrangements constitutes loans.

The Sarbanes-Oxley bill barred loans to executives. Industry officials have tried without success to get the Treasury to rule that split dollar arrangements are not loans for tax purposes.

"We're very disappointed in them. As we read them initially, they will institute a new tax regime for split-dollar life insurance policy arrangements," commented Jack Dolan, ACLI media relations director.

For example, Dolan noted, an employee with an interest in a policy -- not an owner -- will be taxed on the value of the cash value and the current death benefit protection.

"We are reviewing our options to address this ruling," he added.

Split dollar policies are sometimes used by corporations as part of executive compensation. There are two basic types. In one, the corporation owns the policy for a period and endorses part of the death benefit to the executive, allowing the executive to designate a beneficiary.

The other version, known as collateral assignment arrangements, is what has come under scrutiny since Sarbanes-Oxley. In this case, the company is designated a having an interest in the cash surrender value and death proceeds in the policy, which is otherwise owned by the employee.

The ACLI has also asked the Securities and Exchange Commission for a ruling on split dollar but the SEC has yet to it act on its request. Before sarbanes-Oxley, the SEC held that the policies were compensation. □