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ADVANCED MARKET INSIGHTS

MORRISSETTE II:
ESTATE OF MORRISSETTE V. COMMISSIONER

ABSTRACT

INTRODUCTION[1]

"Morrissette II" is the second intergenerational split-dollar Tax Court case involving the Morrissette family, and the fourth case in a series of court cases addressing Intergenerational split-dollar arrangements.

Intergenerational split dollar refers to a life insurance financing arrangement where an older generation (Generation one) funds life insurance insuring the lives of Generation two for the benefit of Generation three. In return, Generation one is provided rights in the policy cash value, death benefit, or both.

Intergenerational split-dollar arrangements have drawn IRS scrutiny when reporting substantial discounts on the early transfer of Generation one's rights. For the taxpayers, the results have been mixed.

MORRISSETTE I

"Morrissette I", (*Estate of Morrissette v. Commissioner, 146 T.C. No 11 (April 13, 2016)*), validated the use of Economic Benefit Regime split dollar for estate planning purposes. The Tax Court, in partial summary judgment, held the Morrissettes had a valid economic benefit regime split-dollar arrangement under split-dollar regulations (*Treas. Reg. 1.61-22*). Mrs. Morrissette's trust was the deemed owner of the life insurance policies even when another party's trust owned the policy, and because Mrs. Morrissette advanced the premiums, had the right to be repaid the greater of the premium paid or the policy cash surrender value.

MORRISSETTE II

Morrissette II addressed the valuation of the split-dollar rights and held that Mrs. Morrissette's transfers of premiums during her life were not included in the value of her gross estate under IRC §§ 2036, 2038, and 2703 by meeting the bona fide business exceptions under those sections. Contrast this result with the 2018 Tax Court case, *Estate of Cahill* (*TCM 2018-84*), where the Court ruled that IRC §§ 2036, 2038, and 2703 applied and required Mr. Cahill's gross estate to include the transferred premiums.

While this was seemingly a win for the Morrissettes, it was only a pyrrhic victory. Ultimately, the Tax Court found that the estate had grossly undervalued the economic benefit receivable and ruled that the estate had a significant tax deficiency and would be subject to a 40% penalty.

Unlike *Cahill*, which is a bad facts case, the Morrissette case was not all-in a totally bad facts case. For instance, the Tax Court found that the family, long mired in mistrust and business disputes, had valid business purposes for the arrangement such as the successful intrafamily transfer of the company to meet the founder's wishes that the business remain family owned. Additionally, Mrs. Morrissette actually advanced the premiums for credible investment purposes, earning a higher interest rate on the policy cash values than previously earned. In balance, the Tax Court had a sufficient basis to determine that the "bona fide business" exceptions of IRC §§ 2036, 2038 and 2703 applied.

However, unfavorable facts were also considered. The arrangement had been promoted to the family as a tax-savings device by an insurance agent and an attorney. The record also contained facts about one of the brothers questioning if the policies should be canceled. The attorney advised that the IRS had three years to audit the estate tax return and insisted the policies stay in force until after the audit was settled. The IRS is "going to have issues with the amount of discounts we are claiming," he wrote, six months before the estate tax return was filed. In assessing the additional 40% gross under valuation penalty, Justice Goeke wrote that the Morrissettes "did not act reasonably or in good faith in the valuation of the split-dollar rights."

RELEVANT FACTS

In 1943, Arthur Morrissette, Sr. formed a moving company that would grow into a large privately held family enterprise, Interstate Group Holdings, Inc. (Interstate).

In 1996, Arthur and Clara Morrissette (Mrs. Morrissette) established an estate plan determined to keep Interstate in the family explicitly excluding "anyone who was not of their own blood" from ever owning Interstate stock. Mrs. Morrissette revised the plan when Mr. Morrissette died in April 1996.

Interstate had long employed Mr. and Mrs. Morrissette's three sons, Arthur Jr. "Buddy," Donald "Don," and Kenneth "Ken," as well as Buddy's sons, J.D. and Bud. The relationship between the three brothers (Buddy, Don, and Ken) was very hostile. Buddy, in particular, was angered at his brothers' lack of commitment to Interstate. Buddy was also frustrated by his parents' impartial treatment of the three brothers despite his commitment to the enterprise. Ken and Don resorted to communicating through memos and emails even though they had adjacent offices. Buddy, as CEO, made major decisions without his family's input that the others felt were detrimental to the company. Buddy's brothers and Buddy's sons wanted him to step down.

Arthur and Clara wanted to keep the business in the family even though they knew it was difficult for their sons to work together. The brothers were aware of their parents' wishes, but animosity persisted.

After their father's death and as their mother's health deteriorated, the brothers became concerned that there was no definite plan to pay estate taxes at Mrs. Morrissette's death. The estate was not eligible for the 10-year deferral under IRC § 6166. The family was concerned that the estate would need to sell Interstate stock to outside parties which might harm their careers and shift ownership of the company outside the family.

In addition to planning for Mrs. Morrissette's death, the company also needed to put a management transition plan in place for Bud and J.D. to take the reins from Buddy, Ken, and Don.

In 2006, Mrs. Morrissette's grandson Bud, was introduced to an insurance producer. Bud introduced the producer and an attorney to his father and his uncles. The attorney presented Economic Benefit Intergenerational Split Dollar as an estate tax-saving strategy. He supported the concept with marketing materials on his firm's letterhead which suggested that the estate could report the split-dollar receivable for estate tax purposes for 5% to 15% of the total premiums advanced. When asked to be specific about how the plan would work for the family, the attorney said the split-dollar arrangement could save $9.4 million in estate tax.

The Morrissettes engaged the attorney to plan for Mrs. Morrissette's impending death. This overall plan included a buy-sell provision among the brothers—long sought by Ken—ensuring they would retain ownership of Interstate during their lifetime and the business would successfully transition to Buddy's sons.

Mrs. Morrissette suffered from advanced Alzheimer's disease. The brothers petitioned to have a long-time Interstate employee appointed as a conservator for Mrs. Morrissette and act on her behalf in completing the split-dollar transaction supporting the buy/sell arrangement.

Mrs. Morrissette's trustee created a dynasty trust for each son. To fund the buy-sell arrangement, each trust would own life insurance policies on the other brothers. The trust agreements: authorized the dynasty trusts to buy life insurance on each of the three brothers, required the trusts own the policies, and tied the policy proceeds to the buy-sell provisions. The dynasty trusts were authorized to enter into split-dollar agreements with any appropriate person.

Four days after the dynasty trusts were formed, (September 19, 2006), Mrs. Morrissette's trust was amended to include paying premiums on life insurance policies tied to the buy-sell provision, making loans,

entering into split-dollar agreements, and making other arrangements to facilitate funding tax and obligations tied to the succession plan. Mrs. Morrissette's new trust would advance the $29.9 million of life insurance premiums on her sons' lives under the split-dollar agreement. Her revised trust gave the trustees (her sons), at Mrs. Morrissette's passing, the sole and absolute authority to distribute the revised trust's split-dollar rights by a formula tied to Mrs. Morrissette's unused generation-skipping transfer tax exemption to her sons or to each dynasty trust that was a counterparty to the agreements. Six days after the dynasty trusts were formed, (September 21, 2006), the brothers began business planning that included an amendment to the shareholder agreement to accomplish the buy-sell.

On October 4, 2006, each brother's dynasty trust bought life insurance policies on each of the other two brothers. The total face amount of approximately $58 million was spread between two life insurance companies. The policies featured high early cash surrender values and 3% minimum guaranteed annual interest rates. These features were desirable to the family for investment purposes because Mrs. Morrissette's assets in her trust were only earning an average of 2.95%. The brothers wanted to pay a single lump sum payment into the policies to cover all of the future costs. They were concerned that if premiums were paid annually, the poor relationship between the brothers could upset the planning.

Mrs. Morrissette's trust entered into two split-dollar agreements with each dynasty trust in which the trustees agreed to contribute $29.9 million to the dynasty trusts to fund the life insurance policies. In return for contributing the premiums, the split-dollar agreements gave Mrs. Morrissette's trust "split-dollar rights," to receive the greater of the amount of premiums paid or the cash surrender value of the life insurance policies upon the insured's death or the termination of the split-dollar agreement. The dynasty trusts collaterally assigned the policies to Mrs. Morrissette's trust. At the death of an insured, the dynasty trust would receive any death benefit in excess of the split-dollar rights of Mrs. Morrissette's trust.

Under the split-dollar agreements, the dynasty trusts had a unilateral right to cancel the life insurance policies. Termination of the split-dollar agreements would not force cancellation of the underlying policies. Upon the termination of the split-dollar agreements, the dynasty trust would hold a claim to reimbursement but not receive reimbursement from the policies. Instead, cash values from policy surrender, or death benefits paid by reason of the death of the insured would be paid to the corresponding dynasty trusts which would then reimburse Mrs. Morrissette's trust.

As required by the economic benefit split-dollar regulations, *Treas. Reg. 1.61-22*, Mrs. Morrissette, reported annual gifts to each son equal to the economic benefit cost of the value for current life insurance protection. The total amount of the economic benefits for years 2006-2008 was $1,443,526, of which the dynasty trusts paid $806,869 towards the total economic benefit cost. Mrs. Morrissette's gifts of the remainder were reported as $636,657.

Clara Morrissette passed away on September 25, 2009. Her three sons were the personal representatives of the estate. On October 30, 2009, Mrs. Morrissette's trust transferred the split-dollar agreements to the dynasty trust that owned the respective life insurance policies in a part gift-part sale transaction. The dynasty trusts executed promissory notes totaling $4.95 million to cover the sale part of the transaction and sought to claim this amount as the estate's value of the split-dollar rights. The transfer of the split-dollar rights to the dynasty trust effectively terminated the split-dollar agreements because the trusts were both their recipients and owners, ultimately standing on both sides of the transaction.

In July 2010, Don inquired about canceling the life insurance policies and was advised by the attorney who brought the family the split-dollar plan that the policies should stay in force until any IRS audits were settled because the IRS was "going to have issues with the amount of discounts we are claiming." Don was told to wait until after the statute of limitations on the IRS's claims on the estate ran out on December 31, 2013.

The estate filed the estate tax return on December 10, 2010. The promoting attorney recommended an appraiser to assess the fair market value (fmv) of the split-dollar rights held by Mrs. Morrissette's trust at the time of her death. The estate reported the value of the split-dollar rights for $7,479,000.

The IRS valued the contract rights at $32,060,070, equal to the cash surrender values of the life insurance

policies. The IRS issued a total estate tax deficiency of approximately $39.4 million dollars to the estate, partly reflecting the increased fmv of the decedent's contract rights in the six split-dollar life insurance arrangements. The IRS also assessed underpayment penalties of 40%, adding $4,424,593 to the final tally.

EXCEPTIONS TO §§ 2036 AND 2038 PREVENTED THEIR APPLICATION

The Morrissette estate and the IRS conceded that Mrs. Morrissette's gross estate included the fmvs of the split-dollar rights.

IRC §§ 2036 and 2038 are estate tax provisions that apply to property that the grantor has either a retained or revocable interest in—either alone or in conjunction with any other person. Earlier, in *Cahill,* the IRS successfully argued that the rights provided by the split-dollar arrangement (the rights to recover the greater of the premiums paid or the policy cash surrender value) were property subject to IRC §§ 2036, 2038, and 2703. This ruling pulled the full cash value of the policies back into Mr. Cahill's estate.

The IRS argued that IRC §§ 2036 and 2038 should apply to the transfer of the premiums paid by Mrs. Morrissette's trust because it retained possession, enjoyment, or a right to income and the right to designate the power to another, or power to alter rights under the agreements. Consequently, the IRS asserted the value of the premiums ($29.9 million) or the cash surrender value ($32.6 million) should be the amount included in Mrs. Morrissette's gross estate.[2]

BONA FIDE SALE EXCEPTIONS OF SECTIONS 2036 AND 2038

Here, the Tax Court held that IRC §§ 2036 and 2038 did not apply because the transfers qualified for the bona fide sale exceptions of both sections which required passing two tests:

1. There must be a legitimate and significant nontax purpose.
2. There must be adequate and full consideration for money or money's worth.

The IRS contended the dynasty trusts did not pay any consideration to Mrs. Morrissette's trust, arguing a retained right to repayment under the split-dollar agreements is not consideration, and the premium payments did not constitute a sale for the purpose of the exceptions. The Tax Court disagreed citing that neither IRC §§ 2036 nor 2038 defined what a "sale" was, and the regulations interpret the term "sale" broadly including transactions that are not strictly sales.

The Tax Court determined Mrs. Morrissette's trust parted with an interest in the premiums because it could not obtain immediate repayment. The bargained-for exchange by each agreement constituted a sale for purposes of the bona fide sale exceptions.

Test 1: Legitimate Nontax Purpose

The Tax Court evaluated whether Mrs. Morrissette had a legitimate and significant nontax motive for entering into the split-dollar agreement under IRC §§ 2036 and 2038. Intrafamily transfers require heightened scrutiny to ensure that the transaction is not a sham or a disguised gift. There must be a nontax motivation accompanied by objective proof that the nontax reason was a significant motivation to entering into the split-dollar arrangement.

The Tax Court determined the family's reason for creating the split-dollar arrangements—the collective desire to maintain family control of Interstate and pass control to downstream generations—was a legitimate nontax purpose. Judge Goeke wrote "An important purpose of the transfer was to promote the management succession and efficiency and protect corporate profits for the accumulation of capital to develop the business … . We find that unrelated parties would have agreed to similar terms."

The Tax Court also cited many cases, giving specific examples of other possible legitimate nontax purposes such as:

- Efficient, and active management of a business and management succession[3]
- Maintaining control over a family business[4]
- Management of family assets[5]
- Resolving intrafamily disputes that had led to past litigation[6]

Test 2: Adequate and Full Consideration

In order to meet the second test of the bona fide sale exceptions to §§ 2036 and 2038, the transfer must reflect adequate and full consideration in money or money's worth. Under §§ 2036 and 2038, adequate and full consideration requires an exchange of a roughly equivalent value that does not deplete the estate.

The Morrissettes argued that satisfying the tax requirements of economic benefit regime split dollar, by itself, reflected full and adequate consideration.

The IRS argued that adequate and full consideration is determined by the willing buyer/willing seller standard where hypothetical parties are dedicated to achieving the maximum economic advantage.

The Tax Court rejected the IRS argument explaining the willing buyer/willing seller standard applied to determining the fmv of a transaction rather than defining adequate and full consideration. The economic benefit regime regulations (income tax regulations and not estate tax regulations) do not invoke the idea of "adequate and full consideration" nor do they require a comparison of the premiums paid with the value of the rights Mrs. Morrissette's trust received from the arrangements. The Tax Court reasoned that an arm's length transaction was not a requirement to meet the bona fide sale exceptions of IRC §§ 2036 and 2038, nor was maximizing financial return, instead referring to such a transaction as "a classic informed trade-off."[7] Such investments may be made for other intangible benefits such as "management expertise, security or preservation of assets, and capital appreciation."

§ 2703 DID NOT REQUIRE DISREGARDING MUTUAL TERMINATION RESTRICTIONS WITHIN THE SPLIT-DOLLAR AGREEMENTS

The Tax Court examined and ultimately denied the application of IRC § 2703 — the special valuation rule — holding that the Morrissette transaction constituted a bona fide business exception under Section 2703(b).

Generally, Section 2703 states that the value of any asset includable in the gross estate shall be determined without regard to any option or right to acquire or use the property for less than its fmv, and without regard to any restrictions on the use or sale of the property. Like IRC§§ 2036 and 2038, IRC§ 2703 also contains a bona-fide business arrangement exception that can be used if the arrangement is not a device to transfer property to members of the decedent's family for less than adequate and full consideration, and is comparable to similar arrangements in arm's-length transactions.

The Tax Court was convinced that the split-dollar agreements were a safe investment with an adequate interest rate. Ken had developed terminal cancer and even though Mrs. Morrissette had Alzheimer's disease, she was in good health, and could have outlived any of her sons. The agreement's repayment terms credited interest to cash value that was higher than rates previously earned. In addition, the agreements provided tax deferral and tax-free death benefits for the beneficiaries. The Court also cited the intangible benefits to Mrs. Morrissette and her trust "including retained family control… smooth management succession, organizational stability," and capital protection.

The Tax Court, on its own accord, considered whether Mrs. Morrissette's trust received adequate and full consideration as part of a bona fide sale on the transfer date, and if so, what the fmv of the split-dollar rights was on the valuation date.

The Court analyzed the various prongs under IRC§ 2703. In its testamentary "device" analysis, the Court disregarded whether the split-dollar agreements were a testamentary device, drawing its focus on the mutual termination restrictions. The Court held that the mutual termination restrictions were not such a device, and a reasonable investor would accept the arrangements' terms. The Court also relied heavily on the family's strained relationships and its business continuation objectives, finding that the parties did not enter into the split-dollar agreements with an intent to evade estate tax.

The Court next evaluated whether the mutual termination restriction would have been part of a comparable arm's length transaction. The Court "described the exception as more of a safe harbor than an absolute requirement." The IRS presented as evidence split-dollar arrangements that were part of public company employee compensation plans. The Tax Court rejected this comparison as Interstate had been closely held for nearly 75 years. The Court also drew a distinction between the owner of the policies, finding that they were owned by dynasty trusts rather than by a public company.

VALUING THE SPLIT-DOLLAR RIGHTS FOR GIFT AND ESTATE TAX REPORTING

"[T]he estate substantially undervalued the split-dollar rights for reporting purposes," the Tax Court found. Even though the Tax Court refused to apply § 2703, the Tax Court set on the path to determining the value of the split-dollar receivables. Mrs. Morrissette's trust

had advanced $29.9 million in premiums but reported the value of the receivable as $7,479,000 on the estate tax return.

The Tax Court evaluated the testimony and valuation by three different experts: two for the Estate and one for the IRS. All three experts applied the discounted cash flow method of valuation which calculated an expected policy fmv for each year of the insured's life expectancy. Each expert then discounted the expected value to a present value using a determinable discount rate. The discount rate was determined differently by each expert, largely explaining the range of values presented by the experts to the Court.

The Morrissette experts used a discount rate of approximately 15% based on life settlement yields, asserting such yields are suitable alternatives to split-dollar agreements because both have uncertain holding periods and uncertain yields due to the insured's life expectancy.[8]

The IRS expert provided two values affected by the mutual termination restrictions and the timing of any termination of the agreements, asserting that the split-dollar arrangements remained in effect until the brothers' deaths, and the fmv would have been $17,501,391. The expert also considered that the brothers would have terminated the agreements on December 31, 2013, three years after the estate tax return was filed, and determined the fmv to be $27,857,709.[9] The IRS expert also considered an investment value for the split-dollar rights of $21.2 million.

Morrissette Expert Value #1:	$10,449,000 (corrected from $7,479,000)
Morrissette Expert Value #2:	$7,808,314
IRS Expert Value #1:	$17,501,391 (Assuming termination at insured's death)
IRS Expert Value #2:	$27,857,709 (Assuming termination post statute of limitations)

"We Measure the Adequacy of Consideration on the Transfer Date, Not the Decedent's Death Date."[10]

The Court hit on the intervening events between the date that the split-dollar rights were transferred to the dynasty trusts and the date the rights were valued for estate tax purposes. The Court carefully evaluated the expert assumptions around the termination of the agreements, finding that the values clearly had changed substantially between the two potential termination dates. Even the IRS expert applied a substantial discount of 42.7% where the agreements were terminated by the death of the insureds.

The IRS argued that the brothers intended to terminate the agreements before the insured's death, assuming a date of December 31, 2013, and the value should be the $27,857,709 value on December 31, 2013.

The Morrissettes objected, claiming no prearranged plan to terminate the agreements, but the Court was not convinced. When the plan was implemented, Mrs. Morrissette's trust was amended to distribute the split-dollar rights to the respective dynasty trusts owning the policies. The parties did, in fact, distribute the rights to their respective dynasty trusts which the Court took as an indication that the parties intended "to give the dynasty trusts full control over the policies once the distribution occurred." The Tax Court held that the proper valuation date was December 31, 2013, the day the statute of limitations was up.[11]

The Tax Court directed the parties to revalue the split-dollar receivables with 8.85% and 6.4% discount rates to determine the fmv.[12]

40% UNDERPAYMENT PENALTY FOR A GROSS VALUATION MISSTATEMENT

The Tax Court disregarded a process argument by the Morrissettes and also held that the estate could not rely on the reasonable cause defense by relying on the professional appraisal. It found that the Morrissettes' valuation experts were not credible and that the Morrissettes "should have known that the claimed value was unreasonable and not supported by the facts."

The Court also focused on the family's legal and insurance professionals. While there were substantial

business reasons for entering into the transactions, the Morrissettes were also aware the professionals "were marketing the agreements as an estate tax-saving strategy, clearly indicating that the estate tax benefits of the split-dollar arrangements would be achieved by undervaluing the split-dollar rights." The legal professional warned the family that the IRS would "likely see problems" with the values claimed on a tax return. Further, the lawyer intervened with the appraiser arguing for a lower valuation. Even so, the estate still substantially discounted the values on the return.

FORWARD LOOKING CONSIDERATIONS AFTER MORRISSETTE II

There is more to come. There is still not a decision in *Estate of Marion Levine*, a case with similar facts to *Morrissette*, but with issues at trial still not adjudicated. The trial was held two years ago, but the judge has not rendered an opinion.

An appeal of *Morrissette* could raise some interesting issues. In *Estate of Cahill*, the court found that IRC §§ 2036, 2038, and § 2703 applied. So, although the facts favor the Morrissettes, one must wonder whether the IRS will still raise a challenge and whether the parties will appeal the valuation date or the formula?

The Tax Court citing *Cahill* acknowledged that Economic Benefit Regime Split Dollar is an income tax regulation and only applies for income, gift, employment, and self-employment tax purposes. The regulation is silent on whether it applies to estate taxes.

Loan Regime Split Dollar is a Simpler and Possibly More Defensible Arrangement.

Consider Loan Regime Split Dollar. So far, the courts have focused on the valuation of Economic Benefit Regime Split-Dollar rights. The Court in Morrissette II carefully stated, "The parties to the split-dollar arrangements could have merely structured the transfer as a loan with interest and repayment due when the proceeds were collected from the policies."

The Court also discussed that economic benefit regime regulations are income tax regulations and did not directly apply to the estate tax. IRC § 7872 applies for Federal tax purposes and thus to estate taxes.[13]

In a Loan Regime arrangement, however, the lender is considered the "non-owner," and the borrower who owns the life insurance policy is the "owner." What constitutes a loan is clearly defined, and it is understood there is no "property" for the IRS to argue about, making it probable that a loan split-dollar arrangement will not fall under IRC §§ 2036, 2038, and §2703.

In addition to numerous other features of Loan Regime Split Dollar, including its simplicity and the ability to lock in the long-term Applicable Federal Rate, the promissory note can be valued using market rates. To this author, this seems like a more certain road to tread when compared with the complex analysis the Court accepted in valuing the economic benefit split-dollar receivables.

Economic Benefit Regime Split Dollar is Still Viable

If an economic benefit arrangement is used, to avoid IRC §§ 2036, 2038, and § 2703, clients must be able to prove that there was a substantial legitimate nontax reason for such a plan. The Court leaned heavily on the family issues and past actions as strong facts favoring the family. But the Court also set out a number of legitimate nontax purposes which this author believes provides guide rails to practitioners and examiners. Legitimate nontax purposes can include efficient and active management of a business and management succession, maintaining control over a family business, and managing family assets. The Tax Court also held that "closely held, family entities can provide a legitimate, nontax purpose even where the entity does not have an active business and was formed merely to perpetuate the decedent's buy-hold investment philosophy with respect to publicly traded stock."[14]

Any plan needs to carefully consider who shall be a party to the arrangement. In *Morrissette*, the sons ultimately stood on both sides of the arrangement and forced a deemed termination. But consider if 2036(a)(2) would apply to an individual party or non-independent or independent Trustee, or a separate downstream trust with different interests?

LESSONS TO LEARN

Be Mindful of Professional Responsibility

Be careful of what you tell clients or prospects. The Tax Court leaned in on the legal and life insurance professionals' marketing materials and warnings that the program helped avoid estate taxes. The IRS was able to get all of this material for examination. Consider if such promotion violates professional rules of responsibility.

Avoid aggressive discounts (Pigs Get Fat, Hogs Get Slaughtered)

In Morrissette, the family took a 75% discount. The IRS expert even gave a 42.7% discount when the policies were held until death. The aggressive discounts subjected the estate to an estate tax deficiency and a 40% penalty. The Tax Court ultimately allowed discount rates ranging between 6.4% and 8.85%. If policies are going to be held until death, a larger discount may be considered reasonable.

Inherently Lower Cash Value Policies May Help

The valuation experts on both sides placed great weight on the cash surrender values of the life insurance policies in question. Guaranteed Universal Life policies with low cash values may provide an additional shield for families engaging in intergenerational split-dollar transactions. They develop very little cash value, so even conceding the full cash value as the value of the arrangement would be a large discount from the premium paid. Further, because there is a low surrender value, it increases the probability the policies will be held until the death of insureds.

This piece was created by M Financial's Advanced Markets experts and produced by the marketing team.

ENDNOTES

[1] Thank you to Morgan Scott of M Financial and Richard Harris of Greenberg and Rapp for their assistance in preparing this summary.

[2] In Estate of Cahill v. Commissioner, T.C. Memo. 2018-84, the Tax Court "held that a decedent's right to terminate a split-dollar agreement and to recover at least the cash surrender values were rights, held in conjunction with another person, to designate the persons who would possess or enjoy the transferred property under 2036(a)(2) and to alter, amend, revoke, or terminate the transfer under 2038(a)(1)." In Cahill, the Tax Court denied the estate's argument that the bona fide sale exception of 2036 or 2038 was met where the interest was merely an investment account of marketable securities.

[3] Estate of Bigelow v. Commissioner, 503 F.3d 955 (9th Cir. 2007), aff'g T.C. Memo. 3005-65; Estate of Strangi v. Commissioner, 417 F.3d at 481; Estate of Reynolds v. Commissioner, 55 T.C. 172 (1970).

[4] Estate of Bischoff v. Commissioner, 69 T.C. 32 (1977).

[5] Kimbell v. United States F.3d 257 (5th Cir. 2004); Estate of Mirowski v. Commissioner, T.C. Memo. 2008-74; Estate of Stone v. Commissioner, T.C. Memo. 2003-309; Estate of Harrison v. Commissioner, T.C. Memo. 1987-8.

[6] Estate of Stone v. Commissioner, T.C. Memo. 2003-309.

[7] Estate of Thompson v. Commissioner, 382 F.3d.

[8] Morrissette expert one relied on a single magazine article from 2009 for a range of life settlement yields from 15% to 18%, resting on an average of 15.83%. Morrissette expert two also determined a 15% discount rate based upon a variety of sources, but presented a range of 9.3% to 23.2%

[9] The IRS expert disagreed with the use of life settlement yields primarily because the cash surrender values were likely to increase each year the brothers were alive and that payouts would continue to increase if a brother outlived life expectancy.

[10] Estate of D'Ambrosio V. Commissioner, 101 F.3d 309, 313 (3d Cir. 1996), rev'g 105 T.C. 252 (1995).

[11] In this decision the Court stated there were grounds for setting an even earlier date but declined.

[12] The policies on one of the brothers was with American General Life, which at the time of Mrs. Morrissette's death was in dire economic circumstances. The other policies were with MassMutual, a highly-rated carrier and hence the lower discount rate was used because of the lower risk as reflected in the rate on the company's bonds.

[13] Treas. Reg. 1.7872-15(a)(2)(i)

[14] Estate of Schutt v. Commissioner, T.C. Memo. 2005-126, 2005 WL 1244686.

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