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BOLI Exchanges and Restructuring

Clark Consulting Webcast



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- Exchanges in general
- Interest deductions
- COLI Best Practices
- MEC aggregation

- **Actual Exchanges**
 - “External” and “internal” exchanges
- **Deemed Exchanges**
 - Concept of “material changes”
 - » Some benefit increases, changes to guaranteed terms, etc.
 - » Broadly interpreted
- **Why should I care?**
 - Certain tax rules triggered when contract “issued”
 - Normally, exchange = newly “issued” contract
 - Normally, material change = “exchange”

- **Disallows general interest deductions for COLI owners**
 - Exception for employee coverage
- **PLR 200627021**
 - Exchange = new contract
 - If insured ≠ employee at time of exchange, then exception n/a
 - So exchanges involving former employees will trigger § 264(f), causing interest deduction disallowance

- **Death benefits taxable ...**
 - Unless notice and consent, other rules met
- **Grandfather clauses:**
 - Basic:
 - » Applies to contracts “issued” after 08/17/06
 - § 1035:
 - » N/A to contract issued in a § 1035 exchange for contract that was originally issued on or before 08/17/06
 - Material change:
 - » Material increases in DB or other material change = new contract
 - » Specific examples of what ≠ material change

- **PLR 200715006**
 - Grandfather applies after § 1035 exchange
 - But no “material change” involved
 - Interaction between § 1035 and material change grandfather clauses?

- **Does an exchange re-trigger notice & consent rules?**
 - Rules must be met before contract “issued”
 - » Normally, material change = exchange = newly issued contract
 - Do § 101(j) effective date rules save the day?
 - » N/A if contract already subject to § 101(j)?

- **MEC Aggregation**
 - All MECs issued in same year to same owner by same carrier are treated as one
 - LIFO rule applies based on aggregate gain
- **Rev. Rul. 2007-38**
 - § 1035 exchange “breaks” aggregation
 - Caution: IRS concern with tax avoidance

- **Example:**
 - 2 MECs aggregated, each w/ \$10 basis and \$10 gain
 - Could surrender 1, pay tax on \$20, OR
 - Could exchange 1 to “break” aggregation, surrender it, pay tax on \$10

- **Relationship to “partial exchange” issue**
 - Rev. Proc. 2008-24
 - » Exchange disregarded if withdraw w/in 1 year
 - PLRs 200801001 and 200715006
 - » § 1035 of MECs where PH had “no intent” to take withdrawals

Contact your Clark Consulting representative with any questions.