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Notice 2018-41: Future regulations, information reporting on reportable policy sales of life insurance contracts (new section 6050Y)

The IRS today released an advance version of Notice 2018-41 that describes the new information reporting requirements under Code section 6050Y and that sets out details of future regulations that will be issued as guidance to assist taxpayers in complying with these information reporting requirements for reportable policy sales of life insurance contracts.

Section 6050Y was added to the Code by the new tax law (Pub. L. No. 115-97, enacted December 22, 2017).

Notice 2018-41 [PDF 63 KB] reports that the IRS and Treasury intend to issue proposed regulations as guidance to assist taxpayers in complying with the new information reporting obligations for certain life insurance contract transactions under section 6050Y. Today's IRS notice also:

- States that the future proposed regulations will provide guidance on a modification to the transfer for valuable consideration rules for life insurance contracts, added to Code section 101(a) by the new tax law
- Provides transitional guidance delaying any reporting under section 6050Y until final regulations are issued
- Provides taxpayers additional time to satisfy any reporting obligations arising prior to publication of final regulations

The IRS today also issued a press release—**IR-2018-104**—concerning Notice 2018-41.

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Overview

Under Notice 2018-41, information returns need to be filed in the following situations:

- By anyone who acquires a life insurance contract, or any interest in a life insurance contract, in a "reportable policy sale"
- By an issuer of a life insurance contract upon notice of a transaction required to be reported above or upon any notice of a transfer of a life insurance contract, or any interest in a life insurance contract, to a foreign person
- By any payor of "reportable death benefits"

A "reportable policy sale" is generally the acquisition of an interest in a life insurance contract, directly or indirectly, if the acquirer has no substantial family, business, or financial relationship to the insured.

A "reportable death benefit" is an amount paid at the death of the insured under a life insurance contract that was transferred in a reportable policy sale.

Intended proposed guidance

Information reporting for certain life insurance contract transactions

Section 6050Y provides that each of the returns required by section 6050Y must be made "at such time and in such manner as the Secretary shall prescribe." Treasury and the IRS intend to propose regulations under section 6050Y describing the manner by which and time at which the reporting requirements of section 6050Y must be satisfied. The proposed regulations will also clarify which parties are subject to the reporting requirements and other definitional issues.

For example, Treasury and the IRS intend to define the term "reportable policy sale" in the proposed regulations to include a viatical settlement. A viatical settlement (a subset of life settlement transactions) may involve the sale of a life insurance contract, but may not be taxed as a sale. Under a viatical settlement, a policyholder may sell or assign a life insurance contract after the insured has become terminally ill or chronically ill.

In addition, Treasury and the IRS intend to clarify the extent to which section 6050Y applies to sales or acquisitions effected by transferors and transferees outside the United States and to sellers and issuers that are foreign persons for purposes of reporting under section 6050Y(b) or (c).

Section 6050Y(a) reporting of payments by acquirer in a reportable policy sale

Treasury and the IRS intend to propose regulations that will accomplish the following:

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- Require every person who acquires a life insurance contract or any interest in a life insurance contract in a reportable policy sale to file an information return, to be made according to forms and instructions to be published by the IRS.

- Require every person that is required to file a return under section 6050Y(a)(1) to furnish written statements to each payment recipient and issuer whose name is required to be set forth in such return.

- Provide a definition of "acquirer" for purposes of section 6050Y, defined as any person who acquires a life insurance contract, or an interest in a life insurance contract, directly or indirectly, and who has no substantial family, business, or financial relationship with the insured apart from the acquirer's interest in such life insurance contract. The future proposed regulations may further refine the definition of an "acquirer" for purposes of section 6050Y. For example, the proposed regulations may define "acquirer" in a reportable policy sale to include any person, including the life settlement or viatical settlement provider or financing entity that takes title or possession for state law purposes or acquires a beneficial interest in the life insurance contract at any time. The statute defines "indirectly" for purposes of a reportable policy sale as the acquisition of an interest in a partnership, trust, or other entity that holds an interest in the life insurance contract. The proposed regulations may further refine the definition of "indirectly" for purposes of section 6050Y reporting.

- Clarify the definition of a "reportable payment" for purposes of section 6050Y. Under section 6050Y(d)(1), "payment" is defined with respect to any reportable policy sale, as "the amount of cash and the fair market value of any consideration transferred in the sale." Treasury and the IRS intend to clarify that a reportable payment may include payments to persons other than the seller—such as brokers and, potentially, life settlement providers acting as intermediaries.

- Clarify that the "payment" to the seller reported under section 6050Y(a) is the seller's net proceeds. The net proceeds equal the gross proceeds minus any selling expenses (for example, broker's fees and commissions).

Section 6050Y(b) reporting of transferor's investment in the contract by issuer (reportable policy sale or transfer to a foreign person)

Treasury and the IRS intend to propose regulations to accomplish the following:

- Implement reporting obligations under section 6050Y(b) on any issuer of a life insurance contract who has either: (1) received the statement required by section 6050Y(a)(2) to be furnished by the acquirer in a reportable policy sale; or (2) received notice of a transfer of a life insurance contract to a foreign person.

- Limit the information reporting obligations imposed under section 6050Y(b) to the life insurance company that is responsible for administering the contract, including paying death benefits under the life insurance contract. Under the future proposed regulations, the reporting obligations would not apply, for instance, to a reinsurer in

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an indemnity contract covering all or a portion of the risks that the original issuer (and continuing contract administrator) might otherwise have incurred with respect to a life insurance contract. This proposed definition of “issuer” will reduce the burden on reporting life insurance companies and prevent duplicative reporting.

- Require under section 6050Y(b)(1) issuers who have received a statement under section 6050Y(a)(2) to report a reportable policy sale or notice of a transfer of a life insurance contract to a foreign person to file an information return, to be made according to forms and instructions to be published by the IRS.

- Require every issuer to make a return under section 6050Y(b)(1) to furnish written statements to each seller whose name is required to be set forth in a return.

- Define “seller” for purposes of section 6050Y(b) to include any person who transfers an interest in a life insurance contract to an acquirer in a reportable policy sale or to a foreign person.

- Define the term “investment in the contract” that is required to be reported by the issuer with respect to a seller. Section 6050Y(b) requires an issuer to report the “investment in the contract (as defined in section 72(e)(6)) with respect to such seller.”

- Define notice of a transfer of a life insurance contract to a foreign person for purposes of section 6050Y(b) as any notice, including information provided for non-tax purposes such as change of address notices for purposes of sending statements or for other purposes, or information relating to loans, premiums, or death benefits with respect to the contract.

- Provide that issuers who have not received a written statement from an acquirer under section 6050Y(a)(2), but who have received notice of a transfer of a life insurance contract to a domestic person, may optionally file a return with the IRS under section 6050Y(b)(1) and furnish written statements to sellers under section 6050Y(b)(2), unless the issuer knows the transfer is not a reportable policy sale.

Section 6050Y(c) reporting of reportable death benefits by payor

Treasury and the IRS intend to do the following:

- Propose regulations related to the reporting obligations under section 6050Y(c) on persons making payments of reportable death benefits during any tax year.

- Propose regulations under section 6050Y(c)(1) requiring a payor of reportable death benefits to file an information return, to be made according to forms and instructions to be published by the IRS, reporting the following information to the IRS.

- Propose regulations under section 6050Y(c)(2) requiring every person required to file a return under section 6050Y(c)(1) to furnish written statements to each

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recipient of reportable death benefits whose name is required to be set forth in a return made under section 6050Y(c)(1).

- Define the term “estimate of the investment in the contract” that is required to be reported by the payor with respect to a buyer to include only the amount of premiums paid by the buyer under the contract, less the aggregate amount received by the buyer under the contract.

- Define “buyer” in the proposed regulations. For example, the proposed regulations may define “buyer” to include any person either holding a beneficial interest in the life insurance contract or taking title or possession for state law purposes.

The definition of “reportable policy sale” applies only to transfers made after December 31, 2017. Section 6050Y(d)(4) defines “reportable death benefits” as “amounts paid by reason of the death of the insured under a life insurance contract that has been transferred in a reportable policy sale.” Accordingly, death benefits are “reportable death benefits” under section 6050Y(d)(4), and are subject to the reporting requirements of section 6050Y(c), only if the death benefits are paid by reason of the death of the insured under a life insurance contract transferred after December 31, 2017, in a reportable policy sale.

Timing of section 6050Y reporting

The following items with regard to timing are included in the IRS notice:

- The recipients of the written statements required to be furnished under section 6050Y may use the information therein to determine their taxable income. To facilitate recipients’ proper tax reporting, Treasury and the IRS intend to require that an acquirer furnish the written statements required under section 6050Y(a)(2) to an issuer by the later of: (1) 20 days after the reportable policy sale; or (2) five (5) days after the end of the applicable state law rescission period, if any, but in no event later than January 15 of the year following the calendar year in which the reportable policy sale occurs. Treasury and the IRS intend to require that all other written statements required under sections 6050Y(a)(2), (b)(2), and (c)(2) be furnished to the recipients identified in the statute and regulations no later than January 31 of the year following the calendar year in which the reportable policy sale or reportable death benefit payment occurs.

- Treasury and the IRS intend to propose regulations requiring the returns required by sections 6050Y(a)(1), (b)(1), and (c)(1) to be filed with the IRS no later than February 28 of the year following the calendar year in which the reportable policy sale or reportable death benefit payment occurs, for paper returns; and no later than March 31 of the year following the calendar year in which the reportable policy sale or reportable death benefit payment occurs, for electronically filed returns.

- Treasury and the IRS intend to propose regulations regarding reporting obligations upon the rescission of a reportable policy sale or transfer to a foreign person.

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Upon receiving notice of the rescission, any person who has filed a return required by section 6050Y with respect to the reportable policy sale or transfer would have 15 days to file a corrected return.

- The reporting requirements of section 6050Y apply to reportable policy sales that occur after December 31, 2017, and reportable death benefits paid after December 31, 2017. For reportable policy sales and payments of reportable death benefits occurring after December 31, 2017, and before the date final regulations under section 6050Y are published in the Federal Register, Treasury and the IRS intend to allow additional time after the date final regulations are published to file the returns and furnish the written statements required by section 6050Y.

Modification to the transfer for value consideration rules

Treasury and the IRS intend to propose amendments to Reg. section 1.101-1 to reflect the addition of section 101(a)(3) (added by section 13522 of H.R. 1—the bill that eventually became the new tax law).

Request for comments

Treasury and the IRS have requested comments on the proposed rules described in today's notice and on any additional issues that should be addressed by the regulations. Comments are to be submitted in writing on or before June 13, 2018.

KPMG observation

Tax professionals have observed that this is a very helpful notice that describes new tax reform information reporting requirements for certain life insurance contract transactions and that provides transitional guidance delaying reporting until final regulations are issued.

It further has been observed that Notice 2018-41 is also beneficial because there has been ambiguity regarding what is defined as a reportable policy sale. The expected section 101 regulation will help identify what qualifies as a substantial interest. In addition, it is viewed as being very beneficial that there is an opportunity for a comment period. There may be some questions as to why viatical settlements (which are covered by section 101(g)) are included given that these are not life settlement-type transactions.

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