



# TaxNewsFlash

United States



No. 2021-163  
April 12, 2021

## U.S. Tax Court: Split-dollar arrangement distributions; benefits under compensatory arrangement taxable as ordinary income

The U.S. Tax Court today released a “reviewed opinion” holding that economic benefits received by the taxpayer-husband under a split-dollar arrangement were not “distributions” under section 301, but were benefits received under a compensatory arrangement and as such were taxable as “compensation for services” under section 61(a)(1) as ordinary income.

The case is: *De Los Santos v. Commissioner*, 156 T.C. No. 9 (April 12, 2021). Read the [Tax Court opinion](#) [PDF 102 KB] (that does not include any separate concurring or dissenting opinions)

### Summary

The Tax Court summarized the facts in this case, as follows:

- The taxpayer-husband (a medical doctor) during 2011 and 2012 was the sole shareholder of an S corporation that employed him and his wife.
- The S corporation adopted an employee welfare benefit plan that provided benefits to the husband, the wife, and four other employees.
- The taxpayers received these benefits in their capacity as employees.
- The benefit plan afforded life insurance protection to the taxpayers and was found in a prior Tax Court memorandum opinion to constitute a compensatory “split-dollar” life insurance arrangement. Thus, the taxpayers were taxable on the economic benefits they realized by participating in the plan.
- In the notice of deficiency, the IRS determined that these economic benefits from the plan were taxable to the taxpayers as ordinary compensation income.
- The taxpayers in the instant action filed a motion for partial summary judgment contending that, because the taxpayer-husband was a shareholder of the S corporation, the economic benefits he realized were taxable to him as a distribution under section 301.
- The taxpayers further claimed that the economic benefits received by a shareholder pursuant to a split-dollar life insurance arrangement constitute a distribution under section 301—regardless of

whether the taxpayer receives the benefits in his capacity as an employee or as a shareholder. In support of this position, the taxpayers looked to the decision of the Sixth Circuit in *Machacek v. Commissioner*, 906 F.3d 429 (6th Cir. 2018), rev'g and remanding T.C. Memo. 2016-55.

The Tax Court held that given that the compensatory split-dollar life insurance arrangement afforded benefits to the taxpayer-husband in his capacity as an employee of the S corporation, the benefits were not characterized as a distribution "by a corporation to a shareholder with respect to its stock."

The court further held that for purposes of taxing employee fringe benefits, the taxpayer-husband was to be treated as a partner of a partnership, and the economic benefits that he realized were therefore taxable under section 707(c) as "guaranteed payments" and thus as ordinary income.

The purpose of this *TaxNewsFlash* is to provide text of the opinion.

The information contained in TaxNewsFlash is not intended to be "written advice concerning one or more Federal tax matters" subject to the requirements of section 10.37(a)(2) of Treasury Department Circular 230, as the content of this document is issued for general informational purposes only, is intended to enhance the reader's knowledge on the matters addressed therein, and is not intended to be applied to any specific reader's particular set of facts. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. Applicability of the information to specific situations should be determined through consultation with your tax adviser.

KPMG International is a Swiss cooperative that serves as a coordinating entity for a network of independent member firms. KPMG International provides no audit or other client services. Such services are provided solely by member firms in their respective geographic areas. KPMG International and its member firms are legally distinct and separate entities. They are not and nothing contained herein shall be construed to place these entities in the relationship of parents, subsidiaries, agents, partners, or joint venturers. No member firm has any authority (actual, apparent, implied or otherwise) to obligate or bind KPMG International or any member firm in any manner whatsoever.

Direct comments, including requests for subscriptions, to [Washington National Tax](#). For more information, contact KPMG's Federal Tax Legislative and Regulatory Services Group at + 1 202.533.4366, 1801 K Street NW, Washington, DC 20006-1301.

To unsubscribe from TaxNewsFlash-United States, reply to [Washington National Tax](#).

[Privacy](#) | [Legal](#)