MassMutual
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SUCCESS STRATEGIES
Advanced Sales

Intra-Family Loans & Family Switch Dollar

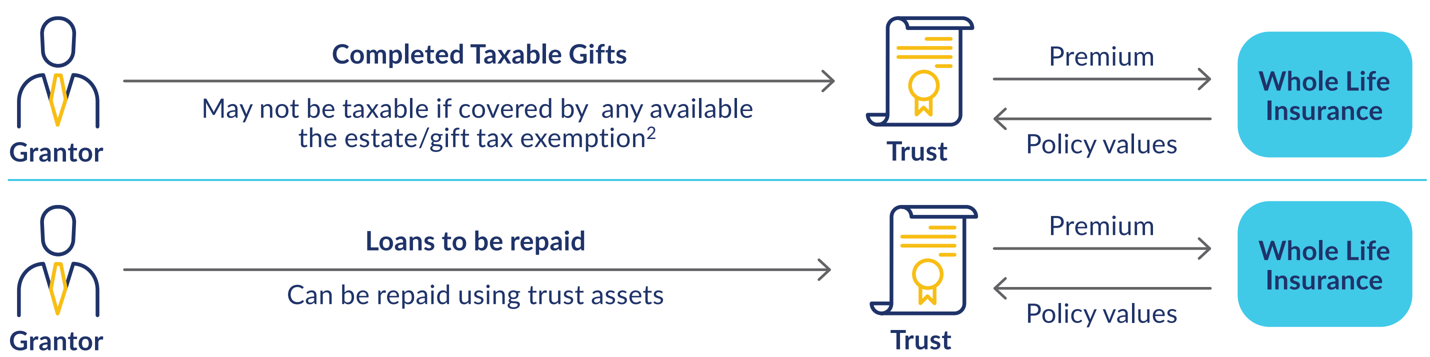
Planning for High Net Worth (HNW) Families

Loans vs. Gifts. In a nutshell, HNW families can lend cash — or sell an asset — to their heirs, or to a family trust for their benefit. **Because the loans must be repaid, they are not taxable gifts**. By making loans, parents have flexibility depending on changing circumstances and tax law because the loan can be:

- repaid, from trust assets and/or policy values.
- refinanced.
- forgiven later.[1]

Loans can be made to a trust to pay annual premiums. The cumulative loan will then need to be repaid from trust assets.

GIFT VS. LOAN



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[1] Note that when a loan is forgiven, it is then a completed gift. As such, the amount of forgiveness is taxable, in which case gift or estate taxes on the amount of forgiveness is due. However, the lifetime gift and estate tax exemption can be used to cover the taxes, if available.

[2] The 2017 Tax Act temporarily increased the total amount that individuals and couples can transfer to heirs, during lifetime and/or at death. The combined estate and gift tax-free amount in 2024 is $13,610,000 per individual, or $27,220,000 per married couple. The exemption amounts are indexed annually for inflation. However, the increased exemptions are due to expire ("sunset") in 2026, when they revert to their 2017 level, roughly $6,800,000+ per individual, or $13,600,000+ per couple, subject to retroactive adjustments for inflation.

This discussion of premium-funding strategies is intended to be a simplified summary of common loan strategies that can be used to fund life insurance in wealth transfer planning. In actual practice, the transactions discussed may be somewhat complex and therefore may require the attention, review and expertise of professional advisors such as your clients CPA and their tax or estate planning attorney.

The information provided is not intended as specific tax or legal advice. MassMutual®, its subsidiaries, employees and representatives are not authorized to give tax or legal advice. Individuals are encouraged to seek advice from their own tax or legal counsel.

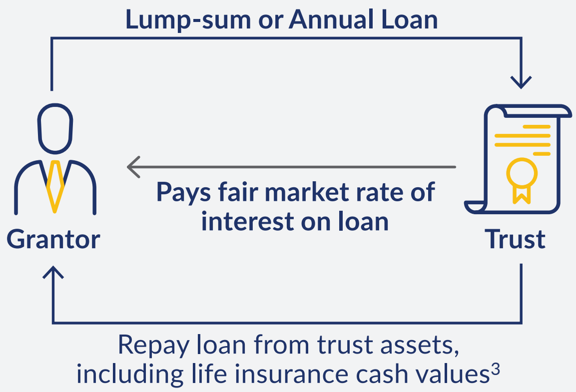
Loans

An intra-family loan or family switch dollar approach allows families with limited or no gift/estate tax exemptions to fund needed life insurance without incurring gift tax.[2] With loan interest rates climbing, a family switch dollar plan can minimize the out-of-pocket costs of the plan since the measure of the imputed gift is the term cost of the death benefit, and not loan interest. There are a number of ways to design an intra-family loan plan, two of which are described below:

SCENARIO A: INTRA-FAMILY LOAN

Loan of Cash to Fund Premium

Lump sum or annual loans designed as a privately financed note that charges a fair market rate of loan interest



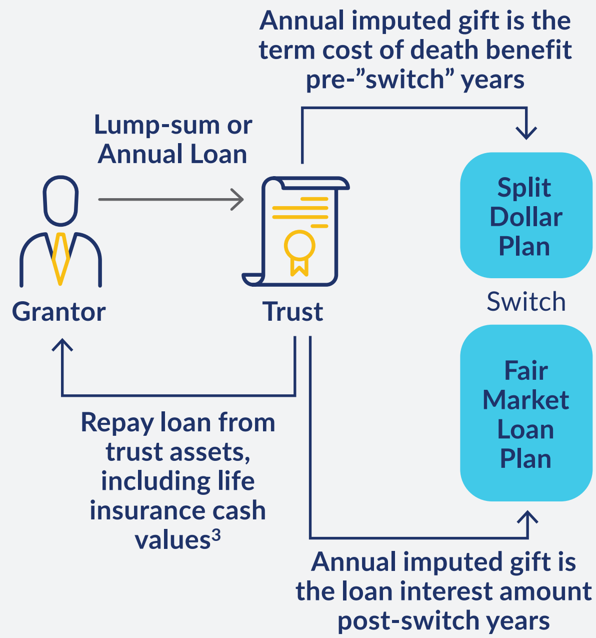
Con: Loan interest rates are climbing

Pro: Unlike premium financing through a bank or third party, higher rates do not prohibit planning with intra-family notes since the funds stay within the family.

SCENARIO B: FAMILY “SWITCH” DOLLAR

Loan of Cash to Fund Premium

Split dollar loan that switches to a privately financed loan when cash values exceed cumulative premiums paid



Con: The switch to a privately financed note is not automatic and must be actively changed.

Pro: Paying Term costs during the premium payment years lowers the overall gift tax costs of the arrangement; The cash values of the whole life policy can provide flexibility to help repay the loan.

[3] Distributions under the policy (including cash dividends and partial/full surrenders) are not subject to taxation up to the amount paid into the policy (cost basis). If the policy is a Modified Endowment Contract, policy loans and/or distributions are taxable to the extent of gain and are subject to a 10 percent tax penalty if the policyowner is under age 59½. Access to cash values through borrowing or partial surrenders will reduce the policy’s cash value and death benefit, increase the chance the policy will lapse, and may result in a tax liability if the policy terminates before the death of the insured.

Loans

When an intra-family loan is established, it must be structured as a privately financed fair market loan, or as a combination split dollar plan/privately financed arrangement. The life insurance policy values are split between the trust and the grantor during the term of the arrangement.

Elements of a Privately Financed Arrangement:

The AFR Rate. The Applicable Federal rate (AFR) published monthly by the government is used to determine loan interest in private loan arrangements between a grantor and the trust. The loan interest can be accrued or paid annually.

Fair Market Loan. For a loan to be considered an arm's length transaction, the IRS requires, among other qualifications, a fair market rate of interest be charged and that there to be sufficient funds in the trust to repay the loan. The government AFR rates are considered fair rates of interest. The AFR rate can be locked in for the term of the loan at the time the loan is established:

- Short-term AFR rate is used for loans less than 3 years.
- Mid-term AFR rate is used for loans with a term of 3-9 years.
- Long-term AFR rate is used for loans of more than 9 years.

Switch before policy cash value exceeds cumulative premium paid

Split Dollar Plan → **Fair Market Loan Plan**

Split Dollar Plan

- All policy cash values remain with the grantor until switch year.
- Death Benefit equal to cumulative loan is assigned to grantor; balance to trust.

Fair Market Loan Plan

- At switch year, the greater of cumulative premiums paid or policy cash value is the initial amount of the new loan payable to Grantor and remains with grantor. Balance of policy equity is allocated to trust.
- Death Benefit equal to cumulative loan is assigned to grantor; balance to trust.

Elements of a Family "Switch" Dollar plan:

Family "Switch Dollar" begins as a non-equity split dollar arrangement in which the value of the annual gift made to the trust is based on the term cost of the life insurance that the trust is to receive. The arrangement then switches to a privately financed loan.

- The economic benefit is the term cost of the death benefit based on either a government published table (Table 2001) or the insurer's term rates, if it qualifies under IRS rules.
- The economic benefit is the imputed gift to the trust and can be covered by annual exclusion gifts. or gift tax exemption amounts, if available.[2]
- The trust beneficiaries will receive the death benefit, net of the loan repayment to the grantor.
- If and when the loan is repaid during lifetime, either from policy cash values or other trust assets, the policy death benefit is no longer split with the grantor.
- During the split dollar term, all of the cash value must remain with the grantor until the loan is repaid, or until the arrangement is switched to a privately financed loan, in which a fair market rate of interest (AFR) is charged. Otherwise, the cash value is subject to gift tax.
- When the cash value exceeds cumulative premiums paid (meaning that there is "equity" in the policy), the split dollar arrangement is terminated and replaced with a privately financed note that includes a loan balance that represents the greater of cumulative premiums paid or cash value *in the year of switch*. At this point, the cash values are now split so that any excess equity in the policy, net of the cumulative loan to be paid to the grantor, inures to the benefit of the trust.

The cash values of the whole life policy can provide flexibility to help repay the intra family loan.

CHART B

		POLICY DETAILS[4, 5]				
Year	Age	Prem	Cumulative Premiums	Net Cash Value End Year	Policy Equity*	Death Benefit End Year
1	48	235,700	235,700	81,100	–	5,018,169
2	49	235,700	471,400	226,099	–	5,056,961
3	50	235,700	707,100	442,818	–	5,114,652
4	51	235,700	942,800	673,876	–	5,191,524
5	52	235,700	1,178,500	920,131	–	5,288,244
6	53	235,700	1,414,200	1,181,631	–	5,402,303
7	54	235,700	1,649,900	1,458,919	–	5,533,487
8	55	235,700	1,885,600	1,752,939	–	5,681,808
9	56	235,700	2,121,300	2,064,541	–	5,847,307
10	57	235,700	2,357,000	2,394,792	37,792	6,030,067
11	58	235,700	2,592,700	2,752,132	159,432	6,246,034
12	59	235,700	2,828,400	3,137,834	309,434	6,494,669
13	60	0	2,828,400	3,310,266	481,866	6,683,086
14	61	0	2,828,400	3,491,477	663,077	6,877,318
15	62	0	2,828,400	3,682,071	853,671	7,078,048
16	63	0	2,828,400	3,883,903	1,055,503	7,288,376
17	64	0	2,828,400	4,096,302	1,267,902	7,506,097
18	65	0	2,828,400	4,319,493	1,491,093	7,731,466
19	66	0	2,828,400	4,554,061	1,725,661	7,964,847
20	67	0	2,828,400	1,814,082	1,814,082	5,220,130
21	68	0	2,828,400	1,905,945	1,905,945	5,303,566

Chart C (on the following page) illustrates a Family "Switch" Dollar design based on Chart B to the left of this page.

Chart B assumes 12 annual premium loans made to a trust that owns a WL12 policy with a $5M initial death benefit. The annual premium is $235,700, payable for 12 years. The illustration assumes a policy distribution in the form of a loan in year 20 based on an adjustable loan rate of 5.58%.

The design assumes a non-equity split dollar arrangement for the first 9 years in which the imputed gift is based on the term cost of the death benefit.

The plan then switches to a privately financed fair market loan in year 10 and assumes a hypothetical loan interest rate of 4.83% (November 2023 AFR Rate for loan terms greater than 9 years). The loan interest rate in the future will be more or less than current rates. It is assumed that the loan will be repaid from non-guaranteed policy cash value in year 20.[3]

* Policy equity refers to the policy cash value in excess of the cumulative premiums loaned and is based on the current dividend schedule, which is not guaranteed.

[4] These illustrated amounts are not guaranteed. They include dividends, which are neither estimates nor guarantees, but are based on the 2024 dividend schedule. Dividends in future years may be lower or higher, depending on the company's actual experience. Due to this fact, we strongly recommend you look at a lower schedule illustration.

[5] This supplemental illustration is not valid unless accompanied by or preceded by a Massachusetts Mutual Life Insurance Company Whole Life 12 Pay Basic Illustration dated November 9, 2023. Refer to the Basic Illustration for guaranteed elements, assumptions, explanations, and other important information.

Life Insurance

FEMALE, AGE 47, ULTRA-PREFERRED NON-TOBACCO WL12 $5,000,000 INITIAL DEATH BENEFIT/$235,700 ANNUAL PREMIUM[4,5]

	NON-GUARANTEED VALUES									
	GRANTOR/ MOM				IRREVOCABLE LIFE INSURANCE TRUST					
Year	Annual Premium Loan Made to Trust	Cumulative Loan	Net Cash Value Assigned to Grantor End Year	Death Benefit Assigned to Grantor End Year	Imputed Gift: Economic Benefit	Imputed Gift: Loan Interest @4.83%	Cumulative Loan to Repay	Trust Portion of Net Cash Value End Year	Policy Distributions[3]	Trust Portion of Death Benefit End Year
1	235,700	235,700	81,100	235,700	2,774	0	0	0	0	4,782,469
2	235,700	471,400	226,099	471,400	2,843	0	0	0	0	4,585,561
3	235,700	707,100	442,818	707,100	2,909	0	0	0	0	4,407,552
4	235,700	942,800	673,876	942,800	2,974	0	0	0	0	4,248,724
5	235,700	1,178,500	920,131	1,178,500	3,041	0	0	0	0	4,109,744
6	235,700	1,414,200	1,181,631	1,414,200	3,111	0	0	0	0	3,988,103
7	235,700	1,649,900	1,458,919	1,649,900	3,262	0	0	0	0	3,883,587
8	235,700	1,885,600	1,752,939	1,885,600	3,455	0	0	0	0	3,796,208
9	235,700	2,121,300	2,064,541	2,121,300	3,651	0	0	0	0	3,726,007
10	235,700	2,357,000	2,357,000	2,357,000	0	113,843	2,357,000	37,792	0	3,673,067
11	235,700	2,592,700	2,592,700	2,592,700	0	125,227	2,592,700	159,432	0	3,653,334
12	235,700	2,828,400	2,828,400	2,828,400	0	136,612	2,828,400	309,434	0	3,666,269
13	0	2,828,400	2,828,400	2,828,400	0	136,612	2,828,400	481,866	0	3,854,686
14	0	2,828,400	2,828,400	2,828,400	0	136,612	2,828,400	663,077	0	4,048,918
15	0	2,828,400	2,828,400	2,828,400	0	136,612	2,828,400	853,671	0	4,249,648
16	0	2,828,400	2,828,400	2,828,400	0	136,612	2,828,400	1,055,503	0	4,459,976
17	0	2,828,400	2,828,400	2,828,400	0	136,612	2,828,400	1,267,902	0	4,677,697
18	0	2,828,400	2,828,400	2,828,400	0	136,612	2,828,400	1,491,093	0	4,903,066
19	0	2,828,400	2,828,400	2,828,400	0	136,612	2,828,400	1,725,661	0	5,136,447
20	0	2,828,400	2,828,400	2,828,400	0	0	0	1,814,082	2,828,400	5,220,130
21	0	0	0	0	0	0	0	**1,905,945**	0	**5,303,566**

[4] These illustrated amounts are not guaranteed. They include dividends, which are neither estimates nor guarantees, but are based on the 2024 dividend schedule. Dividends in future years may be lower or higher, depending on the company's actual experience. Due to this fact, we strongly recommend you look at a lower schedule illustration.

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Life insurance proceeds are generally excluded from the beneficiary's gross income for income tax purposes.
There have been a few exceptions such as when a life insurance policy has been transferred for valuable consideration.

The products and/or certain features may not be available in all states. State variations will apply.

MassMutual Whole Life Legacy series policies (Policy Forms: MMWL-2018 and ICC18-MMWL in certain states, including North Carolina, and MMWLA-2018 and ICC18-MMWLA in certain states, including North Carolina) are level-premium, participating, permanent life insurance policies issued by Massachusetts Mutual Life Insurance Company (MassMutual), Springfield, MA 01111-0001.

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