

provide for sufficient interest, then section 7872 applies to the loan and the loan is treated as a below-market demand loan subject to paragraph (e)(3)(iii) of this section. For each year that the loan is outstanding, however, the rate used in the determination of forgone interest under paragraph (e)(3)(iii) of this section is not the blended annual rate but rather is the AFR (based on annual compounding) appropriate for the loan's term as of the month in which the loan is made. See paragraph (e)(5)(iii)(C) of this section to determine the loan's term.

(C) *Term of loan.* The term of a split-dollar loan described in paragraph (e)(5)(iii)(A)(1) of this section is based on the period from the date the loan is made until the loan's stated maturity date. However, if a split-dollar loan described in paragraph (e)(5)(iii)(A)(1) of this section does not have a stated maturity date, the term of the loan is presumed to be seven years.

(D) *Retirement and reissuance of loan.* If a split-dollar loan described in paragraph (e)(5)(iii)(A)(1) of this section remains outstanding longer than the term determined under paragraph (e)(5)(iii)(C) of this section because of the continued performance of substantial services, the split-dollar loan is treated for purposes of this section as retired and reissued as a split-dollar demand loan at that time for an amount of cash equal to the loan's adjusted issue price on that date. The loan is retested at that time to determine whether the loan provides for sufficient interest.

(iv) *Gift split-dollar term loans—(A) Applicability.* This paragraph (e)(5)(iv) applies to gift split-dollar term loans.

(B) *Treatment of loan.* A split-dollar loan described in paragraph (e)(5)(iv)(A) of this section is tested under paragraph (e)(4)(ii) of this section to determine if the loan provides for sufficient interest. If the loan provides for sufficient interest, then section 7872 does not apply to the loan and the interest on the loan is taken into account under paragraph (f) of this section. If the loan does not provide for sufficient interest, then section 7872 applies to the loan and the loan is treated as a below-market demand loan subject to paragraph (e)(3)(iii) of this section. For each year that the loan is outstanding, however, the rate used in the determination of forgone interest under paragraph (e)(3)(iii) of this section is not the blended annual rate but rather is the AFR (based on annual compounding) appropriate for the loan's term as of the month in which the loan is made. See paragraph (e)(5)(iv)(C) of this section to determine the loan's term.

(C) *Term of loan.* For purposes of paragraph (e)(5)(iv)(B) of this section, the term of a gift split-dollar term loan is the term determined under paragraph (e)(4)(iii) of this section.

(D) *Limited application for gift split-dollar term loans.* The rules of paragraph (e)(5)(iv)(B) of this section apply to a gift split-dollar term loan only for Federal income tax purposes. For purposes of Chapter 12 of the Internal Revenue Code (relating to the gift tax), gift below-market split-dollar term loans are treated as term loans under section 7872(b) and paragraph (e)(4) of this section. See section 7872(d)(2).

(v) *Split-dollar loans payable on the later of a term certain and another specified date—(A) Applicability.* This paragraph (e)(5)(v) applies to any split-dollar term loan payable upon the later of a term certain or—

(1) The death of an individual; or

(2) For a loan described in paragraph (e)(5)(iii)(A)(1) of this section, the date on which the condition to perform substantial future services by an individual ends.

(B) *Treatment of loan—(1) In general.* A split-dollar loan described in paragraph (e)(5)(v)(A) of this section is a split-dollar term loan, subject to paragraph (e)(4) of this section.

(2) *Term of the loan.* The term of a split-dollar loan described in paragraph (e)(5)(v)(A) of this section is the term certain.

(3) *Appropriate AFR.* The appropriate AFR for a split-dollar loan described in paragraph (e)(5)(v)(A) of this section is based on a term of the longer of the term certain or the loan's expected term as determined under either paragraph (e)(5)(ii) or (iii) of this section, whichever is applicable.

(C) *Retirement and reissuance.* If a split-dollar loan described in paragraph (e)(5)(v)(A) of this section remains outstanding longer than the term certain, the split-dollar loan is treated for purposes of this section as retired and reissued at the end of the term certain for an amount of cash equal to the loan's adjusted issue price on that date. The reissued loan is subject to paragraph (e)(5)(ii) or (iii) of this section, whichever is applicable. However, the loan is not retested at that time to determine whether the loan provides for sufficient interest. For purposes of paragraph (e)(3)(iii) of this section, the appropriate AFR for the reissued loan is the AFR determined under paragraph (e)(5)(v)(B)(3) of this section on the day the loan was originally made.

(vi) *Example.* The provisions of this paragraph (e)(5) are illustrated by the following example:

Example. (i) On January 1, 2009, Corporation Y and Shareholder B, a 65 year-old male, enter into a split-dollar life insurance arrangement under which B is named as the policy owner. On January 1, 2009, Y makes a \$100,000 premium payment, repayable, without interest, from the death benefits of the underlying contract upon B's death. The premium payment is a split-dollar term loan. Repayment of the premium payment is fully recourse to B. Assume the long-term AFR (based on annual compounding) at the time of the loan is 7 percent. Both Y and B use the calendar year as their taxable years.

(ii) Based on Table 1 in § 1.72–9, the expected term of the loan is 15 years. Under paragraph (e)(5)(ii)(C) of this section, the long-term AFR (based on annual compounding) is the appropriate test rate. Based on a 15-year term and a discount rate of 7 percent, compounded annually (the long-term AFR), the present value of the payments under the loan is \$36,244.60, determined as follows: $\$100,000/[1+(0.07/1)]^{15}$. Under paragraph (e)(5)(ii)(B) of this section, this loan is a below-market split-dollar term loan because the imputed loan amount of \$36,244.60 (the present value of the amount required to be repaid to Y) is less than the amount loaned (\$100,000).

(iii) Under paragraph (e)(5)(ii)(B) of this section, the amount of forgone interest for 2009 (and each subsequent full calendar year that the loan remains outstanding) is \$7,000, which is the amount of interest that would have been payable on the loan for the calendar year if interest accrued on the loan's adjusted issue price (\$100,000) at the long-term AFR (7 percent, compounded annually). Under section 7872 and paragraph (e)(1)(i) of this section, on December 31, 2009, Y is treated as making a section 301 distribution to B of \$7,000. In addition, Y has \$7,000 of imputed interest income for 2009.

(f) *Treatment of stated interest and OID for split-dollar loans—(1) In general.* If a split-dollar loan provides for stated interest or OID, the loan is subject to this paragraph (f), regardless of whether the split-dollar loan has sufficient interest. Except as otherwise provided in this section, split-dollar loans are subject to the same Internal Revenue Code and regulatory provisions for stated interest and OID as other loans. For example, the lender of a split-dollar loan that provides for stated interest must account for any qualified stated interest (as defined in § 1.1273–1(c)) under its regular method of accounting (for example, an accrual method or the cash receipts and disbursements method). See § 1.446–2 to determine the amount of qualified stated interest that accrues during an accrual period. In addition, the lender must account under § 1.1272–1 for any OID on a split-dollar loan. However,