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IRS says split dollar loans should be reported on Form 990, Schedule L

Many exempt organizations are filing their Form 990 tax filings with the IRS this week. The deadline is May 15 for any organization with a fiscal year ending on December 31.

Under instructions for Schedule L (updated for this year), the IRS has clarified that any loans outstanding under a split dollar arrangement should be reported on Schedule L. This affects many credit unions and other exempt organizations with split dollar loans outstanding between the employer and its key executives.

Split dollar loans are used under “collateral assignment” split dollar arrangements. Under these arrangements, the employer loans money to key executives in order to fund a life insurance policy that is owned by the executive. However, certain value in the policy is assigned to the employer. Typically, the policy is intended to build up cash value in order to provide a retirement income stream to the executive. The employer often retains a right to recover its investment in the policy by receiving loan repayment upon the executive’s death.

For many types of tax-exempt organizations, split dollar arrangements can provide a tax-efficient mechanism to fund retirement benefits for valued executives. Other benefit programs, such as those used by for-profit organizations, can come with a heavy tax cost when used by tax exempt organizations due to the special tax rules that can apply to deferred compensation payments made by a tax-exempt employer.

Exempt organizations with collateral assignment split dollar loan arrangements should be sure to have their preparers include the applicable Schedule L disclosures. If a tax exempt organization has already filed Form 990 but has omitted Schedule L disclosures for a split dollar loan, an amended return should be considered. Those exempt organizations with later or extended filing deadlines should ensure that their Form 990 preparers are aware of any outstanding split dollar loans so that the loans can be reported appropriately on Schedule L of the Form 990.

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This is a general client alert and is not legal or financial advice.

The information contained herein is based on a summary of legal principles. It is not to be construed as legal advice. Individuals should consult with legal counsel before taking any action based on these principles to ensure their applicability in a given situation.

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