

Modified Endowment Contract Summary



This summary is intended for use with policies issued by Sun Life Assurance Company of Canada or Sun Life Assurance Company of Canada (U.S.), both members of the Sun Life Financial group of companies.

The Technical and Miscellaneous Revenue Act of 1988 and Life Insurance

This is meant to be a summary of the major life insurance provisions of the Technical and Miscellaneous Revenue Act of 1988 (TAMRA) only. Please consult your tax advisor for specific details.

Tax Advantages of Life Insurance

Life insurance enjoys a number of favorable income tax advantages. Among them are:

- Income Tax free proceeds payable at death.
- Tax deferred internal build-up of account values.
- Ability to recover all premiums paid before tax is due on interest gains.

Technical and Miscellaneous Revenue Act

In an effort to limit the potential abuse of using life insurance as a tax free income device, TAMRA created a new class of insurance called "modified endowment contracts." If a contract is classified as a modified endowment, the tax free proceeds and the tax deferred internal build up advantages are retained. However, any distribution such as contract loans, surrenders, partial surrenders, and collateral assignments are subject to taxes and penalties similar to annuities.

How Does a Policy Become a Modified Endowment Contract?

A modified endowment contract is a life insurance contract which is either funded more rapidly during the first seven years than would be required by paying the level annual premiums set by Section 7702A of the Internal Revenue Code or undergoes a "material change." A material change includes an increase in the contract's face amount and exchanges to a new contract. The premium limit varies by face amount, sex, coverages provided and risk class of the insured.

What If I Have a Modified Endowment?

Most of the tax advantages of life insurance remain unchanged. However, in the event of a distribution from a contract in the form of a contract loan, surrender, partial surrender, or collateral assignment, any amount considered "gain" is subject to current income tax (similar to interest gains on annuities). Also, a 10% penalty tax is imposed if the distribution is taken before the policyowner's age 59½ except in the case of disability or death.

When Did These Limits Go Into Effect?

Contracts issued after June 20, 1988, are subject to TAMRA's rules. Contracts issued before June 21, 1988, are not subject to these rules unless they are "materially changed." Many people's life insurance plans are not affected. Only those contracts that are classified as a modified endowment are subject to these rules. Also, only when distributions are taken or the contract is assigned are the tax penalties applicable.