Jeffrey T. Webber v. Commissioner of Internal Revenue, 144 T. C. 324 (2015)

In *Webber v. Comm'r*, the U. S. Tax Court held that Jeffrey T. Webber was taxable on the income from assets in a separate account of his variable life insurance policies due to his substantial control over the investments. The court applied the "investor control" doctrine, affirming the IRS's longstanding position that policyholders who direct investments in separate accounts are treated as owners of those assets for tax purposes. This ruling underscores the limits of tax-favored treatment for insurance products when policyholders exert control over underlying investments.

Parties

Jeffrey T. Webber was the Petitioner, with the Commissioner of Internal Revenue as the Respondent. Webber was the taxpayer and plaintiff at the trial level and the appellant in this case before the U. S. Tax Court.

Facts

Jeffrey T. Webber, a venture-capital investor and private-equity fund manager, established a grantor trust that purchased two variable life insurance policies from Lighthouse Capital Insurance Co. , a Cayman Islands company. The policies insured the lives of two of Webber's relatives, with Webber and his family members as beneficiaries. The premiums paid for the policies were placed in separate accounts managed by Butterfield Private Bank and Experta Trust Co. , both based in the Bahamas. These accounts invested in startup companies in which Webber had personal financial interests, including serving on their boards and investing through personal accounts or funds he managed. Despite the policies stipulating that the investment manager had sole discretion over investment choices, Webber effectively controlled the investments through intermediaries, dictating which securities the accounts would buy, sell, and hold.

Procedural History

Following an IRS examination, the Commissioner determined that Webber retained sufficient control over the separate account assets to be treated as their owner for federal income tax purposes under the investor control doctrine. The IRS issued a notice of deficiency to Webber for tax years 2006 and 2007, asserting deficiencies of $507,230 and $148,588, respectively, along with accuracy-related penalties. Webber timely petitioned the U. S. Tax Court for review. The court, after considering the facts and arguments, held that Webber was taxable on the income from the separate account assets but was not liable for the penalties due to his good faith reliance on professional tax advice.

Issue(s)

Whether a policyholder who retains significant control over the investments in the

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separate accounts of a variable life insurance policy should be treated as the owner of those assets for federal income tax purposes?

Rule(s) of Law

The controlling legal principle is the "investor control" doctrine, which the IRS has enunciated in a series of revenue rulings starting with Revenue Ruling 77-85. This doctrine holds that if a policyholder has sufficient incidents of ownership over the assets in a separate account, the policyholder, rather than the insurance company, is considered the owner of those assets for federal income tax purposes. Key legal tests include the policyholder's power to direct investments, vote shares, extract cash, and derive other benefits from the assets.

Holding

The U. S. Tax Court held that Webber, by actively managing the investments in the separate accounts and directing the purchase, sale, and exchange of securities, retained significant incidents of ownership over those assets. Consequently, Webber was taxable on the income realized by the separate accounts during the tax years in issue, consistent with the investor control doctrine.

Reasoning

The court's reasoning was based on a comprehensive analysis of the facts and the application of the investor control doctrine. The court found that Webber's control over the separate account investments was substantial, including directing which securities were bought and sold, voting shares, and extracting cash from the accounts. The court cited Supreme Court precedents like *Corliss v. Bowers* and *Helvering v. Clifford*, which emphasize that tax liability attaches to ownership and control over assets rather than formal title. The court also gave deference to the IRS's revenue rulings, which consistently applied the investor control doctrine over decades. The court rejected Webber's arguments that the doctrine should not apply to life insurance or that statutory provisions like sections 7702 and 817(h) of the Internal Revenue Code precluded its application. The court concluded that Webber's control over the investments made him the owner of the separate account assets for tax purposes.

Disposition

The court's final action was to enter a decision under Rule 155, sustaining the tax deficiencies determined by the IRS but relieving Webber of the accuracy-related penalties based on his good faith reliance on professional tax advice.

Significance/Impact

This case is significant for its reaffirmation of the investor control doctrine and its application to variable life insurance policies. It highlights the importance of the

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policyholder’s level of control over investments in separate accounts and the potential tax consequences of such control. The ruling may impact how life insurance products are structured and marketed, emphasizing the need for clear separation of investment control between policyholders and insurance companies to maintain tax-favored treatment. The decision also underscores the IRS’s consistent position on this issue over nearly four decades, reinforcing the stability and predictability of tax law in this area.

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