

§ 1.809-10

26 CFR Ch. I (4-1-04 Edition)

(i) The life insurance company's average equity base for the taxable year; multiplied by

(ii) The recomputed differential earnings rate for that taxable year.

(2) *Recomputed differential earnings rate.* The recomputed differential earnings rate for any taxable year equals the excess of—

(i) The imputed earnings rate for the taxable year; over

(ii) The average mutual earning rate for the calendar year in which the taxable year begins.

(c) *Effective date.* The regulations are effective for all taxable years beginning after December 31, 1986.

[T.D. 8499, 58 FR 64899, Dec. 10, 1993]

§ 1.809-10 Computation of equity base.

(a) *In general.* For purposes of section 809, the equity base of a life insurance company includes the amount of any asset valuation reserve and the amount of any interest maintenance reserve.

(b) *Effective date.* This section is effective for taxable years ending after December 31, 1991.

[T.D. 8484, 58 FR 47061, Sept. 7, 1993, as amended by T.D. 8564, 59 FR 49579, Sept. 29, 1994]

§ 1.810-1 Taxable years affected.

Sections 1.810-2 through 1.810-4 are applicable only to taxable years beginning after December 31, 1957, and all references to sections of part I, subchapter L, chapter 1 of the Code are to the Internal Revenue Code of 1954, as amended by the Life Insurance Company Income Tax Act of 1959 (73 Stat. 112).

[T.D. 6535, 26 FR 531, Jan. 20, 1961]

§ 1.810-2 Rules for certain reserves.

(a) *Adjustment for decrease or increase in certain reserve items—*(1) *Adjustment for decrease.* Section 810(a) provides that if the sum of the items described in section 810(c) and paragraph (b) of this section at the beginning of the taxable year exceeds the sum of such items at the end of the taxable year (reduced by the amount of investment yield not included in gain or loss from operations for the taxable year by reason of section 809(a)(1)), the amount of such excess shall be taken into account

as a net decrease referred to in section 809(c)(2) and paragraph (a)(2) of § 1.809-4 in determining gain or loss from operations.

(2) *Adjustment for increase.* Section 810(b) provides that if the sum of the items described in section 810(c) and paragraph (b) of this section at the end of the taxable year (reduced by the amount of investment yield not included in gain or loss from operations for the taxable year by reason of section 809(a)(1)) exceeds the sum of such items at the beginning of the taxable year, the amount of such excess shall be taken into account as a net increase referred to in section 809(d)(2) and paragraph (a)(2) of § 1.809-5 in determining gain or loss from operations.

(b) *Items taken into account.* The items described in section 810(c) and referred to in section 810 (a) and (b) and paragraph (a) of this section are:

(1) The life insurance reserves (as defined in section 801(b) and § 1.801-4);

(2) The unearned premiums and unpaid losses included in total reserves under section 801(c)(2) and § 1.801-5;

(3) The amounts (discounted at the rates of interest assumed by the company) necessary to satisfy the obligations under insurance or annuity contracts (including contracts supplementary thereto), but only if such obligations do not involve (at the time with respect to which the computation is made under this subparagraph) life, health, or accident contingencies;

(4) Dividend accumulations, and other amounts, held at interest in connection with insurance or annuity contracts (including contracts supplementary thereto); and

(5) Premiums received in advance, and liabilities for premium deposit funds.

(6) Special contingency reserves under contracts of group term life insurance or group health and accident insurance which are established and maintained for the provision of insurance on retired lives, for premium stabilization, or for a combination thereof.

For purposes of this paragraph, the same item shall be counted only once and deficiency reserves (as defined in section 801(b)(4) and paragraph (e)(4) of

§1.801-4) shall not be taken into account.

(c) *Special rules.* For purposes of section 810 (a) and (b) and paragraph (a) of this section, in determining whether there is a net increase or decrease in the sum of the items described in section 810(c) and paragraph (b) of this section for the taxable year, the following rules shall apply:

(1) *Computation of net increase or decrease in reserves.* The sum of the items described in section 810(c) and paragraph (b) of this section at the beginning of the taxable year shall be the aggregate of the sums of each of such items at the beginning of the taxable year. The sum of the items described in section 810(c) and paragraph (b) of this section at the end of the taxable year shall be the aggregate of the sums of each of such items at the end of the taxable year. However, in order to determine whether there is a net increase or decrease in such items for the taxable year, the aggregate of the sums of the items at the end of the taxable year must first be reduced by the amount of investment yield not included in gain or loss from operations for the taxable year by reason of section 809(a)(1).

(2) *Effect of change in basis in computing reserves.* Any increase or decrease in the sum of the items described in section 810(c) and paragraph (b) of this section for the taxable year which is attributable to a change in the basis used in computing such items during the taxable year shall not be taken into account under section 810 (a) or (b) and paragraph (a) of this section but shall be taken into account in the manner prescribed in section 810(d) and paragraph (a) of § 1.810-3.

(3) *Effect of section 818(c) election.* If a company which computes its life insurance reserves on a preliminary term basis elects to revalue such reserves on a net level premium basis under section 818(c), the sum of such reserves at the beginning and end of all taxable years (including the first taxable year) for which the election applies shall be the sum of such reserves computed on such net level premium basis.

(4) *Cross references.* For taxable years beginning before January 1, 1970, see section 810(e) (as in effect for such

years) and § 1.810-4 for special rules for determining the net increase or decrease in the sum of the items described in section 810(c) and paragraph (b) of this section in the case of certain voluntary employees' beneficiary associations. For similar special rules in the case of life insurance companies issuing variable annuity contracts, see section 801(g)(4) and the regulations thereunder.

(d) *Illustration of principles.* The provisions of section 810 (a) and (b) and this section may be illustrated by the following examples:

Example 1. Assume the following facts with respect to R, a life insurance company:

Sum of items described in section 810(c) (1) through (6) at beginning of taxable year	\$940
Sum of items described in section 810(c) (1) through (6) at end of taxable year	1,060
Required interest (as defined in section 809(a)(2))	70
Investment yield (as defined in section 804(c)) ..	100
Amount of investment yield not included in gain or loss from operations for the taxable year by reason of section 809(a)(1)	70

In order to determine the adjustment for decrease or increase in the sum of the items described in section 810(c) for the taxable year, R must first reduce the sum of such items at the end of the taxable year (\$1,060) by the amount of investment yield (\$70) not included in gain or loss from operations for the taxable year by reason of section 809(a)(1). Since the adjusted sum of such items at the end of the taxable year, \$990 (\$1,060 minus \$70), exceeds the sum of such items at the beginning of the taxable year, \$940, the excess of \$50 (\$990 minus \$940) shall be taken into account as a net increase under section 809(d)(2) and paragraph (a)(2) of § 1.809-5 in determining gain or loss from operations.

Example 2. Assume the facts are the same as in example 1, except that the sum of the items described in section 810(c) at the beginning of the taxable year is \$1000. Since the sum of the items described in section 810(c) at the beginning of taxable year, \$1000, exceeds the sum of such items at the end of the taxable year after adjustment for the amount of investment yield not included in gain or loss from operations for the taxable year by reason of section 809(a)(1), \$990 (\$1060 minus \$70), the excess of \$10 (\$1000 minus \$990) shall be taken into account as a net decrease under section 809 (c)(2) and paragraph (a)(2) of § 1.809-4 in determining gain or loss from operations.

Example 3. Assume the following facts with respect to S, a life insurance company:

Sum of items described in section 810(c) (1) through (6) at beginning of taxable year	\$1,970
Sum of items described in section 810(c) (1) through (6) at the end of taxable year	2,040

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Required interest (as defined in section 809(a)(2))	60
Investment yield (as defined in section 804(c)) ..	40
Amount of investment yield not included in gain or loss from operations by reason of section 809(a)(1)	40

Under the provisions of section 809(a)(1), since the required interest (\$60) exceeds the investment yield (\$40), the share of each and every item of investment yield set aside for policyholders and not included in gain or loss from operations for the taxable year shall be 100 percent. Thus, applying the provisions of section 810 (a) and (b), the sum of the items described in section 810(c) at the end of the taxable year (\$2,040) must first be reduced by the entire amount of the investment yield (\$40) in order to determine the net increase or decrease in the sum of such items for the taxable year. Since the adjusted sum of such items at the end of the taxable year, \$2,000 (\$2,040 minus \$40), is greater than the sum of such items at the beginning of the taxable year, \$1,970, the excess of \$30 (\$2,000 minus \$1,970) shall be taken into account as a net increase under section 809(d)(2) and paragraph (a)(2) of § 1.809-5 in determining gain or loss from operations. No additional deduction is allowed under section 809(d) for the amount (\$20) by which the required interest exceeds the investment yield for the taxable year.

Example 4. Assume the facts are the same as in example 1, except that as a result of a change in the basis used in computing an item described in section 810(c) during the taxable year, the sum of such items at the end of the taxable year is \$1,200. Under the provisions of paragraph (c)(2) of this section, any increase or decrease in the sum of the section 810(c) items for the taxable year which is attributable to a change in the basis used in computing such items during the taxable year shall not be taken into account under section 810 (a) and (b). Thus, for purposes of section 810 (a) and (b), the sum of the items described in section 810(c) at the end of the taxable year shall be \$1,060 (the amount computed without regard to the change in basis) and S shall treat the \$50 computed in the manner described in example 1 as a net increase under section 809(d)(2) and paragraph (a)(2) of § 1.809-5 in determining its gain or loss from operations for the taxable year. The amount of the increase in the section 810(c) items which is attributable to the change in basis during the taxable year, \$140 (\$1,200 minus \$1,060), shall be taken into account in the manner prescribed in section 810(d) and paragraph (a) of § 1.810-3.

Example 5. The life insurance reserves of M, a life insurance company, computed with respect to contracts for which such reserves are determined on a recognized preliminary term basis amount to \$100 on January 1, 1960, and \$110 on December 31, 1960. For the tax-

able year 1960, M elects to revalue such reserves on a net level premium basis under section 818(c). Such reserves computed under section 818(c) amount to \$115 on January 1, 1960, and \$127 on December 31, 1960. Under the provisions of paragraph (c)(3) of this section, a company which makes the section 818(c) election must use the net level premium basis in computing the sum of its life insurance reserves at the beginning and end of all taxable years for which the election applies. Thus, for purposes of section 810 (a) and (b), in determining whether there is a net increase or decrease in the sum of the section 810(c) items for the taxable year 1960, M shall include \$115 as its reserves with respect to such contracts under section 810(c)(1) at the beginning of the taxable year and \$127 as its reserves with respect to such contracts under section 810(c)(1) at the end of the taxable year.

[T.D. 6535, 26 FR 531, Jan. 20, 1961, as amended by T.D. 7163, 37 FR 4189, Feb. 29, 1972; T.D. 7172, 37 FR 5619, Mar. 17, 1972]

§ 1.810-3 Adjustment for change in computing reserves.

(a) *Reserve strengthening or weakening.* Section 810(d)(1) provides that if the basis for determining any item referred to in section 810(c) and paragraph (b) of § 1.810-2 at the end of any taxable year differs from the basis for such determination at the end of the preceding taxable year, then so much of the difference between:

- (1) The amount of the item at the end of the taxable year, computed on the new basis, and
- (2) The amount of the item at the end of the taxable year, computed on the old basis,

as is attributable to contracts issued before the taxable year shall be taken into account as follows:

- (i) If the amount of the item at the end of the taxable year computed on the new basis exceeds the amount of the item at the end of the taxable year computed on the old basis, 1/10 of such excess shall be taken into account, for each of the succeeding 10 taxable years as a net increase to which section 809(d)(2) and paragraph (a)(2) of § 1.809-5 applies; or
- (ii) If the amount of the item at the end of the taxable year computed on the old basis exceeds the amount of the item at the end of the taxable year computed on the new basis, 1/10 of such excess shall be taken into account, for