

§ 1.810-3

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

each of the 10 succeeding taxable years, as a net decrease to which section 809(c)(2) and paragraph (a)(2) of § 1.809-4 applies.

(b) *Illustration of principles.* The provisions of section 810(d)(1) and paragraph (a) of this section may be illustrated by the following examples:

Example 1. Assume that the amount of an item described in section 810(c) of L, a life insurance company, at the beginning of the taxable year 1959 is \$100. Assume that at the end of the taxable year 1959, as a result of a change in the basis used in computing such item during the taxable year, the amount of the item (computed on the new basis) is \$200 but computed on the old basis would have been \$150. Since the amount of the item at the end of the taxable year computed on the new basis, \$200, exceeds the amount of the item at the end of the taxable year computed on the old basis, \$150, by \$50, 1/10 of the amount of such excess, or \$5, 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 for each of the 10 taxable years immediately following the taxable year 1959. Any increase (or decrease) in the sum of the section 810(c) items computed on the old basis at the end of the taxable year 1959 (\$150) after adjustment for investment yield not included in gain or loss from operations for the taxable year by reason of section 809(a)(1), over the sum of such items computed on the old basis at the beginning of the taxable year 1959 (\$100), shall be taken into account in the manner prescribed in section 810 (a) or (b) and § 1.810-2 for purposes of determining L's gain or loss from operations for 1959.

Example 2. Assume the facts are the same as in example 1, and that the sum of the items described in section 810(c) (computed on the new basis) is \$200 on January 1, 1960, and \$260 on December 31, 1960. Under the provisions of section 810(d)(1), as a result of the reserve strengthening attributable to the change in basis which occurred in 1959, L would include \$5 (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 1960. In addition to this amount, any increase (or decrease) in the sum of the items described in section 810(c) at the end of the taxable year 1960 (\$260) after adjustment for investment yield not included in gain or loss from operations for the taxable year by reason of section 809(a)(1), over the sum of such items at the beginning of the taxable year 1960 (\$200), shall be taken into account in the manner prescribed in section 810 (a) or (b) and § 1.810-2 for purposes of

determining L's gain or loss from operations for 1960.

(c) *Termination as life insurance company.* Section 810(d)(2) provides, subject to the provisions of section 381(c)(22) and the regulations thereunder (relating to carryovers in certain corporate readjustments), that if for any taxable year a company which previously was a life insurance company no longer meets the requirements of section 801(a) and paragraph (b) of § 1.801-3 (relating to the definition of a life insurance company), the balance of any adjustments remaining to be made under section 810(d)(1) and paragraph (a) of this section shall be taken into account for the preceding taxable year.

(d) *Illustration of principles.* The provisions of section 810(d)(2) and paragraph (c) of this section may be illustrated by the following example:

Example. Assume the facts are the same as in example 1 of paragraph (b) of this section, except that for the taxable year 1962, L no longer meets the requirements of section 801(a) (relating to the definition of a life insurance company) and that the provisions of section 381(c)(22) are not applicable. Under the provisions of section 810 (d)(2), the entire balance of the adjustment remaining to be made with respect to the change in basis which occurred in 1959, 8/10 of \$50, or \$40, shall be taken into account for the taxable year 1961, the last year L was a life insurance company. Thus, for the taxable year 1961, the total amount to be taken into account by L as a net increase referred to in section 809(d)(2) and paragraph (a)(2) of § 1.809-5 in determining its gain or loss from operations shall be \$45. Of this amount, \$5 (1/10 of \$50) represents the amount determined under the provisions of section 810(d)(1), and \$40 represents the amount determined under the provisions of section 810(d)(2).

(e) *Effect of preliminary term election.* (1) Section 810(d)(3) provides that 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), such election shall not be treated as a change in basis within the meaning of section 810(d)(1) and paragraph (a) of this section. Thus, any increase or decrease in reserves attributable to such election shall not be taken into account under section 810(d)(1) and paragraph (a) of this section but shall be taken into account in the manner prescribed in section 810 (a)

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and (b) and paragraph (a) of § 1.810-2. See paragraph (c)(3) of § 1.810-2.

(2) Section 810(d)(3) further provides that where an election under section 818(c) would apply to an item referred to in section 810(c) but for the fact that the basis used in computing such item has actually been changed, any increase or decrease in such item attributable to such actual change in basis shall be subject to the adjustment required under section 810(d)(1) and paragraph (a) of this section. In such a case, however, for purposes of section 810(d)(1)(B) and paragraph (a)(2) of this section, the amount of such item at the end of the taxable year computed on the old basis shall be the amount of such item at the end of the taxable year computed as if the election under section 818(c) applied in respect of such item for the taxable year.

(f) *Illustration of principles.* The provisions of section 810(d)(3) and paragraph (e) of this section may be illustrated by the following examples:

Example 1. Assume that S, a life insurance company which computes its life insurance reserves on a 3-percent assumed rate and the Commissioner's reserve valuation method (one of the recognized preliminary term reserve methods), elects to revalue such reserves on a net level premium method under section 818(c) and that the significant facts are as follows:

	Jan. 1, 1958	Dec. 31, 1958
Book reserves at 3-percent assumed rate, Commissioner's reserve valuation method	100	118
Reserves at 3-percent assumed rate, after restatement under section 818(c)	110	131

Under the provisions of section 810(d)(3), an election under section 818(c) is not treated as a change in basis for purposes of section 810(d)(1). Accordingly, the increase of \$21 (\$131 minus \$110) attributable to such election shall not be subject to the adjustment provided by section 810(d)(1) but shall be taken into account in the manner prescribed in section 810(b). For purposes of determining the amount to be taken into account under section 810(b), the reserves with respect to the contracts subject to the section 818(c) election shall be \$110 at the beginning of the taxable year 1958 and \$131 at the end of the taxable year 1958. However, as a result of making the election under section 818(c), the difference (\$10) between the reserves computed on the preliminary term basis on

January 1, 1958 (\$100) and the reserves restated on the net level premium basis on January 1, 1958 (\$110) shall not be taken into account under section 809(d) for the year 1958, or for any subsequent taxable year.

Example 2. Assume the facts are the same as in example 1, except that during the taxable year 1959, S actually changed from the preliminary term basis to a net level premium basis which was identical with the net level premium basis used under the section 818(c) election and that the significant facts are as follows:

	Jan. 1, 1959	Dec. 31, 1959
Book reserves at 3-percent assumed rate, Commissioner's reserve valuation method	118	127
Reserves at 3-percent assumed rate, after restatement under section 818(c)	131	142
Strengthened reserves at 3-percent assumed rate and net level premium method		142

Under the provisions of section 810(d)(3), if a company which has made an election under section 818(c) which has not been revoked actually changes the basis used by it in computing the reserves subject to such election, any increase or decrease in reserves attributable to such change in basis shall be taken into account in the manner prescribed in section 810(d)(1). Since S actually changed to the same basis which it used in computing its reserves under section 818(c), the reserves at the end of the taxable year computed on the new basis (\$142) are the same as the reserves at the end of the taxable year computed on the old basis (\$142), i.e., the basis which would have applied under section 818(c) if the election applied for 1959. Accordingly, no adjustment under section 810(d)(1) is required.

Example 3. Assume the facts are the same as in example 1, except that during the taxable year 1960, S actually changed the basis used by it in computing its reserves on a certain block of contracts subject to the election under section 818(c) and that the significant facts with respect to this block of contracts are as follows:

	Jan. 1, 1960	Dec. 31, 1960
Book reserves at 3-percent assumed rate, Commissioner's reserve valuation method	50	63
Reserves at 3-percent assumed rate, after restatement under section 818(c)	60	75
Strengthened reserves at 2-percent assumed rate and net level premium method		95

Under the provisions of section 810(d)(3), the amount of the reserves subject to the section

818(c) election at the end of the taxable year computed on the old basis shall be the amount of such reserves at the end of the taxable year determined under section 818(c) (\$75). Since the reserves at the end of the taxable year computed on the new basis, \$95, exceed the reserves at the end of the taxable year computed on the old basis, \$75, by \$20, 1/10 of the excess of \$20, or \$2, 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 for each of the 10 taxable years immediately following the taxable year 1960. For purposes of determining whether there is a net increase or decrease in the sum of the items described in section 810(c) for the taxable year 1960 under section 810 (a) or (b), the sum of the reserves with respect to such block of contracts shall be \$60 at the beginning of the taxable year and \$75 at the end of the taxable year (the amount of such reserves computed under section 818(c) at the beginning and end of the taxable year). The difference (\$10) between the reserves computed on the preliminary term basis on January 1, 1960 (\$50) and the reserves restated on the net level premium basis on January 1, 1960 (\$60) shall not be taken into account under section 809(d) for the year 1960, or for any subsequent taxable year.

[T.D. 6535, 26 FR 532, Jan. 20, 1961]

§ 1.810-4 Certain decreases in reserves of voluntary employees' beneficiary associations.

(a) *Decreases due to voluntary lapses of policies issued before January 1, 1958.* (1) Section 810(e) provides that if for any taxable year a life insurance company which meets the requirements of section 501(c)(9), other than the requirement of subparagraph (B) thereof, makes an election in the manner provided in section 810(e)(3) and paragraph (b) of this section, only 11½ percent of any decrease in life insurance reserves (as defined in section 801(b) and § 1.801-4) attributable to the voluntary lapse on or after January 1, 1958, of any policy issued prior to that date shall be taken into account under section 810 (a) or (b) and paragraph (a) of § 1.810-2 in determining the net increase or decrease in the sum of the items described in section 810(c) during the taxable year. In applying the preceding sentence, the decrease in the reserve for any policy shall be determined by reference to the amount of such reserve at the beginning of the taxable year, reduced by any amount allowable as a

deduction under section 809(d)(1) and paragraph (a)(1) of § 1.809-5 in respect of such policy by reason of such lapse. The election under section 810(e) shall be adhered to in computing the company's gain or loss from operation for the taxable year for which the election is made and for all subsequent taxable years, unless consent to revoke such election is obtained from the Commissioner.

(2) The application of the election provided under section 810(e) and subparagraph (1) of this paragraph may be illustrated by the following example:

Example. For the taxable year 1960, M, a life insurance company which meets the requirements of section 501(c)(9), other than the requirement of subparagraph (B) thereof, makes the election under section 810(e). Assume the following facts with respect to a policy issued in 1955 which voluntarily lapsed during the taxable year:

(1) Life insurance reserve on January 1, 1960	\$600
(2) Amount allowable as a deduction under sec. 809(d)(1)	200
(3) Decrease in life insurance reserves for sec. 810(e) purposes (item (1) minus item (2))	400
(4) Amount taken into account under sec. 810 (a) and (b) by reason of sec. 810(e) election (11 1/2%×\$400)	46

Under the provisions of section 810(e) and subparagraph (1) of this paragraph, M would include \$46 as its life insurance reserve with respect to such policy under section 810(c)(1) at the beginning of the taxable year 1960 for purposes of determining the net increase or decrease in the sum of the items described in section 810(c) for the taxable year under section 810 (a) or (b).

(b) *Time and manner of making election.* The election provided by section 810(e)(3) shall be made in a statement attached to the life insurance company's income tax return for the first taxable year for which the company desires the election to apply. The return and statement must be filed not later than the date prescribed by law (including extensions thereof) for filing the return for such taxable year. However, if the last day prescribed by law (including extensions thereof) for filing a return for the first taxable year for which the company desires the election to apply falls before January 20, 1961, the election provided by section 810(e)(3) may be made for such year by filing the statement and an amended return for such taxable year (and all