

(d) *Years of applicability.* Section 821(f)(4) provides that the special reduction of statutory underwriting income allowed by section 821(f)(2) and paragraph (b) of this section shall apply to any taxable year beginning after December 31, 1962, and before January 1, 1968, for which the taxpayer is subject to the tax imposed by section 821(a).

[T.D. 6681, 28 FR 11112, Oct. 17, 1963]

§ 1.822-1 Taxable income and deductions.

(a) *In general.* For taxable years beginning after December 31, 1953, but before January 1, 1955, and ending after August 16, 1954, the taxable income of a mutual insurance company subject to the tax imposed by section 821 is its gross investment income, namely, the gross amount of income during the taxable year from interest, dividends, rents, and gains from sales or exchanges of capital assets, less the deductions provided in section 822(c) for wholly tax-exempt interest, investment expenses, real estate expenses, depreciation, interest paid or accrued, capital losses to the extent provided in subchapter P (sec. 1201 and following), chapter 1 of the Code, and the special deductions provided in part VIII (section 241 and following), except section 248, subchapter B, chapter 1 of the Code. In addition to the limitations on deductions relating to real estate owned and occupied by a mutual insurance company subject to the tax imposed by section 821 provided in section 822(d)(1), the adjustment for amortization of premium and accrual of discount provided in section 822(d)(2), and the limitation on the deduction for investment expenses where general expenses are allocated to investment income provided in section 822(c)(2), mutual insurance companies subject to the tax imposed by section 821 are subject to the limitation on deductions relating to wholly tax-exempt income provided in section 265. Such companies are not entitled to the net operating loss deduction provided in section 172.

(b) *Wholly tax-exempt interest.* Interest which in the case of other taxpayers is excluded from gross income by section 103 but included in the gross invest-

ment income by section 822(b) is allowed as a deduction from gross investment income by section 822(c)(1).

(c) *Investment expenses.* The deduction allowed by section 822(c)(2) for investment expenses is the same as that allowed life insurance companies by section 803(g)(2). See paragraph (c) of § 1.803-4.

(d) *Taxes and expenses with respect to real estate.* The deduction allowed by section 822(c)(3) for taxes and expenses with respect to real estate owned by the company is the same as that allowed life insurance companies by section 803(g)(3). See paragraph (d) of § 1.803-4.

(e) *Depreciation.* The deduction allowed by section 822(c)(4) for depreciation is the same as that allowed life insurance companies by section 803(g)(4). See paragraph (e) of § 1.803-4.

(f) *Interest paid or accrued.* The deduction allowed by section 822(c)(5) for interest on indebtedness is the same as that allowed other corporations by section 163. See § 1.163-1.

(g) *Capital losses.* (1) The deduction for capital losses under section 822(c)(6) includes not only capital losses to the extent provided in subchapter P but in addition thereto losses from capital assets sold or exchanged to provide funds to meet abnormal insurance losses and to provide for the payment of dividends and similar distributions to policyholders. Losses in the latter case may be deducted from ordinary income while the deduction for losses under subchapter P is limited to the gains. See section 1211.

(2) Capital assets are considered as sold or exchanged to provide for the funds or payments specified in section 822(c)(6), to the extent that the gross receipts from the sale or exchange of such assets are not greater than the excess, if any, for the taxable year of the sum of dividends and similar distributions paid to policyholders, and losses and expenses paid over the sum of interest, dividends, rents, and net premiums received. If, by reason of a particular sale or exchange of a capital asset, gross receipts are greater than such excess, the gross receipts and the resulting loss should be apportioned and the excess included in capital

losses subject to the provisions of subchapter P. Capital losses actually used to reduce net income in any taxable year may not again be used in a succeeding taxable year as an offset against capital gains in that year and for that purpose a special rule is set forth for the application of section 1212.

(3) The application of section 822(c)(6) may be illustrated by the following examples:

Example 1. The X Company, a mutual fire insurance company subject to the tax imposed by section 821, in the taxable year 1954 sells capital assets in order to obtain funds to meet abnormal insurance losses and to provide for the payment of dividends and similar distributions to policyholders. The gross receipts from the sale are \$60,000, resulting in losses of \$20,000. It pays dividends to policyholders of \$150,000. It sustains losses of \$25,000, and pays expenses of \$25,000. It receives interest of \$50,000, dividends of \$5,000, rents of \$4,000, and net premiums of \$66,000. The excess of the sum of dividends, losses, and expenses paid (\$200,000) over the sum of interest, dividends, rents, and net premiums received (\$125,000) is \$75,000. As the gross receipts from the sale of capital assets (\$60,000) do not exceed such excess (\$75,000), the losses of \$20,000 are allowable as a deduction from gross investment income.

Example 2. If in example 1 the gross receipts were \$76,000 and the last capital asset sold, for the purpose therein specified, resulted in gross receipts of \$2,000 and a loss of \$500, the losses allowable as a deduction from gross investment income would be \$19,750. The last sale made the gross receipts of \$76,000 exceed by \$1,000 the excess (\$75,000) of the sum of dividends, losses, and expenses paid (\$200,000) over the sum of interest, dividends, rents, and net premiums received (\$125,000). The gross receipts and the resulting loss from the last sale are apportioned on the basis of the ratio of the excess of \$1,000 to the gross receipts of \$2,000, or 50 percent. Fifty percent of the loss of \$500 is deducted from the total loss of \$20,000. The remaining gross receipts of \$1,000 and the proportionate loss of \$250 should be reported as capital losses under subchapter P.

Example 3. If in example 1 the X Company had mutual insurance company taxable income for purposes of the surtax of \$9,750 and, under the provisions of subchapter P, had capital losses of \$18,000 and capital gains of \$10,000, the net capital loss for the taxable year 1954, in applying section 1212 for the purposes of section 822(c)(6), would be \$8,000. This is determined by subtracting from total losses of \$38,000 (\$18,000 capital losses under subchapter P plus \$20,000 other capital losses under section 822(c)(6)) the sum of capital

gains of \$10,000 and losses from the sale or exchange of capital assets sold or exchanged to obtain funds to meet abnormal insurance losses and to provide for the payment of dividends and similar distributions to policyholders of \$20,000. Such losses of \$20,000 are added to capital gains of \$10,000, since they are less than taxable income for purposes of the surtax, computed without regard to gains or losses from sales or exchanges of capital assets, of \$29,750 (\$9,750 taxable income for purposes of the surtax plus \$20,000 other capital losses under section 822(c)(6) plus the portion of capital losses allowable under subchapter P of \$10,000 minus capital gains under subchapter P of \$10,000).

(h) *Special deductions.* Section 822(c)(7) allows a mutual insurance company the special deductions provided by part VIII (section 241 and following), except section 248, subchapter B, chapter 1 of the Code, relating to partially tax-exempt interest and to dividends received.

§ 1.822-2 Real estate owned and occupied.

The limitation in section 822(d)(1) on the amount allowable as a deduction for taxes, expenses, and depreciation upon or with respect to any real estate owned and occupied in whole or in part by a mutual insurance company subject to the tax imposed by section 821 is the same as that provided in the case of life insurance companies by section 803(h). See § 1.803-5.

§ 1.822-3 Amortization of premium and accrual of discount.

Section 822(d)(2) makes provision for the appropriate amortization of premium and the appropriate accrual of discount, attributable to the taxable year, on bonds, notes, debentures or other evidences of indebtedness held by a mutual insurance company subject to the tax imposed by section 821. Such amortization and accrual is the same as that provided for life insurance companies by section 803(i) and shall be determined in accordance with § 1.803-6, except that in determining the premium and discount of a mutual insurance company subject to the tax imposed by section 821 the basis provided in section 1012 shall be used in lieu of the acquisition value.