

Part I

Section 807.—Rules for certain reserves

Rev. Rul. 2008-37

ISSUE(S)

What is the amount of a life insurance company's statutory reserves within the meaning of § 807(d)(6) if the company does business in several States with different minimum reserve requirements?

FACTS

Situation 1

IC is a life insurance company as defined in § 816(a) of the Internal Revenue Code, and is the issuer of Contract A, which is a "life insurance contract" as defined in § 7702.

IC does business in forty-five States. IC is subject to regulation under the insurance laws of each State in which it does business. Each State has express statutory provisions, or rules and regulations promulgated in the exercise of a power conferred by statute, for determining the minimum amount of the reserves that IC is

required to set aside to mature or liquidate policyholder or beneficiary claims arising from its insurance and annuity contracts.

To avoid State-by-State variations, IC actually holds and reports to each State insurance regulatory authority on its annual statement approved by the National Association of Insurance Commissioners (NAIC) the highest aggregate minimum amount of reserves required for its insurance and annuity contracts under the statutes, regulations, or rules of any State in which IC transacts business. The State insurance regulatory authorities in each State accept the amount of reserves reported on the annual statement as the amount IC has set aside to mature or liquidate policyholder or beneficiary claims arising from its insurance and annuity contracts.

On its 2007 annual statement, IC reported end-of-year aggregate reserves of \$405,955,000 with regard to items described in § 807(c). The \$405,955,000 aggregate reserves included \$9,992 of life insurance reserves with respect to Contract A.

Had IC reported on its 2007 annual statement the minimum aggregate reserves required under the statutes, regulations or rules of either the State in which IC was chartered, or the State in which Contract A was issued or delivered, IC would have reported only \$402,540,000 of end-of-year aggregate reserves with regard to the items described in § 807(c). The \$402,540,000 aggregate reserves would have included \$9,942 of life insurance reserves with respect to Contract A. The \$402,540,000 aggregate reserve amount would not have satisfied the minimum legal reserve requirements of one or more States in which IC does business.

Situation 2

The facts are the same as in Situation 1, except that on its annual statement IC reported to each State insurance regulatory authority the minimum amount of reserves required for its insurance and annuity contracts under the statutes, regulations, or rules of that particular State. As in Situation 1, however, IC actually holds the highest aggregate minimum amount of reserve required for its insurance contracts under the rules of any State in which IC does business.

On its 2007 annual statement filed with and accepted by the insurance regulatory authorities in State X, which is the State in which IC is chartered, IC reported \$402,540,000 of end-of-year aggregate reserves with regard to items described in § 807(c). This amount (\$402,540,000) was the lowest amount of reserves reported by IC on the annual statement filed with and accepted by any State, and would not have satisfied the minimum legal reserve requirements of one or more States in which IC does business. The \$402,540,000 aggregate reserves included \$9,942 of life insurance reserves with respect to Contract A.

On its 2007 annual statement filed with and accepted by the insurance regulatory authorities in State Y, IC reported \$405,955,000 of end-of-year aggregate reserves with regard to items described in § 807(c). This amount (\$405,955,000) was the lowest amount of reserves that satisfied minimum requirements of State Y, which has the highest minimum reserve requirements of any of the States in which IC does business. The \$405,955,000 aggregate reserves included \$9,992 of life insurance reserves with respect to Contract A.

LAW AND ANALYSIS

In general, a life insurance company must pay tax on its life insurance company taxable income, which is defined in § 801(b) to mean life insurance gross income less life insurance deductions. Life insurance gross income is defined in § 803(a) to mean the sum of (i) premiums, (ii) net decreases in certain reserves under § 807(a), and (iii) other amounts generally included by a taxpayer in gross income. Section 805(a)(2) authorizes a deduction for the net increase in certain reserves under § 807(b).

For purposes of determining a life insurance company's income or deduction from decreases or increases in life insurance reserves, § 807(d)(1) provides that the amount of the life insurance reserves for any contract is the greater of-- (i) the contract's net surrender value, or (ii) the contract's tax reserve determined under § 807(d)(2). However, the life insurance reserves for a contract cannot exceed the amount that would be taken into account with respect to the contract in determining "statutory reserves", as defined in § 807(d)(6). Accordingly, the statutory reserves with respect to a contract operate as a limit on the amount of the contract's life insurance reserves that might otherwise be taken into account in determining a life insurance company's taxable income. Section 807(d)(1) (flush language).

Section 807(d)(6) defines "statutory reserves" to mean "the aggregate amount set forth in the annual statement with respect to items described in § 807(c)." See § 807(c)(1) (relating to "life insurance reserves" as defined in § 816(b)). Statutory reserves do not include any reserve attributable to deferred and uncollected premium if the establishment of such reserve is not permitted under § 811(c).

In Situation 1, IC held and reported \$405,955,000 of reserves with regard to items described in § 807(c) on its 2007 annual statement filed in each State in which IC does business. This amount was the highest aggregate minimum amount of reserves required under the statutes, regulations, or rules of any State in which IC does business. That the minimum requirements of some States in which IC does business would have permitted IC to hold and report a lower aggregate minimum amount of reserves has no effect on the determination of IC's statutory reserves under §807(d)(6). The \$405,955,000 of reserves was required to be held, was actually held, and was set forth in IC's annual statement, which was filed with and accepted by the insurance regulatory authority of each State in which IC does business. The amount of IC's "statutory reserves" as defined in § 807(d)(6), therefore, is \$405,955,000.

IC's \$405,955,000 of statutory reserves under § 807(d)(6) includes \$9,992 of life insurance reserves with respect to Contract A. Accordingly, \$9,992 is the amount taken into account with respect to Contract A in applying the statutory reserves limitation contained in § 807(d)(1).

In Situation 2, IC held and reported \$405,955,000 of reserves with regard to items described in § 807(c) on its 2007 annual statement filed with and accepted by the insurance regulatory authority in State Y. This amount was the minimum amount of reserves required under the statutes, regulations, or rules of State Y. That \$405,955,000 was larger than the amount of reserves that would have been required under the rules of State X has no effect on the determination of IC's statutory reserves under § 807(d)(6). The \$405,955,000 of reserves was required to be held, was actually

held, and was set forth in IC's annual statement, which was filed with and accepted by the insurance regulatory authority in State Y. The amount of IC's "statutory reserves" as defined in § 807(d)(6), therefore, is \$405,955,000. Cf. § 1.801-5(a) (permitting an insurance company to determine "total reserves" (as defined in § 816(c)) using the highest aggregate reserve required by any State or Territory or the District of Columbia in which the company transacts business, provided the company actually holds the reserve).

IC's \$405,955,000 of statutory reserves under § 807(d)(6) includes \$9,992 of life insurance reserves with respect to Contract A. Accordingly, \$9,992 is the amount taken into account with respect to Contract A in applying the statutory reserves limitation contained in § 807(d)(1).

HOLDING(S)

In both Situation 1 and Situation 2, the amount of IC's 2007 end-of-year statutory reserves under § 807(d)(6) is \$405,955,000 -- the highest aggregate reserve amount for § 807(c) items actually held and set forth on the annual statement pursuant to the minimum reserve requirements of any State in which IC does business.

IC's \$405,955,000 of statutory reserves under § 807(d)(6) includes \$9,992 of life insurance reserves with respect to Contract A. Accordingly, \$9,992 is the amount taken into account with respect to Contract A in applying the statutory reserves limitation contained in the flush language of § 807(d)(1).

DRAFTING INFORMATION

The principal authors of this revenue ruling are Linda Boyd and Stephen Hooe of the Office of Associate Chief Counsel (Financial Institutions & Products). For further information regarding this revenue ruling, contact Linda Boyd at (202) 622-3970 or Stephen Hooe at (202) 622-3900 (not a toll-free call).