INTERNAL REVENUE SERVICE
NATIONAL OFFICE TECHNICAL ADVICE MEMORANDUM
March 20, 2003

Number: **200328006**
Release Date: 7/11/2003
Index (UIL) No.: 807.00-00
CASE MIS No.: TAM-165476-02/CC:FI&P:B04

Team Manager
LMSB Financial Services
LMSB:CTM:1362

Taxpayer's Name:

Taxpayer's Address:

Taxpayer's Identification No:
Years Involved:
Date of Conference:

LEGEND:

Taxpayer =

Holding =

Parent =

Annuities =

X =

Year 1 =

Year 2 =

Year 3 =

Year 4 =

Plan Y =

Plan Z =

ISSUE:

May Actuarial Guideline 33 (AG33) be used in computing Taxpayer's CARVM tax reserves for annuity contracts that were issued before the date on which the guideline took effect, or the date of adoption by the National Association of Insurance Commissioners (NAIC), whichever is later, under section 807(d)(2) of the Internal Revenue Code.

CONCLUSION:

The issuance of AG 33 by the NAIC affects the computation of tax reserves under section 807(d)(2) of the Internal Revenue Code only for annuity contracts issued on or after the date on which AG 33 took effect or was adopted by the NAIC, whichever is later. Taxpayer's use of AG 33 in computing its tax reserves for Annuities issued before December 31, 1995, is impermissible under section 807(d)(2) of the Internal Revenue Code.

FACTS:

Taxpayer is a life insurance company within the meaning of section 816(a) of the Internal Revenue Code and is subject to the tax imposed by section 801. Taxpayer is the principal subsidiary of Holding, which in turn is a subsidiary of Parent. During the taxable years involved, Taxpayer joined with Parent and other eligible life insurance company members of Parent's consolidated group in filing a life/nonlife consolidated return pursuant to section 1504(c) and section 1.1502-76 of the Income Tax Regulations.

Taxpayer issues Annuities to X. The National Association of Insurance Commissioners (NAIC) adopted Actuarial Guideline, Determining Minimum Commissioners' Annuities Reserve Valuation Method (CARVM) Reserves for Individual Annuity Contracts (AG 33), which took effect on December 31, 1995, for all contracts issued on or after January 1, 1981.

For Years 1, 2, 3, and 4, in computing its end of the year life insurance reserves for annuity contracts issued prior to December 31, 1995, Taxpayer implemented the changes which had been set forth by the NAIC in AG 33. Prior to the issuance of AG 33,Taxpayer used Plan Y valuation rates for all of its annuity products. In an attempt to comply with AG 33, Taxpayer changed to Plan Z valuation rates for certain products where the policyholder could receive the full annuity value without reduction if received in periodic payments over a time period of at least three years. Prior to AG 33, Taxpayer held constant interest rates throughout the deferred period of the policy. After AG 33 was enacted, Taxpayer began using different valuation interest rates when different assumed annuitization dates affected the estimated duration. In addition, after AG33 was enacted, Taxpayer began to consider partial annuitization and withdrawal scenarios in the calculation of the greatest present value of future benefits. Taxpayer's reserve strengthening represented the company's application of the changes necessary to comply with the guidance provided in AG 33 and the changes were applied for both statutory accounting and tax accounting purposes.

APPLICABLE LAW AND ANALYSIS

Section 807(d)(1) provides that, other than for purposes of section 816 (relating to qualification as a life insurance company), the amount of the life insurance reserve with respect to any contract is the greater of: (i) the net surrender value of the contract, or (ii) the reserve determined under section 807(d)(2). At no time may the reserve for any contract exceed the amount taken into account with respect to that contract as of that time in determining statutory reserves.

Section 807(d)(2) provides in part that the reserve for any contract must be determined using the tax reserve method applicable to that type of contract. The tax reserve method applicable to annuity contracts is the CARVM (Commissioners' Annuities Reserve Valuation Method) prescribed by the NAIC.

Under section 807(d)(3)(B)(ii), the CARVM to be used for a particular contract is that which is in effect on the date of the issuance of the contract. The legislative history of section 807 confirms Congressional intent that, with one exception specifically provided for in that legislative history, an actuarial guideline be applied only to contracts issued after the guideline took effect. See H.R. Conf. Rep. No. 861, 98th Cong. 2d Sess. 1052 (1984), 1984-2 C.B. (Vol. 2) 1052; H.R. Rep. No. 426, 99th Cong. (1986), 1986-3 C.B. (Vol. 2) 945; S. Rep. No. 313, 99th Cong. 2d Sess. 944 (1986), 1986-3 C.B. (Vol. 3) 964.

Accordingly, we conclude that, because AG 33 was not in effect on the date of issuance of the Annuities, Taxpayer may not use AG 33 in determining the tax reserves for those Annuities.

CAVEATS:

A copy of this technical advice memorandum is to be given to the taxpayer(s). Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.