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DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

JUN 23 2005

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We have received your request for a ruling on the income tax treatment for an annuity. We believe that you may not need a letter ruling, and we are hesitant to issue one to you until we are sure that this is exactly what you need. Below you will find general information which may be of use to you in understanding your tax situation.

In general, annuity contracts may have two distinct kinds of distributions. The standard annuity distribution refers to a distribution which is part of fixed, determinate obligation on the part of the company to make stated payments over a period of years or over a lifetime. Typically, once the obligation has become fixed and annuity payments have started the annuitant cannot request changes in the arrangement. Alternatively, some contracts allow the owner to take amounts out of the account prior to the initiation of a fixed, determinate annuity obligation. Often, the owner may alter these distribution amounts by his own preferences and needs, or stop them altogether. This second kind of distribution is referred to as an amount received not as an annuity.

Under section 72 of the Internal Revenue Code, any amount received under an annuity contract is taxable as ordinary income except to the extent it represents a return of your previously taxed investment in the contract. This tax treatment anticipates that the investment in the contract will be recovered tax-free during the course of the reception of regular annuity payments. For each regular annuity payment received, normally part of the payment represents a return of your original investment money itself, and part represents income and earnings on your investment. Only the first part is received tax free as part of your annuity payment.

Amounts received not as an annuity are treated differently: if an amount received not as an annuity is received before the date upon which fixed, specified payments become obligatory (i.e. before the annuity payment obligation becomes determinate) then these non-annuity distributions are fully taxable to the extent of the earnings on the contract. The non-annuity distribution is first out of earnings, and is fully taxable, until these earnings are used up. If non-annuity distributions are made which exceed the earnings, so that the only amount left in the account are the original invested funds, then such distribution amounts are tax-free as a recovery of the investment.

We have contacted the life insurance company issuing the contract, and based so far on the general information we were able to obtain about their contracts, it is possible that the distributions you have received may represent payments received not as an annuity. If so, this would mean that the payments would be fully includible in your gross income to the extent that they do not exceed the earnings on the contract. This would also mean that the 1099-R forms they sent are accurate in identifying the taxable amount as the same as the gross annuity amount.

If this information is sufficient to satisfy your concerns, please let us know so that we can close your file. If not, there are certain questions we would have to clarify before we could undertake to issue a ruling on the manner in which your benefits are treated in relation to be above-mentioned rules. If possible, please call us at the phone number below. If you do not respond within 30 days we will close your file.

If you have any question concerning this matter, please contact (not a toll-free number). Or you may contact Acting Manager, Actuarial Group 1, at (also not a toll-free number).

Sincerely yours,

Larry Isaacs, Acting Manager
Employee Plan Actuarial Group 1