amount ($150,000) by which the gain from operations ($400,000) exceeds the taxable investment income ($250,000).

Example 3. For the taxable year 1959, W, a life insurance company, has taxable investment income of zero (0) and a gain from operations of $90,000. W made no subtractions from the policyholders surplus account during such taxable year. For the taxable year 1959, W has life insurance company taxable income of $45,000, computed by adding taxable investment income (0) and 50 percent ($45,000) of the amount ($90,000) by which the gain from operations ($90,000) exceeds the taxable investment income (0).

Example 4. For the taxable year 1961, Z, a life insurance company, has taxable investment income of $100,000, a policyholders surplus account of $50,000 as of the beginning of such taxable year, a loss from operations (as defined in section 809(b)(2)) of $25,000, and subtractions from the policyholders surplus account in the amount of $20,000. For the taxable year 1961, Z has life insurance company taxable income of $20,000, as only the amount ($20,000) subtracted from the policyholders surplus account is taken into account.

[T.D. 6513, 25 FR 12658, Dec. 10, 1960]

§ 1.802–5 Special rule for 1959 and 1960.

(a) *Transitional rule.* Section 802(a)(3) provides a transitional rule for the determination of the tax liability of a life insurance company for the taxable years 1959 and 1960 by reason of the operation of section 802(b)(3). Except as limited by section 802(a)(3) and paragraph (b) of this section, any increase in a life insurance company's tax that is attributable to the operation of section 802(b)(3) is taken into account only to the extent of one-third and two-thirds for the taxable years 1959 and 1960, respectively. To the extent there is an increase in a life insurance company's tax that is attributable to the operation of section 802(b)(3) which is not taken into account for the taxable years 1959 and 1960 because of the transitional rule provided by section 802(a)(3) and this paragraph, such amounts shall be included in ''other accounts'' under section 815(a)(3). For taxable years commencing after December 31, 1960, the full amount of any increase in tax due to the operation of section 802(b)(3) shall be imposed without any further transitional reduction.

(b) *Limitations.* The transitional rule provided by section 802(a)(3) is limited solely to an increase in tax under section 802(b)(3) that is occasioned by the operation of section 815(c)(3) (relating to subtractions from the policyholders surplus account by reason of distributions to shareholders). This rule is further limited to actual distributions that are made by life insurance companies in 1959 or 1960 and does not extend to other distributions that are treated under section 815(d)(2)(B) as made by life insurance companies in 1959 or 1960. Furthermore, section 802(a)(3) shall not apply to any increase in tax under section 802(b)(3) that is attributable to other subtractions from the policyholders surplus account by reason of the operation of the special rules contained in section 815(d). However, the transitional rule provided by section 802(a)(3) does apply in the case of a distribution to which section 815(e)(1)(B)(ii) applies.

(c) *Illustration of principles.* The provisions of section 802(a)(3) and this section may be illustrated by the following example:

Example. For the taxable year 1960, X, a life insurance company, had taxable investment income of $9,000, gain from operations of $27,000, and subtractions from the policyholders surplus account of $22,000. Based upon these figures, X had life insurance company taxable income of $40,000 for 1960, of which $18,000 was includible under section 802(b) (1) and (2) and $22,000 under section 802(b)(3). Applying the tax imposed by section 802(a)(1) (at rates as in effect for 1960), without regard to the transitional rule of section 802(a)(3), X would have a tax liability of $15,300 ($40,000 multiplied by 52 percent, less $5,500). However, applying the transitional rule of section 802(a)(3), the actual tax liability of X, for 1960, would be $12,000, computed as follows:

(1) Total tax liability (without regard to sec. 802(a)(3))		$15,300
(2) Life insurance company taxable income	$40,000	
(3) Amount subtracted from policyholders surplus account	22,000	
(4) Item (2) less item (3)	18,000	
(5) Tax on amount includible under sec. 802(b) (1) and (2) (30% of $18,000)		5,400
(6) Tax attributable to sec. 802(b)(3) (item (1) less item (5))		9,900
(7) Less: 33 1/3 percent of tax attributable to sec. 802(b)(3) (1/3 of $9,900)		3,300
(8) Tax liability for 1960 after application of sec. 802(a)(3) (item (1) less item (7))		12,000

[T.D. 6513, 25 FR 12659, Dec. 10, 1960]