Example. The books of Y, an insurance company, selling life insurance, noncancellable health and accident insurance, and cancellable accident and health insurance, reflect (after adjustment under sections 806(a) and 801(d)) the following facts for the taxable year 1958:

	Jan. 1	Dec. 31	Mean of year
1. Life insurance reserves	$3,000	$5,000	$4,000
2. Unearned premiums, and unpaid losses (whether or not ascertained), on noncancellable accident and health insurance not included in life insurance reserves	400	600	500
3. Unearned premiums, and unpaid losses (whether or not ascertained), on cancellable accident and health insurance	1,800	2,200	2,000
4. All other insurance reserves required by law	900	1,100	1,000
5. Total reserves	....	....	7,500

The rules provided by section 801 require that the sum of the mean of the year figures in items 1 and 2 comprise more than 50 percent of the mean of the year figure in item 5 for an insurance company to qualify as a life insurance company. Thus, Y would qualify as a life insurance company for the taxable year 1958 as the sum of the mean of the year figures in items 1 and 2 ($4,500) comprise 60 percent of the mean of the year figure in item 5 ($7,500).

[T.D. 6513, 25 FR 12657, Dec. 10, 1960]

§ 1.801–6 Adjustments in reserves for policy loans.

(a) *In general*. Section 801(d) provides that for purposes only of determining whether or not an insurance company is a life insurance company (as defined in section 801(a) and paragraph (b) of § 1.801–3), the life insurance reserves (as defined in section 801(b) and § 1.801–4), and the total reserves (as defined in section 801(c) and paragraph (a) of § 1.801–5), shall each be reduced by an amount equal to the mean of the aggregates, at the beginning and end of the taxable year, of the policy loans outstanding with respect to contracts for which life insurance reserves are maintained. Such reduction shall be made after any adjustments required under section 806(a) and § 1.806–3 have been made.

(b) *Policy loans defined*. The term *policy loans* includes loans made by the insurance company, by whatever name called, for which the reserve on a contract is the collateral.

(c) *Illustration of principles*. The provisions of section 801(d) and this section may be illustrated by the following example:

Example. The books of T, an insurance company, selling only life insurance and cancellable accident and health insurance, reflect (after adjustment under section 806 (a)) the following facts for the taxable year 1958:

	Jan. 1	Dec. 31	Mean of year
1. Life insurance reserves	$1,000	$2,000	$1,500
2. Policy loans	50	850	450
3. Life insurance reserves less policy loans	....	....	1,050
4. Unearned premiums, and unpaid losses (whether or not ascertained), on cancellable accident and health insurance	900	1,600	1,250
5. Total reserves adjusted for policy loans (item 3 plus item 4)	....	....	2,300

As the rules provided by section 801 (a) and (d) require that the figure in item 3 ($1,050) be more than 50 percent of the mean of the year figure in item 5 ($2,300) for an insurance company to qualify as a life insurance company, T would not qualify as a life insurance company for the taxable year 1958.

[T.D. 6513, 25 FR 12657, Dec. 10, 1960]

§ 1.801–7 Variable annuities.

(a) *In general*. (1) Section 801(g)(1) provides that for purposes of part I, subchapter L, chapter 1 of the Code, an annuity contract includes a contract which provides for the payment of a variable annuity computed on the basis of recognized mortality tables and the investment experience of the company issuing such a contract. A variable annuity differs from the ordinary or fixed dollar annuity in that the annuity benefits payable under a variable annuity contract vary with the insurance company's investment experience with respect to such contracts while the annuity benefits paid under a fixed dollar annuity contract are guaranteed irrespective of the company's actual investment earnings.

(2) The reserves held with respect to the annuity contracts described in section 801(g)(1) and subparagraph (1) of this paragraph shall qualify as life insurance reserves within the meaning of

section 801(b)(1) and paragraph (a) of §1.801–4 provided such reserves are required by law (as defined in paragraph (b) of §1.801–5) and are set aside to mature or liquidate, either by payment or reinsurance, future unaccrued claims arising from such contracts involving, at the time with respect to which the reserve is computed, life, health, or accident contingencies. Accordingly, a company issuing variable annuity contracts shall qualify as a life insurance company for Federal income tax purposes if it satisfies the requirements of section 801(a) (relating to the definition of a life insurance company) and paragraph (b) of §1.801–3.

(b) *Special rules for variable annuities*—(1) *Adjusted reserves rate; assumed rate.* The adjusted reserves rate for any taxable year with respect to the annuity contracts described in section 801(g)(1) and paragraph (a)(1) of this section, and the rate of interest assumed by the taxpayer for any taxable year in calculating the reserve on any such contract, shall be a rate equal to the current earnings rate determined under section 801(g)(3) and subparagraph (2) of this paragraph. However, any change in the rate of interest assumed by the taxpayer in calculating the reserve on a variable annuity contract for any taxable year which is attributable to an increase or decrease in the current earnings rate, shall not be treated as a change of basis in computing reserves for purposes of section 806(b) (relating to certain changes in reserves) or section 810 (d)(1) (relating to adjustment for change in computing reserves).

(2) *Current earnings rate.* (i) The current earnings rate for any taxable year with respect to the annuity contracts described in section 801(g)(1) and paragraph (a)(1) of this section shall be the current earnings rate determined under section 805(b)(2) and paragraph (a)(2) of §1.805–5 with respect to such contracts, reduced by the percentage obtained by dividing (*a*) the amount of the actuarial margin charge on all such variable annuity contracts issued by the taxpayer, by (*b*) the mean of the reserves for such contracts.

(ii) For purposes of section 801(g)(3) and subdivision (i) of this subparagraph, the term *actuarial margin charge* means any amount retained by the company from gross investment income pursuant to the terms of the variable annuity contract in excess of any portion of the investment expenses which is attributable to such contract and which is deductible under section 804(c) and paragraph (b) of §1.804–4.

(3) *Increases and decreases in reserves.* (i) Section 801(g)(4) provides that for purposes of section 810 (a) and (b) (relating to adjustments for increases or decreases in certain reserves), the sum of the items described in section 810(c) and paragraph (b) of §1.810–2 taken into account as of the close of the taxable year shall be adjusted:

(*a*) By subtracting therefrom the sum of any amounts added from time to time (for the taxable year) to the reserves for variable annuity contracts described in section 801(g)(1) and paragraph (a)(1) of this section by reason of realized or unrealized appreciation in the value of the assets held in relation thereto, and

(*b*) By adding thereto the sum of any amounts subtracted from time to time (for the taxable year) from such reserves by reason of realized or unrealized depreciation in the value of such assets.

(ii) The application of section 801(g)(4) and subdivision (i) of this subparagraph may be illustrated by the following example:

Example. Company M, a life insurance company issuing only variable annuity contracts of the type described in section 801(g)(1) and paragraph (a)(1) of this section, increased its life insurance reserves held with respect to such contracts during the taxable year 1959 by $275,000. Of the total increase in the reserves, $100,000 was attributable to premium receipts, $50,000 to dividends and interest, $100,000 to unrealized appreciation in the value of the assets held in relation to such reserves, and $25,000 to realized capital gains on the sale of such assets. As of the close of the taxable year 1959, the reserves held by company M with respect to all variable annuity contracts amounted to $1,275,000. However, under section 801(g)(4) and subdivision (i) of this subparagraph, this amount must be reduced by the $100,000 unrealized asset value appreciation and the $25,000 of realized capital gains. Accordingly, for purposes of section 810 (a) and (b), the amount of these reserves which is to be taken into account as of the close of the taxable year 1959 under section 810(c) is $1,150,000 ($1,275,000 less $125,000).

(c) *Companies issuing variable annuities and other contracts.* (1) In the case of a life insurance company which issues both annuity contracts described in section 801(g)(1) and paragraph (a)(1) of this section and other contracts, the policy and other contract liability requirements (as defined in section 805(a) and paragraph (b) of §1.805–4) of such a company for any taxable year shall be considered to be the sum of:

(i) The policy and other contract liability requirements computed with respect to the items which relate to such variable annuity contracts, and

(ii) The policy and other contract liability requirements computed by excluding the items taken into account under subdivision (i) of this subparagraph.

(2) [Reserved for regulations to be issued under section 801(g)(5)(B).]

(d) *Termination.* Paragraphs (1), (2), (3), (4), and (5) of section 801(g) and paragraphs (a), (b), (c), and (d) of this section shall not apply with respect to any taxable year beginning after December 31, 1962.

[T.D. 6610, 27 FR 8717, Aug. 31, 1962]

§ 1.801–8 Contracts with reserves based on segregated asset accounts.

(a) *Definitions*—(1) *Annuity contracts include variable annuity contracts.* Section 801(g)(1)(A) provides that for purposes of part I, subchapter L, chapter 1 of the Code, an annuity contract includes a contract which provides for the payment of a variable annuity computed on the basis of recognized mortality tables and the investment experience of the company issuing such a contract. A variable annuity differs from the ordinary or fixed dollar annuity in that the annuity benefits payable under a variable annuity contract vary with the insurance company's investment experience with respect to such contracts while the annuity benefits paid under a fixed dollar annuity contract are guaranteed irrespective of the company's actual investment earnings.

(2) *Contracts with reserves based on a segregated asset account.* (i) For purposes of part I, section 801(g)(1)(B) defines the term *contract with reserves based on a segregated asset account* as a contract (individual or group):

(*a*) Which provides for the allocation of all or part of the amounts received under the contract to an account which, pursuant to State law or regulation, is segregated from the general asset accounts of the company,

(*b*) Which provides for the payment of annuities, and

(*c*) Under which the amounts paid in, or the amount paid as annuities, reflect the investment return and the market value of the segregated asset account.

(ii) The term *contract with reserves based on a segregated asset account* includes a contract such as a variable annuity contract, which reflects the investment return and the market value of the segregated asset account, even though such contract provides for the payment of an annuity computed on the basis of recognized mortality tables, but the term includes such contract only for the period during which it satisfies the requirements of section 801(g)(1)(B) and subdivision (i) of this subparagraph. However, such term does not include a pension contract written on the basis of the so-called new-money concept. Thus, for example, such term does not include a pension contract whereby reserves are credited on the basis of the company's new high yield investments. Furthermore, such term does not include a contract which during the taxable year contains a right to participate in the divisible surplus of the company where such right merely reflects the company's investment return. Nevertheless, the term does include a contract which meets the requirements of section 801(g)(1)(B) and of this subparagraph even if part of the amounts received are, for example, allocated to reserves under provisions of the contract which are written on the basis of the new-money concept. However, such reserves do not qualify as a segregated asset account referred to in section 801(g) and this section.

(iii) If at any time during the taxable year a contract otherwise satisfying the requirements of section 801(g)(1)(B) and subdivision (i) of this subparagraph ceases to reflect current investment return and current market value, such contract shall not be considered as meeting the requirements of section 801(g)(1)(B)(iii) and subdivision (i)(*c*) of