

of this section, means any distribution of property made by a life insurance company to its shareholders. For purposes of the preceding sentence, the term *property* means any property (including money, securities, and indebtedness to the company) other than stock, or rights to acquire stock, in the company making the distribution. Thus, for example, the term includes a distribution which is considered a dividend under section 316, but is not limited to the extent that such distribution must be made out of the accumulated or current earnings and profits of the company making the distribution. For example, except as otherwise provided in section 815(f) and subparagraph (2) of this paragraph, there is a distribution within the meaning of this paragraph in any case in which a corporation acquires the stock of a shareholder in exchange for property in a redemption treated as a distribution in exchange for stock under section 302(a) or treated as a distribution of property under section 302(d). For special rules relating to distributions to shareholders in acquisition of stock pursuant to a plan of mutualization, see section 815(e) and paragraph (e) of § 1.815-6.

(2) The term *distribution*, as used in section 815(a) and paragraph (b) of this section, does not (except for purposes of section 815(a)(3) and (e)(2)(B)) include any distribution in redemption of stock issued prior to January 1, 1958, where such stock was at all times on and after the date of its issuance and on and before the date of its redemption limited as to the amount of dividends payable and was callable, at the option of the issuer, at a price not in excess of 105 percent of the sum of its issue price plus the amount of contribution to surplus (if any) made by the original purchaser at the time of his purchase.

[T.D. 6535, 26 FR 542, Jan. 20, 1961, as amended by T.D. 7189, 37 FR 12793, June 29, 1972]

§ 1.815-3 Shareholders surplus account.

(a) *In general.* Every stock life insurance company subject to the tax imposed by section 802 shall establish and maintain a shareholders surplus account. This account shall be estab-

lished as of January 1, 1958, and the beginning or opening balance of the shareholders surplus account on that date shall be zero.

(b) *Additions to shareholders surplus account.* (1) The amount added to the shareholders surplus account for any taxable year beginning after December 31, 1957, shall be the amount by which the sum of:

(i) The life insurance company taxable income (computed without regard to section 802(b)(3)),

(ii) In the case of a taxable year beginning after December 31, 1958, the amount (if any) by which the net long-term capital gain exceeds the net short-term capital loss, reduced (in the case of a taxable year beginning after December 31, 1961) by the amount referred to in subdivision (i) of this subparagraph,

(iii) The deduction for partially tax-exempt interest provided by section 242 (as modified by section 804(a)(3)), the deductions for dividends received provided by sections 243, 244, and 245 (as modified by section 809(d)(8)(B)), and the amount of interest excluded from gross income under section 103, and

(iv) The small business deduction provided by section 809(d)(10). Exceeds the taxes imposed for the taxable year by section 802(a), computed without regard to section 802(b)(3).

(c) *Subtractions from shareholders surplus account—(1) In general.* There shall be subtracted from the cumulative balance in the shareholders surplus account at the end of any taxable year, computed without diminution by reason of distributions made during the taxable year, the amount which is treated as being distributed out of such account under section 815(a) and paragraph (b) of § 1.815-2.

(2) *Special rule; distributions in 1958.* There shall be subtracted from the shareholders surplus account (to the extent thereof) for any taxable year beginning in 1958 the amount of the distributions to shareholders made by the company during 1958. For example, assume S, a stock life insurance company, had additions to its shareholders surplus account (as determined under section 815(b)(2) and paragraph (b) of this section) for the taxable year 1958 of \$10,000, and actually distributed as

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dividends to its shareholders \$8,000 during the year 1958. The balance in S's shareholders surplus account as of January 1, 1959, shall be \$2,000. If S had distributed \$12,000 as dividends in 1958, the balance in its shareholders surplus account as of January 1, 1959, would be zero and the other accounts referred to in section 815(a)(3) and paragraph (b)(1)(iii) of §1.815-2 would be reduced by \$2,000.

(d) *Illustration of principles.* The application of section 815(b) and this section may be illustrated by the following example:

Example. The books of S, a stock life insurance company, reflect the following items for the taxable year 1960.

| | |
|---|---------|
| Balance in shareholders surplus account as of 1-1-60 | \$5,000 |
| Life insurance company taxable income computed without regard to sec. 802(b)(3) | 4,000 |
| Excess of net long-term capital gain over net short-term capital loss | 1,700 |
| Tax-exempt interest included in gross investment income under sec. 804(b) | 100 |
| Small business deduction (determined under sec. 809(d)(10)) | 200 |
| Tax liability under sec. 802(a) (1) and (2) computed without regard to sec. 802(b)(3) | 1,625 |
| Amount distributed to shareholders | 9,000 |

For purposes of determining the amount to be subtracted from its shareholders surplus account for the taxable year, S would first make up the following schedule in order to determine the cumulative balance in the shareholders surplus account at the end of the taxable year, computed without diminution by reason of distributions made during the taxable year:

| | |
|--|---------|
| (1) Balance in shareholders surplus account as of 1-1-60 | \$5,000 |
| (2) Additions to account: | |
| (a) Life insurance company taxable income computed without regard to sec. 802(b)(3) | \$4,000 |
| (b) Excess of net long-term capital gain over net short-term capital loss | 1,700 |
| (c) Tax-exempt interest included in gross investment income under sec. 804(b) ... | 100 |
| (d) Small business deduction (determined under sec. 809(d)(10)) | 200 |
| Total | 6,000 |
| Less: | |
| Tax liability under sec. 802(a) (1) and (2) computed without regard to sec. 802(b)(3) | 1,625 |
| | 4,375 |
| (3) Cumulative balance in shareholders surplus account as of 12-31-60 (item (1) plus item (2)) | 9,375 |

Since the amount distributed to shareholders during the taxable year, \$9,000, does not exceed the cumulative balance in the shareholders surplus account at the end of the taxable year, computed without diminution by reason of distributions made during the taxable year, \$9,375, under the provisions of section 815(a), the entire distribution shall be treated as being made out of the shareholders surplus account. Thus, \$9,000 shall be subtracted from the shareholders surplus account (leaving a balance of \$375 in such account at the end of the taxable year) and S shall incur no additional tax liability by reason of the distribution to its shareholders during the taxable year 1960.

[T.D. 6535, 26 FR 542, Jan. 20, 1961, as amended by T.D. 7189, 37 FR 12793, June 29, 1972]

§ 1.815-4 Policyholders surplus account.

(a) *In general.* Every stock life insurance company subject to the tax imposed by section 802 shall establish and maintain a policyholders surplus account. This account shall be established as of January 1, 1959, and the beginning or opening balance of the policyholders surplus account on that date shall be zero.

(b) *Additions to policyholders surplus account.* The amount added to the policyholders surplus account for any taxable year beginning after December 31, 1958, shall be the sum of:

- (1) An amount equal to 50 percent of the amount by which the gain from operations for the taxable year exceeds the taxable investment income,
- (2) The deduction allowed or allowable under section 809(d)(5) (as limited by section 809(f)) for certain non-participating contracts, and
- (3) The deduction allowed or allowable under section 809(d)(6) (as limited by section 809(f)) for taxable years beginning before January 1, 1963, for group life and group accident and health insurance contracts, and for taxable years beginning after December 31, 1962, for accident and health insurance and group life insurance contracts.

(c) *Subtractions from policyholders surplus account—(1) In general.* There shall be subtracted from the cumulative balance in the policyholders surplus account at the end of any taxable year, computed without diminution by reason of distributions made during the