



FINANCIAL SERVICES

- Insurance Tax Bulletin

PRICEWATERHOUSECOOPERS 

Tax Consequences of Assumption of Insurance, Annuity Contracts

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The IRS ruled in PLR 200820009 that neither the assumption of insurance and annuity contracts nor modifications to those contracts resulting from the assumption will affect the contracts under the relevant code sections, constitute a disqualifying distribution, or result in income to contract beneficiaries.

The relevant transaction arose in the context of a plan for the rehabilitation of Ceding Company (the Plan) and involves the transfer by assumption reinsurance of Ceding Company's life insurance and other contracts to Assuming Company under the supervision of the State A Court. The Plan indicates that each contract which is in force on the closing date of the reinsurance transaction will be modified by Ceding Company through one or more endorsements, effective as of the closing date but immediately prior to the closing of the reinsurance of the endorsed contracts. Pursuant to the Plan, the endorsements will include the following provisions. Certain "tax-qualified" contracts will be authorized to receive compensation for the extinguishment of mutual membership interests in the form of credits to the policy values (Plan credits). Mutual members who hold non-trusted tax qualified retirement funding contracts will not receive, or be entitled to receive, distributable equity with respect to such tax-qualified contracts. Instead, they will receive credits to the Plan credits in the form of additional paid-up insurance or account value credits. The value of the Plan credits will be equal to the value of the cash otherwise allocable to the qualified contract-holders with respect to their tax-qualified contracts. Assuming Company will receive assets from Ceding Company for purposes of paying the Plan credit amounts.

In addition to examining PLR 200814005, the IRS relied upon the following sections of the Internal Revenue Code: 72(e)(5), 401, 402, 403, 408, or 408A. This ruling supplements the IRS' prior conclusions in PLR 200814005 but does not supersede it. The IRS stated that based upon the taxpayer's representations that the transferred life insurance contracts and annuity contracts qualify as such for federal tax purposes, neither the modification of a contract by endorsement, nor any amount paid or credited with respect to a contract pursuant to court approval, nor the assumption reinsurance of an endorsed contract pursuant to the plan without a change of terms or conditions will, in the case of a contract that is part of a qualified plan, have any effect of such contract for purposes of Sections 72(e)(5), 401, 402, 403, 408, or 408A.

As such, the IRS concluded that the investment in the contract under Section 72 for each endorsed contract immediately after the assumption will remain the same as an unendorsed contract immediately prior to endorsement. The IRS also stated that either the addition of a credit nor the right thereto constitutes a distribution in violation of Section 403(a), 402(b)(11), or 408(e), and addition of a credit to a non-trusted retirement funding account does not constitute a distribution nor a contribution and thus will not result in gross income to the employee or other beneficiary of such contract prior to actual receipt.

PwC Observes: Although this ruling touches on similar issues as those raised in PLR 200814005, it supplements but does not supersede the prior ruling. PLR 200814005 examined a transaction involving two life insurance companies where one's contracts were transferred to the other by way of assumption reinsurance. Taxpayers should contact their tax professional to see how this new ruling might impact them.

For additional information please call Anthony DiGilio at (202) 414-1702 or contact your local insurance tax professional. Please visit us at: <http://www.pwc.com/us/insurance/tax>

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