

Insurance Tax Update Preview of the 2009 Review



In this edition of Insurance Tax Update (ITU)...

Deloitte Tax practitioners provide a sneak peek at their "2009 Insurance Tax Year in Review" article which will be published by Tax Analysts in the March 2010 edition of *The Insurance Tax Review*.

Preview of the 2009 Review

For the thirteenth year running, Deloitte Tax LLP has produced its "2009 Insurance Tax Year in Review" article that will appear in the March 2010 edition of the Tax Analysts journal, *The Insurance Tax Review*. The publication of this year's article is being held until March so that it might include a discussion of developments relating to health care reform and other legislation of interest to insurance companies that are anticipated to occur in the coming weeks.

In this year's article, Rich Burness and Jean Kunz discuss the year's significant domestic insurance company tax developments in Part I — Federal Insurance Tax Matters; Rick Gelfond and Yvonne Fujimoto provide an overview of 2009 insurance product tax issues in Part II — Product Tax Matters; Fred von Rueden and Brett Whitcomb delve into important state and local tax issues in Part III — State and Local Insurance Tax Matters; and Richard Safraneck and Mary Gillmarten explore 2009 international tax developments in Part IV — International Tax Matters. This "Preview

of the Review" provides a quick glimpse of some of the highlights of *The Insurance Tax Review* article.

Overview

The year 2009 proved to be a particularly busy year in the insurance tax area. This included both proposed and enacted legislation, as well as IRS guidance on many topics of interest to insurance tax practitioners, particularly in the insurance product and reinsurance areas.

Part I — Federal Tax Matters

In addition to health care reform that began in 2009 but is still taking shape, there was the extension of the 2008 or 2009 net operating loss carryback period to five years¹ and the release of SSAP 10R² which temporarily revises the rules relating to the recognition of deferred tax assets for statutory accounting purposes. SSAP 10R was a continuation of, and response to, the discussions that began in 2008 on expanding the limitations on admitting deferred tax assets under SSAP 10.

A few of the other domestic insurance tax issues covered in the "2009 Insurance Tax Year in Review" are:

- An overview of the 2009-2010 priority guidance plan that lists the projects the government expects to complete by June 2010. The list is similar to that in last year's plan with only one project completed as of the end of 2009.
- An update on principle-based reserves.
- Guidance involving life insurance companies in merger transactions.

¹ Worker, Homeownership, and Business Assistance Act of 2009, P.L. 111-92.

² Statement of Statutory Accounting Principles No. 10R — Income Taxes-Revised, A Temporary Replacement of SSAP No. 10 ("SSAP 10R").

In addition, the article describes new guidance on the qualification of entities as tax-exempt insurance companies and the granting of administrative relief permitting insurance companies to file late section 953(d) and 831(b) elections.

Part II — Product Tax Matters

The insurance product tax area saw guidance relating to the emerging life settlements arena, including the release of revenue rulings relating to sales and receipts of death benefits by investors in existing life insurance contracts, as well as the tax treatment of original insured-owners under such contracts. Other interesting developments included a letter ruling in which the IRS allowed a bank to recognize a loss on the surrender of its insurance policies and the Federal Circuit's affirmation of the decision in the *Fisher* case,³ which permitted policyholders of a former mutual life insurance company to allocate basis to the stock received upon demutualization.

These pieces of guidance establish the Service's view of certain seemingly basic concepts such as basis and character of income in the sale of life insurance contracts. While those rulings do present the Service's and one court's view on some questions, those same rulings also lead to more questions as to the reasoning behind the stated conclusions.

Other insurance product tax guidance described in the article includes the following:

- Notice 2009-47 on a proposed safe harbor addressing the application of sections 7702 and 7702A to life insurance contracts that mature after the insured individual attains age 100.
- Notice 2009-48 providing guidance on employer-owned life insurance contracts.
- Characteristics of an annuity contract.
- Segregated asset accounts owning shares of funds invested in "public funds."

In addition, the article includes several rulings involving the treatment of various types of benefit riders on life insurance and annuity contracts.

Part III — State and Local Tax Matters

In 2009, the major state and local tax developments continued to be a reflection of the impact of the economic slowdown on state budgets. State revenues were down and spending demands imposed by safety net programs such as Medicaid were up. In turn, as states chose between raising revenues and cutting spending, they knew that either choice risked deepening the economic downturn in the state. A few of the revenue-raising methods considered by some states included, for example, raising tax rates, creating a moratorium on state tax credit programs, and requiring combined reporting.

The momentum generated in 2008 for a greater federal role in the regulation of the insurance industry continued into 2009. In April 2009, legislation (H.R. 1880) was introduced that would have established an office in the Treasury Department to provide national oversight of the insurance industry. At the end of 2009, the U.S. House of Representatives passed financial reform legislation (H.R. 4173) that would establish the Federal Insurance Office within the Department of the Treasury. The bill is currently being considered by the Senate.

The state and local section of the article outlines some of the more significant state regulatory, legislative, judicial, and administrative developments affecting insurance companies.

Part IV — International Tax Matters

As seen in the other sections of the article, 2009 was a busy year for legislative proposals. Rep. Neal reintroduced his bill (H.R. 3424) that would disallow certain deductions for reinsurance premiums paid to foreign affiliates. Sen. Levin and Rep. Doggett each introduced a new version of the Stop Tax Haven Abuse Act. The Foreign Account Tax Compliance Act of 2009 (H.R. 3933, S. 1934), introduced concurrently by Rep. Rangel and Sen. Baucus, draws on the Stop Tax Haven Abuse Act introduced by Sen. Levin, the Obama administration's FY 2010 budget package, and a draft anti-tax haven proposal circulated by Sen. Baucus earlier this year. Under that legislation as currently proposed, the terms "financial institution" and "financial account" could potentially apply to insurance companies and insurance policies, respectively.

Among some of the other significant international tax developments relevant to insurance companies are the following:

- Rev. Rul. 2009-26 in which the Service acknowledged that insurance could exist in cases where all business written by a reinsurer derives from a single contract with an unrelated insurer.
- Guidance on pooling arrangements.
- Notice 2010-1 in which the Service designated an additional exception whereby the new target and old target are treated as the same corporation under a section 338(g) or section 338(h)(10) election. That exception applies for purposes of section 807(e)(4) related to qualified foreign contracts issued by foreign branches of domestic life insurance companies.

The article also provides an update on treaties with Belgium, France, Gibraltar, Hungary, Italy, Liechtenstein, Luxembourg, Malta, Monaco, New Zealand, and Switzerland.

³ *Eugene A. Fisher, Trustee, Seymour P. Nagan Irrevocable Trust v. United States*, No. 2009-5001 (Fed. Cir., October 9, 2009).

Conclusion

For the full article, see the “2009 Insurance Tax Year in Review” in the March 2010 edition of *The Insurance Tax Review*. Just as 2009 proved to be full of activity, 2010 is expected to be an eventful year, so please watch for “Halftime 2010 — Selected Insurance Tax Developments” in the summer.

Editorial Board

Co-Editors-In-Chief & Contributors

Rich Burness

Partner
Deloitte Tax LLP
+1 860 725 3034
rburness@deloitte.com

Rick Gelfond

Principal
Deloitte Tax LLP
+1 202 220 2017
rgelfond@deloitte.com

For further information, visit our website at
www.deloitte.com/us/insurance

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