

upon which the evidence of indebtedness was acquired. Thus, where a convertible evidence of indebtedness was acquired before January 1, 1958, and a portion or all of the premium attributable to the conversion features of the evidence of indebtedness has been amortized for taxable years beginning before January 1, 1958, no adjustment for such amortization will be required by reason of section 818(b)(2)(B). Such amortization will, however, require an adjustment to the basis of the evidence of indebtedness under section 1016(a)(17). For taxable years beginning after December 31, 1957, no further amortization of the premium attributable to the conversion features of such an evidence of indebtedness will be taken into account.

(e) *Adjustments to basis.* Section 1016(a)(17) (relating to adjustments to basis) provides that in the case of any evidence of indebtedness referred to in section 818(b) and this section, the basis shall be adjusted to the extent of the adjustments required under section 818(b) (or the corresponding provisions of prior income tax laws) for the taxable year and all prior taxable years. The basis of any evidence of indebtedness shall be reduced by the amount of the adjustment required under section 818(b) (or the corresponding provision of prior income tax laws) on account of amortizable premium and shall be increased by the amount of the adjustment required under section 818(b) on account of accruable discounts.

(f) *Denial of double inclusion.* Any amount which is includible in gross investment income by reason of section 818(b) and paragraph (a) of this section shall not be includible in gross income under section 1232(a) (relating to the taxation of bonds and other evidences of indebtedness). See section 1232(a)(2)(C) and the regulations thereunder.

[T.D. 6558, 26 FR 2786, Apr. 4, 1961]

§ 1.818-4 Election with respect to life insurance reserves computed on preliminary term basis.

(a) *In general.* Section 818(c) permits a life insurance company issuing contracts with respect to which the life insurance reserves are computed on one of the recognized preliminary term

bases to elect to revalue such reserves on a net level premium basis for the purpose of determining the amount which may be taken into account as life insurance reserves for purposes of part I, subchapter L, chapter 1 of the Code, other than section 801 (relating to the definition of a life insurance company). If such an election is made, the method to be used in making this revaluation of reserves shall be either the exact revaluation method (as described in section 818(c)(1) and paragraph (b)(1) of this section) or the approximate revaluation method (as described in section 818(c)(2) and paragraph (b)(2) of this section).

(b) *Revaluation of reserves computed on preliminary term basis.* If a life insurance company makes an election under section 818(c) in the manner provided in paragraph (e) of this section, the amount to be taken into account as life insurance reserves with respect to contracts for which such reserves are computed on a preliminary term basis may be determined on either of the following bases:

(1) *Exact revaluation method.* As if the reserves for all such contracts had been computed on a net level premium basis (using the same mortality or morbidity assumptions and interest rates for both the preliminary term basis and the net level premium basis).

(2) *Approximate revaluation method.* The amount computed without regard to section 818(c):

(i) Increased by \$21 per \$1,000 of insurance in force (other than term insurance) under such contracts, less 2.1 percent of reserves under such contracts, and

(ii) Increased by \$5 per \$1,000 of term insurance in force under such contracts which at the time of issuance cover a period of more than 15 years, less 0.5 percent of reserves under such contracts.

(c) *Exception.* If a life insurance company which makes an election under section 818(c)(2) and paragraph (b)(2) of this section has life insurance reserves with respect to both life insurance and noncancellable accident and health contracts for which such reserves are computed on a preliminary term basis, it shall use the approximate revaluation method for all its life insurance

reserves other than that portion of such reserves held with respect to its noncancellable accident and health contracts, and shall use the exact revaluation method for all its life insurance reserves held with respect to such noncancellable accident and health contracts.

(d) *Reserves subject to recomputation.*

(1) For the first taxable year for which the election under section 818(c) and paragraph (b) of this section applies, a company making such election must revalue all its life insurance reserves held with respect to contracts for which such reserves are computed on a preliminary term basis at the end of such taxable year on the basis elected under section 818(c) and paragraph (b) of this section. However, for purposes of the preceding sentence, an election under section 818(c) shall not apply with respect to such reserves which would not be treated as being computed on the preliminary term basis at the end of such taxable year except for the provisions of section 810 (a) or (b). See paragraph (c)(2) of § 1.810-2. For example, if S, a life insurance company which computes its life insurance reserves on a recognized preliminary term basis at the beginning of the taxable year 1958, strengthens a portion of such reserves during the taxable year by actually changing to a net level premium basis in computing such reserves, and then makes the election under section 818(c) and paragraph (b) of this section for 1958, such election shall not apply with respect to the strengthened contracts.

(2) For any taxable year other than the first taxable year for which the election under section 818(c) and paragraph (b) of this section applies, a company making such election must revalue all its life insurance reserves held with respect to contracts for which such reserves are computed on a preliminary term basis at the beginning or end of the taxable year on the basis elected under section 818(c) and paragraph (b) of this section. For example, if M, a life insurance company which made a valid outstanding election under section 818(c) in the manner provided in paragraph (e) of this section for the taxable year 1959, sells a block of contracts subject to such elec-

tion on September 1, 1960, M would value such contracts on the basis elected under section 818(c) and paragraph (b) of this section on January 1, 1960, for purposes of determining the net decrease or increase in the sum of the items described in section 810(c) for the taxable year under section 810 (a) or (b).

(3) For the effect of an election under section 818(c) and paragraph (b) of this section in determining gain or loss from operations for the taxable year, see paragraph (c)(3) of § 1.810-2 and paragraph (e) of § 1.810-3.

(e) *Time and manner of making election.* The election provided by section 818(c) shall be made in a statement attached to the life insurance company's income tax return for the first taxable year for which the company desires the election to apply. The return and statement must be filed not later than the date prescribed by law (including extensions thereof) for filing the return for such taxable year. However, if the last day prescribed by law (including extensions thereof) for filing a return for the first taxable year for which the company desires the election to apply falls before April 4, 1961, the election provided by section 818(c) may be made for such year by filing the statement and an amended return for such taxable year (and all subsequent taxable years for which returns have been filed) before July 4, 1961. The statement shall indicate whether the exact or the approximate method of revaluation has been adopted. The statement shall also set forth sufficient information as to mortality and morbidity assumptions; interest rates; the valuation method used; the amount of the reserves and the amount and type of insurance in force under all contracts for which reserves are computed on a preliminary term basis; and such other pertinent data as will enable the Commissioner to determine the correctness of the application of the revaluation method adopted and the accuracy of the computations involved in revaluing the reserves. The election to use either the exact revaluation method or the approximate revaluation method shall, except for the purposes of section 801, be adhered to in making the computations under part I for the taxable year

for which such election is made and for all subsequent taxable years.

(f) *Scope of election.* An election made under section 818(c) and paragraph (b) of this section to use either the exact or the approximate method of revaluing the company's life insurance reserves shall be binding for the taxable year for which made, and, except as provided in paragraph (g) of this section, shall be binding for all succeeding taxable years, unless consent to revoke the election is obtained from the Commissioner. However, for taxable years beginning prior to April 4, 1961, a company may revoke the election provided by section 818(c) without obtaining consent from the Commissioner by filing, before July 4, 1961, a statement that the company desires to revoke such election. An amended return reflecting such revocation must accompany the statement for all taxable years for which returns have been filed with respect to such election.

(g) *Special rule for 1958.* If an election is made for a taxable year beginning in 1958 to use the approximate revaluation method described in section 818(c)(2) and paragraph (b)(2) of this section the company may, for its first taxable year beginning after 1958, elect to change to the exact revaluation method described in section 818(c)(1) and paragraph (b)(1) of this section without obtaining the consent of the Commissioner. In such case, the election to change shall be made in a statement attached to the company's income tax return for such taxable year and filed not later than the date prescribed by law (including extensions thereof) for filing the return for such year. The statement shall indicate that the company has elected to change from the approximate to the exact revaluation method for such taxable year and shall include such information and data referred to in paragraph (e) of this section as will enable the Commissioner to determine the correctness and accuracy of the computations involved.

[T.D. 6558, 26 FR 2787, Apr. 4, 1961; 26 FR 3276, Apr. 18, 1961]

§ 1.818-5 Short taxable years.

(a) *In general.* Section 818(d) provides that if any return of a corporation

made under part I, subchapter L, chapter 1 of the Code, is for a period of less than the entire calendar year, then section 443 (relating to returns for a period of less than 12 months) shall not apply. This section further provides certain rules to be used in determining the life insurance company taxable income for a period of less than the entire calendar year.

(b) *Returns for periods of less than the entire calendar year.* A return for a short period, that is, for a taxable year consisting of a period of less than the entire calendar year, shall be made only under the following circumstances:

(1) If a company which qualifies as a life insurance company is not in existence for the entire taxable year, a return is required for the short period during which the taxpayer was in existence. For example, a life insurance company organized on August 1, is required to file a return for the short period from August 1 to December 31, and returns for each calendar year thereafter. Similarly, if a company which qualifies as a life insurance company completely dissolves during the taxable year it is required to file a return for the short period from January 1 to the date it goes out of existence. All items entering into the computation of taxable investment income and gain or loss from operations for the short period shall be determined on a consistent basis and in the manner provided in paragraph (c) of this section.

(2) A return must be filed for a short period resulting from the termination by the district director of a taxpayer's taxable year for jeopardy. See section 6851 and the regulations thereunder.

A company which was an insurance company for the preceding taxable year (but not a life insurance company as defined in section 801(a) and paragraph (b) of § 1.801-3) and which for the current taxable year qualifies as a life insurance company shall not file a return for the short period from the time during the taxable year that it first qualifies as a life insurance company to the end of the taxable year. Similarly, an insurance company which was a life insurance company for the preceding taxable year but which for the current taxable year does not qualify as a life