§ 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 premium (or discount) as the number of months in the taxable year during which the security was owned by the life insurance company bears to the number of months between the date of acquisition of the security and its maturity or earlier call date, determined in accordance with this section. For purposes of this section, a fractional part of a month shall be disregarded unless it amounts to more than half a month, in which case it shall be considered a month.

(c) Acquisitions after December 31, 1957.

(1) In the case of:

(i) Any bond, as defined in section 171(d), acquired after December 31, 1957, the amount of the premium and the amortizable premium for the taxable year, shall be determined under section 171(b) and the regulations thereunder, as if the election set forth in section 171(c) had been made, and

(ii) Any bond, note, debenture, or other evidence of indebtedness not described in subdivision (i) of this subparagraph and acquired after December 31, 1957, the amount of the premium and the amortizable premium for the taxable year, shall be determined under paragraph (b) of this section.

(2) In the case of any bond, note, debenture, or other evidence of indebtedness acquired after December 31, 1957, the amount of the discount and the accrual of discount attributable to the taxable year shall be determined under paragraph (b) of this section.

(d) Convertible evidences of indebtedness. Section 818(b)(2)(B) provides that in no case shall the amount of premium on a convertible evidence of indebtedness (including any bond, note, or debenture) include any amount attributable to the conversion features of the evidence of indebtedness. This provision is the same as the one contained in section 171(b), and the rules prescribed in paragraph (c) of §1.171–2 shall be applicable for purposes of section 818(b)(2)(B). This provision is to be applied without regard to the date 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]
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 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 beginning of the taxable year for which such election is made.

(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 1958, such election shall not apply with respect to the strengthened contracts.
(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 method of revaluation 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.


§ 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...