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risk shall cease to be a risk in connection with the life or health of a resident of such particular foreign country for the policy period in which the insured gives such notice or such circumstances are known to the insurer, and for each subsequent policy period. In determining the country of residence of an insured, the principles of §§ 301.7701(b)–1 through 301.7701(b)–9 of this chapter, relating to the determination of residence and nonresidence in the United States and of foreign residence, shall apply. Citizens of the United States are not residents of the United States merely because of their citizenship. The application of this paragraph may be illustrated by the following example:

Example. Controlled foreign corporation A is a wholly owned subsidiary of domestic corporation M. Corporation A uses the calendar year as the taxable year and is engaged in the life insurance business in foreign country X. In 1963, A Corporation issues ordinary life insurance contracts on the lives of residents of the United States, including one issued on February 1, 1963, to R, a citizen of foreign country Y and a resident of the United States on such date. All activity in connection with the issuing of such contracts is transacted by mail. On May 1, 1963, R abandons his United States residence and establishes residence in foreign country Z. There are no circumstances known to A Corporation that R has changed his residence until R, on March 1, 1964, actually notifies A Corporation of that change. Income of A Corporation for the policy period of February 1, 1963, to January 31, 1964, from issuing such insurance contracts is income derived from the insurance of United States risks. However, income of A Corporation derived for the policy period of February 1, 1964, to January 31, 1965, from R's insurance contract is not income derived from the insurance of United States risks.

(Secs. 913(m) (92 Stat. 3106; 26 U.S.C. 913(m)), and 7805 (68A Stat. 917; 26 U.S.C. 7805), Internal Revenue Code of 1954)

[T.D. 6781, 29 FR 18202, Dec. 23, 1964, as amended by T.D. 7736, 45 FR 76143, Nov. 18, 1980; T.D. 8411, 57 FR 15241, Apr. 27, 1992]

§ 1.953–3 Risks deemed to be United States risks.

(a) *Artificial arrangements.* For purposes of paragraph (a) of § 1.953–1, the term ''United States risks'' also includes under section 953(a)(1)(B) risks which are deemed to be United States risks. They are risks (other than United States risks described in section 953(a)(1)(A) and § 1.953–2) which a controlled foreign corporation reinsures under an insurance or annuity contract, or with respect to which a controlled foreign corporation issues any insurance or annuity contract, in accordance with any arrangement whereby another corporation which is not a controlled foreign corporation receives an amount of premiums (for reinsuring or issuing any insurance or annuity contract in connection with the United States risks described in section 953(a)(1)(A) and § 1.953–2) which is substantially equal to the amount of premiums which the controlled foreign corporation receives under its contracts. Arrangements to which this rule applies include those entered into by the controlled foreign corporation, by its United States shareholders, or by a related person.

(b) *Evidence of arrangements.* The determination of the existence of an arrangement referred to in paragraph (a) of this section shall depend on all the facts and circumstances in each case. In making this determination, it will be recognized that arrangements of this type generally are orally entered into outside the United States and that direct evidence of such an arrangement is not ordinarily available. Therefore, in determining the existence of such an arrangement, consideration will be given to whether or not there is substantial similarity between the type, location, profit margin expected, and loss experience of the risks which the corporation which is not a controlled foreign corporation insures or reinsures and the risks which the controlled foreign corporation insures or reinsures. Further, consideration will be given to the existence of prior similar arrangements between, and the identity of the directors or shareholders of, the corporation which is not a controlled foreign corporation, its shareholders, or related persons and the controlled foreign corporation, its shareholders, or related persons. However, the absence of such prior arrangements or identity of directors or shareholders will not of itself establish the nonexistence of an arrangement referred to in paragraph (a) of this section. In determining whether the

amounts received by the controlled foreign corporation and the corporation which is not a controlled foreign corporation are substantially equal, the period in which the controlled foreign corporation receives premiums need not be the same as, or identical in length with, that of the corporation which is not a controlled foreign corporation nor limited to a taxable year of the controlled foreign corporation.

(c) *Illustrations.* The application of this section may be illustrated by the following examples:

Example 1. Controlled foreign corporation A is a wholly owned subsidiary of domestic corporation M. Foreign corporation B is a wholly owned subsidiary of foreign corporation R. All corporations use the calendar year as the taxable year. Corporations M and R, which are not related persons, agree that from July 1, 1963, through December 31, 1963, B Corporation will reinsure all risks of M Corporation which are United States risks described in section 953(a)(1)(A), and that from January 1, 1964, through June 30, 1964, A Corporation will reinsure all risks of R Corporation which are not United States risks described in section 953(a)(1)(A). The amount of premiums received by A Corporation and B Corporation, respectively, as a result of the agreement are substantially equal. The income of A Corporation derived in 1964 from reinsuring the risks of R Corporation is income derived from the insurance of United States risks described in section 953(a)(1)(B).

Example 2. Assume the same facts as in example 1, except that M and R Corporations also agree, as part of their arrangement, that from July 1, 1964, through December 31, 1964, B Corporation will reinsure all risks of M Corporation which are United States risks described in section 953(a)(1)(A), and that from January 1, 1965, through June 30, 1965, A Corporation will reinsure all risks of R Corporation which are not United States risks described in section 953(a)(1)(A). The amount of premiums derived by B Corporation from July 1, 1963, through December 31, 1963, under the agreement is not substantially equal to the amount of premiums derived by A Corporation from January 1, 1964, through June 30, 1964, and the amount of premiums derived by B Corporation from July 1, 1964, through December 31, 1964, is not substantially equal to the amount of premiums derived by A Corporation from January 1, 1965, through June 30, 1965. However, the aggregate amount of premiums received by B Corporation under the arrangement is substantially equal to the aggregate amount of premiums received by A Corporation. The income of A Corporation derived in 1964 and 1965 from reinsuring the risks of R Corporation is income derived from the insurance of United States risks described in section 953(a)(1)(B).

Example 3. Assume the same facts as in example 1, except that foreign corporation C is also a wholly owned subsidiary of R Corporation. Assume that C Corporation uses the calendar year as its taxable year. Assume further that M Corporation and R Corporation agree that from July 1, 1963, through December 31, 1963, B Corporation and C Corporation together will reinsure the United States risks described in section 953(a)(1)(A) of M Corporation. The amount of premiums received by B Corporation in respect of such United States risks is equal to one-third of the amount received by A Corporation in respect of the risks which are not United States risks described in section 953(a)(1)(A), and the amount of premiums received by C Corporation in respect of such United States risks is equal to two-thirds of the amount so received by A Corporation. The income of A Corporation derived in 1964 from reinsuring the risks of R Corporation is income derived from the insurance of United States risks described in section 953(a)(1)(B).

Example 4. Assume the same facts as in example 3, except that controlled foreign corporation D is also a wholly owned subsidiary of M Corporation and uses the calendar year as its taxable year. Assume further that M Corporation and R Corporation agree that in 1964 R Corporation will pay premiums of $300,000 to A Corporation and $700,000 to D Corporation to reinsure all risks of R Corporation which are not United States risks described in section 953(a)(1)(A), and that in 1963 M Corporation will pay premiums of $400,000 to B Corporation and $600,000 to C Corporation to reinsure all risks of M Corporation which are United States risks described in section 953(a)(1)(A). The income of A Corporation and D Corporation derived in 1964 from reinsuring the risks of R Corporation is income derived from the insurance of United States risks described in section 953(a)(1)(B).

Example 5. Controlled foreign corporation A is a wholly owned subsidiary of domestic insurance corporation M. Controlled foreign corporation B is a wholly owned subsidiary of domestic insurance corporation N. All corporations use the calendar year as the taxable year. As a result of an arrangement between M Corporation and N Corporation, in 1963 A Corporation reinsures all the United States risks described in section 953(a)(1)(A) of N Corporation, and B Corporation reinsures all the United States risks described in section 953(a)(1)(A) of M Corporation. The premiums and other consideration received by A Corporation and B Corporation in respect of such reinsurance are not substantially equal. The income of A Corporation and B Corporation in 1962 from reinsuring the risks of N Corporation and M Corporation, respectively, is income derived from

the insurance of United States risks described in section 953(a)(1)(A) and is not income derived from the insurance or United States risks described in section 953(a)(1)(B).

Example 6. Assume the same facts as in example 5, except that B Corporation is not a controlled foreign corporation. The income of A Corporation in 1963 from reinsuring the risks of N Corporation is income derived from the insurance of United States risks described in section 953(a)(1)(A) and is not income derived from the insurance of United States risks described in section 953(a)(1)(B).

[T.D. 6781, 29 FR 18207, Dec. 23, 1964]

§ 1.953–4 Taxable income to which section 953 applies.

(a) *Taxable income defined*—(1) *Life insurance taxable income.* For a controlled foreign corporation which is engaged in the business of reinsuring or issuing insurance or annuity contracts and which, if it were a domestic corporation engaged only in such business, would be taxable as a life insurance company to which part I (sections 801 through 820) of subchapter L of the Code applies, the term ''taxable income'' means for purposes of paragraph (a) of §1.953–1 the gain from operations, as defined in section 809(b) and as modified by this section, derived from, and attributable to, the insurance of United States risks. For purposes of determining such taxable income, the provisions of section 802(b) (relating to the definition of life insurance company taxable income) shall not apply. Determinations for purposes of this subparagraph shall be made without regard to section 501(a).

(2) *Mutual and other insurance taxable income.* For a controlled foreign corporation which is engaged in the business of reinsuring or issuing insurance or annuity contracts and which, if it were a domestic corporation engaged only in such business, would be taxable as a mutual insurance company to which part II (sections 821 through 826) of subchapter L of the Code applies or a mutual marine insurance or other insurance company to which part III (sections 831 and 832) of subchapter L of the Code applies, the term ''taxable income'' means for purposes of paragraph (a) of §1.953–1 taxable income, as defined in section 832(a) and as modified by this section, derived from, and attributable to, the insurance of United States risks. Determinations for purposes of this subparagraph shall be made without regard to section 501(a).

(3) *Corporations not qualifying as insurance companies.* For special rules applicable under this section in the case of a controlled foreign corporation which, if it were a domestic corporation, would not qualify as an insurance company, see §1.953–5.

(b) *Certain provisions inapplicable.* In determining taxable income under this section, the following provisions of subchapter L of the Code shall not apply:

(1) Section 809(d)(4), relating to the operations loss deduction;

(2) Section 809(d)(5), relating to certain nonparticipating contracts;

(3) Section 809(d)(6), relating to certain accident and health insurance and group life insurance;

(4) Section 809(d)(10), relating to small business deduction;

(5) Section 817(b), relating to gain on property held on December 31, 1958, and certain substituted property acquired after 1958; and

(6) Section 832(c)(5), relating to capital losses.

(c) *Computation of reserves required by law*—(1) *Law applicable in determining reserves.* The reserves which will be taken into account as reserves required by law under section 801(b)(2), both in determining for any taxable year whether a controlled foreign corporation is a controlled foreign corporation described in paragraph (a)(1) or (2) of this section and in determining taxable income of such corporation for the taxable year under paragraph (a) of this section, shall be the following reserves:

(i) *Reserves required by the law of a State.* The reserves which are required by the law of the State or States to which the insurance business of the controlled foreign corporation is subject, but only with respect to its United States business, if any, which is taxable under section 819(a).

(ii) *Reserves deemed to be required.* To the extent of such controlled foreign corporation's insurance business not taxable under section 819(a)—

(*a*) Except as provided in (*b*) of this subdivision (ii), the reserves which would result if such reserves were determined by applying the minimum