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Date:
January 31, 2020

Taxpayer =
Insurer 1 =
Insurer 2 =
Date 1 =
Date 2 =

Dear :

This letter is in response to the request by the authorized representative of Taxpayer for a ruling that for purposes of sections 101(j), 264(f), 7702, and 7702A of the Internal Revenue Code (the "Code"), a reinsurance transaction will not constitute a material change of certain life insurance contracts and will not affect the date the contracts were issued or entered into.

FACTS

Taxpayer is the common parent of a consolidated group of corporations and files its tax return on a calendar year basis. Taxpayer is a publicly traded holding company engaged in financial services through its subsidiaries. On Date 1, certain members of Taxpayer's consolidated group (in aggregate, "Policyholder") entered into letter agreements with Insurer 1 for the issuance of life insurance contracts (each, a "Policy", and together, the "Policies"). The Policies were private placement variable life insurance contracts that insured the lives of selected employees of Policyholder in order to finance certain employee benefit liabilities.

The Policies qualify as life insurance contracts under section 7702. At the time each Policy was issued (1) the individual insured was a director, highly compensated employee, or highly compensated individual of Policyholder within the meaning of section 101(j)(2)(A)(ii) and (2) the individual insured was an officer, director, or employee of Policyholder within the meaning of section 264(f)(4)(A). Before each Policy was issued, the notice and consent requirements of section 101(j)(4) were met.

The Policies provide that upon the occurrence of one of several enumerated events, generally involving an unfavorable or potentially unfavorable development with respect to the condition of the insurer (a "Reinsurance Event"), and at the request of Policyholder and subject to any regulatory requirements, the insurer will use its best efforts to enter into an assumption reinsurance agreement (a "Reinsurance Transaction") with an assuming reinsurer designated by Policyholder (a "Reinsurer") to reinsure the Policies. Any Reinsurer will be licensed to conduct an insurance business in the state or territory in which it is located and in the states and territories in which the Policies were issued.

On Date 2, Insurer 1 was sold and renamed Insurer 2.

A Reinsurance Event occurred, and Policyholder has requested Insurer 2 to use its best efforts to enter into a Reinsurance Transaction. The consummation of the Reinsurance Transaction, however, is contingent on the receipt of the requested ruling.

Taxpayer has represented that:

1. Prior to a Reinsurance Transaction, none of the Policies will have been altered or changed in a manner that would cause them to be treated as newly issued or exchanged for federal income tax purposes.
2. Other than substituting a new insurer, the Policies will not be modified or restructured as a result of a Reinsurance Transaction. The terms and obligations under the Policies will remain unchanged, including the amount and pattern of death benefits, the premium pattern, the interest rate or rates, and the mortality and expense charges guaranteed under the Policies.
3. After a Reinsurance Transaction, Policyholder will have no further recourse against the original insurer except for retained liabilities described in the Policies.

REQUESTED RULING

For purposes of sections 101(j), 264(f), 7702, and 7702A, the reinsurance of the Policies as described above will not constitute a material change of the Policies and will not affect the date each Policy was issued or entered into.

LAW AND ANALYSIS

Law

Section 101(a) generally provides that “[e]xcept as otherwise provided in . . . [section 101(j)], gross income does not include amounts received . . . under a life insurance contract, if such amounts are paid by reason of the death of the insured.”

Section 101(j)(1) provides that, in the case of an employer-owned life insurance contract, the amount excluded from gross income of an applicable policyholder under section 101(a)(1) shall not exceed an amount equal to the sum of the premiums and other amounts paid by the policyholder for the contract. Under section 101(j)(3)(A), an employer-owned life insurance contract is generally a life insurance contract that (i) is owned by a person engaged in a trade or business and under which that person is a beneficiary under the contract and (ii) covers the life of an insured who is an employee on the date the contract is issued. As described in section 101(j)(3)(B), an applicable policyholder is generally a person who owns an employer-owned life insurance contract.

Section 101(j)(2) provides exceptions to the general rule of section 101(j)(1) in the case of certain employer-owned life insurance contracts with respect to which the notice and consent requirements of section 101(j)(4) are satisfied. Such exceptions are available if the insured was, with respect to an applicable policyholder, (i) an employee at any time during the 12-month period before the insured’s death or (ii) a director, a highly compensated employee, or high compensated individual at the time the contract was issued.

Section 264(f)(1) provides that no deduction is allowed for that portion of the taxpayer’s interest expense that is allocable to unborrowed policy cash values.

Section 264(f)(2) describes the portion of the taxpayer’s interest expense that is allocable to “unborrowed policy cash values,” which is described in section 264(f)(3).

Section 264(f)(4) provides an exception to the pro rata interest expense disallowance rule of section 264(f)(1) for certain policies and contracts. Under section 264(f)(4)(A), section 264(f)(1) does not apply to any policy or contract owned by an entity engaged in a trade or business if the policy or contract covers only one individual and if that individual is (at the time first covered by the policy or contract) (i) a 20-percent owner of the entity or (ii) an individual (not described in (i)) who is an officer, director, or employee of the trade or business.

Section 7702 provides a statutory definition that a life insurance contract must meet to be treated as a life insurance contract for federal income tax purposes. More specifically, a contract must be a life insurance contract under applicable law and must

also meet either of two alternative tests: (i) the cash value accumulation test of section 7702(b) or (ii) the guideline premium and cash value corridor test of sections 7702(c) and (d), respectively. Also, under sections 7702(f)(7)(B) through (E), certain changes in benefits during the first 15 years beginning on the issue date of a life insurance contract may trigger cash distributions that receive less favorable tax treatment than distributions after that period.

Section 7702(c)(3)(B) sets limits on the amount of mortality and expense charges that may be taken into account in determining whether an insurance contract satisfies the definition of a life insurance contract under either the cash value accumulation test or the guideline premium test of section 7702.

Section 7702A provides that a contract meeting the requirements of section 7702 is a modified endowment contract for purposes of section 72 if the contract either (i) is entered into on or after June 21, 1988, and fails to meet the 7-pay test of section 7702A(b) or (ii) is received in exchange for a contract described in (i).

Section 7702A(b) states that a contract fails to meet the 7-pay test if the accumulated amount paid under the contract at any time during the first 7 contract years exceeds the sum of the net level premiums that would have been paid on or before such time if the contract provided for paid-up future benefits after the payment of 7 level annual premiums. Section 7702A(c)(1) provides that the determination under section 7702A(b) of the 7 level annual premiums shall be made at the time the contract is issued.

Section 7702A(c)(3)(A) provides that if there is a material change in the benefits under (or other terms of) a contract, such contract is treated as a new contract entered into on the day on which such material change takes effect and appropriate adjustments must be made in determining whether the contract meets the 7-pay test to take into account the cash surrender value of the contract.

Section 7702A(c)(3)(B) states that for purposes of section 7702A(c)(3)(A), a material change includes any increase in the death benefit under the contract or any increase in, or addition of, a qualified additional benefit under the contract, but that a material change does not include any increase that is attributable to the payment of premiums necessary to fund the lowest level of the death benefit and qualified additional benefits payable in the first 7 contract years (determined after taking into account death benefit increases described in subparagraph (A) or (B) of section 7702(e)(2)) or to crediting of interest or other earnings (including policyholder dividends) in respect of such premiums.

Analysis

A material change to a life insurance contract will cause the contract to be considered exchanged for a new life insurance contract, and the new life insurance

contract will be considered newly issued or newly entered into. Such a new life insurance contract will be re-tested to determine whether it meets the tests and criteria described above.

In a Reinsurance Transaction, the Reinsurer will assume all obligations under the Policies, with the exception of a certain limited category of retained liabilities described in the Policies. The terms and obligations of the Policies will remain unchanged, including the amount and pattern of death benefits, the premium pattern, the interest rate or rates, and the mortality and expense charges guaranteed. The Policies that Policyholder will own after a Reinsurance Transaction will be the same Policies that Policyholder originally purchased except for the change in insurer.

RULING

A Reinsurance Transaction will not constitute a material change or an exchange of the Policies for purposes of sections 101(j), 264(f), 7702, and 7702A and will not affect the date the Policies were issued or entered into.

CAVEATS

The ruling contained in this letter is based upon information and representations Taxpayer submitted, accompanied by penalty of perjury statements executed by appropriate parties. This office has not verified any of the material submitted in support of the ruling request, and it is subject to verification on examination.

Except as provided above, no opinion is expressed or implied concerning the federal income tax consequences of any other aspect of this or other transactions or item of income of Taxpayer. This ruling letter is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

A copy of this letter should be attached to the federal income tax return of the taxpayers involved for the taxable year in which the transaction covered by this ruling is consummated.

Pursuant to a power of attorney on file in this office, a copy of this ruling is being furnished to your authorized representatives.

Sincerely,

Dan Phillips
Senior Counsel, Branch 4
Associate Chief Counsel
(Financial Institutions and Products)