

Internal Revenue Service

Department of the Treasury
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Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
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PLR-122451-14

Date:
July 15, 2014

LEGEND:

Parent =

LifeSub1 =

LifeSub2 =

State1 =

State2 =

Group of Businesses =

Contracts =

Contractholders =

Business Activities =

Year =

Dear _____ :

This is in reply to your request for a ruling that the transfer of Contracts from LifeSub1 and LifeSub2 to a potential Reinsurer, pursuant to an assumption reinsurance agreement, will not (1) affect the date the Contracts were issued, entered into, purchased, or came into existence or (2) require re-testing the Contracts or the start of new test periods.

Parent is a publicly traded corporation organized under State1. It is a holding company that owns Group of Businesses and files its federal income tax returns on a calendar year basis as the common parent of a life/non-life consolidated group of companies.

LifeSub1 and LifeSub2 are a State2 companies taxed as life insurance companies under Part I of Subchapter L of the Internal Revenue Code. Both are wholly-owned indirect subsidiaries of Parent and are part of its life subgroup. LifeSub1 and LifeSub2 issued Contracts.

Parent has decided to focus exclusively on Business Activities and, since Year, has been exiting its life insurance business. Accordingly, pursuant to a yet to be agreed upon assumption reinsurance contract with a potential Reinsurer (an unrelated life insurance company) and, subject to required state regulatory approval and the consent of the Contractholders, Parent will transfer the Contracts to Reinsurer.

The taxpayer makes the following representations:

- Contracts are life insurance contracts under the laws of the jurisdiction in which they were issued.
- Other than substituting a new insurer for LifeSub1 or LifeSub2, as applicable, the Contracts will not be modified or restructured as a result of the assumption transaction, and all terms of the Contracts will remain unchanged, including the amount and pattern of death benefit, the premium pattern, the rate or rates, and mortality and expense charges guaranteed under the Contracts.
- The assumption transaction will not be implemented without approval by insurance regulatory authorities in each of the applicable jurisdictions.
- Reinsurer will be licensed to conduct an insurance business in the state in which it is located and in the states and territories in which the reinsured contracts were issued.

ISSUE

Whether the assumption reinsurance agreement between Parent and Reinsurer constitutes a “material change” to the existing policies causing them to be (1) treated as “exchanged” for new policies, newly “issued” or “entered into” or “reissued” and therefore subject to new tax rules, (2) re-tested under the rules applicable when they were originally issued, or (3) subject to the start of new test periods.

LAW

Reinsurance is “insurance for insurance companies.” Atkinson & Dallas, LIFE INSURANCE PRODUCTS AND FINANCE (Soc. Of Actuaries 2000) at 384.

Describing assumption reinsurance, the United States Supreme Court stated:

[T]he reinsurer steps into the shoes of the ceding company with respect to the reinsured policy, assuming all its liabilities and its responsibility to maintain required reserves against potential claims. The assumption reinsurer thereafter receives all premiums directly and becomes directly liable to the holders of the policies it has reinsured

Colonial Am. Life Ins. Co. v. Commissioner, 491 U.S. 244, 247 (1989).

Treas. Reg. § 1.809-5(a)(7)(ii) defines assumption reinsurance as “an arrangement whereby another person (the reinsurer) becomes solely liable to the policyholders on the contracts transferred by the taxpayer. Such term does not include indemnity reinsurance or reinsurance ceded.”

In general, the tax rules that applies to a contract depends on when a contract was “issued” or “entered into”. The contract is then “grandfathered” under those rules (*i.e.*, not subject to changes in the tax law that apply to policies “issued” or entered into” on or after an effective date). However, certain life insurance provisions of the Code provide that, if there is a “material change” to a policy, it loses its “grandfathered” status and (1) is subject to the new provision; (2) must be re-tested; or (3) new test periods commence.

ANALYSIS

Among other reasons, insurance companies enter assumption reinsurance contracts to completely withdraw from a line of business.

Policyholders must consent to an assumption reinsurance arrangement but do not initiate it. Also, although the reinsurer replaces the direct writer for all purposes of the contract, assumption reinsurance does not cancel the original policy in exchange for a new one nor change the existing contractual obligations of the underlying life insurance policies.

After Reinsurer assumes all obligations under the Contracts, their terms -- including the amount and pattern of death benefit, the premium pattern, the rate guaranteed on the issuance of the contract, and the mortality and expense charges -- will remain the same.

The assumption reinsurance agreement between Parent and Reinsurer does not constitute a "material change" or an exchange of Contracts for new policies for purposes of §§ 72, 101(f), 101(j), 264, 7702, and 7702A causing them to lose their "grandfathered" status. Accordingly, the assumption reinsurance agreement, will not (1) affect the date the Contracts were issued, entered into, purchased, or came into existence; (2) require retesting the Contracts; or (3) require the start of new test periods.

Sincerely,

DONALD J. DREES, JR.
Senior Technician Reviewer (CC:FIP:B04)