



Instructions for Form 1120-L

U.S. Life Insurance Company Income Tax Return

Section references are to the Internal Revenue Code unless otherwise noted.

Contents	Page
Photographs of Missing Children	1
Unresolved Tax Issues	1
How To Get Forms and Publications	2
IRS E-Services	2
General Instructions	2
Purpose of Form	2
Who Must File	2
Where To File	2
Definitions	2
When To File	3
Who Must Sign	3
Paid Preparer Authorization	3
Other Forms That May Be Required	3-4
Consolidated Return	4
Statements	4
Assembling the Return	4
Accounting Methods	4
Accounting Periods	5
Rounding Off to Whole Dollars	5
Recordkeeping	5
Depository Methods of Tax Payment	5
Estimated Tax Payments	5
Interest and Penalties	5
Specific Instructions	6
Period Covered	6
Address	6
Employer Identification Number	6
Item A(2)	6
Item D	6
Item E	6
Life Insurance Company Taxable Income	6-10
Schedule A	10-12
Schedule B	12
Schedule C	12
Schedule E	13
Schedule F	13-14
Schedule G	14
Schedule H	14
Schedule I	15
Schedule J, Part I	15
Schedule J, Part II	15
Schedule K	15-18
Schedule L	18
Schedule M	18
Index	20

What's New

- When the 2004 Form 1120-L was released to the public, the differential earnings rate for 2004 had not yet been determined. The Secretary of the Treasury will announce the 2004 differential earnings rate in early 2005.
- Section 809 is repealed for tax years beginning after December 31, 2004. Therefore, for 2004, only mutual life

insurance companies are required to file Form 8390, Information Return for Determination of Life Insurance Company Earnings Rate Under Section 809; mutual life insurance companies compute a differential earnings amount to use to determine policyholder dividends. See the instructions for Schedules C and E on pages 12 and 13.

- Charitable contributions made in January 2005 for the relief of victims in areas affected by the Indian Ocean tsunami may be treated as if made on December 31, 2004.

- Corporations can file new Form 8895, Section 965(f) Election for Corporations that are U.S. Shareholders of a Controlled Foreign Corporation, to elect the 85% dividends-received deduction on repatriated dividends received under section 965. Changes are made to Form 1120-L, Schedule A.

- For tax years beginning after October 22, 2004, corporations can elect to be taxed on income from qualifying shipping activities using an alternative tax method. See page 6.

- Corporations can elect to deduct a limited amount of business start-up and organizational costs paid or incurred after October 22, 2004. See page 7.

- For charitable contributions of certain property made after June 3, 2004, a corporation must file Form 8283 and obtain a qualified appraisal if claiming a deduction of more than \$5,000. See page 9.

- For charitable contributions of patents and certain other intellectual property made after June 3, 2004, corporations will receive a reduced deduction but can deduct certain qualified donee income. See page 9.

- Special rules apply to charitable contributions after 2004 of used motor vehicles, boats, or airplanes with a claimed value of more than \$500. See section 170(f)(12).

- The deduction for certain travel, meals, and entertainment expenses incurred after October 22, 2004, is limited to the amount treated as compensation to officers, directors, and more-than-10% shareholders. See section 274(e)(2).

- If the corporation is an expatriated entity or a partner in an expatriated entity, the corporation's taxable income cannot be less than its inversion gain for the tax year. See section 7874.

Photographs of Missing Children

The Internal Revenue Service is a proud partner with the National Center for Missing and Exploited Children. Photographs of

missing children selected by the Center may appear in instructions on pages that would otherwise be blank. You can help bring these children home by looking at the photographs and calling 1-800-THE-LOST (1-800-843-5678) if you recognize a child.

Unresolved Tax Issues

If the corporation has attempted to deal with an IRS problem unsuccessfully, it should contact the Taxpayer Advocate. The Taxpayer Advocate independently represents the corporation's interests and concerns within the IRS by protecting its rights and resolving problems that have not been fixed through normal channels.

While Taxpayer Advocates cannot change the tax law or make a technical tax decision, they can clear up problems that resulted from previous contacts and ensure that the corporation's case is given a complete and impartial review.

The corporation's assigned personal advocate will listen to its point of view and will work with the corporation to address its concerns. The corporation can expect the advocate to provide:

- A "fresh look" at a new or ongoing problem.
- Timely acknowledgment.
- The name and phone number of the individual assigned to its case.
- Updates on progress.
- Timeframes for action.
- Speedy resolution.
- Courteous service.

When contacting the Taxpayer Advocate, the corporation should be prepared to provide the following information.

- The corporation's name, address, and employer identification number (EIN).
- The name and telephone number of an authorized contact person and the hours he or she can be reached.
- The type of tax return and year(s) involved.
- A detailed description of the problem.
- Previous attempts to solve the problem and the office that was contacted.
- A description of the hardship the corporation is facing and verifying documentation (if applicable).

The corporation can contact a Taxpayer Advocate by calling 1-877-777-4778 (toll free). Persons who have access to TTY/TDD equipment can call 1-800-829-4059 and ask for Taxpayer Advocate assistance. If the corporation prefers, it can call, write, or fax the Taxpayer Advocate office in its area. See Pub. 1546, The Taxpayer Advocate Service of the IRS, for a list of addresses and fax numbers.

How To Get Forms and Publications

Personal computer

You can access the IRS website 24 hours a day, 7 days a week, at www.irs.gov to:

- Order IRS products online.
- Download forms, instructions, and publications.
- See answers to frequently asked tax questions.
- Search publications online by topic or keyword.
- Send us comments or request help by email.
- Sign up to receive local and national tax news by email.

You can also reach us using file transfer protocol at [ftp.irs.gov](ftp://ftp.irs.gov).

CD-ROM

Order Pub. 1796, Federal Tax Products on CD-ROM, and get:

- Current year forms, instructions, and publications.
- Prior year forms, instructions, and publications.
- Frequently requested tax forms that can be filled in electronically, printed out for submission, and saved for recordkeeping.
- The Internal Revenue Bulletin.

Buy the CD-ROM on the Internet at www.irs.gov/cdorders from the National Technical Information Service (NTIS) for \$22 (no handling fee) or call 1-877-CDFORMS (1-877-233-6767) toll free to buy the CD-ROM for \$22 (plus a \$5 handling fee).

By Phone and in Person

You can order forms and publications by calling 1-800-TAX-FORM (1-800-829-3676). You can also get most forms and publications at your local IRS office.

IRS E-Services Make Taxes Easier

Now more than ever before, businesses can enjoy the benefits of filing and paying their federal taxes electronically. Whether you rely on a tax professional or handle your own taxes, the IRS offers you convenient programs to make taxes easier.

- You can *e-file* your Form 940 and 941 employment tax returns, Form 1099, and other information returns. Visit www.irs.gov/efile for more information.
- You can pay taxes online or by phone using the free Electronic Federal Tax Payment System (EFTPS). Visit www.eftps.gov or call 1-800-555-4477 for more information.

Use these electronic options to make filing and paying taxes easier.

General Instructions

Purpose of Form

Use Form 1120-L, U.S. Life Insurance Company Income Tax Return, to report the income, gains, losses, deductions, credits, and to figure the income tax liability of life insurance companies.

Who Must File

Every domestic life insurance company and every foreign corporation that would qualify as a life insurance company if it were a U.S. corporation must file Form 1120-L. This includes organizations described in section 501(m)(1) that provide commercial-type life insurance.

Mutual savings banks conducting life insurance business

Mutual savings banks conducting life insurance business and meeting the requirements of section 594 are subject to an alternative tax consisting of:

- A partial tax computed on Form 1120, U.S. Corporation Income Tax Return, on the taxable income of the bank excluding the life insurance department and
- A partial tax on the taxable income computed on Form 1120-L of the life insurance department.

Enter the combined tax on line 3 of Schedule J, Form 1120. File Form 1120 and attach Form 1120-L as a schedule (and identify it as such) or attach a statement showing the computation of the taxable income of the life insurance department (including all relevant information that would be reported on Form 1120-L).

Foreign life insurance companies

A foreign life insurance company that sells a U.S. real property interest must file Form 1120-L and Schedule D (Form 1120) to report the sale. Gain or loss from the sale of a U.S. real property interest is considered effectively connected with the conduct of a U.S. business, even though the foreign life insurance company does not carry on any insurance business in the United States and is not otherwise required to file a U.S. income tax return. See sections 842 and 897, and the Schedule K, line 9, instructions on page 17 for additional information.

Other insurance companies

Insurance companies, other than life insurance companies, should file Form 1120-PC, U.S. Property and Casualty Insurance Company Income Tax Return. A burial or funeral benefit insurance company that directly manufactures funeral supplies or performs funeral services is taxable under section 831 and should file Form 1120-PC.

Definitions

An "insurance company" means any corporation if more than half of its business during the tax year is from the issuance of insurance or annuity contracts or the

Where To File

File the corporation's return at the applicable IRS address listed below.

If the corporation's principal business, office, or agency is located in:	And the total assets at the end of the tax year (Form 1120-L, Schedule L, Part I, line 6, column (b)) are:	Use the following Internal Revenue Service Center address:
Connecticut, Delaware, District of Columbia, Illinois, Indiana, Kentucky, Maine, Maryland, Massachusetts, Michigan, New Hampshire, New Jersey, New York, North Carolina, Ohio, Pennsylvania, Rhode Island, South Carolina, Vermont, Virginia, West Virginia, Wisconsin	Less than \$10 million	Cincinnati, OH 45999-0012
	\$10 million or more	Ogden, UT 84201-0012
Alabama, Alaska, Arizona, Arkansas, California, Colorado, Florida, Georgia, Hawaii, Idaho, Iowa, Kansas, Louisiana, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New Mexico, North Dakota, Oklahoma, Oregon, South Dakota, Tennessee, Texas, Utah, Washington, Wyoming	Any amount	Ogden, UT 84201-0012
A foreign country or U.S. possession (or the corporation is claiming the possessions corporation tax credit under sections 30A and 936)	Any amount	Philadelphia, PA 19255-0012

A group of corporations with members located in more than one service center area will often keep all the books and records at the principal office of the managing corporation. In this case, the tax returns of the corporations may be filed with the service center for the area in which the principal office of the managing corporation is located.

reinsuring of risks underwritten by insurance companies.

A "life insurance company" is an insurance company in the business of issuing life insurance and annuity contracts either separately or combined with health and accident insurance, or noncancelable contracts of health and accident insurance that meet the reserves test in section 816(a). Guaranteed renewable life, health, and accident insurance that the corporation cannot cancel but reserves the right to adjust premium rates by classes, according to experience under the kind of policy involved, are treated as noncancelable.

The "reserves test" requires that life insurance reserves, as defined in section 816(b), plus unearned premiums and unpaid losses (whether or not ascertained) on noncancelable life, health, or accident policies not included in life insurance reserves must make up more than 50% of total reserves as defined in section 816(c). When determining whether the reserves test has been met:

1. Life insurance reserves and total reserves must each be reduced by an amount equal to the mean of the aggregates, at the beginning and end of the tax year, of the policy loans outstanding with respect to contracts for which life insurance reserves are maintained;
2. Amounts set aside and held at interest to satisfy obligations under contracts which do not contain permanent guarantees with respect to life, accident, or health contingencies must not be included in either life insurance reserves (section 816(c)(1)) or other reserves required by law (section 816(c)(3)); and
3. Deficiency reserves must not be included in either life insurance reserves or total reserves.

When To File

Generally, a corporation must file its income tax return by the 15th day of the 3rd month after the end of its tax year. A new corporation filing a short-period return must generally file by the 15th day of the 3rd month after the short period ends. A corporation that has dissolved must generally file by the 15th day of the 3rd month after the date it dissolved.

If the due date falls on a Saturday, Sunday, or legal holiday, the corporation can file on the next business day.

Private delivery services. Corporations can use certain private delivery services designated by the IRS to meet the "timely mailing as timely filing/paying" rule for tax returns and payments. These private delivery services include only the following.

- DHL Express (DHL): DHL Same Day Service, DHL Next Day 10:30 am, DHL Next Day 12:00 pm, DHL Next Day 3:00 pm, and DHL 2nd Day Service.
- Federal Express (FedEx): FedEx Priority Overnight, FedEx Standard Overnight, FedEx 2Day, FedEx International Priority, and FedEx International First.
- United Parcel Service (UPS): UPS Next Day Air, UPS Next Day Air Saver, UPS 2nd Day Air, UPS 2nd Day Air A.M., UPS Worldwide Express Plus, and UPS Worldwide Express.

The private delivery service can tell you how to get written proof of the mailing date.



Private delivery services cannot deliver items to P.O. boxes. You must use the U.S. Postal Service to mail any item to an IRS P.O. box address.

Extension. File Form 7004, Application for Automatic Extension of Time To File Corporation Income Tax Return, to request a 6-month extension of time to file.

Who Must Sign

The return must be signed and dated by:

- The president, vice-president, treasurer, assistant treasurer, chief accounting officer or
- Any other corporate officer (such as tax officer) authorized to sign.

If a return is filed on behalf of a corporation by a receiver, trustee, or assignee, the fiduciary must sign the return, instead of the corporate officer. Returns and forms signed by a receiver or trustee in bankruptcy on behalf of a corporation must be accompanied by a copy of the order or instructions of the court authorizing signing of the return or form.

If an employee of the corporation completes Form 1120-L, the paid preparer's space should remain blank. Anyone who prepares Form 1120-L but does not charge the corporation should not complete that section. Generally, anyone who is paid to prepare the return must sign it and fill in the "Paid Preparer's Use Only" area.

The paid preparer must complete the required preparer information and—

- Sign the return in the space provided for the preparer's signature.
- Give a copy of the return to the taxpayer.

Note. A paid preparer may sign original returns, amended returns, or requests for filing extensions by rubber stamp, mechanical device, or computer software program.

Paid Preparer Authorization

If the corporation wants to allow the IRS to discuss its 2004 tax return with the paid preparer who signed it, check the "Yes" box in the signature area of the return. This authorization applies only to the individual whose signature appears in the "Paid Preparer's Use Only" section of the corporation's return. It does not apply to the firm, if any, shown in that section.

If the "Yes" box is checked, the corporation is authorizing the IRS to call the paid preparer to answer any questions that may arise during the processing of its return. The corporation is also authorizing the paid preparer to:

- Give the IRS any information that is missing from the return,
- Call the IRS for information about the processing of the return or the status of any related refund or payment(s), and
- Respond to certain IRS notices that the corporation has shared with the preparer about math errors, offsets, and return preparation. The notices will not be sent to the preparer.

The corporation is not authorizing the paid preparer to receive any refund check, bind the corporation to anything (including

any additional tax liability), or otherwise represent the corporation before the IRS. If the corporation wants to expand the paid preparer's authorization, see Pub. 947, Practice Before the IRS and Power of Attorney.

The authorization cannot be revoked. However, the authorization will automatically end no later than the due date (excluding extensions) for filing the corporation's 2005 tax return.

Other Forms That May Be Required

The life insurance company may have to file some of the forms listed below. See the form for more information.

For a list of additional forms the life insurance company may need to file, see *Other Forms That May Be Required* in the Instructions for Forms 1120 and 1120-A.

- **Form W-2**, Wage and Tax Statement. Use this form to report wages, tips, other compensation, withheld income, social security, and Medicare taxes for employees.
 - **Form 720**, Quarterly Federal Excise Tax Return. Use this form to report and pay environmental taxes, communications and air transportation taxes, fuel taxes, manufacturers taxes, ship passenger taxes, and certain other excise taxes.
 - **Form 851**, Affiliations Schedule. The parent corporation of an affiliated group of corporations must attach this form to its consolidated return. If this is the first year one or more subsidiaries are being included in a consolidated return, also see Form 1122, Authorization and Consent of Subsidiary Corporation To Be Included in a Consolidated Income Tax Return, below.
 - **Form 941**, Employer's Quarterly Federal Tax Return. Employers must file this form to report income tax withheld, and employer and employee social security and Medicare taxes. Also, see *Trust fund recovery penalty* on page 6.
 - **Form 945**, Annual Return of Withheld Federal Income Tax. File Form 945 to report income tax withheld from nonpayroll distributions or payments, including pensions, annuities, IRAs, gambling winnings, and backup withholding. Also, see *Trust fund recovery penalty* on page 6.
 - **Form 1042-S**, Foreign Person's U.S. Source Income Subject to Withholding.
 - **Form 1099-MISC**, Miscellaneous Income. Use this form to report payments: to providers of health and medical services, of rent or royalties, nonemployee compensation, etc.
- Note.** Every corporation must file Form 1099-MISC if it makes payments of rents, commissions, or other fixed or determinable income (see section 6041) totaling \$600 or more to any one person in the course of its trade or business during the calendar year.
- **Form 1122**, Authorization and Consent of Subsidiary Corporation To Be Included in a Consolidated Income Tax Return. File this form if this is the first year a consolidated return is being filed.
 - **Form 5471**, Information Return of U.S. Persons With Respect to Certain Foreign Corporations. This form is filed by a domestic life insurance company that controls a foreign corporation; acquires,

disposes of, or owns 10% or more in value or vote of the outstanding stock of a foreign corporation; or had control of a foreign corporation for an uninterrupted period of at least 30 days during the annual accounting period of the foreign corporation. See Question 4 of Schedule N (Form 1120).

• **Form 5472**, Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business. This form is filed by a domestic life insurance company that is 25% or more foreign-owned. See Question 8 on page 18.

• **Form 8302**, Electronic Deposit of Tax Refund of \$1 Million or More. This form must be filed to request an electronic deposit of a tax refund of \$1 million or more.

• **Form 8390**, Information Return for Determination of Life Insurance Company Earnings Rate Under Section 809. This form is used to gather information regarding the earnings rates of the 50 largest domestic stock life insurance companies (stock companies), as determined by the IRS, and all domestic mutual life insurance companies (mutual companies).

• **Form 8621**, Return by a Shareholder of a Passive Foreign Investment Company or Qualified Electing Fund. A domestic life insurance company uses this form to make certain elections by shareholders in a passive foreign investment company and to figure certain deferred taxes.

• **Form 8816**, Special Loss Discount Account and Special Estimated Tax Payments for Insurance Companies. This form must be filed by any insurance company that elects to take an additional deduction under section 847.

• **Form 8865**, Return of U.S. Persons With Respect to Certain Foreign Partnerships. A domestic life insurance company may have to file Form 8865 if it:

1. Controlled a foreign partnership (owned more than a 50% direct or indirect interest in the partnership).
2. Owned at least a 10% direct or indirect interest in a foreign partnership while U.S. persons controlled that partnership.
3. Had an acquisition, disposition, or change in proportional interest in a foreign partnership that:
 - a. Increased its direct interest to at least 10% or reduced its direct interest of at least 10% to less than 10%.
 - b. Changed its direct interest by at least a 10% interest.
4. Contributed property to a foreign partnership in exchange for a partnership interest if:

- a. Immediately after the contribution, the domestic life insurance company owned, directly or indirectly, at least a 10% interest in the foreign partnership or

- b. The fair market value of the property the domestic life insurance company contributed to the foreign partnership, when added to other contributions of property made to the foreign partnership during the preceding 12-month period, exceeds \$100,000.

The domestic life insurance company may also have to file Form 8865 to report certain dispositions by a foreign partnership of property it previously contributed to that

partnership if it was a partner at the time of the disposition.

For more details, including penalties for failing to file Form 8865, see Form 8865 and its separate instructions.

• **Form 8895**, Section 965(f) Election for Corporations that are U.S. Shareholders of a Controlled Foreign Corporation. Use this form to elect the 85% dividends-received deduction on repatriated dividends under section 965.

Consolidated Return

If an affiliated group of corporations includes one or more domestic life insurance companies taxed under section 801, the common parent may elect to treat those life insurance companies as includible corporations. The life insurance companies must have been members of the group for the 5 tax years immediately preceding the tax year for which the election is made. See section 1504(c)(2) and Regulations section 1.1502-47(d)(12).

Note. If an election under section 1504(c)(2) is in effect for an affiliated group for the tax year, all items of members of the group that are not life insurance companies must not be taken into account in figuring the tentative life insurance company taxable income (LICTI) of members that are life insurance companies.

File supporting statements for each corporation included in the consolidated return. Do not use Form 1120-L as a supporting statement. On the supporting statement, use columns to show the following, both before and after adjustments.

1. Items of gross income and deductions.
2. A computation of taxable income.
3. Balance sheets as of the beginning and end of the tax year.
4. A reconciliation of income per books with income per return.
5. A reconciliation of retained earnings.

Enter the totals for the consolidated group on Form 1120-L. Attach consolidated balance sheets and a reconciliation of consolidated retained earnings. For more information on consolidated returns, see the regulations under section 1502.

Note. If a nonlife insurance company is a member of an affiliated group, file Form 1120-PC as an attachment to the consolidated return in lieu of filing supporting statements. Across the top of page 1 of Form 1120-PC, write "Supporting Statement to Consolidated Returns."

Statements

NAIC Annual Statement. Regulations section 1.6012-2(c) requires that the NAIC Annual Statement be filed with Form 1120-L. A penalty for the late filing of a return may be imposed for not including the annual statement when the return is filed.

Reconciliation. A schedule must be attached that reconciles the NAIC Annual Statement to Form 1120-L.

Stock ownership in foreign personal holding companies (FPHC). Attach the statement required by section 551(c) if:

1. The corporation owned 5% or more in value of the outstanding stock of a FPHC and

2. The corporation was required to include in its gross income any undistributed FPHC income from a FPHC.

Transfers to a corporation controlled by the transferor. If a person receives stock of a corporation in exchange for property, and no gain or loss is recognized under section 351, the person (transferor) and the transferee must attach to their tax returns the information required by Regulations section 1.351-3.

Assembling the Return

To ensure that the corporation's tax return is correctly processed, attach all schedules and other forms after page 8, Form 1120-L, and in the following order:

1. Schedule N (Form 1120).
2. Form 8302.
3. Form 4136.
4. Form 4626.
5. Form 851.
6. Additional schedules in alphabetical order.
7. Additional forms in numerical order.

Complete every applicable entry space on Form 1120-L. Do not enter "See Attached" instead of completing the entry spaces. If more space is needed on the forms or schedules, attach separate sheets using the same size and format as on the printed forms. If there are supporting statements and attachments, arrange them in the same order as the schedules or forms they support and attach them last. Show the totals on the printed forms. Also be sure to enter the corporation's name and EIN on each supporting statement or attachment.

Accounting Methods

The return of a life insurance company must be filed using the accrual method of accounting or, to the extent permitted under regulations, a combination of the accrual method with any other method, except the cash receipts and disbursements method. In all cases, the method used must clearly show LICTI.

Accrual method. Under the accrual method, an amount is includable in income when:

1. All the events have occurred that fix the right to receive the income, which is the earliest of the date: (a) the required performance takes place, (b) payment is due, or (c) payment is received and
2. The amount can be determined with reasonable accuracy.

See Regulations section 1.451-1(a) for details.

Generally, an accrual basis taxpayer can deduct accrued expenses in the tax year when:

- All events that determine the liability have occurred,
- The amount of the liability can be figured with reasonable accuracy, and
- Economic performance takes place with respect to the expense.

There are exceptions to the economic performance rule for certain items, including

recurring expenses. See section 461(h) and the related regulations for the rules for determining when economic performance takes place.

Change in Accounting Method

To change its method of accounting used to report taxable income (for income as a whole or for the treatment of any material item), the corporation must file Form 3115, Application for Change in Accounting Method. For more information, see Form 3115 and Pub. 538, Accounting Periods and Methods.

Section 481(a) adjustment. The corporation may have to make an adjustment under section 481(a) to prevent amounts of income or expense from being duplicated or omitted. The section 481(a) adjustment period is generally 1 year for a negative adjustment and 4 years for a net positive adjustment. However, a corporation can elect to use a 1-year adjustment period if the net section 481(a) adjustment for the change is less than \$25,000. The corporation must complete the appropriate lines of Form 3115 to make the election.

Include any net positive section 481(a) adjustment on page 1, line 7. If the net section 481(a) adjustment is negative, report it on page 1, line 18.

Accounting Periods

An insurance company must figure its taxable income on the basis of a tax year. A tax year is the annual accounting period an insurance company uses to keep its records and report its income and expenses.

As a general rule under section 843, the tax year for every insurance company is the calendar year. However, if an insurance company joins in the filing of a consolidated return, it may adopt the tax year of the common parent corporation even if that year is not a calendar year.

Rounding Off to Whole Dollars

The corporation can round off cents to whole dollars on its return and schedules. If the corporation does round to whole dollars, it must round all amounts. To round, drop amounts under 50 cents and increase amounts from 50 to 99 cents to the next dollar (for example, \$1.39 becomes \$1 and \$2.50 becomes \$3).

If two or more amounts must be added to figure the amount to enter on a line, include cents when adding the amounts and round off only the total.

Recordkeeping

Keep the corporation's records for as long as they may be needed for the administration of any provision of the Internal Revenue Code. Usually, records that support an item of income, deduction, or credit on the return must be kept for 3 years from the date the return is due or filed, whichever is later. Keep records that verify the corporation's basis in property for as long as they are needed to figure the basis of the original or replacement property.

The corporation should keep copies of any returns filed. They help in preparing future and amended returns.

Depository Methods of Tax Payment

The corporation must pay the tax due in full no later than the 15th day of the 3rd month after the end of the tax year. The two methods of depositing corporate income taxes are discussed below.

Electronic Deposit Requirement

The corporation must make electronic deposits of all depository taxes (such as employment tax, excise tax, and corporate income tax) using the Electronic Federal Tax Payment System (EFTPS) in 2005 if:

- The total deposits of such taxes in 2003 were more than \$200,000 or
- The corporation was required to use EFTPS in 2004.

If the corporation is required to use EFTPS and fails to do so, it may be subject to a 10% penalty. If the corporation is not required to use EFTPS, it can participate voluntarily. To enroll in or get more information about EFTPS, call 1-800-555-4477 or 1-800-945-8400. To enroll online, visit www.eftps.gov.

Depositing on time. For EFTPS deposits to be made timely, the corporation must initiate the transaction at least 1 business day before the date the deposit is due.

Deposits With Form 8109

If the corporation does not use EFTPS, deposit corporation income tax payments (and estimated tax payments) with Form 8109, Federal Tax Deposit Coupon. If you do not have a preprinted Form 8109, use Form 8109-B to make deposits. You can get this form by calling 1-800-829-4933. Be sure to have your EIN ready when you call.

Do not send deposits directly to an IRS office; otherwise, the corporation may have to pay a penalty. Mail or deliver the completed Form 8109 with the payment to an authorized depository (a commercial bank or other financial institution authorized to accept federal tax deposits). Make checks or money orders payable to that depository.

If the corporation prefers, it can mail the coupon and payment to Financial Agent, Federal Tax Deposit Processing, P.O. Box 970030, St. Louis, MO 63197. Make the check or money order payable to "Financial Agent."

To help ensure proper crediting, enter the corporation's employer identification number, the tax period to which the deposit applies, and "Form 1120-L" on the check or money order. Be sure to darken the "1120" box under "Type of Tax" and the appropriate "Quarter" box under "Tax Period" on the coupon. Records of these deposits will be sent to the IRS. For more information, see "Marking the Proper Tax Period" in the instructions for Form 8109.

For more information on deposits, see the instructions in the coupon booklet (Form 8109) and Pub. 583, Starting a Business and Keeping Records.



If the corporation owes tax when it files Form 1120-L, do not include the payment with the tax return. Instead, mail or deliver the payment with Form 8109 to an authorized depository, or use EFTPS, if applicable.

Estimated Tax Payments

Generally, the following rules apply to the corporation's payments of estimated tax.

- The corporation must make installment payments of estimated tax if it expects its total tax for the year (less applicable credits) to be \$500 or more.
- The installments are due by the 15th day of the 4th, 6th, 9th, and 12th months of the tax year. If any date falls on a Saturday, Sunday, or legal holiday, the installment is due on the next regular business day.
- Use Form 1120-W, Estimated Tax for Corporations, as a worksheet to compute estimated tax.
- If the corporation does not use EFTPS, use the deposit coupons (Forms 8109) to make deposits of estimated tax.

For more information on estimated tax payments, including penalties that apply if the corporation fails to make required payments, see the instructions for line 30 on page 10.

Overpaid Estimated Tax

If the corporation overpaid estimated tax, it may be able to get a quick refund by filing Form 4466, Corporation Application for Quick Refund of Overpayment of Estimated Tax. The overpayment must be at least 10% of the corporation's expected income tax liability and at least \$500. File Form 4466 after the end of the corporation's tax year, and no later than the 15th day of the third month after the end of the tax year. Form 4466 must be filed before the corporation files its income tax return.



Foreign insurance companies, see Notice 90-13, 1990-1 C.B. 321, before computing estimated tax.

Interest and Penalties

Interest. Interest is charged on taxes paid late even if an extension of time to file is granted. Interest is also charged on penalties imposed for failure to file, negligence, fraud, substantial valuation misstatements, and substantial understatements of tax from the due date (including extensions) to the date of payment. The interest charge is figured at a rate determined under section 6621.

Penalty for late filing of return. A corporation that does not file its tax return by the due date, including extensions, may have to pay a penalty of 5% of the unpaid tax for each month or part of a month the return is late, up to a maximum of 25% of the unpaid tax. The minimum penalty for a return that is over 60 days late is the smaller of the tax due or \$100. The penalty will not be imposed if the corporation can show that the failure to file on time was due to reasonable cause. Corporations that file late should attach a statement explaining reasonable cause.

Penalty for late payment of tax. A corporation that does not pay the tax when

due generally may have to pay a penalty of $\frac{1}{2}$ of 1% of the unpaid tax for each month or part of a month the tax is not paid, up to a maximum of 25% of the unpaid tax. The penalty will not be imposed if the corporation can show that the failure to pay on time was due to reasonable cause.

Trust fund recovery penalty. This penalty may apply if certain excise, income, social security, and Medicare taxes that must be collected or withheld are not collected or withheld, or these taxes are not paid. These taxes are generally reported on Form 720, Quarterly Federal Excise Tax Return, Form 941, Employer's Quarterly Federal Tax Return, or Form 945, Annual Return of Withheld Federal Income Tax (see *Other Forms That May Be Required* on page 3). The trust fund recovery penalty may be imposed on all persons determined by the IRS to have been responsible for collecting, accounting for, and paying over these taxes, and who acted willfully in not doing so. The penalty is equal to the unpaid trust fund tax. See the instructions for Form 720 or Pub. 15 (Circular E), Employer's Tax Guide, for details, including the definition of responsible persons.

Other penalties. Other penalties can be imposed for negligence, substantial understatement of tax, and fraud. See sections 6662 and 6663.

Specific Instructions

Period Covered

Section 843 requires all insurance companies to file on a calendar year basis, unless they join in the filing of a consolidated return. If a consolidated return is filed, indicate the period covered on the parent corporation's return.

Address

Include the suite, room, or other unit number after the street address. If the post office does not deliver mail to the street address and the corporation has a P.O. box, show the box number instead.

If the corporation receives its mail in care of a third party (such as an accountant or an attorney), enter on the street address line "C/O" followed by the third party's name and street address or P.O. box.

Employer Identification Number (EIN)

Enter the corporation's EIN. If the corporation does not have an EIN, it must apply for one. An EIN can be applied for:

- Online—Click on the EIN link at www.irs.gov/businesses/small. The EIN is issued immediately once the application information is validated.
- By telephone at 1-800-829-4933 from 7:00 a.m. to 10:00 p.m. in the corporation's local time zone.
- By mailing or faxing Form SS-4, Application for Employer Identification Number.

If the corporation has not received its EIN by the time the return is due, enter

"Applied for" in the space for the EIN. For more details, see Pub. 583.

Note. The online application process is not yet available for corporations with addresses in foreign countries or Puerto Rico.

Item A(2)

If box A(1) is checked and nonlife insurance companies are included in the consolidated return, also check box A(2). See Regulations section 1.1502-47(s) for the filing requirements of a life-nonlife company consolidated return.

Item D. Section 953 Elections

Check the appropriate box if the corporation is a foreign corporation and elects under:

1. Section 953(c)(3)(C) to treat its related person insurance income as effectively connected with the conduct of a trade or business in the United States or
2. Section 953(d) to be treated as a domestic corporation.

Generally, a foreign corporation making either election should file its return with the Internal Revenue Service Center, Philadelphia, PA 19255. See Notice 87-50, 1987-2 C.B. 357, and Rev. Proc. 2003-47, 2003-28 I.R.B. 55, for the procedural rules, election statement formats, and filing addresses for making the respective elections under section 953(c)(3)(C) or section 953(d).

Note. Once either election is made, it will apply to the tax year for which made and all subsequent tax years unless revoked with the consent of the IRS. Also, any loss of a foreign corporation electing to be treated as a domestic insurance company under section 953(d) will be treated as a dual-consolidated loss and may not be used to reduce the taxable income of any other member of the affiliated group for the tax year or any other tax year.

Note. If a section 953(d) election is made, include the additional tax required to be paid, on line 11, Schedule K. On the dotted line to the left of line 11, Schedule K, write "Section 953(d)" and the amount. Attach a schedule showing the computation. See section 953(d) for more details.

Item E. Final Return, Name Change, Address Change, or Amended Return

Indicate a final return, name change, address change, or amended return by checking the appropriate box.

Note. If a change of address occurs after the return is filed, use Form 8822, Change of Address, to notify the IRS of the new address.

Life Insurance Company Taxable Income

Income

Except as otherwise provided in the Internal Revenue Code, gross income includes all income from whatever source derived.

Extraterritorial income. Gross income generally does not include extraterritorial income that is qualifying foreign trade income. However, the extraterritorial income exclusion is reduced by 20% for transactions after 2004, unless made under a binding contract with an unrelated person in effect on September 17, 2003, and at all times thereafter. Use Form 8873, Extraterritorial Income Exclusion, to figure the exclusion. Include the exclusion in the total for "Other deductions" on line 18.

Income from qualifying shipping activities. For tax years beginning after October 22, 2004, the corporation's gross income does not include income from qualifying shipping activities (as defined in section 1356) if the corporation makes an election under section 1354 to be taxed on its notional shipping income (as defined in section 1353) at the highest corporate tax rate (35%). If the election is made, the corporation generally may not claim any loss, deduction, or credit with respect to qualifying shipping activities. A corporation making this election also may elect to defer gain on the disposition of a qualifying vessel under section 1359.

Report the section 1352(1) tax on Schedule K, line 3, and report the section 1352(2) tax on Schedule K, line 10. For Schedule K, line 10, check the "Other" box and attach a schedule that shows the computation of the section 1352(2) amount.

Line 1. Enter gross premiums and other consideration received on insurance and annuity contracts less return premiums and premiums and other consideration paid for indemnity reinsurance.

Gross premiums and other consideration includes advance premiums, deposits, fees, assessments, consideration received for assuming liabilities under contracts not issued by the corporation, and any amount treated as premiums received under section 808(e) (see the Schedule E instructions).

Return premiums include amounts rebated or refunded due to policy cancellations or incorrectly computed premiums, but do not include amounts returned to policyholders when such amounts are not fixed in the contract but instead depend on the corporation's experience or the management's discretion.

Line 2. Net decrease in reserves. If there is a decrease in reserves, complete line 2 by doing the following:

1. Pencil in the amount from line 8, Schedule F, on line 2, to tentatively compute life insurance company gross income (LICGI).

2. Enter this tentative LICGI on Schedule F, line 12, and complete the remainder of Schedule F.

After completing steps 1 and 2 above, erase the numbers penciled in for step 1 and then enter on line 2 the net decrease in reserves shown on line 37, Schedule F.

Line 3. 10% of certain decreases in reserves under section 807(f)(1)(B)(ii). If the amount of any item referred to in section 807(c) decreases as a result of a change in the basis used to determine that item, 10% of the decrease must be included in LICGI for each of the 10 succeeding tax years. See section 807(f)(1).

Note. If a corporation no longer qualifies as a life insurance company, the balance of any adjustments under section 807(f) must be taken into account in the last tax year the corporation is qualified to file Form 1120-L. See section 807(f)(2).

Line 4. Investment income. Enter the amount from Schedule B, line 8, less 50% of interest income of an ESOP loan made prior to August 20, 1996. Also, see Act section 1602 of the Small Business Job Protection Act of 1996 ("1996 Act") for binding contracts and refinancing rules.

Line 5. Net capital gain. Unless specifically excluded by section 1221, each asset held by a corporation (whether or not connected with its business) is a "capital asset."

Under section 1221, capital asset does not include:

1. Assets that can be inventoried or property held mainly for sale to customers.
2. Depreciable or real property used in the trade or business.
3. Certain copyrights; or, literary, musical, or artistic compositions.
4. Accounts or notes receivable acquired in the ordinary course of trade or business for services rendered or from the sale of property described in 1 above.
5. Certain publications of the U.S. Government.

Section 818(b) modifies the above definition so only property used in carrying on an insurance business will be considered as "depreciable or real property used in the corporation's trade or business." For life insurance companies, gains or losses from the sale or exchange of depreciable assets of any business other than an insurance business will be treated as gains or losses from the sale or exchange of capital assets.

See section 818(c) and the related regulations for how to limit the gain from the sale or exchange of any section 818(c) property.

Line 6. Income from a special loss discount account. Enter the total from Form 8816, Part II, line 6. See section 847(5) and the Instructions for Form 8816 for more information.

Line 7. Other income. Enter any other taxable income, includible in LICGI, not reported on lines 1 through 6. List the type and amount of income on an attached schedule. If the life insurance company has only one item of other income, describe it in parentheses on line 7. The following are examples of other income to report on line 7.

- All income from noninsurance business (defined in section 806(b)(3)), but list it separately from all other income.

- Gains and losses (including ordinary gains and losses) from sales or exchanges of assets used in a trade or business and from involuntary conversions reported on Form 4797, Sales of Business Property. Section 818(b)(1) provides that, for section 1231(a), "property used in a trade or business" includes only:

1. Property used in carrying on an insurance business that is either real or depreciable property held for more than 1 year.
2. Timber, coal, and domestic iron ore to which section 631 applies.

For paragraph 1 above, property used in a trade or business does not include property includible in inventory, property held primarily for sale to customers, or certain copyrights, literary, musical, or artistic compositions, letters, memoranda, and similar property.

- Ordinary income from trade or business activities of a partnership (from Schedule K-1 (Form 1065 or 1065-B)). Do not offset ordinary losses against ordinary income. Instead, include the losses on line 18. Show the partnership's name, address, and EIN on a separate statement attached to this return. If the amount entered is from more than one partnership, identify the amount from each partnership.

Deductions

Limitations on Deductions

Section 263A uniform capitalization rules. The uniform capitalization rules of section 263A require corporations to capitalize certain costs.

For details on the uniform capitalization rules, see Regulations sections 1.263A-1 through 1.263A-3.

Transactions between related taxpayers. Generally, an accrual basis taxpayer can only deduct business expenses and interest owed to a related party in the year the payment is included in the income of the related party. See sections 163(e)(3), 163(j), and 267 for limitations on deductions for unpaid interest and expenses.

Section 291 limitations. Corporations may be required to adjust certain deductions. See section 291 to determine the amount of the adjustment. Also, see section 43.

Golden parachute payments. A portion of the payments made by a corporation to key personnel that exceeds their usual compensation may not be deductible. This occurs when the corporation has an agreement (golden parachute) with these key employees to pay them these excess amounts if control of the corporation changes. See section 280G and Regulations section 1.280G-1.

Business start-up and organizational costs. Business start-up and organizational costs must be capitalized unless an election is made to deduct or amortize them. For costs paid or incurred before October 23, 2004, the corporation must capitalize them unless it elects to amortize these costs over a period of 60 months or more. For costs paid or incurred after October 22, 2004, the following rules apply separately to each category of costs.

- The corporation can elect to deduct up to \$5,000 of such costs for the year the corporation begins business operations.
- The \$5,000 deduction is reduced (but not below zero) by the amount the total costs exceed \$50,000. If the total costs are \$55,000 or more, the deduction is reduced to zero.
- If the election is made, any costs that are not deductible must be amortized ratably over a 180-month period beginning with the month the corporation begins business operations.

For more details on the election for business start-up costs, see section 195 and attach the statement required by Regulations section 1.195-1(b). For more details on the election for organizational costs, see section 248 and attach the statement required by Regulations section 1.248-1(c). Report the deductible amount of these costs and any amortization on line 18. For amortization that begins during the 2004 tax year, complete and attach Form 4562.

Reducing certain expenses for which credits are allowable. For each credit listed below, the corporation must reduce the otherwise allowable deductions for expenses used to figure the credit by the amount of the current year credit.

- Work opportunity credit.
- Research credit.
- Orphan drug credit.
- Disabled access credit.
- Enhanced oil recovery credit.
- Empowerment zone and renewal community employment credit.
- Indian employment credit.
- Employer credit for social security and Medicare taxes paid on certain employee tips.
- Welfare-to-work credit.
- Credit for small employer pension plan startup costs.
- Credit for employer-provided childcare facilities and services.
- New York Liberty Zone business employee credit.
- Low sulfur diesel fuel production credit.

If the corporation has any of these credits, figure each current year credit before figuring the deduction for expenses on which the credit is based.

Line 9. Death benefits, etc. Enter all claims and benefits accrued and losses incurred (whether or not ascertained) during the year on insurance and annuity contracts.

Losses incurred (whether or not ascertained) includes a reasonable estimate both of losses incurred but not reported and of reported losses, when the amount of the losses cannot be determined by the end of the tax year. Losses incurred must be adjusted to take into account recoveries (e.g., for reinsurance) for those losses together with estimates of those recoveries that may be recovered on those losses in future years.



Under section 807(c), the amount of unpaid losses (other than losses on life insurance contracts) must be the amount of the discounted unpaid losses under section 846. See the instructions for Schedule F, line 2, for more information on the discounting provisions.

Line 11. 10% of increase in reserves under section 807(f)(1)(B)(i). If the amount of any item referred to in section 807(c) increases as a result of a change in the basis used to determine that item, 10% of the increase will be allowed as a deduction in computing LICTI for each of the 10 succeeding tax years. See section 807(f)(1).

Termination as life insurance company. If a corporation ceases to qualify as a life insurance company, the balance of any adjustments under section 807(f) must be taken into account in the last year that the corporation is qualified to file Form 1120-L. See section 807(f)(2).

Line 13. Assumption by another person of liabilities under insurance, etc., contracts. Enter the total consideration paid by the corporation to another person (other than for indemnity reinsurance) for the assumption by that person of liabilities under insurance and annuity contracts (including supplementary contracts).

Line 14. Dividends reimbursable by taxpayer. Enter the amount of policyholder dividends:

1. Paid or accrued by another insurance company for policies this corporation has reinsured and
2. That are reimbursable by the corporation under the terms of the reinsurance contract.

Line 15a. Interest. Enter all interest paid or accrued during the tax year. No deduction is allowed under section 163 for interest on the items described in section 807(c). Also, do not include interest included on Schedule G, line 9 (general deductions).

Limitations. The deduction for interest is limited when the corporation is a policyholder or beneficiary with respect to a life insurance, endowment, or annuity contract issued after June 8, 1997. For details, see section 264(f). Attach a statement showing the computation of the deduction.

Line 15b. Less tax-exempt interest expense. Enter interest paid or accrued on indebtedness incurred or continued to purchase or carry obligations, the interest on which is wholly tax-exempt.

Line 17. Additional deduction. Enter the total from Form 8816, Part II, line 5.

Any insurance company taking the additional deduction must:

- Make special estimated tax payments equal to the tax benefit from the deduction and
- Establish and maintain a Special Loss Discount Account. See section 847 and Form 8816 for more information.

Line 18. Other deductions. Attach a schedule, listing by type and amount, all allowable deductions in computing LICTI (including the amortization of premiums under section 811(b)) not included on lines 9 through 17. Examples of other deductions include:

- Certain business start-up and organizational costs that the corporation elects to deduct. See page 7.
- Legal and professional fees.
- Supplies used and consumed in the business.
- Utilities.

- Ordinary losses from trade or business activities of a partnership (from Schedule K-1 (Form 1065 or 1065-B)). Do not offset ordinary income against ordinary losses. Instead, include the income on line 7. Show the partnership's name, address, and EIN on a separate statement attached to this return. If the amount is from more than one partnership, identify the amount from each partnership.

- Extraterritorial income exclusion (from Form 8873, line 52a or 52b).
- Deduction for clean-fuel vehicle and certain refueling property (see Pub. 535).
- Dividends paid in cash on stock held by an employee stock ownership plan. However, a deduction may only be taken if, according to the plan, the dividends are:

1. Paid in cash directly to the plan participants or beneficiaries;
2. Paid to the plan which distributes them in cash to the plan participants or their beneficiaries no later than 90 days after the end of the plan year in which the dividends are paid;
3. At the election of the participants or their beneficiaries; (i) payable as provided under 1 or 2 above or (ii) paid to the plan and reinvested in qualifying employer securities; or
4. Used to make payments on a loan described in section 404(a)(9).

See section 404(k) for more details and the limitation on certain dividends.

- Deductions from any noninsurance business (defined in section 806(b)(3)). Deductions from any noninsurance business should be listed separately from all other deductions.
- Depreciation or amortization (attach Form 4562, Depreciation and Amortization, if required). Attach Form T (Timber), Forest Activities Schedule, if a deduction for depletion of timber is taken. Foreign intangible drilling costs and foreign exploration and development costs must either be added to the corporation's basis for cost depletion purposes or be deducted ratably over a 10-year period. See sections 263(i), 616, and 617 for details.



Do not deduct fines or penalties paid to a government for violating any law.

Also include on line 18 the following:

Compensation of officers. Include deductible officers' compensation. Do not include compensation deductible elsewhere on the return, such as elective contributions to a section 401(k) cash or deferred arrangement or amounts contributed under a salary reduction SEP agreement or a SIMPLE IRA plan.

Include only the deductible part of each officer's compensation on line 18. (See *Disallowance of deduction for employee compensation in excess of \$1 million*, below.) Attach a schedule for compensation of all officers using the following columns:

1. Name of officer.
2. Social security number.
3. Percentage of time devoted to business.
4. Amount of compensation.

If a consolidated return is filed, each member of an affiliated group must furnish this information.

Disallowance of deduction for employee compensation in excess of \$1 million. Publicly held corporations may not deduct compensation to a "covered employee" to the extent that the compensation exceeds \$1 million. Generally, a covered employee is:

- The chief executive officer of the corporation (or an individual acting in that capacity) as of the end of the tax year or
- An employee whose total compensation must be reported to shareholders under the Securities Exchange Act of 1934 because the employee is among the four highest compensated officers for that tax year (other than the chief executive officer).

For this purpose, compensation does not include the following.

- Income from certain employee trusts, annuity plans, or pensions.
- Any benefit paid to an employee that is excluded from the employee's income.

The deduction limit does not apply to:

- Commissions based on individual performance,
- Qualified performance-based compensation, and
- Income payable under a written binding contract in effect on February 17, 1993.

The \$1 million limit is reduced by amounts disallowed as excess parachute payments under section 280G.

For details, see section 162(m) and Regulations section 1.162-27.

Salaries and wages. Include the total salaries and wages paid for the tax year, reduced by any current year work opportunity credit from Form 5884, empowerment zone and renewal community employment credit from Form 8844, Indian employment credit from Form 8845, welfare-to-work credit from Form 8861, or New York Liberty Zone business employee credit from Form 8884. See the instructions for these forms for more information. Do not include salaries and wages deductible elsewhere on the return, such as elective contributions to a section 401(k) cash or deferred arrangement or amounts contributed under a salary reduction SEP agreement or a SIMPLE IRA plan.

Pension, profit-sharing, etc. plans. Include the deduction for contributions to qualified pension, profit-sharing, or other funded deferred compensation plans. Employers who maintain such a plan generally must file one of the forms listed below, even if the plan is not a qualified plan under the Internal Revenue Code. The filing requirement applies even if the corporation does not claim a deduction for the current tax year. There are penalties for failure to file these forms on time and for overstating the pension plan deduction. See sections 6652(e) and 6662(f).

Form 5500, Annual Return/Report of Employee Benefit Plan. File this form for a plan that is not a one-participant plan (see below).

Form 5500-EZ, Annual Return of One-Participant (Owners and Their Spouses) Retirement Plan. File this form for a plan that only covers the owner (or the

owner and his or her spouse) but only if the owner (or the owner and his or her spouse) owns the entire business.

Charitable contributions. Include contributions or gifts actually paid within the tax year to or for the use of charitable and governmental organizations described in section 170(c) and any unused contributions carried over from prior years.

Life insurance companies reporting LICTI on the accrual method can elect to treat as paid during the tax year any contributions paid by the 15th day of the 3rd month after the end of the tax year if the contributions were authorized by the board of directors during the tax year. Attach a declaration to the return stating that the resolution authorizing the contributions was adopted by the board of directors during the tax year. The declaration must include the date the resolution was adopted.

Limitation on deduction. The total amount claimed may not be more than 10% of LICTI computed without regard to the following.

- Any deduction for contributions.
- The deduction for policyholder dividends.
- The deduction for dividends received.
- The small life insurance company deduction.
- Any operations loss carryback to the tax year under section 810.
- Any capital loss carryback to the tax year under section 1212(a)(1).

Carryover. Charitable contributions over the 10% limitation may not be deducted for the tax year but may be carried over to the next 5 tax years.

A contributions carryover is not allowed, however, to the extent that it increases an operations loss.

Substantiation requirements.

Generally, no deduction is allowed for any contribution of \$250 or more unless the corporation obtains a written acknowledgment from the donee organization that shows the amount of cash contributed, describes any property contributed, and, either gives a description and a good faith estimate of the value of any goods or services provided in return for the contribution or states that no goods or services were provided in return for the contribution. The acknowledgment must be obtained by the due date (including extensions) of the corporation's return, or, if earlier, the date the return is filed. Do not attach the acknowledgment to the tax return, but keep it with the corporation's records. These rules apply in addition to the filing requirements for Form 8283, Noncash Charitable Contributions, discussed below.

For more information on charitable contributions including substantiation and recordkeeping requirements, see section 170 and the related regulations and Pub. 526, Charitable Contributions.

Contributions of property other than cash. If a corporation (other than a closely held or personal service corporation) contributes property other than cash and claims over a \$500 deduction for the property, it must attach a schedule to the return describing the kind of property contributed and the method used to determine its fair market value (FMV).

Closely held corporations and personal service corporations must complete Form 8283 and attach it to their returns. All other corporations generally must complete and attach Form 8283 to their returns for contributions of property (other than money) if the total claimed deduction for all property contributed was more than \$5,000.

If the corporation made a "qualified conservation contribution" under section 170(h), also include the FMV of the underlying property before and after the donation, as well as the type of legal interest contributed, and describe the conservation purpose benefited by the donation. If a contribution carryover is included, show the amount and how it was determined.

Contributions after June 3, 2004. For contributions of certain property made after June 3, 2004, a corporation must file Form 8283 and get a qualified appraisal if claiming a deduction of more than \$5,000. Do not attach the appraisal to the tax return unless claiming a deduction of more than \$500,000 or, for art, a deduction of \$20,000 or more. See Form 8283.

Contributions of used vehicles.

Special rules apply to contributions after 2004 of used motor vehicles, boats, or airplanes with a claimed value of more than \$500. See section 170(f)(12).

Reduced deduction for contributions of certain property.

For a charitable contribution of property, the corporation must reduce the contribution by the sum of:

- The ordinary income and short-term capital gain that would have resulted if the property were sold at its FMV and
- For certain contributions, the long-term capital gain that would have resulted if the property were sold at its FMV.

The reduction for the long-term capital gain applies to:

- Contributions of tangible personal property for use by an exempt organization for a purpose or function unrelated to the basis for its exemption,
- Contributions of any property to or for the use of certain private foundations except for stock for which market quotations are readily available (section 170(e)(5)), and
- Any patent or certain other intellectual property contributed after June 3, 2004. See section 170(e)(1)(B). However, the corporation can deduct certain qualified donee income from this property. See section 170(m).

Larger deduction. A larger deduction is allowed for certain contributions of:

- Inventory and other property to certain organizations for use in the care of the ill, needy, or infants (see section 170(e)(3) and Regulations section 1.170A-4A);
- Scientific equipment used for research to institutions of higher learning or to certain scientific research organizations (other than by personal holding companies and service organizations) (see section 170(e)(4)); and
- Computer technology and equipment for educational purposes. See section 170(e)(6).

Travel, meals, and entertainment.

Subject to limitations and restrictions discussed below, a corporation can deduct ordinary and necessary travel, meals, and entertainment expenses paid or incurred in

its trade or business. Also, special rules apply to deductions for gifts, skybox rentals, luxury water travel, convention expenses, and entertainment tickets. See section 274 and Pub. 463, Travel, Entertainment, Gift, and Car Expenses for more details.

Travel. The corporation cannot deduct travel expenses of any individual accompanying a corporate officer or employee, including a spouse or dependent of the officer or employee, unless:

- That individual is an employee of the corporation and
- His or her travel is for a bona fide business purpose and would otherwise be deductible by that individual.

Meals and entertainment. Generally, the corporation can deduct only 50% of the amount otherwise allowable for meals and entertainment expenses paid or incurred in its trade or business. In addition (subject to exceptions under section 274(k)(2)):

- Meals must not be lavish or extravagant;
- A bona fide business discussion must occur during, immediately before, or immediately after the meal; and
- An employee of the corporation must be present at the meal.

See section 274(n)(3) for a special rule that applies to expenses for meals consumed by individuals subject to the hours of service limits of the Department of Transportation.

Membership dues. The corporation can deduct amounts paid or incurred for membership dues in civic or public service organizations, professional organizations (such as bar and medical associations), business leagues, trade associations, chambers of commerce, boards of trade, and real estate boards. However, no deduction is allowed if a principal purpose of the organization is to entertain, or provide entertainment facilities for, members or their guests. In addition, corporations cannot deduct membership dues in any club organized for business, pleasure, recreation, or other social purpose. This includes country clubs, golf and athletic clubs, airline and hotel clubs, and clubs operated to provide meals under conditions favorable to business discussion.

Entertainment facilities. The corporation cannot deduct an expense paid or incurred for a facility (such as a yacht or hunting lodge) used for an activity usually considered entertainment, amusement, or recreation.

Amounts treated as compensation. Generally, the corporation may be able to deduct otherwise nondeductible travel, meals, and entertainment expenses if the amounts are treated as compensation to the recipient and reported on Form W-2 for an employee or on Form 1099-MISC for an independent contractor.

However, if the recipient is an officer, director, or beneficial owner (directly or indirectly) of more than 10% of any class of stock, the deduction for otherwise nondeductible meals, travel, and entertainment expenses incurred after October 22, 2004, is limited to the amount treated as compensation. See section 274(e)(2).

Lobbying expenses. Generally, lobbying expenses are not deductible. These expenses include:

- Amounts paid or incurred in connection with influencing federal or state legislation (but not local legislation) or
- Amounts paid or incurred in connection with any communication with certain federal executive branch officials in an attempt to influence the official actions or positions of the officials. See Regulations section 1.162-29 for the definition of “influencing legislation.”

Dues and other similar amounts paid to certain tax-exempt organizations may not be deductible. See section 162(e)(3). If certain in-house lobbying expenditures do not exceed \$2,000, they are deductible. For information on contributions to charitable organizations that conduct lobbying activities, see section 170(f)(9).

For more information on other deductions that may apply to corporations, see Pub. 535.

Line 20. Operations loss deduction. The operations loss deduction (OLD) is the total of the operations loss carryovers from prior tax years. However, the OLD cannot exceed the corporation’s LICTI (after the dividends-received deduction). See section 810(c). If this deduction is taken, show its computation on an attached schedule.

Generally, a life insurance company can carry an operating loss back to each of the 3 years preceding the year of the loss and carry it over to each of the 15 years following the year of the loss.

There is also an irrevocable election to waive the carryback period and instead carry an operating loss forward to years following the year of the loss. To make this election, check the box in line 12, Schedule M. To be valid, the election must be made by the due date (including extensions) for filing Form 1120-L. If the life insurance company is a new company for the loss year, the loss may be carried over to each of the 18 years following the year of the loss.

After applying the operating loss to the first tax year to which it may be carried, the portion of the loss the corporation may carry to each of the remaining tax years is the excess, if any, of the loss over the sum of the offsets for each of the prior tax years to which the corporation may carry the loss. See section 810(b)(2).

See section 810 for special rules, limitations, and definitions pertaining to operating loss carrybacks and carryovers.

If an ownership change occurs, the amount of the taxable income of a loss corporation that may be offset by the pre-change NOL carryovers may be limited (see section 382 and the related regulations). A loss corporation must file an information statement with its income tax return for each tax year that certain ownership shifts occur (see Temporary Regulations section 1.382-2T(a)(2)(ii) for details). See Regulations section 1.382-6(b) for details on how to make the closing-of-the-books election.

See section 844 for special loss carryover rules for an insurance company that has changed its form of organization or

has had a change in the nature of its insurance business.

Line 27. Total taxable income. The total taxable income reported on line 27 cannot be less than line 26 of the Form 1120-L.

Also, line 27 cannot be less than the largest of the following amounts.

- The amount of nondeductible CFC dividends under section 965. This amount is equal to the difference between columns (a) and (c) of Form 1120-L, Schedule A, line 14.
- The inversion gain of the corporation for the tax year, if the corporation is an expatriated entity or a partner in an expatriated entity. For details, see section 7874.

Tax and Payments

Line 29b. Prior year(s) special estimated tax payments to be applied. The amount entered on line 29b must agree with the amount(s) from Form 8816, Part III, line 11. See Form 8816 and section 847(2) for additional information.

Line 29c. Estimated tax payments. Enter any estimated tax payments the corporation made for the tax year. Do not include any amount being applied on line 29d.

Line 29d. Special estimated tax payments. If the deduction under section 847 is claimed on line 17, page 1, special estimated tax payments must be made in an amount equal to the tax benefit of the deduction. These payments must be made on or before the due date (without regard to extensions) of this tax return. See Form 8816 and section 847(2) for additional information.

Tax benefit rule. Section 847(8) requires that if a corporation carries back net operating losses or capital losses that arise in years after a year in which a section 847 deduction was claimed, then the corporation must recompute the tax benefit attributable to the previously claimed section 847 deduction taking into account the loss carrybacks. Tax benefits also include those derived from filing a consolidated return with another insurance company (without regard to section 1503(c)).

Therefore, if the recomputation changes the amount of the section 847 tax benefit, then the taxpayer must provide a computation schedule and attach it to Form 8816.

Line 29f. Enter the total of lines 29a through 29c less line 29e. Do not include line 29d in the total for line 29f.

Line 29h. Credit for tax paid on undistributed capital gains. Enter the credit (from Form 2439, Notice to Shareholder of Undistributed Long-Term Capital Gains) for the corporation’s share of the tax paid by a regulated investment company (RIC) or a real estate investment trust (REIT) on undistributed long-term capital gains included in the corporation’s income. Attach Form 2439 to Form 1120-L.

Line 29i. Credit for federal tax paid on fuels. Enter the credit from Form 4136, Credit for Federal Tax Paid on Fuels, if the corporation qualifies to take this credit. Attach Form 4136 to Form 1120-L.

Line 29j. U.S. income tax paid or withheld at source. Enter the amount of any U.S. income tax paid or withheld as reported on Form 1042-S.

Line 29k. Total payments. Add the amounts on lines 29f through 29j and enter the total on line 29k.

Backup withholding. If the corporation had federal income tax withheld from any payments it received because, for example, it failed to give the payer its correct EIN, include the amount withheld in the total for line 29k. Write the amount withheld and the words “Backup Withholding” in the blank space above line 29k.

Line 30. Estimated tax penalty. A corporation that does not make estimated tax payments when due may be subject to an underpayment penalty for the period of underpayment. Generally, a corporation is subject to the penalty if its tax liability is \$500 or more and it did not timely pay the smaller of:

- Its tax liability for 2004 or
- Its prior year’s tax.

See section 6655 for details and exceptions, including special rules for large corporations.

Use Form 2220, Underpayment of Estimated Tax by Corporations, to see if the corporation owes a penalty and to figure the amount of the penalty. Generally, the corporation does not have to file this form because the IRS can figure the amount of any penalty and bill the corporation for it. However, even if the corporation does not owe the penalty, complete and attach Form 2220 if:

- The annualized income or adjusted seasonal installment method is used or
- The corporation is a large corporation computing its first required installment based on the prior year’s tax. (See the Instructions for Form 2220 for the definition of a large corporation.)

If Form 2220 is attached, check the box on line 30 and enter the amount of any penalty on that line.

Line 33. Electronic deposit of tax refund of \$1 million or more. If the corporation is due a refund of \$1 million or more and wants it electronically deposited into its checking or savings account at any U.S. bank or other financial institution instead of having a check sent to the corporation, complete Form 8302 and attach it to the corporation’s tax return.

Schedule A—Dividend Income and Dividends-Received Deduction

For purposes of the 20% ownership test on lines 1 through 7, the percentage of stock owned by the corporation is based on voting power and value of the stock. Preferred stock described in section 1504(a)(4) is not taken into account. Corporations filing a consolidated return should see Regulations sections 1.1502-13, 1.1502-26, and 1.1502-27 before completing Schedule A.

Corporations filing a consolidated return must not report as dividends on Schedule A

any amounts received from corporations within the tax consolidation group. Such dividends are eliminated in consolidation rather than offset by the dividends-received deduction.

Line 1, column (a). Enter dividends (except those received on debt-financed stock acquired after July 18, 1984 (see section 246A)) that:

- Are received from less-than-20%-owned domestic corporations subject to income tax and
- Qualify for the 70% deduction under section 243(a)(1).

Also include on line 1:

- Taxable distributions from an IC-DISC or former DISC that are designated as eligible for the 70% deduction and certain dividends of Federal Home Loan Banks. See section 246(a)(2).
- Dividends (except those received on debt-financed stock acquired after July 18, 1984) from a regulated investment company (RIC). The amount of dividends eligible for the dividends-received deduction under section 243 is limited by section 854(b). The corporation should receive a notice from the RIC specifying the amount of dividends that qualify for the deduction.

Report so-called dividends or earnings received from mutual savings banks, etc., as interest. Do not treat them as dividends.

Line 2, column (a). Enter on line 2:

- Dividends (except those received on debt-financed stock acquired after July 18, 1984) that are received from 20%-or-more-owned domestic corporations subject to income tax and that are subject to the 80% deduction under section 243(c) and
- Taxable distributions from an IC-DISC or former DISC that are considered eligible for the 80% deduction.

Line 3, column (a). Enter dividends that are:

- Received on debt-financed stock acquired after July 18, 1984, from domestic and foreign corporations subject to income tax that would otherwise be subject to the dividends-received deduction under section 243(a)(1), 243(c), or 245(a). Generally, debt-financed stock is stock that the corporation acquired by incurring a debt (e.g., it borrowed money to buy the stock).
- Received from a RIC on debt-financed stock. The amount of dividends eligible for the dividends-received deduction is limited by section 854(b). The corporation should receive a notice from the RIC specifying the amount of dividends that qualify for the deduction.

Line 3, columns (b) and (c). Dividends received on debt-financed stock acquired after July 18, 1984, are not entitled to the full 70% or 80% dividends-received deduction. The 70% or 80% deduction is reduced by a percentage that is related to the amount of debt incurred to acquire the stock. See section 246A. Also, see section 245(a) before making this computation for an additional limitation that applies to dividends received from foreign corporations. Attach a schedule showing how the amount on line 3, column (c), was figured.

Line 4, column (a). Enter dividends received on the preferred stock of a less-than-20%-owned public utility that is

subject to income tax and is allowed the deduction provided in section 247 for dividends paid.

Line 5, column (a). Enter dividends received on the preferred stock of a 20%-or-more-owned public utility that is subject to income tax and is allowed the deduction provided in section 247 for dividends paid.

Line 6, column (a). Enter the U.S.-source portion of dividends that:

- Are received from less-than-20%-owned foreign corporations and
- Qualify for the 70% deduction under section 245(a). To qualify for the 70% deduction, the corporation must own at least 10% of the stock of the foreign corporation by vote and value.

Also include dividends received from a less-than-20%-owned FSC that:

- Are attributable to income treated as effectively connected with the conduct of a trade or business within the United States (excluding foreign trade income) and
- Qualify for the 70% deduction under 245(c)(1)(B).

Line 7, column (a). Enter the U.S.-source portion of dividends received from 20%-or-more-owned foreign corporations that qualify for the 80% deduction under section 245(a). Also include dividends received from a 20%-or-more-owned FSC that:

- Are attributable to income treated as effectively connected with the conduct of a trade or business within the United States (excluding foreign trade income) and
- Qualify for the 80% deduction under section 245(c)(1)(B).

Line 8, column (a). Enter dividends received from wholly owned foreign subsidiaries that are eligible for the 100% deduction under section 245(b) but that do not qualify as "100% dividends" under section 805(a)(4)(C).

In general, the deduction under section 245(b) applies to dividends paid out of the earnings and profits of a foreign corporation for a tax year during which:

- All of its outstanding stock is owned (directly or indirectly) by the domestic corporation receiving the dividends and
- All of its gross income from all sources is effectively connected with the conduct of a trade or business within the United States.

Do not include dividends received from a life insurance company.

Also, include on line 8, column (a), dividends from FSCs that are attributable to foreign trade income and that are eligible for the 100% deduction provided in section 245(c)(1)(A).

Line 9, column (a). Enter only those dividends that qualify under section 243(b) for the 100% dividends-received deduction described in section 243(a)(3) but that do not qualify as "100% dividends" under section 805(a)(4)(C). Corporations taking this deduction are subject to the provisions of section 1561. Do not include dividends received from a life insurance company.

The 100% deduction does not apply to affiliated group members that are joining in the filing of a consolidated return.

Line 10, column (c). Limitation on dividends-received deduction. Generally, line 10 of column (c), may not exceed the

Worksheet for Schedule A, line 10
(keep for your records)

1. Refigure line 8, page 1, without any adjustment under section 1059 and without any capital loss carryback to the tax year under section 1212(a)(1). Add this refigured line 8 amount to the amount on line 25, page 1. Subtract from that total the sum of lines 9 through 18, page 1	_____
2. Complete line 13, column (c) and enter the total of that amount, line 9, column (c), and the portion of the deduction on line 8, column (c), that is attributable to dividends from FSCs that are attributable to foreign trade income	_____
3. Subtract line 2 from line 1	_____
4. Multiply line 3 by 80%	_____
5. Add lines 2, 5, and 7, column (c); the portion of the deduction on line 8, column (c) that is attributable to wholly owned foreign subsidiaries; and the portion of the deduction on line 3, column (c) that is attributable to dividends received from 20%-or-more-owned corporations	_____
6. Enter the smaller of line 4 or line 5. If line 5 is greater than line 4, stop here and enter the amount from line 6 on line 10, column (c). Do not complete the rest of the worksheet	_____
7. Enter the total amount of dividends from 20%-or-more-owned corporations that are included on lines 2, 3, 5, and 7, column (a), and the portion of the deduction on line 8, column (a), that is attributable to wholly owned subsidiaries	_____
8. Subtract line 7 from line 3	_____
9. Multiply line 8 by 70%	_____
10. Subtract line 5 above from line 10 of column (c)	_____
11. Enter the smaller of line 9 or line 10	_____
12. Dividends-received deduction after limitation (section 246(b)). Add lines 6 and 11. Enter the result here and on line 10, column (c)	_____

amount from the worksheet below. However, in a year in which a loss from operations occurs, this limitation does not apply even if the loss is created by the dividends-received deduction. (See sections 246(b) and 810.)

Line 13, column (a). In general, enter "100% dividends" as defined in section 805(a)(4)(C). That is, in general, enter dividends that qualify for the 100% dividends-received deduction under sections 243, 244, and 245(b) and were not reported on line 8 or 9 because they were (a) not distributed out of tax-exempt interest or out of dividends that do not qualify as 100% dividends or (b) paid by a life insurance company.

Note. Certain dividends received by a foreign corporation are not subject to proration. Attach a schedule showing computations.

Line 14, column (a). Enter qualifying dividends from Form 8895.

Line 15, column (a). Include the following:

1. Foreign dividends not reportable on lines 3, 6, 7, 8, or 14, column (a). Include on line 15 the corporation's share of the ordinary earnings of a qualified electing fund from line 1c of Form 8621. Exclude distributions of amounts constructively taxed in the current year or in prior years under subpart F (sections 951 through 964).

2. Income constructively received from CFCs under subpart F. This amount should equal the total subpart F income reported on Schedule I, Form 5471.

3. Gross-up of dividends for taxes deemed paid under sections 902 and 960.

4. Dividends (other than capital gain distributions reported on Schedule D (Form 1120) and exempt-interest dividends) that are received from RICs and that are not subject to the 70% deduction.

5. Dividends from tax-exempt organizations.

6. Dividends (other than capital gain dividends) received from a REIT that, for the tax year of the trust in which the dividends are paid, qualifies under sections 856 through 860.

7. Dividends not eligible for a dividends-received deduction, which include the following.

a. Dividends received on any share of stock held for less than 46 days during the 91-day period beginning 45 days before the ex-dividend date. When counting the number of days the corporation held the stock, you cannot count certain days during which the corporation's risk of loss was diminished. See section 246(c)(4) and Regulations section 1.246-5 for more details.

b. Dividends attributable to periods totaling more than 366 days that the corporation received on any share of preferred stock held for less than 91 days during the 181-day period that began 90 days before the ex-dividend date. When counting the number of days the corporation held the stock, you cannot count certain days during which the corporation's risk of loss was diminished. See section 246(c)(4) and Regulations section 1.246-5 for more details. Preferred dividends attributable to periods totaling less than 367 days are

subject to the 46-day holding period rule above.

c. Dividends on any share of stock to the extent the corporation is under an obligation (including a short sale) to make related payments with respect to positions in substantially similar or related property.

8. Any other taxable dividend income not properly reported above (including distributions under section 936(h)(4)).

Schedule B—Gross Investment Income

Line 1. Interest. Enter the total taxable interest received or accrued during the tax year, less any amortization of premium, plus any accrual of discount required by section 811(b). Generally, the appropriate amortization of premium and accrual of discount for the tax year on bonds, notes, debentures, or other evidence of indebtedness held by a life insurance company should be determined:

1. Under the method regularly employed by the company, if reasonable, and
2. In all other cases, under the regulations.

For bonds (as defined in section 171(d)) issued after September 27, 1985, the appropriate amount of amortization of premium must be determined using the yield to maturity method described in section 171(b)(3). Market discount is not required to be accrued under section 811(b). Attach a statement showing the method and computation used.

Note. The Small Business Job Protection Act of 1996 repealed section 133, which provided for the 50% interest income exclusion with respect to ESOP loans. The Act also repealed section 812(g), which provided for the exclusion of interest income from ESOP loans for company/policyholder proration. The repeal of these exclusions is effective for ESOP loans made after August 20, 1996. See Act section 1602 for special rules for binding contract agreements in effect prior to June 10, 1996, and certain refinancings made after August 20, 1996.

Line 3. Gross rents. Enter the gross rents received or accrued during the tax year. Related expenses, such as repairs, taxes, and depreciation should be reported as "Other deductions" on line 18, page 1.

Line 4. Gross royalties. Enter the gross royalties received or accrued during the tax year. Report the depletion deduction on line 18, page 1.

Line 5. Leases, terminations, etc. Enter the gross income received from entering into, altering, or terminating any lease, mortgage, or other instrument from which the corporation derives interest, rents, or royalties.

Line 6. Excess of net short-term capital gain over net long-term capital loss. See the instructions for line 5, page 1, on page 7, for a definition of capital assets.

Line 7. Gross income from a trade or business other than insurance. Enter the gross income from a trade or business (other than insurance carried on by the life insurance company or by a partnership of

which the life insurance company is a partner). Include section 1245, section 1250, and other ordinary gains on assets used in a noninsurance business from Form 4797. Report expenses related to any trade or business other than insurance on line 18, page 1.

Line 10. The increase in policy cash value of section 264(f) policies as defined in section 805(a)(4)(F). Generally, this applies to contracts issued after June 8, 1997, in tax years ending after that date. However, it also applies to contracts issued prior to June 9, 1997, that have been subject to a material increase in death benefits or other material change. See section 1084(d) of the Taxpayer Relief Act of 1997.

Line 12. 100% qualifying dividends. Enter the total amount of dividends if the percentage used to determine the deduction allowable under sections 243, 244, and 245(b) is 100%. Do not include dividends to the extent they are funded with tax-exempt interest or dividends that would not qualify as 100% dividends in the hands of the corporation. See section 812(e).

Note. Multi-tiered corporate arrangements cannot be used to change the character of the tax-exempt interest income and dividends received in an attempt to avoid exclusion.

Schedule C—Differential Earnings Amount

The differential earnings rate (DER) and the recomputed differential earnings rate (RDER) for each tax year are computed by the IRS on the basis of information submitted by the 50 largest domestic stock life insurance companies and all mutual life insurance companies. Neither rate can be negative. See Regulations section 1.809-9.

As previously stated under *What's New*, on page 1, the DER for 2004 will be announced by the Secretary of the Treasury in early 2005. The RDER for 2003 is zero. See Section 809(j) and Notice 2002-33, 2002-21 I.R.B. 989.

The differential earnings amount is figured by multiplying the average equity base (line 12, Schedule C) by the DER. Enter the result on line 13, Schedule C. When determining the equity base, no item should be taken into account more than once.

See section 809 for more information.

Line 1. Enter the amount from the Capital and Surplus Account of the Annual Statement. Do not include surplus notes.

Line 2. Nonadmitted financial assets are financial assets not permitted to be included as part of the corporation's financial condition for state regulatory purposes.

Generally, the amount entered on line 2 includes the sum of lines 1 through 9, column 2, of the "Assets" section of the Annual Statement. This also includes, at their FMV, financial assets shown on the Annual Statement. Attach a schedule of all nonadmitted assets (both financial and nonfinancial) other than:

- Due and accrued investment income,

- Investments in office furnishings or fixtures, or
- Agents' balances owed to the corporation.

Line 3. Enter the excess of "statutory reserves" over "tax reserves."

Statutory reserves means the total amount included in the annual statement for items described in section 807(c). Such term must not include any reserve attributable to a deferred and uncollected premium if the establishment of such reserve is not permitted under section 811(c).

Tax reserves means the total of the items described in section 807(c) as determined for purposes of section 807.

Line 6. Attach a schedule showing the nature and amount of:

1. Each voluntary reserve and
2. Any Annual Statement reserve that is not:
 - a. An item listed in section 807(c),
 - b. Part of the policyholder dividend reserve,
 - c. A deficiency reserve included on line 4a, and
 - d. Included on line 6.

For a stock company, any reserve treated as a voluntary reserve for the base period must be treated as a voluntary reserve for subsequent years unless there is a demonstrated change in circumstances.

Line 7. Include 50% of the total Annual Statement provision for policyholder dividends payable in the following year, whether accrued or unaccrued for tax purposes at the end of the tax year.

Policyholder dividends include excess interest, premium adjustments, and experience-rated refunds. Any Annual Statement provision for policyholder dividends payable after the close of the following tax year is treated as a voluntary reserve.

Schedule E—Policyholder Dividends

A policyholder dividend is any dividend or similar distribution to policyholders in their capacity as such.

Policyholder dividends include:

- Any amounts paid or credited (including an increase in benefits) when the amount is not fixed in the contract but depends on the corporation's experience or management's discretion, plus
- Excess interest,
- Premium adjustments, and
- Experience-rated refunds.

Also, under section 808(e), any policyholder dividend which:

1. Increases either the cash surrender value of the contract or other benefits payable under the contract or
2. Reduces the premium otherwise required to be paid, is treated as paid to, and returned by, the policyholder to the company as a premium.

When this happens, these amounts must be included in income on line 1, page 1.

Line 2. Excess interest means any amount in the nature of interest:

- Paid or credited to policyholders in their capacity as such and
- In excess of interest determined at the prevailing state assumed interest rate (SAIR) for such contract.

Line 3. Premium adjustment means any reduction in the premium under an insurance or annuity contract which (except for the reduction) would have been required to be paid under the contract.

Line 4. Experience-rated refund means any refund or credit based on the experience of the contract or group involved.

Lines 7 and 8. Generally, a deduction for policyholder dividends is the amount actually paid or accrued during the tax year. However, mutual life insurance companies must reduce this amount (but not below zero) by the differential earnings amount. If a mutual life insurance company's differential earnings amount exceeds total policyholder dividends for the tax year, the company must reduce its ending reserves by the amount of the excess.

Schedule F—Increase (Decrease) in Reserves and Company/Policyholder Share Percentage

Schedule F is used to compute:

1. The company's share percentage used in determining the company's share of the dividends-received deduction under section 805(a)(4);
2. The policyholders' share percentage used in determining the policyholders' share of tax-exempt interest for determining the increase or decrease in reserves under section 807 (and the increase in policy cash value of section 264(f) policies as defined in section 805(a)(4)(F)); and
3. To determine if, under section 807, certain reserves decreased or increased for the tax year. A net decrease will be includible in gross income, while a net increase will be a deduction in computing LICIT.

The net increase or net decrease in reserves is figured by comparing the opening balance for reserves to the closing balance for reserves reduced by:

1. The policyholders' share of tax-exempt interest (and the increase in policy cash value of section 264(f) policies as defined in section 805(a)(4)(F)) and
2. For mutual life insurance companies, the excess, if any (shown on line 8, Schedule E) of the differential earnings amount over deductible policyholder dividends determined without regard to section 809. For rules on how to compute reserves on contracts when interest is guaranteed beyond the end of the tax year, see section 811(d).

Reserve adjustments are not treated as interest expenses for allocation purposes under section 864(c). See section 818(f).

There are special rules for computing reserves of unearned premiums of certain nonlife contracts. See section 807(e)(7)(A).

Note. If the basis for determining the amount of any item referred to in section 807(c) (life insurance reserves, etc.) at the end of the tax year differs from the basis for the determination at the beginning of the tax year, see section 807(f).

Line 1. Life insurance reserves. For rules on how to compute life insurance reserves, see sections 807(d) and (e). Section 807(d)(2)(B) provides that the interest rate used to compute life insurance reserves is the greater of the applicable federal interest rate (AFIR) or the prevailing state assumed interest rate (SAIR). The applicable rates for tax years beginning in 2004 will be published in the Internal Revenue Bulletin when available. The applicable rates for tax years beginning in 2003 are available at Rev. Rul. 2004-14, 2004-8 I.R.B. 511. For modified guaranteed contracts described in section 817A, see Notice 97-32, 1997-1 C.B. 420.

Note. A change in a life insurance company's computation of existing life insurance reserves for annuity contracts to take into account specific factors issued by the NAIC is a change in basis subject to section 807(f). See Rev. Rul. 2002-6, 2002-6 I.R.B. 460.

Line 2. Unearned premiums and unpaid losses. For purposes of sections 807 and 805(a)(1), the amount of the unpaid losses (other than losses on life insurance contracts) must be the amount of the discounted unpaid losses determined under section 846.

Section 846 provides that the amount of the discounted unpaid losses must be computed separately by each line of business (multiple peril lines must be treated as a single line of business) and by each accident year and must be equal to the present value of those losses determined by using the:

1. Amount of the undiscounted unpaid losses,
2. Applicable interest rate, and
3. Applicable loss payment pattern.

Special rules apply with respect to unpaid losses related to disability insurance (other than credit disability insurance), noncancelable accident and health insurance, cancelable accident and health insurance, and to the international and reinsurance lines of business. With regard to the special rules for discounting unpaid losses on accident and health insurance (other than disability income insurance), unpaid losses are assumed to be paid in the middle of the year following the accident year.

Generally, the amount of undiscounted unpaid losses means the unpaid losses shown in the annual statement. The amount of discounted unpaid losses with respect to any line of business for an accident year cannot exceed the total amount of unpaid losses with respect to any line of business for an accident year as reported on the annual statement.

The applicable interest rate for each calendar year and the applicable loss payment patterns for each accident year for each line of business are determined by the IRS. The applicable interest rate and loss

payment patterns for 2004 are published in Rev. Proc. 2004-69, 2004-49 I.R.B. 906. The applicable interest rate and loss payment patterns for 2002 and 2003 are published in Rev. Proc. 2003-17, 2003-6 I.R.B. 427, and Rev. Proc. 2004-9, 2004-2 I.R.B. 275, respectively.

Corporations having sufficient historical experience to determine a loss payment pattern may, under certain circumstances, elect under section 846(e) to use their own historical experience (instead of the loss payment patterns determined by the IRS). If this election is made, the loss payment patterns will be based on the most recent calendar year for which an annual statement was filed before the beginning of the accident year. The election will not apply to any international or reinsurance line of business. If the corporation makes this election, check the "Yes" column for question 9 in Schedule M, Other Information. For more information, see section 846(e), Regulations section 1.846-2, and Rev. Proc. 92-76, 1992-2 C.B. 453.

Section 807(d)(4)(A)(ii) permits an election to recompute the federal interest rate every 5 years. In general, a life insurance company would apply the greater of the AFIR or the prevailing SAIR for the calendar year in which the contract is issued and the following 4 calendar years. In the 5th calendar year after the calendar year in which the contract was issued, the life insurance company would begin using the AFIR in effect for that 5th calendar year or the prevailing SAIR for the calendar year in which the contract was issued, whichever is greater. This rate would then remain in effect for the 4 subsequent years. For each subsequent 5-year period, a similar recomputation would be required. Once made, the election is effective for contracts issued during that calendar year and any subsequent years, and may only be revoked with the consent of the IRS.

Line 3. Supplementary contracts. Enter the amount (discounted at the appropriate rate of interest) necessary to satisfy the obligations under insurance and annuity contracts, but only if the obligations do not involve (at the time the computation is made) life, accident, or health contingencies.

For this item, the appropriate rate of interest is the higher of the prevailing SAIR at the time the obligation first did not involve life, accident, or health contingencies or the rate of interest assumed by the corporation (at that time) in determining the guaranteed benefit. However, the amount of any contract may not be less than the net surrender value of the contract.

Line 4. Dividend accumulations and other amounts. Enter the total dividend accumulations and other amounts held at interest in connection with insurance and annuity contracts.

Line 5. Advance premiums. Enter the total premiums received in advance and liabilities for premium deposit funds. See section 807(e)(7)(A) for special rules for treatment of certain nonlife reserves.

Line 6. Special contingency reserves. Enter the total reasonable special contingency reserves under contracts of

group term life insurance or group accident and health insurance which are established and maintained for the provision of insurance on retired lives, premium stabilization, or for a combination thereof.

Line 8. Increase (decrease) in reserves.

In figuring the amount on line 8, any decrease in reserves must be computed without any reduction of the closing balance of section 807 reserves by the policyholders' share of tax-exempt interest.

Note. In figuring the company's and policyholders' share percentages, carry the computations to enough decimal places to ensure substantial accuracy and to eliminate any significant error in the resulting tax.

Lines 9 and 12. Do not include any of the interest income received on an ESOP loan made prior to August 21, 1996. For binding contract and refinancing rules, see section 1602 of the Small Business Job Protection Act of 1996.

Line 12. If there is an increase in reserves, enter the amount from page 1, line 8. If there is a decrease in reserves, see the instructions for line 2, page 1.

Line 13. Do not include the exempt portion of any of the interest income received on an ESOP loan made prior to August 21, 1996. For binding contract and refinancing rules, see section 1602 of the Small Business Job Protection Act of 1996.

Line 16. In computing the amount entered on line 16, any decrease in reserves must be figured without any reduction of the closing balance of section 807 reserve items by the policyholders' share of tax-exempt interest.

Line 28. Multiply gross investment income (line 9) by 90% or, in the case of gross investment income related to assets held in segregated asset accounts under variable contracts, by 95%. Enter the result on line 28.

Schedule G—Policy Acquisition Expenses

For purposes of section 848(b), all life insurance company members of the same controlled group are treated as one company. Any deduction determined for the group must be allocated among the life insurance companies in the group in such a manner as the IRS may prescribe.

Line 1. Gross premiums and other consideration. Generally, gross premiums and other consideration is the total of:

1. All premiums and other consideration (other than amounts on reinsurance agreements) and
2. Net positive consideration for any reinsurance agreement (see Regulations section 1.848-2(b)).

Also include on this line:

- Advanced premiums,
- Amounts in a premium deposit fund or similar account, as permitted by Regulations section 1.848-2(b)(3),
- Fees,
- Assessments,
- Amounts that the insurance company charges itself representing premiums with respect to benefits for its employees

(including full-time insurance salesmen treated as employees under section 7701(a)(20)), and

- The value of a new contract issued in an exchange described in Regulations section 1.848-2(c)(2) or (3).

Line 2. Return premiums and premiums and other consideration incurred for reinsurance. For purposes of section 848(d)(1)(B) and Regulations section 1.848-2(e), return premiums means amounts (other than policyholder dividends or claims and benefit payments) returned or credited to the policyholder. See Regulations sections 1.848-2(f) and 1.848-3 for how to treat amounts returned to another insurance company under a reinsurance agreement.

Line 5. The entries in columns 5(a), (b), or (c) may be positive or negative.

Line 6. If the sum of columns 5(a), (b), and (c) is negative, enter this negative amount on line 6 and enter -0- on lines 7 and 8. The result is a negative capitalization amount under section 848(f).

Line 9. General deductions. These are deductions under sections 161 through 198, relating to itemized deductions, and sections 401 through 424, relating to pension, profit-sharing, stock bonus plans, etc. Also, include on this line ceding commissions incurred for the reinsurance of a specified insurance contract. Do not include amortization deductions of specified policy acquisition expenses under sections 848(a) or (b). Skip line 9 if the corporation has elected out of the general deductions limitation. See Regulations section 1.848-2(g)(8).

Note. If interest expense is included on line 9, do not also include it on page 1, line 15a.

Line 13. Unamortized specified policy acquisition expenses from prior years. Enter the balance of unamortized specified policy acquisition expenses from prior years as of the beginning of the tax year. See section 848(f)(1)(B).

Line 16. Phase-out amount. The amount of amortization for members of a controlled group and the phase-out of the group's specified policy acquisition expenses under section 848(b) must be allocated to each member in proportion to that member's specified policy acquisition expenses for the tax year.

Schedule H—Small Life Insurance Company Deduction

To qualify for the small life insurance company deduction, a life insurance company must have less than:

- \$15 million of tentative LICTI and
- \$500 million in assets.

The deduction for qualifying small life insurance companies is 60% of the first \$3 million of tentative LICTI for the tax year. If tentative LICTI exceeds \$3 million, the deduction is phased out. The reduction in the deduction is equal to 15% of the tentative LICTI for the tax year that exceeds \$3 million.

In computing the small life insurance company deduction, all life insurance company members of the same controlled group are treated as one company. Any small life insurance company deduction determined for the group must be allocated among the life insurance companies in the group in proportion to their respective tentative LICTIs.

Do not include any items from noninsurance businesses when figuring tentative LICTI for purposes of computing the small life insurance company deduction.

Noninsurance business generally means any activity which is not an insurance business. However, under section 806(b)(3)(B), any activity which is not an insurance business shall be treated as an insurance business if:

1. It is of a type traditionally carried on by life insurance companies for investment purposes, but only if the carrying on of the activity (other than real estate) does not constitute the active conduct of a trade or business or

2. It involves the performance of administrative services in connection with plans providing life insurance, pension, or accident and health benefits.

For the assets test, the assets of all members of a controlled group, as defined in section 806(c)(3), must be included, whether or not they are life insurance companies. For information regarding the valuation of assets, see the instructions for Schedule L, Part I.

Schedule I—Limitation on Noninsurance Losses

Section 806(b)(3)(C) provides that, in computing LICTI, any loss from noninsurance business (defined above in the instructions for Schedule H) is limited to the smaller of:

- 35% of the loss or
- 35% of LICTI (computed by excluding any noninsurance loss included in arriving at LICTI on line 24, page 1).

For more information on either the computation of the allowable loss deduction or on applicable carryback provisions, see section 1503(c).

Schedule J Part I—Shareholders Surplus Account

Any stock life insurance company that had a policyholders surplus account (PSA) on December 31, 1983, will continue to maintain a shareholders surplus account (SSA). See section 815(c)(1) for more information.

Line 2d. Do not include the increase in cash value for section 264(f) policies.

Line 4. In figuring the tax liability on line 4, adjustments must be made for any year in which the alternative minimum tax is imposed or the minimum tax credit has been taken.

Line 6. Enter all amounts treated under section 815 as distributions to shareholders.

Any distribution to shareholders is treated as having been made first out of the SSA, to the extent thereof.

Part II—Policyholders Surplus Account

Any stock life insurance company that had an existing PSA on December 31, 1983, will continue to maintain the account. See section 815(d)(1). While no additions can be made to this account, it must be decreased by amounts specified in section 815(d)(3). Also, section 815(f) provides that, in general, the provisions of subsections (d), (e), (f), and (g) of section 815 as in effect before the enactment of the Tax Reform Act of 1984 ("Act of 1984") continue to apply to any PSA that had a balance as of December 31, 1983.

Amounts subtracted from the PSA for a tax year are added to LICTI and are subject to tax under section 801.

Line 8. If the balance at the end of the preceding tax year differs from the balance at the beginning of the current tax year (for example, due to section 815(d)(5) as in effect prior to the Act of 1984), attach a schedule showing the adjustments made. Prior to the Act of 1984, section 815(d)(5) provided that, if any addition to the PSA increases or creates a loss from operations and part or all of the loss cannot be used in any other year to reduce LICTI, then the loss will reduce the PSA at the time that the addition was made. In this case, the beginning balance of the PSA must be adjusted before any subtractions for the current tax year are made.

Line 9b. To figure the tax increase due to the amount entered on line 9a:

1. Subtract the corporation's tax rate from 100%.
2. Divide the distributions on line 9a by the result of step 1.
3. Subtract the amount on line 9a from the result of step 2, and
4. Enter the result of step 3 on line 9b.

Line 9c. To figure the amount to enter on line 9c:

1. Determine the total amount to be subtracted from the PSA under sections 815(d)(1) and 815(d)(4) as in effect prior to the Act of 1984 (do this only after the amounts on lines 9a and 9b are subtracted from the beginning balance in the PSA).
2. Add 100% to the corporation's tax rate.
3. Divide the result of step 1 by the result of step 2, and
4. Enter the result of step 3 on line 9c.

The amount entered on line 9c must be added to the SSA at the beginning of the next tax year.

Line 9d. Subtract the result of step 3, line 9c, from the result of step 1, line 9c. Enter the result on line 9d.

Line 9e. Enter the total amount to be subtracted from the PSA under section 815(d)(2) as in effect prior to the Act of 1984. At that time, section 815(d)(2) provided that if, for any tax year, a corporation was not an insurance company, or if for any 2 successive tax years a corporation was not a life insurance

company, then any balance remaining in the PSA at the end of the last tax year that the corporation was a life insurance company must be included in taxable income for that tax year.

Schedule K—Tax Computation

Line 1. Members of a controlled group. A member of a controlled group must check the box on line 1 and complete lines 2a and 2b of Schedule K, Form 1120-L. The term "controlled group" means any parent-subsidiary group, brother-sister group, or combined group. See the definitions below.

Parent-subsidiary group. A parent-subsidiary group is one or more chains of corporations connected through stock ownership with a common parent corporation if:

- Stock possessing at least 80% of the total combined voting power of all classes of stock entitled to vote or at least 80% of the total value of shares of all classes of stock of each of the corporations, except the common parent corporation, is directly or indirectly owned by one or more of the other corporations; and
- The common parent corporation directly or indirectly owns stock possessing at least 80% of the total combined voting power of all classes of stock entitled to vote or at least 80% of the total value of shares of all classes of stock of at least one of the other corporations, excluding, in computing such voting power or value, stock owned directly by such other corporations.

Brother-sister group. A brother-sister group is two or more corporations if 5 or fewer persons who are individuals, estates, or trusts directly or indirectly own stock possessing:

1. At least 80% of the total combined voting power of all classes of stock entitled to vote or at least 80% of the total value of shares of all classes of the stock of each corporation, and
2. More than 50% of the total combined voting power of all classes of stock entitled to vote or more than 50% of the total value of shares of all classes of stock of each corporation, taking into account the stock ownership of each such person only to the extent such stock ownership is identical with respect to each such corporation.

For tax years beginning after October 22, 2004, the definition of brother-sister group does not include (1) above, but only for purposes of the taxable income bracket, alternative minimum tax, exemption amounts and accumulated earnings credit.

Combined group. A combined group is three or more corporations each of which is a member of a parent-subsidiary group or a brother-sister group, and one of which is:

- A common parent corporation included in a group of corporations in a parent-subsidiary group, and also
- Included in a group of corporations in a brother-sister group.

For more details on controlled groups, see section 1563.

Line 2a. Members of a controlled group are entitled to one \$50,000, one \$25,000, and one \$9,925,000 taxable income bracket amount (in that order) on line 2a.

When a controlled group adopts or later amends an apportionment plan, each member must attach to its tax return a copy of its consent to this plan. The copy (or an attached statement) must show the part of the amount in each taxable income bracket apportioned to that member. See Regulations section 1.1561-3(b) for other requirements and for the time and manner of making the consent.

Unequal apportionment plan.

Members of a controlled group can elect an unequal apportionment plan and divide the taxable income brackets as they want. There is no need for consistency among taxable income brackets. Any member may be entitled to all, some, or none of the taxable income bracket. However, the total amount for all members cannot be more than the total amount in each taxable income bracket.

Equal apportionment plan. If no apportionment plan is adopted, members of a controlled group must divide the amount in each taxable income bracket equally among themselves. For example, Controlled Group AB consists of Corporation A and Corporation B. They do not elect an apportionment plan. Therefore, each corporation is entitled to:

- \$25,000 (one-half of \$50,000) on line 2a(1),
- \$12,500 (one-half of \$25,000) on line 2a(2), and
- \$4,962,500 (one-half of \$9,925,000) on line 2a(3).

Line 2b. Members of a controlled group are treated as one group to figure the applicability of the additional 5% tax and the additional 3% tax. If an additional tax applies, each member will pay that tax based on the part of the amount used in each taxable income bracket to reduce that member's tax. See section 1561(a). If an additional tax applies, attach a schedule showing the taxable income of the entire group and how the corporation figured its share of the additional tax.

Line 2b(1). Enter the corporation's share of the additional 5% tax on line 2b(1).

Line 2b(2). Enter the corporation's share of the additional 3% tax on line 2b(2).

Line 3. Most corporations figure their tax by using the Tax Rate Schedule, below. Exceptions apply to members of a controlled group. See the Tax Computation Worksheet for Members of a Controlled Group on this page. Members of a controlled group must attach a statement showing the computation of the tax entered on line 3.

Tax Rate Schedule

If taxable income on line 27, page 1 is:

Over—	But not over—	Tax is:	Of the amount over—
\$0	\$50,000	15%	\$0
50,000	75,000	\$ 7,500 + 25%	50,000
75,000	100,000	13,750 + 34%	75,000
100,000	335,000	22,250 + 39%	100,000
335,000	10,000,000	113,900 + 34%	335,000
10,000,000	15,000,000	3,400,000 + 35%	10,000,000
15,000,000	18,333,333	5,150,000 + 38%	15,000,000
18,333,333	-----	35%	0

Note. Gain recognized by a life insurance company from the redemption of market discount bonds issued before July 19, 1984, and acquired on or before September 25, 1985, is taxed at a rate of 31.6% only if it is less than the tax that otherwise would be imposed. See section 1011(d) of the Tax Reform Act of 1986 as amended by The Technical and Miscellaneous Revenue Act of 1988. On the dotted line to the left of line 3, write "Tax differential rate of 31.6% used" and the amount.

Deferred tax under section 1291. If the corporation was a shareholder in a passive foreign investment company (PFIC) and received an excess distribution or disposed of its investment in the PFIC during the year, it must include the total increase in taxes due under section 1291(c)(2) in the total for

line 3. On the dotted line to the left of line 3, enter "Section 1291" and the amount.

Do not include on line 3 any interest due under section 1291(c)(3). Instead, show the amount of interest owed in the bottom margin of page 1, Form 1120-L, and enter "Section 1291 interest." For details, see Form 8621.

Additional tax under section 197(f). A corporation that elects to pay tax on the gain from the sale of an intangible under the related person exception to the anti-churning rules should include any additional tax due under section 197(f)(9)(B) in the total for line 3. On the dotted line next to line 3, enter "Section 197" and the amount. For more information, see Pub. 535, Business Expenses.

Line 4. Alternative minimum tax (AMT).

 A corporation that is not a small corporation exempt from the AMT (see page 17) may be required to file Form 4626 if it claims certain credits, even though it does not owe any AMT. See Form 4626 for details.

Unless the corporation is treated as a small corporation exempt from the AMT, it may owe the AMT if it has any of the adjustments and tax preference items listed on Form 4626. A life insurance company must file Form 4626 if its LICIT before the operations loss deduction, combined with these adjustments and tax preference items, is more than the smaller of \$40,000 or the

Tax Computation Worksheet for Members of a Controlled Group
(keep for your records)

Note. Each member of a controlled group must compute its tax using this worksheet.

1. Enter taxable income (line 27, page 1) _____
2. Enter line 1 or the corporation's share of the \$50,000 taxable income bracket, whichever is less _____
3. Subtract line 2 from line 1 _____
4. Enter line 3 or the corporation's share of the \$25,000 taxable income bracket, whichever is less _____
5. Subtract line 4 from line 3 _____
6. Enter line 5 or the corporation's share of the \$9,925,000 taxable income bracket, whichever is less _____
7. Subtract line 6 from line 5 _____
8. Multiply line 2 by 15% _____
9. Multiply line 4 by 25% _____
10. Multiply line 6 by 34% _____
11. Multiply line 7 by 35% _____
12. If the taxable income of the controlled group exceeds \$100,000, enter this member's share of the smaller of: 5% of the taxable income in excess of \$100,000, or \$11,750 (see instructions for Schedule K, line 2b). _____
13. If the taxable income of the controlled group exceeds \$15 million, enter this member's share of the smaller of 3% of the taxable income in excess of \$15 million, or \$100,000 (see instructions for Schedule K, line 2b). _____
14. **Total.** Add lines 8 through 13. Enter here and on line 3, Schedule K _____

life insurance company's allowable exemption amount (from Form 4626).

See Form 4626 and its instructions for details.

Note. See section 56(g)(4)(B)(ii) for special rules for life insurance companies for the computation of adjusted current earnings.

Exemption for small corporation. A corporation is treated as a small corporation exempt from the AMT for its tax year beginning in 2004 if that year is the corporation's first tax year in existence (regardless of its gross receipts) or:

1. It was treated as a small corporation exempt from the AMT for all prior tax years beginning after 1997 and

2. Its average annual gross receipts for the 3-tax-year period (or portion thereof during which the corporation was in existence) ending before its tax year beginning in 2004 did not exceed \$7.5 million (\$5 million if the corporation had only 1 prior tax year).

Line 6a. Foreign tax credit. To find out when a corporation can take this credit for payment of income tax to a foreign country or U.S. possession, see Form 1118, Foreign Tax Credit—Corporations.

Line 6b. Other credits. Include any other credits on line 6b. On the dotted line to the left of the entry space, write the amount of the credit and identify it.

Possessions tax credit. The Small Business Job Protection Act of 1996 repealed the possessions credit. However, existing credit claimants may qualify for a credit under the transitional rules. See Form 5735, Possessions Corporation Tax Credit (Under Sections 936 and 30A).

Nonconventional source fuel credit. A credit is allowed for the sale of qualified fuels produced from a nonconventional source. Section 29 contains a definition of qualified fuels, provisions for figuring the credit, and other special rules. Attach a separate schedule to the return showing the computation of the credit.

Qualified electric vehicle (QEV) credit. Include on line 6b any credit from Form 8834, Qualified Electric Vehicle Credit.

Line 6c. General Business Credit. Enter on line 6c the corporation's total general business credit.

If the corporation is filing Form 8844, Empowerment Zone and Renewal Community Employment Credit, Form 8884, New York Liberty Zone Business Employee Credit, or Form 8835 (see list below) with a credit from Section B, check the "Form(s)" box, enter the form number in the space provided, and include the allowable credit on line 6c.

If the corporation is required to file Form 3800, General Business Credit, check the "Form 3800" box and include the allowable credit on line 6c.

If the corporation is not required to file Form 3800, check the "Form(s)" box, enter the form number in the space provided, and include on line 6c the allowable credit from the applicable form listed below.

- Investment Credit (Form 3468).
- Work Opportunity Credit (Form 5884).

- Credit for Alcohol Used as Fuel (Form 6478).
- Credit for Increasing Research Activities (Form 6765).
- Low-Income Housing Credit (Form 8586).
- Orphan Drug Credit (Form 8820).
- Disabled Access Credit (Form 8826).
- Enhanced Oil Recovery Credit (Form 8830).
- Renewable Electricity and Refined Coal Production Credit (Form 8835).
- Indian Employment Credit (Form 8845).
- Credit for Employer Social Security and Medicare Taxes Paid on Certain Employee Tips (Form 8846).
- Credit for Contributions to Selected Community Development Corporations (Form 8847).
- Biodiesel Fuels Credit (Form 8864).
- Welfare-to-Work Credit (Form 8861).
- New Markets Credit (Form 8874).
- Credit for Small Employer Pension Plan Startup Costs (Form 8881).
- Credit for Employer-Provided Childcare Facilities and Services (Form 8882).
- Low Sulfur Diesel Fuel Production Credit (Form 8896).

Line 6d. Credit for prior year minimum tax. To figure the minimum tax credit and any carryforward of that credit, use Form 8827, Credit for Prior Year Minimum Tax—Corporations. Also see Form 8827 if any of the corporation's 2003 nonconventional source fuel credit or qualified electric vehicle credit was disallowed solely because of the tentative minimum tax limitation. See section 53(d).

Line 6e. Qualified zone academy bond credit. Enter the amount of any credit from Form 8860, Qualified Zone Academy Bond Credit.

Line 9. Foreign Corporations. A foreign corporation carrying on a life insurance business in the United States is taxed as a domestic life insurance company on its income effectively connected with the conduct of a trade or business in the United States (see sections 864(c) and 897 for definition).

Generally, any other U.S.-source income received by the foreign corporation is taxed at 30% (or at a lower treaty rate) under section 881. If the corporation has this income, attach a schedule showing the kind and amount of income, the tax rate, and the amount of tax. Enter the tax on line 9. However, see *Reduction of section 881 tax* below.

Note. Interest received from certain portfolio debt investments that were issued after July 18, 1984, is not subject to the tax. See section 881(c) for details.

See section 842 for more information.

Minimum effectively connected investment income. See section 842(b) and Notice 89-96, 1989-2 C.B. 417, for the general rules for computing this amount. Also, see Rev. Proc. 2004-55, 2004-34 I.R.B. 343, for the domestic asset/liability percentages and domestic yields needed to compute this amount.

Any additional income required by section 842(b) must be included in LICTI (e.g., line 7, page 1).

Reduction of section 881 tax. Additional taxes resulting from the net

investment income adjustment may offset a corporation's section 881 tax on U.S.-source income. The tax reduction is determined by multiplying the section 881 tax by the ratio of the amount of income adjustment to income subject to the section 881 tax, computed without the exclusion for interest on state and local bonds or income exempted from taxation by treaty (section 842(c)(2)). Attach a statement showing how the reduction of section 881 tax was figured. Enter the net tax imposed by section 881 on line 9.

Note. Section 842(c)(1) requires that foreign life insurance companies make the investment income adjustment before claiming a small life insurance company deduction.

Line 10. Other Taxes. Include any of the following taxes and interest in the total on line 10. Check the appropriate box(es) for the form, if any, used to compute the total.

Recapture of investment credit. If the corporation disposed of investment credit property or changed its use before the end of its useful life or recovery period, it may owe a tax. See Form 4255, Recapture of Investment Credit, for details.

Recapture of low-income housing credit. If the corporation disposed of property (or there was a reduction in the qualified basis of the property) for which it took the low-income housing credit, it may owe a tax. See Form 8611, Recapture of Low-Income Housing Credit.

Other. Additional taxes and interest amounts can be included in the total entered on line 10. Check the box for "Other" if the corporation includes any additional taxes and interest such as the items discussed below. See *How to report* below for details on reporting these amounts on an attached schedule.

• Recapture of qualified electric vehicle (QEV) credit. The corporation must recapture part of the QEV credit claimed in a prior year, if, within 3 years of the date the vehicle was placed in service, it ceases to qualify for the credit. See Regulations section 1.30-1 for details on how to figure the recapture.

• Recapture of Indian employment credit. Generally, if an employer terminates the employment of a qualified employee less than 1 year after the date of initial employment, any Indian employment credit allowed for a prior tax year because of wages paid or incurred to that employee must be recaptured. For details, see Form 8845 and section 45A.

• Recapture of new markets credit (see Form 8874).

• Recapture of employer-provided childcare facilities and services credit (see Form 8882).

• Interest on deferred tax attributable to certain nondealer installment obligations (section 453A(c)).

• Interest due on deferred gain (section 1260(b)).

• For tax years beginning after October 22, 2004, tax on notional shipping income. See *Income from qualifying shipping activities*, on page 6.

How to report. If the corporation checked the "Other" box, attach a schedule showing the computation of each item included in the total for line 10 and identify

the applicable Code section and the type of tax or interest.

Line 11. Total Tax. Include any deferred tax on the termination of a section 1294 election applicable to shareholders in a qualified electing fund in the amount entered on line 11. See Form 8621, Part V, and *How to report*, below.

Subtract any deferred tax on the corporation's share of undistributed earnings of a qualified electing fund (see Form 8621, Part II).

How to report. Attach a schedule showing the computation of each item included in, or subtracted from, the total for line 11. On the dotted line next to line 11, specify (a) the applicable Code section, (b) the type of tax, and (c) the amount of tax.

Schedule L

All filers must complete Parts I and II of Schedule L.

Note. Foreign life insurance companies should report assets and insurance liabilities for their U.S. business only.

Part I—Total Assets

For Schedule L, assets means all assets of the corporation. In valuing real property and stocks, use fair market value; for other assets, use the adjusted basis as determined under section 1011 and related sections, without regard to section 818(c). An interest in a partnership or trust is not itself treated as an asset of the corporation. Instead, the corporation is treated as actually owning its proportionate share of the assets held by the partnership or trust. The value of the corporation's share of these assets should be listed on line 3.

Part II—Total Assets and Total Insurance Liabilities

Foreign life insurance companies must maintain a minimum surplus of U.S. assets over their U.S. insurance liabilities. The minimum required surplus is determined by multiplying their U.S. insurance liabilities by a percentage determined by the IRS. The IRS determines the percentage from data supplied by domestic life insurance companies in Schedule L, Part II. See section 842.

For Schedule L, total insurance liabilities means the sum of the following amounts as of the end of the tax year:

1. Total reserves as defined in section 816(c); plus
2. The items referred to in paragraphs (3), (4), (5), and (6) of section 807(c), to the extent such amounts are not included in total reserves.

Foreign life insurance companies, see Notice 89-96 for more information on determining total insurance liabilities on U.S. business.

Schedule M—Other Information

Be sure to complete the items that apply to the corporation.

Question 6. Check the "Yes" box if:

- The corporation is a subsidiary in an affiliated group (defined below), but is not filing a consolidated return for the tax year with that group or
- The corporation is a subsidiary in a parent-subsidiary controlled group (defined on page 15).

Any corporation that meets either of the requirements above should check the "Yes" box. This applies even if the corporation is a subsidiary member of one group and the parent corporation of another.

Note. If the corporation is an "excluded member" of a controlled group (see section 1563(b)(2)), it is still considered a member of a controlled group for this purpose.

Affiliated group. An affiliated group is one or more chains of includible corporations (section 1504(a)) connected through stock ownership with a common parent corporation. The common parent must be an includible corporation and the following requirements must be met.

1. The common parent must own directly stock that represents at least 80% of the total voting power and at least 80% of the total value of the stock of at least one of the other includible corporations and
2. Stock that represents at least 80% of the total voting power and at least 80% of the total value of the stock of each of the other corporations (except for the common parent) must be owned directly by one or more of the other includible corporations.

For this purpose, "stock" generally does not include any stock that (a) is nonvoting, (b) is nonconvertible, (c) is limited and preferred as to dividends and does not participate significantly in corporate growth, and (d) has redemption and liquidation rights that do not exceed the issue price of the stock (except for a reasonable redemption or liquidation premium). See section 1504(a)(4).

Question 8. Check the "Yes" box if one foreign person owned at least 25% of (a) the total voting power of all classes of stock of the corporation entitled to vote or (b) the total value of all classes of stock of the corporation.

The constructive ownership rules of section 318 apply in determining if a corporation is foreign owned. See section 6038A(c)(5) and the related regulations.

Enter on line 8a the percentage owned by the foreign person specified in question 8. On line 8b, write the name of the owner's country.

Note. If there is more than one 25%-or-more foreign owner, complete lines 8a and 8b for the foreign person with the highest percentage of ownership.

Foreign person. The term "foreign person" means:

- A foreign citizen or nonresident alien.
- An individual who is a citizen of a U.S. possession (but who is not a U.S. citizen or resident).
- A foreign partnership.
- A foreign corporation.
- Any foreign estate or trust within the meaning of section 7701(a)(31).
- A foreign government (or one of its agencies or instrumentalities) to the extent

that it is engaged in the conduct of a commercial activity as described in section 892.

Owner's country. For individuals, the term "owner's country" means the country of residence. For all others, it is the country where incorporated, organized, created, or administered.

Requirement to file Form 5472. If the corporation checked "Yes" to Question 8, it may have to file Form 5472. Generally, a 25% foreign-owned corporation that had a reportable transaction with a foreign or domestic related party during the tax year must file Form 5472.

See Form 5472 for filing instructions and penalties for failure to file.

Item 12. If the corporation has an operations loss deduction (OLD), it may elect under section 810(b)(3) to waive the entire carryback period for the OLD and instead carry the OLD forward to future tax years. To do so, check the box on line 12 and file the tax return by its due date, including extensions (do not attach the statement described in Temporary Regulations section 301.9100-12T). Once made, the election is irrevocable. See Pub. 542, section 810, and Form 1139 for more details.

Corporations filing a consolidated return must also attach the statement required by Temporary Regulations section 1.1502-21T(b)(3)(i) or (ii).

Item 13. Enter the amount of the operations loss carryover to the tax year from prior years, even if some of the loss is used to offset income on this return. The amount to enter is the total of all operating losses generated in prior years but not used to offset income (either as a carryback or carryover) in a tax year prior to 2004. Do not reduce the amount by any OLD reported on line 20, page 1.

Privacy Act and Paperwork Reduction Act Notice

We ask for the information on this form to carry out the Internal Revenue laws of the United States. You are required to give us the information. We need it to ensure that you are complying with these laws and to allow us to figure and collect the right amount of tax. Section 6109 requires return preparers to provide their identifying numbers on the return.

You are not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by section 6103.

The time needed to complete and file this form will vary depending on individual circumstances. The estimated average time is:

Recordkeeping 83 hr., 56 min.

Learning about the law or the form 40 hr., 28 min.

Preparing the form . . . 64 hr., 6 min.
**Copying, assembling,
and sending the form
to the IRS** 5 hr., 54 min.

If you have comments concerning the accuracy of these time estimates or suggestions for making this form simpler, we would be happy to hear from you. You can write to the Internal Revenue Service, Tax Products Coordinating Committee, SE:W:CAR:MP:T:T:SP, 1111 Constitution Ave. NW, IR-6406, Washington, DC 20224.

Do not send the tax form to this office. Instead, see *Where To File* on page 2.
