

Section 809.—Reduction in Certain Deductions of Mutual Life Insurance Companies

26 CFR 1.809-9: Computation of the differential earnings rate and the recomputed differential earnings rate.

Mutual life insurance companies; differential earnings rate. The differential earnings rate for 1997 and the recomputed differential earnings rate for 1996 are set forth for use by mutual life insurance companies to compute their income tax liabilities for 1997.

Rev. Rul. 98-38

This revenue ruling contains the differential earnings rate for 1997 and the recomputed differential earnings rate for 1996. Under § 809 of the Internal Revenue Code, mutual life insurance companies use these rates in computing their Federal income tax liability for taxable years beginning in 1997. This revenue ruling also contains the figures on which the determinations of these rates are based. Notice 98-19, 1998-13 I.R.B. 24, contained tentative determinations of these rates.

Section 809(a) provides that, in the case of any mutual life insurance company, the amount of the deduction allowable under § 808 for policyholder dividends is reduced (but not below zero) by the “differential earnings amount.” Any excess of the differential earnings amount over the amount of the deduction allowable under § 808 is taken into account as a reduction in the closing balance of reserves under subsections (a) and (b) of § 807. The “differential earnings

amount” for any taxable year is the amount equal to the product of (a) the life insurance company’s average equity base for the taxable year multiplied by (b) the “differential earnings rate” for that taxable year. The “differential earnings rate” for the taxable year is the excess of (a) the “imputed earnings rate” for the taxable year over (b) the “average mutual earnings rate” for the second calendar year preceding the calendar year in which the taxable year begins. The “imputed earnings rate” for any taxable year is the amount that bears the same ratio to 16.5 percent as the “current stock earnings rate” for the taxable year bears to the “base period stock earnings rate.”

Section 809(f) provides that, in the case of any mutual life insurance company, if the “recomputed differential earnings amount” for any taxable year exceeds the differential earnings amount for that taxable year, the excess is included in life insurance gross income for the succeeding taxable year. If the differential earnings amount for any taxable year exceeds the recomputed differential earnings amount for that taxable year, the excess is allowed as a life insurance deduction for the succeeding taxable year. The “recomputed differential earnings amount” for any taxable year is an amount calculated in the same manner as the differential earnings amount for that taxable year, except that the average mutual earnings rate for the calendar year in which the taxable year begins is substituted for the average mutual earnings rate for the second calendar year preceding the calendar year in which the taxable year begins.

The stock earnings rates and mutual

earnings rates taken into account under § 809 generally are determined by dividing statement gain from operations by the average equity base. For this purpose, the term “statement gain from operations” means “the net gain or loss from operations required to be set forth in the annual statement, determined without regard to Federal income taxes, and . . . properly adjusted for realized capital gains and losses. . . .” See § 809(g)(1). The term “equity base” is defined as an amount determined in the manner prescribed by regulations equal to surplus and capital increased by the amount of nonadmitted financial assets, the excess of statutory reserves over the amount of tax reserves, the sum of certain other reserves, and 50 percent of any policyholder dividends (or other similar liability) payable in the following taxable year. See § 809(b)(2), (3), (4), (5) and (6). Section 1.809-10 of the Income Tax Regulations provides that the equity base includes both the asset valuation reserve and the interest maintenance reserve for taxable years ending after December 31, 1991.

Section 1.809-9(a) of the regulations provides that neither the differential earnings rate under § 809(c) nor the recomputed differential earnings rate that is used in computing the recomputed differential earnings amount under § 809(f)(3) may be less than zero.

For purposes of § 809, the differential earnings rate for 1997 and the rate used to calculate the recomputed differential earnings amount for 1996 (the recomputed differential earnings rate for 1996), and the figures on which these two rates are based are set forth in Table 1.

Differential earnings rate for 1997	0
Recomputed differential earnings rate for 1996	0
Imputed earnings rate for 1996	15.669
Imputed earnings rate for 1997	13.813
Base period stock earnings rate	18.221
Current stock earnings rate for 1997	15.254
Stock earnings rate for 1994	11.437
Stock earnings rate for 1995	17.087
Stock earnings rate for 1996	17.238
Average mutual earnings rate for 1995	16.477
Average mutual earnings rate for 1996	16.112

DRAFTING INFORMATION

The principal author of this revenue ruling is Katherine A. Hossofsky of the Assistant Chief Counsel (Financial Institutions and Products). For further information regarding this revenue ruling contact Ms. Hossofsky on (202) 622-3477 (not a toll-free number).