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FROM THE EDITOR IN THIS ISSUE

By Christian DesRochers

To say this has been an unusual fall would be an understatement. I happened to be in Washington, D.C. for the earthquake. And here in Connecticut, thanks to Hurricane Irene and Winter Storm Alfred, our normally quiet neighborhood has featured the sounds of chainsaws and generators running. As I write this, I have snow on the ground in my yard, which is expected in February, but not in late October. For some, a hot shower is a luxury, which makes us appreciate the little things in life when we don't have them.

Getting back to the business of life insurance taxation and *TAXING TIMES*, this issue addresses a variety of topics, including a discussion by Ed Robbins and Stephen Baker related to the treatment of federal income tax in actuarial projections, as well as articles and tidbits on recent guidance. These cover topics ranging from Notice 2011-53 addressing FATCA (the Foreign Account Tax Compliance Act), the economic substance doctrine, the necessary premium test under section 7702A and SEPP guidance on annuities.

As we look to the future, the Obama administration has proposed changes related to life insurance companies and products as a part of the 2012 budget. These include:

1. **Modify the reporting requirements for life settlement contracts**—The proposal would expand information reporting on the sale of life insurance contracts and the payment of death benefits on contracts that were sold, and would modify the “transfer-for-value” exceptions to prevent purchasers of policies from avoiding tax on death benefits that are received. It would apply to sales or assignment of interests in life insurance policies and payments of death benefits for taxable years beginning after Dec. 31, 2011.
2. **Modify the dividends received deduction (DRD)**—The separate account DRD has been the subject of much controversy between the Internal Revenue Service (IRS) and the industry. Under the administration proposal, the DRD with regard to separate account dividends would be based on the proportion of reserves to total assets of the account. The administration has also proposed a change in the general account DRD. Under the proposal, the DRD with regard to general account dividends would be subject to the same flat proration percentage that applies to non-life companies under current law (15 percent). In their “Description of Revenue Provisions Contained in the President’s Fiscal Year 2012 Budget Proposal,” the Joint Committee on Taxation discussed an alternate approach that would base the general account DRD on a percentage determined by the ratio of the tax-exempt assets to total assets. (See JCS-3-11 June 2011, 286.) The proposal would be effective for taxable years beginning after Dec. 31, 2011. (*Editor’s Note: In their discussion of the separate account DRD, the Joint Committee staff cited Susan Hotine’s TAXING TIMES articles related to the issue.*)
3. **Expand the pro-rata interest expense disallowance for corporate-owned life insurance**—The interest deductions of a business other than an insurance company are reduced to the extent the interest is allocable to unborrowed policy cash values on life insurance and annuity contracts. Under the proposal, the exception for officers, directors and employees would be repealed unless those individuals are also 20 percent owners of

the business that is the owner or beneficiary of the contracts. The proposal would apply to contracts issued after Dec. 31, 2011, in taxable years ending after that date.

- 4. Require information reporting for private separate accounts of life insurance companies**—The proposal would require information reporting with regard to each life insurance or annuity contract whose investment in a separate account represents at least 10 percent of the value of the account. The proposal would be effective for taxable years beginning after Dec. 31, 2011.

Given the current political debate in Washington, it is far from clear that any of the proposals will be enacted.

With respect to the IRS, the Year-End 2010-2011 Priority Guidance Plan included a number of issues related to the life insurance industry. Two issues that remain under consideration include:

1. Guidance clarifying whether deficiency reserves should be taken into account in computing the amount of statutory reserves under §807(d)(6) (the “statutory cap”).
2. Guidance under §7702 defining cash surrender value.

The Plan also includes guidance on the separate account DRD issue. As noted above, the issue is included in the administration budget, so the expectation is that it will be handled by legislation rather than guidance.

As always, our authors will provide commentary on these and other issues as they arise. The process of putting *TAXING TIMES* together is truly a team effort, including the editorial board, the authors, the reviewers, editorial staff and the Society of Actuaries’ staff. Together, it always seems to come together, which is a tribute to the entire team. Once again, I’d like to thank everyone who worked on this issue. ◀

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