

§ 845. Certain reinsurance agreements**(a) Allocation in case of reinsurance agreement involving tax avoidance or evasion**

In the case of 2 or more related persons (with- in the meaning of section 482) who are parties to a reinsurance agreement (or where one of the parties to a reinsurance agreement is, with re- spect to any contract covered by the agreement, in effect an agent of another party to such agreement or a conduit between related per- sons), the Secretary may—

- (1) allocate between or among such persons income (whether investment income, pre- mium, or otherwise), deductions, assets, re- serves, credits, and other items related to such agreement,
- (2) recharacterize any such items, or
- (3) make any other adjustment,

if he determines that such allocation, re- characterization, or adjustment is necessary to reflect the proper amount, source, or character of the taxable income (or any item described in paragraph (1) relating to such taxable income) of each such person.

(b) Reinsurance contract having significant tax avoidance effect

If the Secretary determines that any reinsur- ance contract has a significant tax avoidance ef- fect on any party to such contract, the Sec- retary may make proper adjustments with re- spect to such party to eliminate such tax avoid- ance effect (including treating such contract with respect to such party as terminated on De- cember 31 of each year and reinstated on Janu- ary 1 of the next year).

(Added Pub. L. 98-369, div. A, title II, §212(a), July 18, 1984, 98 Stat. 757; amended Pub. L. 108-357, title VIII, §803(a), Oct. 22, 2004, 118 Stat. 1569.)

AMENDMENTS

2004—Subsec. (a). Pub. L. 108-357 substituted “amount, source, or character” for “source and char- acter” in concluding provisions.

EFFECTIVE DATE OF 2004 AMENDMENT

Pub. L. 108-357, title VIII, §803(b), Oct. 22, 2004, 118 Stat. 1569, provided that: “The amendments made by this section [amending this section] shall apply to any risk reinsured after the date of the enactment of this Act [Oct. 22, 2004].”

EFFECTIVE DATE

Pub. L. 98-369, div. A, title II, §217(d), July 18, 1984, 98 Stat. 762, as amended by Pub. L. 99-514, §2, Oct. 22, 1986, 100 Stat. 2095, provided that:

“(1) Subsection (a) of section 845 of the Internal Re- venue Code of 1986 [formerly I.R.C. 1954] (as added by this title) shall apply with respect to any risk reins- ured on or after September 27, 1983.

“(2) Subsection (b) of section 845 of such Code (as so added) shall apply with respect to risks reinsured after December 31, 1984.”

§ 846. Discounted unpaid losses defined**(a) Discounted losses determined****(1) Separately computed for each accident year**

The amount of the discounted unpaid losses as of the end of any taxable year shall be the sum of the discounted unpaid losses (as of such

time) separately computed under this section with respect to unpaid losses in each line of business attributable to each accident year.

(2) Method of discounting

The amount of the discounted unpaid losses as of the end of any taxable year attributable to any accident year shall be the present value of such losses (as of such time) determined by using—

- (A) the amount of the undiscounted unpaid losses as of such time,
- (B) the applicable interest rate, and
- (C) the applicable loss payment pattern.

(3) Limitation on amount of discounted losses

In no event shall the amount of the dis- counted unpaid losses with respect to any line of business attributable to any accident year exceed the aggregate amount of unpaid losses with respect to such line of business for such accident year included on the annual state- ment filed by the taxpayer for the year ending with or within the taxable year.

(4) Determination of applicable factors

In determining the amount of the discounted unpaid losses attributable to any accident year—

- (A) the applicable interest rate shall be the interest rate determined under sub- section (c) for the calendar year with which such accident year ends, and
- (B) the applicable loss payment pattern shall be the loss payment pattern deter- mined under subsection (d) which is in effect for the calendar year with which such acci- dent year ends.

(b) Determination of undiscounted unpaid losses

For purposes of this section—

(1) In general

Except as otherwise provided in this sub- section, the term “undiscounted unpaid losses” means the unpaid losses shown in the annual statement filed by the taxpayer for the year ending with or within the taxable year of the taxpayer.

(2) Adjustment if losses discounted on annual statement

If—

- (A) the amount of unpaid losses shown in the annual statement is determined on a dis- counted basis, and
- (B) the extent to which the losses were dis- counted can be determined on the basis of information disclosed on or with the annual statement,

the amount of the unpaid losses shall be deter- mined without regard to any reduction attrib- utable to such discounting.

(c) Rate of interest**(1) In general**

For purposes of this section, the rate of in- terest determined under this subsection shall be the annual rate determined by the Sec- retary under paragraph (2).

(2) Determination of annual rate

The annual rate determined by the Sec- retary under this paragraph for any calendar

year shall be a rate determined on the basis of the corporate bond yield curve (as defined in section 430(h)(2)(D)(i), determined by substituting “60-month period” for “24-month period” therein).

(d) Loss payment pattern

(1) In general

For each determination year, the Secretary shall determine a loss payment pattern for each line of business by reference to the historical loss payment pattern applicable to such line of business. Any loss payment pattern determined by the Secretary shall apply to the accident year ending with the determination year and to each of the 4 succeeding accident years.

(2) Method of determination

Determinations under paragraph (1) for any determination year shall be made by the Secretary—

(A) by using the aggregate experience reported on the annual statements of insurance companies,

(B) on the basis of the most recent published aggregate data from such annual statements relating to loss payment patterns available on the 1st day of the determination year,

(C) as if all losses paid or treated as paid during any year are paid in the middle of such year, and

(D) in accordance with the computational rules prescribed in paragraph (3).

(3) Computational rules

For purposes of this subsection—

(A) In general

Except as otherwise provided in this paragraph, the loss payment pattern for any line of business shall be based on the assumption that all losses are paid—

(i) during the accident year and the 3 calendar years following the accident year, or

(ii) in the case of any line of business reported in the schedule or schedules of the annual statement relating to auto liability, other liability, medical malpractice, workers' compensation, and multiple peril lines, during the accident year and the 10 calendar years following the accident year.

(B) Treatment of certain losses

(i) 3-year loss payment pattern

In the case of any line of business not described in subparagraph (A)(ii), losses paid after the 1st year following the accident year shall be treated as paid equally in the 2nd and 3rd year following the accident year.

(ii) 10-year loss payment pattern

(I) In general

The period taken into account under subparagraph (A)(ii) shall be extended to the extent required under subclause (II).

(II) Computation of extension

The amount of losses which would have been treated as paid in the 10th year

after the accident year shall be treated as paid in such 10th year and each subsequent year in an amount equal to the amount of the average of the losses treated as paid in the 7th, 8th, and 9th years after the accident year (or, if lesser, the portion of the unpaid losses not theretofore taken into account). To the extent such unpaid losses have not been treated as paid before the 24th year after the accident year, they shall be treated as paid in such 24th year.

(4) Determination year

For purposes of this section, the term “determination year” means calendar year 1987 and each 5th calendar year thereafter.

(e) Other definitions and special rules

For purposes of this section—

(1) Accident year

The term “accident year” means the calendar year in which the incident occurs which gives rise to the related unpaid loss.

(2) Unpaid loss adjustment expenses

The term “unpaid losses” includes any unpaid loss adjustment expenses shown on the annual statement.

(3) Annual statement

The term “annual statement” means the annual statement approved by the National Association of Insurance Commissioners which the taxpayer is required to file with insurance regulatory authorities of a State.

(4) Line of business

The term “line of business” means a category for the reporting of loss payment patterns determined on the basis of the annual statement for fire and casualty insurance companies for the calendar year ending with or within the taxable year, except that the multiple peril lines shall be treated as a single line of business.

(5) Multiple peril lines

The term “multiple peril lines” means the lines of business relating to farmowners multiple peril, homeowners multiple peril, commercial multiple peril, ocean marine, aircraft (all perils) and boiler and machinery.

(6) Special rule for certain accident and health insurance lines of business

Any determination under subsection (a) with respect to unpaid losses relating to accident and health insurance lines of businesses (other than credit disability insurance) shall be made—

(A) in the case of unpaid losses relating to disability income, by using the general rules prescribed under section 807(d) applicable to noncancellable accident and health insurance contracts and using a mortality or morbidity table reflecting the taxpayer's experience; except that the limitation of subsection (a)(3) shall apply, and

(B) in all other cases, by using an assumption (in lieu of a loss payment pattern) that unpaid losses are paid in the middle of the year following the accident year.

(f) Regulations

The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section, including—

(1) regulations providing proper treatment of allocated reinsurance, and

(2) regulations providing appropriate adjustments in the application of this section to a taxpayer having a taxable year which is not the calendar year.

(Added Pub. L. 99-514, title X, §1023(c), Oct. 22, 1986, 100 Stat. 2399; amended Pub. L. 100-647, title I, §1010(e)(1), (2), Nov. 10, 1988, 102 Stat. 3453; Pub. L. 101-508, title XI, §11305(b), Nov. 5, 1990, 104 Stat. 1388-451; Pub. L. 115-97, title I, §§13517(b)(3), 13523(a)-(c), Dec. 22, 2017, 131 Stat. 2147, 2152.)

AMENDMENTS

2017—Subsec. (c)(2). Pub. L. 115-97, §13523(a), amended par. (2) generally. Prior to amendment, text read as follows:

“(A) IN GENERAL.—The annual rate determined by the Secretary under this paragraph for any calendar year shall be a rate equal to the average of the applicable Federal mid-term rates (as defined in section 1274(d) but based on annual compounding) effective as of the beginning of each of the calendar months in the test period.

“(B) TEST PERIOD.—For purposes of subparagraph (A), the test period is the most recent 60-calendar-month period ending before the beginning of the calendar year for which the determination is made; except that there shall be excluded from the test period any month beginning before August 1, 1986.”

Subsec. (d)(3)(B) to (G). Pub. L. 115-97, §13523(b), added subpar. (B) and struck out former subpars. (B) to (G) which related to treatment of certain losses, special rule for certain long-tail lines, long-tail line of business, special rule for international and reinsurance lines of business, adjustments if loss experience information available for longer periods, and special rule for 9th year if negative or zero, respectively.

Subsecs. (e), (f). Pub. L. 115-97, §13523(c), redesignated subsecs. (f) and (g) as (e) and (f), respectively, and struck out former subsec. (e) which related to election to use company’s historical payment pattern.

Subsec. (f)(6)(A). Pub. L. 115-97, §13517(b)(3), substituted “except that the limitation of subsection (a)(3) shall apply, and” for “except that—

“(i) the prevailing State assumed interest rate shall be the rate in effect for the year in which the loss occurred rather than the year in which the contract was issued, and

“(ii) the limitation of subsection (a)(3) shall apply in lieu of the limitation of the last sentence of section 807(d)(1), and”.

Subsec. (g). Pub. L. 115-97, §13523(c), redesignated subsec. (g) as (f).

1990—Subsec. (g). Pub. L. 101-508 inserted “and” at end of par. (1), redesignated par. (3) as (2), and struck out former par. (2) which required regulations providing proper treatment of salvage and reinsurance recoverable attributable to unpaid losses.

1988—Subsec. (f)(6)(B). Pub. L. 100-647, §1010(e)(1), substituted “paid in the middle of the year” for “paid during the year”.

Subsec. (g)(3). Pub. L. 100-647, §1010(e)(2), added par. (3).

EFFECTIVE DATE OF 2017 AMENDMENT

Amendment by section 13517(b)(3) of Pub. L. 115-97 applicable to taxable years beginning after Dec. 31, 2017, with transition rule and transition relief, see section 13517(c) of Pub. L. 115-97, set out as a note under section 807 of this title.

Pub. L. 115-97, title I, §13523(d), Dec. 22, 2017, 131 Stat. 2152, provided that: “The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 2017.”

EFFECTIVE DATE OF 1990 AMENDMENT

Amendment by Pub. L. 101-508 applicable to taxable years beginning after Dec. 31, 1989, see section 11305(c)(1) of Pub. L. 101-508, set out as a note under section 832 of this title.

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100-647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99-514, to which such amendment relates, see section 1019(a) of Pub. L. 100-647, set out as a note under section 1 of this title.

EFFECTIVE DATE

Pub. L. 99-514, title X, §1023(e), Oct. 22, 1986, 100 Stat. 2404, as amended by Pub. L. 100-647, title I, §1010(e)(3), Nov. 10, 1988, 102 Stat. 3453, provided that:

“(1) IN GENERAL.—The amendments made by this section [enacting this section and amending sections 807 and 832 of this title] shall apply to taxable years beginning after December 31, 1986.

“(2) TRANSITIONAL RULE.—For the first taxable year beginning after December 31, 1986—

“(A) the unpaid losses and the expenses unpaid (as defined in paragraphs (5)(B) and (6) of section 832(b) of the Internal Revenue Code of 1986) at the end of the preceding taxable year, and

“(B) the unpaid losses as defined in sections 807(c)(2) and 805(a)(1) of such Code at the end of the preceding taxable year,

shall be determined as if the amendments made by this section had applied to such unpaid losses and expenses unpaid in the preceding taxable year and by using the interest rate and loss payment patterns applicable to accident years ending with calendar year 1987. For subsequent taxable years, such amendments shall be applied with respect to such unpaid losses and expenses unpaid by using the interest rate and loss payment patterns applicable to accident years ending with calendar year 1987.

“(3) FRESH START.—

“(A) IN GENERAL.—Except as otherwise provided in this paragraph, any difference between—

“(i) the amount determined to be the unpaid losses and expenses unpaid for the year preceding the 1st taxable year of an insurance company beginning after December 31, 1986, determined without regard to paragraph (2), and

“(ii) such amount determined with regard to paragraph (2),

shall not be taken into account for purposes of the Internal Revenue Code of 1986.

“(B) RESERVE STRENGTHENING IN YEARS AFTER 1985.—Subparagraph (A) shall not apply to any reserve strengthening in a taxable year beginning in 1986, and such strengthening shall be treated as occurring in the taxpayer’s 1st taxable year beginning after December 31, 1986.

“(C) EFFECT ON EARNINGS AND PROFITS.—The earnings and profits of any insurance company for its 1st taxable year beginning after December 31, 1986, shall be increased by the amount of the difference determined under subparagraph (A) with respect to such company.

“(4) APPLICATION OF FRESH START TO COMPANIES WHICH BECOME SUBJECT TO SECTION 831(a) TAX IN LATER TAXABLE YEAR.—If—

“(A) an insurance company was not subject to tax under section 831(a) of the Internal Revenue Code of 1986 for its 1st taxable year beginning after December 31, 1986, by reason of being—

“(i) subject to tax under section 831(b) of such Code, or

“(ii) described in section 501(c) of such Code and exempt from tax under section 501(a) of such Code, and

“(B) such company becomes subject to tax under such section 831(a) for any later taxable year, paragraph (2) and subparagraphs (A) and (C) of paragraph (3) shall be applied by treating such later taxable year as its 1st taxable year beginning after December 31, 1986, and by treating the calendar year in which such later taxable year begins as 1987; and paragraph (3)(B) shall not apply.”

TRANSITIONAL RULE

Pub. L. 115-97, title I, §13523(e), Dec. 22, 2017, 131 Stat. 2152, provided that: “For the first taxable year beginning after December 31, 2017—

“(1) the unpaid losses and the expenses unpaid (as defined in paragraphs (5)(B) and (6) of section 832(b) of the Internal Revenue Code of 1986) at the end of the preceding taxable year, and

“(2) the unpaid losses as defined in sections 807(c)(2) and 805(a)(1) of such Code at the end of the preceding taxable year,

shall be determined as if the amendments made by this section [amending this section] had applied to such unpaid losses and expenses unpaid in the preceding taxable year and by using the interest rate and loss payment patterns applicable to accident years ending with calendar year 2018, and any adjustment shall be taken into account ratably in such first taxable year and the 7 succeeding taxable years. For subsequent taxable years, such amendments shall be applied with respect to such unpaid losses and expenses unpaid by using the interest rate and loss payment patterns applicable to accident years ending with calendar year 2018.”

[§ 847. Repealed. Pub. L. 115-97, title I, § 13516(a), Dec. 22, 2017, 131 Stat. 2144]

Section, added Pub. L. 100-647, title VI, §6077(a), Nov. 10, 1988, 102 Stat. 3707; amended Pub. L. 101-239, title VII, §7816(n), Dec. 19, 1989, 103 Stat. 2422; Pub. L. 115-97, title I, §12001(b)(8)(B), Dec. 22, 2017, 131 Stat. 2093, related to special estimated tax payments.

EFFECTIVE DATE OF REPEAL

Pub. L. 115-97, title I, §13516(b), Dec. 22, 2017, 131 Stat. 2144, provided that: “The amendments made by this section [repealing this section] shall apply to taxable years beginning after December 31, 2017.”

§ 848. Capitalization of certain policy acquisition expenses

(a) General rule

In the case of an insurance company—

(1) specified policy acquisition expenses for any taxable year shall be capitalized, and

(2) such expenses shall be allowed as a deduction ratably over the 180-month period beginning with the first month in the second half of such taxable year.

(b) 5-year amortization for first \$5,000,000 of specified policy acquisition expenses

(1) In general

Paragraph (2) of subsection (a) shall be applied with respect to so much of the specified policy acquisition expenses of an insurance company for any taxable year as does not exceed \$5,000,000 by substituting “60-month” for “180-month”.

(2) Phase-out

If the specified policy acquisition expenses of an insurance company exceed \$10,000,000 for any taxable year, the \$5,000,000 amount under paragraph (1) shall be reduced (but not below zero) by the amount of such excess.

(3) Special rule for members of controlled group

In the case of any controlled group—

(A) all insurance companies which are members of such group shall be treated as 1 company for purposes of this subsection, and

(B) the amount to which paragraph (1) applies shall be allocated among such companies in such manner as the Secretary may prescribe.

For purposes of the preceding sentence, the term “controlled group” means any controlled group of corporations as defined in section 1563(a); except that subsections (a)(4) and (b)(2)(D) of section 1563 shall not apply, and subsection (b)(2)(C) of section 1563 shall not apply to the extent it excludes a foreign corporation to which section 842 applies.

(4) Exception for acquisition expenses attributable to certain reinsurance contracts

Paragraph (1) shall not apply to any specified policy acquisition expenses for any taxable year which are attributable to premiums or other consideration under any reinsurance contract.

(c) Specified policy acquisition expenses

For purposes of this section—

(1) In general

The term “specified policy acquisition expenses” means, with respect to any taxable year, so much of the general deductions for such taxable year as does not exceed the sum of—

(A) 2.09 percent of the net premiums for such taxable year on specified insurance contracts which are annuity contracts,

(B) 2.45 percent of the net premiums for such taxable year on specified insurance contracts which are group life insurance contracts, and

(C) 9.2 percent of the net premiums for such taxable year on specified insurance contracts not described in subparagraph (A) or (B).

(2) General deductions

The term “general deductions” means the deductions provided in part VI of subchapter B (sec. 161 and following, relating to itemized deductions) and in part I of subchapter D (sec. 401 and following, relating to pension, profit sharing, stock bonus plans, etc.).

(d) Net premiums

For purposes of this section—

(1) In general

The term “net premiums” means, with respect to any category of specified insurance contracts set forth in subsection (c)(1), the excess (if any) of—

(A) the gross amount of premiums and other consideration on such contracts, over

(B) return premiums on such contracts and premiums and other consideration incurred for reinsurance of such contracts.

The rules of section 803(b) shall apply for purposes of the preceding sentence.

(2) Amounts determined on accrual basis

In the case of an insurance company subject to tax under part II of this subchapter, all