SIN. 72.20-04

200118057

Internal Revenue Service

Department of the Treasury

Washington, DC 20224

xxxxx
xxxxx
xxxxx
xxxxx

Attn: xxxxx

Contact Person:
xxxxx
Telephone Number:
xxxxx
In Reference to:
T:EP:RA:T2
Date:
FEB 9 2001

Legend:

| | |
|---|---|
| Taxpayer A | =XXXXX |
| Company B | = xxxxx |
| Contract(s) X | =xXxXx |
| Form F | =XXXXX |
| State I | =xXxXx |
| C Options | =XXXXX |
| C Account | = XxXxX |
| D Options | = XxXxX |
| D Account | = XxXxX |
| Annuity Payments | =XXXXX |
| Program | = xxxxx |
| Method G | = XxXxX |

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Method H = xxxxx

Method I = xxxxx

Dear xxxxx:

This is in response to your request dated xxxxx, 1999, as amended and supplemented by your letters dated xxxxx, 2000, xxxxx, 2000, and xxxxx, 2000, for a ruling that Taxpayer A should treat each automatic payment made pursuant to a systematic withdrawal program adopted with respect to certain deferred variable annuity contracts as part of a series of substantially equal periodic payments within the meaning of section 72(t)(2) of the Internal Revenue Code.

Taxpayer A, a life insurance company within the meaning of section 816(a) of the Code, is organized and operated under the laws of State I. Taxpayer A is licensed to engage in the life insurance and annuity business in several states and is a wholly owned subsidiary of Company B.

Contract(s) X are non-participating, flexible premium, variable deferred annuity contracts which are offered by Taxpayer A. Contract(s) X are issued as either an individual retirement annuity described in section 408(b) of the Code ("IRAs") or an annuity contract described in section 403(b) of the Code ("section 403(b) contract"). Contract(s) X consists of a base contract and either an IRA endorsement or a section 403(b) contract endorsement. The endorsements provide that in the case of any conflict with any provision in Contract(s) X, the provisions of the applicable endorsement will control.

In general, under the terms of Contract(s) X, premiums may be paid at any time prior to the date on which the annuity payments are to begin. With regard to IRAs, contributions must be in cash and the total of such contributions for any taxable year must not exceed the lesser of $2,000 or 100 percent of compensation, except in the case of a rollover contributions (as permitted by Code sections 402(c), 403(a)(4), 403(b)(8) or 408(d)(3)) or as a contribution made in accordance with the terms of a Simplified Employee Pension as escribed in section 408(k) of the Code. With regard to section 403(b) contracts, if premium payments are made pursuant to a salary reduction agreement, the maximum contribution when combined with all other plans, contracts or arrangements may not be more than the amount of the limitation in section 402(g) of the Code. In addition, premium payments under section 403(b) contracts cannot exceed the amount allowed by sections 415 and 403(b) of the Code.

A Contract(s) X holder ("Holder") may allocate premiums and the earnings thereon among C Options which are fixed investment options and D Options which are variable investment options,

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Each C Option corresponds to a C Account identified on the Holder's application. Each C Account earns a fixed rate of interest throughout a certain period, however, such period may differ from the duration of the guaranteed period of other C Accounts. The C Account contract value is subject to a market value adjustment set forth in Contract(s) X in the event that amounts are withdrawn, transferred or annuitized from the C Account prior to the end of a guaranteed period of the corresponding C Option.

Each D Option corresponds to a portfolio of D Account. The portfolios of D Account purchase shares of a corresponding series of a trust that is a registered investment company for federal income tax purposes. Contract values allocated to a portfolio are credited with units in that portfolio. These units of measure are used in the computation of the D Account contract value. The value of these units for each portfolio will vary with the investment performance of the assets underlying the portfolio. The D Account contract value is the sum of all units credited under Contract(s) X.

Before the annuity starting date, the contract value of Contract(s) X equals the sum of the C Account contract value and the D Account contract value. A Holder is required to select an annuity starting date and an annuity payment option. A Holder may change, subject to certain rules, the annuity starting date and the payment option up to seven days before the annuity starting date.

In the case of Contract(s) X with an IRA endorsement, the entire interest of the Holder must be distributed, or commence to be distributed, no later than April 1 of the calendar year following the calendar year in which the Holder attains age 70 ½, over (a) the life of the Holder, or the lives of the Holder and an individual who is his or her designated beneficiary (within the meaning of section 401(a)(9); or (b) a period certain not extending beyond the life expectancy of the Holder, or the joint and last survivor expectancy of the Holder and the designated beneficiary.

In the case of a Contract(s) X with a section 403(b) contract endorsement, distributions under the contract must start no later than April 1 of the calendar year following the later of the calendar year in which (a) Holder attains age 70%; (b) Holder retires (and must be made over (1) the life of the Holder or the lives of the Holder and his or her designated beneficiary (within the meaning of section 401 (a)(9)); or (2) a period certain not extending beyond the life expectancy of the Holder or the joint and last survivor expectancy of the Holder and his or her designated beneficiary. In addition, all distributions from a section 403(b) contract are subject to the distribution requirements of section 403(b)(11) of the Code.

A Holder may elect one of the Annuity Payment Options E. On the annuity starting date, the Holder may choose to receive payments from C

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Account, D Account or both. If a Holder dies before the annuity starting date, a death benefit will be paid to the beneficiaries designated by the Holder.

Prior to the annuity starting date the Holder may withdraw all of a portion of the value of Contract(s) X. In the case of section 403(b) contracts, the Holder may not withdraw any amounts in Contract(s) X attributable to contributions made due to a salary reduction agreement after December 31.1988, and the earnings on such contribution and on amounts held on December 31, 1988, unless the Holder has:
1) attained age 59 1/2;
2) separated from service;
3) died;
4) incurred a hardship; or
5) become disabled (within the meaning of section 72(m)(7)).

Additional limitations apply in connection with withdrawals attributable to amounts that are subject to the Code section 403(b)(7)(A)(ii) restrictions.

Withdrawals and any surrender charges applicable will be deducted from the value of Contract(s) X in proportion to their allocation among C Options and D Options, unless the Holder chooses a different allocation method. A surrender charge may apply to certain withdrawals. The surrender charge will vary in amount depending upon the "Contribution Year" (as defined under the terms of Contract(s) X) of the premium at the time of withdrawal. For purposes of determining the surrender charge, withdrawals will be allocated first to earnings, if any (which may be withdrawn free of a surrender charge), and then to premiums on a first-in, first-out basis so that all withdrawals are allocated to premiums to which the lowest surrender charge applies.

Taxpayer A has developed the Program. Subject to the withdrawal restrictions applicable to section 403(b) contracts, a Holder can arrange to have money sent to the Holder automatically according to a periodic schedule that begins prior to the date on which annuity payments are to start under Holder's Contract(s) X. Taxpayer A offers three methods for the calculation of these automatic payments that commence to be made while Contract(s) X is still in the accumulation phase. The three methods of Taxpayer A correspond to the three methods described in Q&A-12 of Notice 89-25, 1989-1 C.B. 662. Unless the Holder chooses to terminate or modify his or her participation in the Program, Taxpayer A will continue to make these automatic payments to the Holder until the Holder's account value is exhausted. Election of annual, semi-annual, quarterly or monthly payments will be permitted.

To participate in the Program, a Holder is required to submit Form F to Taxpayer A. Form F requires the Holder to specify from which D options and/or C options the automatic payments are to be made. If however a Holder should submit Form F without specifying the sources from which the automatic

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payments are to be made, Taxpayer A will withdraw the automatic payments from each D option and C option on a pro-rata basis. Form F requires the Holder to elect by which of the three methods the automatic payments will be calculated. The three methods, Methods G, H and I are described below.

I. Method G

Taxpayer A will use the method described in section 1.401 (a)(9)-I, Q&A F-l of the Proposed Income Tax Regulations to calculate the automatic payment under this method. Section 1.401 (a)(9)-I, Q&A F-l of the proposed regulations provides that where the account balance of a qualified retirement plan is to be distributed over the life expectancy of an employee, the minimum required distribution is determined by dividing such account balance, generally determined as of the last day of the preceding calendar year, by the employee's life expectancy (as set out in section 1.72-9, Table V of the regulations). Taxpayer A will divide the contract value (as of the last day of the preceding calendar year) by the applicable life expectancy as set out in Table V of section 1.72-9 of the regulations (or the joint life and last survivor expectancy of the Holder and beneficiary as set out in Table VI of section 1.72-9 of the regulations).

II. Method H

Taxpayer A will calculate the automatic payment as the amount necessary to amortize the Holder's contract value over a number of years equal to the life expectancy of the Holder or the joint life and last survivor expectancy of the Holder and beneficiary (with life expectancies determined in accordance with section 1.401 (a)(9)-1 of the proposed regulations, based on an assumed interest rate equal to either 1) 120 percent of the Federal midterm rate in effect under section 1274(d)(l), or 2) 120 percent of the Federal long term rate in effect under section 1274(d)(l) of the Code. Taxpayer A determines the joint and last survivor life expectancy of a Holder and beneficiary by using Table VI of section 1.72-9 of the regulations.

Ill. Method I

Under this method, Taxpayer A will divide the Holder's contract value by an annuity factor (the present value of an annuity of $1 .00 per year beginning at the Holder's age attained in the first distribution year and continuing for the life of the Holder). The annuity factor will be derived using the UP-1984 Mortality Table in the case of a single life (or in the case of joint lives, the Life Table 80 CNSMT) and an assumed interest rate equal to either 1) 120 percent of the Federal midterm rate in effect under section 1274(d)(l), or 2) 120 percent of the Federal long term rate in effect under section 1274(d)(l) of the Code.

Based on the above facts and representations, a ruling is requested that Taxpayer A should treat each automatic payment under the Program from a

 

Contract(s) X as part of a "series of substantially equal periodic payments" within the meaning of section 72(t)(2)(A)(iv) of the Code.

Section 72 of the Code provides rules for determining how amounts received as annuities, endowments, or life insurance contracts and distributions from qualified retirement plans are to be taxed.

Section 72(t) of the Code was added by the Tax Reform Act of 1986 (TRA '86), effective generally for taxable years beginning after December 31, 1986.

Section 72(t)(l) of the Code provides that if any taxpayer receives any amount from a qualified retirement plan (as defined in section 4974(c)), the taxpayer's tax under this chapter for the taxable year in which such amount is received shall be increased by an amount equal to 10 percent of the portion of such amount which is includible in gross income.

The definition of a "qualified retirement plan" under section 4974(c) of the Code includes an annuity contract described in section 403(b) of the Code and an individual retirement annuity described in section 408(b) of the Code.

Section 72(t)(2)(A)(iv) of the Code provides an exception to the tax imposed by section 72(t)(l) in the case of distributions which are part of a series of substantially equal periodic payments (not less frequently than annually) made for the life (or the life expectancy) of the employee or the joint lives (or joint life expectancies of such employee and his or her designated beneficiary.

Section 72(t)(4) of the Code imposes a limitation on distributions excepted, on account of section 72(t)(2)(A)(iv), from the 10 percent additional tax by providing that if the series of payments is subsequently modified (other than by reason of death or disability) before the later of (1) the close of the 5-year period beginning with the date of the first payment, or (2) the employee's attainment of age 59 ½, then the taxpayers tax for the first taxable year in which such modification occurs shall be increased by an amount determined under regulations, equal to the tax which would have been imposed except for the section 72(t)(2)(A)(iv) exception, plus interest for the deferral period.

Section 1.72-9 of the Income Tax Regulations provides tables that are to be used in connection with computations under section 72 and the regulations thereunder. Included in this section are tables giving life expectancies for one life (Table V) and the joint life and last survivor expectancies for two lives (Table VI).

Notice 89-25, 1989-1 C.B. 662, was published on March 20, 1989, and provided guidance, in the form of questions and answers, on certain provisions of the TRA '86. In the absence of regulations under section 72(t) of the Code, Notice 89-25 provides guidance with respect to the exception to the tax on premature distributions provided under section 72(t)(2)(A)(iv) of the Code.

 

Q&A-12 of Notice 89-25 provides that certain payments will be considered substantially equal periodic payments within the meaning of section 72(t)(2)(A)(iv) of the Code if such payments are calculated under one of the three methods set forth in Q&A-12 of Notice 89-25.

Under the Life Expectancy Method, payments will be treated as substantially equal periodic payments within the meaning of Code section 72(t)(2)(A)(iv) if the annual payment is determined using a method that would be acceptable for purposes of calculating the minimum distribution required under Code section 401 (a)(9).

Under the Amortization Method, payments will be treated as substantially equal periodic payments within the meaning of Code section 72(t)(2)(A)(iv) if the amount to be distributed annually is determined by amortizing the taxpayer's account balance over a number of years equal to the life expectancy of the account owner or the joint life and last survivor expectancy of the account owner and beneficiary at a reasonable interest rate on the date payments commence.

Under the Annuity Table Method, payments will be treated as substantially equal periodic payments within the meaning of Code section 72(t)(2)(A)(iv) if the amount to be distributed annually is determined by dividing the taxpayers account balance by an annuity factor with such annuity factor derived using a reasonable mortality table and using reasonable interest rate on the date payments commence.

In this case, payments from Contract(s) X that are limited and paid as described and made pursuant to Taxpayer A's Program satisfy the requirements of each of the three methods set forth in Q&A-12. Method G comports with the Code section 401 (a)(9) life expectancy method in Q&A-12 of Notice 89-25. Methods H and I comport with the amortization method and the annuity table method; respectively, in Q&A-12 of Notice 89-25. The life expectancies, mortality table and the interest rates that will be used are reasonable.

Accordingly, we conclude that Taxpayer A should treat each automatic payment under the Program from a Contract X, as part of a "series of substantially equal periodic payments" within the meaning of section 72(t)(2)(A)(iv) of the Code.

This ruling is directed only to the taxpayer who requested it. Section 611 O(k)(3) of the Code states that it may not be used or cited by others as precedent.

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A copy of this letter has been sent to your authorized representative in accordance with the power of attorney submitted with the ruling request.

Sincerely yours,

(Signed) JOYCE E. FLOYD

Joyce E. Floyd, Manager
Employee Plans Technical Group 2
Tax Exempt and Government Entities
Division

Enclosures:
Deleted copy of this letter
Notice of Intention to Disclose

cc:
EP Manager, xxxxx Area

**xxxxx**
xxxxx
XxXxX
**xxxxx**
**xxxxx**

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