INTERNAL REVENUE SERVICE
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CC:DOM:FI&P:4 - PLR 116158-99
February 8, 2000

C =
F =
G =
P =
Z =
Program =
Agreement A =
Trust Agreement =
Insurance Company =
Trust =
Beneficiary =

Credited Season =
Annuity Board =
Commencement Date =

d =
e =
f =
g =

Dear :

This letter responds to your request dated September 23, 1999 requesting two rulings under section 72 of the Internal Revenue Code regarding a group annuity contract that will be purchased and held by Trust.

Establishment of Trust

The Trust was established as a medium to fund the Program as an agent for and on behalf of C, all of whom are natural persons. The objective of the Program and Trust is to provide a source of income for C between the ages of d and f, as well as later years, through the purchase of annuity contracts. Agreements from earlier years provide that C are eligible for and participate in qualified pension and profit sharing plans that provide income for their retirement years. The earliest point at which C can receive retirement benefits under a qualified plan is d; and C who began their careers after 1993 cannot receive retirement benefits under their qualified defined benefit plan until age e. The Program was designed as a result of recently completed 1998 amendments to the Agreement between F and G. The Program is subject to the requirements of the Taft-Hartley Act and ERISA, but is not intended to be a qualified plan under the Internal Revenue Code. Thus, C will be taxed currently on contributions used to purchase annuity contracts on their behalf.

Trust will establish Insurance Company which will issue Group Annuity Contract in which the interests under the contract would be beneficially owned by C. F and G determined that in order to provide investment and annuity services with lower expense charges than those charged by commercial carriers, Insurance Company would be organized and licensed as a captive insurance company in state Z.

Trust Agreement

Trust Agreement was approved and ratified by Annuity Board. The duties of the Annuity Board in connection with Trust include the collection and receipt of contributions from P; establishment of Insurance Company; negotiation, approval and purchase of a group annuity contract from Insurance Company; appointment of an administrator of Trust; nomination of the directors of the Insurance Company; review of necessary amendments to the Group Annuity Contract; and administration of the Program. The Annuity Board, an administrator and any other fiduciary appointed by the Annuity Board, will discharge their respective duties with respect to Trust solely and exclusively in the interest of C and their beneficiaries. Section 4.2 of the Trust Agreement.

Under the Trust Agreement, the Trust's duties will include receiving contributions of after-tax dollars from P on behalf of C and forwarding such contributions to the Insurance Company for investment in the Group Annuity Contract on behalf of C. The Trust will have no separate economic interest in the Group Annuity Contract, and exercises such powers as it has as agent for C. Section 4.2 of the Trust Agreement. All of the powers of the Trust derive from Agreement A. Under Agreement A and Trust Agreement, assets have or will be placed in the Trust for the benefit of C. The Trust will hold legal title to the Group Annuity Contract solely for the benefit of C.

Under the Trust Agreement, the sole power enjoyed by the Trust but not by C with respect to the Group Annuity Contract will be the Trust's power to terminate the Group Annuity Contract under circumstances where it is prudent to do so, such as where the Insurance Company or the Group Annuity Contract fails to comply with applicable federal or state laws. Section 4.2(f) of the Trust Agreement.

Under the Trust Agreement and the Group Annuity Contract, the Group Annuity Contract is not assignable, transferable, or subject to surrender by either C or the Trust. Section 9.4 of the Trust Agreement.

The Insurance Company will receive premiums from the Trust for the Group Annuity Contract, invest the premiums under the Group Annuity Contract, hold reserves, capital and surplus, and pay benefits in accordance with the terms of the Group Annuity Contract.

Group Annuity Contract

Under the terms of the Group Annuity Contract, the Trust will establish individual accounts for each C to reflect each individual C's interest in the Group Annuity Contract. Each account will be credited with units of interest reflecting contributions made on the respective C's behalf. Contributions on behalf of C will be invested in a commingled segregated asset account of the Insurance Company. Each account will be increased or decreased by investment results of the segregated asset account on periodic valuation dates.

The Group Annuity Contract will contain guarantees as to the basis of the annuity purchase rates. Initially, the Group Annuity Contract guarantees that the 1983 Group Annuity Table will govern the mortality basis for the annuities. Loading will not exceed 2% and the minimum interest rate for fixed annuities will be 3%. Guarantees may not be changed except with respect to future considerations received under the Group Annuity Contract. C are fully vested in their accounts under the Group Annuity Contract.

C may not receive benefits prior to age d. C may elect to begin receiving distribution of C's annuity at any time after the later of d or 5 years after the end of the annuity year containing C's last however payments must begin no later than g. C may elect to receive benefit distributions in substantial equal amounts for the period beginning on the Commencement Date and ending upon C's attainment of the later of the date specified by C or age e[1]; a single life annuity[2]; a joint and survivor annuity[3]; or a lump sum payment if C has attained e. C who elect lump sum payments under the Group Annuity Contract will receive amounts in the C's respective account as of the applicable valuation date. C who elect annuitization will receive annuities during the payout phase of the Group Annuity Contract.

If C dies after making an election to receive benefits but before payments under the

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[1] Provides for the monthly payments in fixed amounts over a period beginning on the Commencement Date and ending upon C's attainment of age e or such later date as C may specify.

[2] Provides for the payment of monthly payments in fixed amounts over a period beginning on the commencement date and ending on the date of C's death.

[3] Provides for the payment of monthly payments in fixed amounts over a period beginning on the commencement date and ending on the date of death of the survivor of C and C's beneficiary.

annuity have commenced, C's account will be distributed in a lump sum to C's beneficiary. The Group Annuity Contract further provides that if a C dies prior to the commencement of annuity benefits, the greater of the value of the C's account or the C's purchase payments will be paid as a lump sum death benefit to C's designated beneficiary. Section 3.2 of the Group Annuity Contract. [4]

Under its terms, the Group Annuity Contract is issued to the Trust as agent for C. Section 4.3 of the Group Annuity Contract. Rights of C under the Group Annuity Contract cannot be transferred, assigned or alienated. Section 4.5 of the Group Annuity Contract. C alone exercise all rights with respect to their individual accounts. The Group Annuity Contract further provides that, " In no event may any amounts held under the Contract revert to the benefit of any person other than C and their beneficiaries." Section 4.7 of the Group Annuity Contract.

Law and Analysis

Section 72 of the Code prescribes the income tax treatment of amounts received under annuity contracts by owners and beneficiaries of an annuity contract. Section 1.72-2(a) of the Income Tax Regulations provides, in part, that contracts under which amounts paid will be subject to provisions of section 72 include contracts which are considered to be annuity contracts in accordance with the customary practice of life insurance companies.

Section 1.72-2(b)(2) of the regulations provides that amounts subject to section 72 in accordance with subparagraph (1) are considered "amounts received as an annuity" only in the event that all of the following tests are met:

(i) they must be received on or after the "annuity starting date" as that term is defined in section 1.72-2(b);

(ii) they must be payable in periodic installments at regular intervals (whether annually, semiannually, quarterly, monthly, weekly, or otherwise) over a period of more than one full year from the annuity starting date; and

(iii) except as indicated in subparagraph (3) the total of the amounts payable must be determinable at the annuity starting date either directly from the terms of the contract or indirectly by the use of either mortality tables or compound interest computations, or both, in conjunction with such terms and in accordance with

[4] The Program provides that if a C dies before making an election as to the type of annuity benefit, then C's named beneficiary may make the election that otherwise would have been available to C. The Group Annuity Contract does not contain this provision. It is represented that Program will be modified to exclude such provision in order to conform to the provisions of the Group Annuity Contract.

sound actuarial theory.

The Group Annuity Contract contains conventional features of a commercial annuity, which would be considered an annuity contract in accordance with the customary practice of life insurance companies including the provision for accumulation of amounts in segregated asset accounts, measurement of individual C interests by accumulation unit values, and guaranteed purchase rates.

The Group Annuity Contract provides for the payment of fixed and determinable periodic payments over periods exceeding one year and for the systematic liquidation of all amounts accumulated in the Group Annuity Contract.

Section 72(s) provides that a contract will not be treated as an annuity contract for federal income tax purposes unless, with certain exceptions, it provides for certain distributions in the event that the holder of the contract dies.

Under Section 72(s)(1)(A), the contract must provide that if any holder dies on or after the annuity starting date and before the entire interest in the contract has been distributed, the remaining portion of such interest will be distributed at least as rapidly as under the method of distribution being used as of the date of death.

Under Section 72(s)(1)(B), the contract must also provide that if any holder dies before the annuity starting date, the entire interest in the contract will be distributed within five years after the holder's death.

Although C may elect among several types of annuity benefits, none of the available benefits provide for distribution of any C's interest in the contract less rapidly after a C's death then before C's death. All forms of annuitization under the Group Annuity Contract provide that payments, if any, after a C's death will at least equal payments before a C's death. The entire interest in the contract will be distributed within 5 years of a C's death should the C die before the annuity starting date.

Section 72(u)(1) provides that if an annuity contract is held by a person who is not a natural person, then such contract shall not be treated as an annuity contract for purposes of subtitle A of the Internal Revenue Code (other than subchapter L) and the income on the contract for any taxable year of the policyholder shall be treated as ordinary income received or accrued by the owner during such taxable year. Section 72(u)(1) provides further, that holding by a trust or other entity as an agent for a natural person shall not be taken into account.

The legislative history to section 72(u)(1) states that if an annuity contract is held by a person who is not a natural person (such as a corporation), then the contract is not treated as annuity contract for Federal income tax purposes and the income on the contract for any taxable year is treated as ordinary income received or accrued by the owner of the contract during the taxable year. In the case of an annuity contract the nominal owner of which is not a natural person (e.g., a corporation or a trust), but the beneficial owner of which is a natural person, the contract is treated as held by a natural person. H.R. Conf. Rep. No. 841, 99th Cong., 2d Sess. Vol II, 401-402 (1986), 1986-3 (Vol. 4) C.B. 401-402.

Under Agreement A, the Trust will hold legal title to the Group Annuity Contract solely for the benefit of C. No amounts can revert to the P or to any person other than C and their beneficiaries. Under the Trust Agreement and the Group Annuity Contract, the Group Annuity Contract is not assignable, transferable, or subject to surrender by C or the Trust. The P will not reflect the Group Annuity Contract as an asset on their financial statements and the Group Annuity Contract will not be subject to claims of creditors of P. Although Trust is the contract owner of the Group Annuity Contract, its ownership interest is nominal compared to C and their beneficiaries all of whom are natural persons.

Accordingly, based solely on the information submitted and the representations made, we hold that:

1) The Group Annuity Contract is an annuity contract for purposes of section 72; and

2) The Group Annuity Contract is held by Trust for a natural person within the meaning of section 72(u).

This ruling letter is directed only to the taxpayer who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

A copy of this letter must be attached to any income tax return to which it is relevant.

Sincerely yours,
Assistant Chief Counsel
(Financial Institutions & Products)
Donald J. Drees, Jr.
Senior Technician Reviewer,
Branch 4