**Internal Revenue Service**

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Department of the Treasury

Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:
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Date:
November 13, 2001

Taxpayer =

Account 1 =

Account 2 =

Dear :

This is in response to your letter dated July 17, 2001, requesting a ruling that new group annuity contracts issued by Taxpayer are variable contracts within the meaning of section 817(d) of the Internal Revenue Code.

FACTS

Taxpayer is a life insurance company within the meaning of section 816(a) and is taxable under section 801. As part of its business, Taxpayer issues individual and group annuity contracts based on separate asset accounts. Two of its separate accounts are Account 1 and Account 2. The contracts at issue in this ruling are certain group annuity contracts based on Account 1 and certain group annuity contracts based on Account 2 (hereinafter collectively referred to as the “Contracts”). Taxpayer intends to issue the Contracts to certain tax-exempt organizations, such as universities and private foundations.

Account 1 and Account 2 were established by the Taxpayer pursuant to state law. Account 1 and Account 2 are pooled, open-end, separate accounts to which gains or losses, realized or unrealized on assets held, will be credited or charged without regard to any other income, gains, or losses of the Taxpayer. Amounts included in Account 1 and Account 2 are owned by the Taxpayer, and the Taxpayer is not a trustee as to these amounts. Under no circumstances will deposits to Account 1 or Account 2, or income, gains, or losses in Account 1 or Account 2, be credited or charged to Taxpayer's general account. Additionally, no amounts will be transferred from Taxpayer's general account to Account 1 or Account 2.

Account 1 and Account 2 are managed by Taxpayer through an operating unit of Taxpayer. Amounts allocated to Account 1 and Account 2 are invested and reinvested in such manner as the managers of such Account deem appropriate. The assets of Account 1 are invested primarily in existing, income-producing properties. Investments in Account 1 are made through direct property ownership, or indirectly through such vehicles as joint ventures, general or limited partnerships, limited liability companies, mortgage loans and other loan types, and debt secured by an interest in the borrowing entity or interests in companies or entities that directly or indirectly hold real estate or real estate interests. Account 2 is a real estate portfolio designed for long-term investment in real estate within the United States. Account 2 investments include apartments, office buildings, and retail properties. Taxpayer represents that the investments made by Account 1 and Account 2 are "adequately diversified" within the meaning of section 817(h) and the regulations thereunder.

A Contract-holder may at any time direct Taxpayer to provide payment of "life," "stated amount," or "stated period" annuities with respect to the amounts held under the Contract. The purchase price of each annuity will be determined from the annuity purchase rate schedule guaranteed under, and set forth in, the Contract. Guarantees may not be changed except with respect to future considerations received under the Contract. For each type of annuity, the total amount payable can be determined when annuity payments begin. Amounts are payable in periodic installments at regular intervals over a period of more than one full year from the date that payments begin, and the total amount payable is determinable, directly or indirectly, as of the date the payments begin.

Under the Contracts, the amounts paid out to the Contract-holders reflect the investment return and market value of the segregated accounts. Thus, Contract-holders participate in the favorable and unfavorable market performance of the segregated accounts. Taxpayer will separately account for various income, exclusion, deduction, asset, reserve, and other liability items properly attributable to the Contracts.

The Contracts provide for required distributions upon the death of a primary annuitant. In the event a primary annuitant dies before the date annuity payments are due to begin, all amounts will be liquidated and distributed to the Contract-holder within five years following the primary annuitant's death. In the event a primary annuitant dies on or after the date the payments have begun, but have not yet been completed, distributions of the remaining amounts payable must be made at least as rapidly as the rate that was being used at the date of death.

LAW AND ANALYSIS

Section 817(d) defines a "variable contract" as a contract that provides for the allocation of all or part of the amounts received under the contract to an account that, pursuant to state law or regulation, is segregated from the general asset accounts of the company and that provides for the payment of annuities, or is a life insurance contract. Section 817(d)(1) and (2). In the case of an annuity contract, the amounts paid in or the amounts paid out reflect the investment return and market value of the segregated asset account. Section 817(d)(3)(A). If a contract ceases to reflect current investment return and current market value, it will not be considered a variable contract after such cessation.  Section 817(d).

Amounts received under the group annuity contract are allocated to Account 1 or Account 2 which, under state law, are segregated from the Taxpayer's general asset account.  Therefore, the Contracts meet the requirements set forth in section 817(d)(1).

Because the Contracts are not life insurance contracts, they must provide for the payment of annuities.  See section 817(d)(2)(A).  As section 817 does not define the phrase "provides for the payment of annuities," it is necessary to look to the guidelines in section 1.72-2(b)(1) and (2) of the Income Tax Regulations, which relate to the amounts received under an annuity contract as "amounts received as an annuity." Section 1.72-2(b)(2) provides that amounts are considered to be "amounts received as an annuity" only if they are received on or after the "annuity starting date" as that term is defined in section 1.72-4(b); they are payable in periodic installments at regular intervals over a period of more than one full year from the annuity starting date; and with an exception not here relevant, the total amount payable is determinable as of 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.  See also section 72(j) (interest payments received under an agreement to pay interest on any amount will be included in gross income, and thus will not be subject to the exclusion ratio applicable to amounts received as an annuity).  The facts, as stated above, indicate that the amounts under the Contracts are not held under an agreement to pay interest thereon and are payable in periodic installments at regular intervals over a period of more than one full year from the date that payments begin and that the total amount payable is determinable, directly or indirectly, as of the date the payments begin. Therefore, the Contracts meet the requirement of section 817(d)(2)(A) that it provide for the payment of annuities.

Section 72(u)(1)(A) provides that an annuity contract that is held by a person who is not a natural person will not be treated as an annuity contract for purposes of subtitle A of the Code (other than for purposes of subchapter L).  Although the Contracts are held by persons who are not natural persons, the Contracts are annuity contracts for purposes of subchapter L of the Code, which includes section 817(d).  See section 72(u)(1)(A).  In view of the Contracts' status as annuity contracts under subchapter L, the tax treatment of a Contract-holder under section 72(u)(1)(A) does not preclude the Contract from satisfying the requirements of section 817(d)(2)(A) for purposes of determining Taxpayer's income.

In order to be a variable contract, a Contract must also satisfy the requirements of section 817(d)(3).  In the case of an annuity contract, including a contract described in section 72 (u)(1), section 817(d)(3) requires that amounts paid in or the amounts paid out reflect the investment return and the market value of the segregated asset account. Under the Contracts, the amounts paid out reflect the investment return and market value of the segregated account.

Accordingly, based on the facts and representations set forth above, the Contracts satisfy the requirements of section 817(d)(1)-(3), and are thus “variable contracts,” as that term is defined in section 817(d).

No opinion is expressed as to the tax treatment of the transaction under the provisions of any other section of the Code or regulations, or to the tax treatment of any conditions existing at the time of, or effects resulting from, the transaction that are not specifically covered by the above ruling.

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.

The rulings contained in this letter are based upon information and representations submitted by the Taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely yours,
DONALD J. DREES, JR.
Senior Technician Reviewer, Branch 4
Office of Associate Chief Counsel
(Financial Institutions & Products)