2 T.C. 15 (1943)

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A reserve fund computed using the American Experience Table of Mortality with 3 1/2 percent interest, or its equivalent, qualifies as a life insurance reserve for combined life, health, and accident insurance contracts under Section 201(a) of the Revenue Acts of 1936 and 1938.

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Summary

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Reliance Benefit Association sought classification as a life insurance company for tax purposes. The Commissioner denied this, arguing that the association's reserve funds were not held for life insurance contracts as defined by Section 201 of the Revenue Acts of 1936 and 1938. The Tax Court held that Reliance was a life insurance company because its reserves, maintained as required by Arizona law, were substantially equivalent to those computed using standard actuarial methods and constituted more than 50% of its total reserves.

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Facts

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Reliance Benefit Association, an Arizona corporation, issued combined life, health, and accident insurance policies. Arizona law required benefit corporations to maintain a mortuary and reserve fund. The Arizona Corporation Commission mandated that these reserves be calculated using the American Experience Table of Mortality with 3 1/2 percent interest or an equivalent method. Reliance issued six policy types, four with reserves based on the American Experience Table, and two with reserves of 25-50% of premiums. An actuary approved all policies, confirming the latter's reserves were equivalent to the former. More than 50% of Reliance's total reserves were maintained for paying policy benefits.

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Procedural History

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The Commissioner of Internal Revenue determined deficiencies in Reliance's income tax for 1937 and 1938, arguing that it was not a life insurance company. Reliance petitioned the Tax Court for review of this determination.

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Issue(s)

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Whether the reserve funds maintained by Reliance Benefit Association qualify as "reserve funds… held for the fulfillment of such contracts" of combined life, health, and accident insurance under Section 201(a) of the Revenue Acts of 1936 and 1938, thus entitling it to be classified as a life insurance company for tax purposes.

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Holding

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Yes, because Reliance was required by Arizona law to maintain reserves that were substantially equivalent to those computed using standard actuarial methods, and these reserves constituted more than 50% of its total reserves, thus satisfying the statutory definition of a life insurance company.

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Court's Reasoning

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The court considered Section 201(a) of the Revenue Acts of 1936 and 1938, which defines a life insurance company as one engaged in issuing life insurance contracts where reserves for those contracts comprise over 50% of total reserves. The court relied on Treasury Regulations requiring reserves to meet specific criteria, including being required by law and dependent on interest earnings. Although some of Reliance's policies used a percentage of premiums for reserves, the court found these were equivalent to actuarially computed reserves, satisfying the regulatory requirements. The court emphasized that the Arizona Corporation Commission ensured that all reserves were sufficient to meet policy obligations, as confirmed by an actuary. The court distinguished prior cases where state law required inadequate

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reserves or where the company’s reserves were not mandated by law. Citing the House Report 2333, the court noted the importance of the 1942 Revenue Act adding that reserves must be based on recognized experience tables. The court presumed the actuary’s report, upon which state officials relied, was accurate, as these officials were charged with ensuring sufficient reserves. Ultimately, the court held that because Reliance was required to maintain reserves equivalent to those computed using the American Experience Table of Mortality, it qualified as a life insurance company.

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Practical Implications

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This case clarifies the definition of a

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