Administrative, Procedural, and Miscellaneous

26 CFR 601.204: Changes in accounting periods and in methods of accounting.
(Also: Part I, Sections 446, 807, 848.)

Rev. Proc. 2019-34

SECTION 1. PURPOSE

This revenue procedure provides simplified procedures under § 446 of the Internal Revenue Code and § 1.446-1(e) of the Income Tax Regulations for an insurance company to obtain the automatic consent of the Commissioner of Internal Revenue (Commissioner) to change its methods of accounting to comply with amendments to §§ 807 and 848 made by Pub. L. No. 115-97 (131 Stat. 2054, 2144, 2148), commonly referred to as the Tax Cuts and Jobs Act (TCJA), for the first taxable year beginning after December 31, 2017. Except as provided in sections 3.02 and 10 of this revenue procedure, these simplified procedures are the exclusive procedures for an insurance company within the scope of section 3 of this revenue procedure to obtain the consent of the Commissioner to change a method of accounting described in this revenue procedure.

This revenue procedure generally is consistent with the simplified procedures provided in Rev. Proc. 2019-30, 2019-33 I.R.B. ___, for an insurance company to obtain the automatic consent of the Commissioner to change its method of accounting for discounting unpaid losses and expenses unpaid, estimated salvage recoverable, and unearned premiums attributable to title insurance to comply with § 846 as amended by the TCJA. This revenue procedure is, however, only available for one taxable year. As a result, the timing of the issuance of this revenue procedure may pose challenges to an insurance company that has already prepared its tax return for the first taxable year beginning after December 31, 2017, and this revenue procedure provides accommodations for such an insurance company.

SECTION 2. BACKGROUND

.01 Life Insurance Reserves.

(1) Section 801(a) imposes a tax on the life insurance company taxable income of a life insurance company. For purposes of computing life insurance company taxable income, §§ 803(a)(2) and 807(a) include in gross income a decrease over the taxable year in reserves described in § 807(c). Sections 805(a)(2) and 807(b) permit a deduction for an increase over the taxable year in such reserves. Life insurance reserves are described in § 807(c)(1).

(2) Section 831(a) imposes a tax on the taxable income of a non-life (property and casualty) insurance company. For purposes of computing taxable income of a property and casualty company, § 832(b)(4) provides that an increase in life insurance reserves over the taxable year reduces premiums earned and a decrease in life

insurance reserves over the taxable year increases premiums earned.

(3) In general, the amount of life insurance reserves is required to be computed as provided in § 807(d). Section 13517 of the TCJA amended § 807(d) to provide a new method for computing the amount of life insurance reserves, effective for taxable years beginning after December 31, 2017.

(4) A transition rule in section 13517(c)(2) of the TCJA provides that for the first taxable year beginning after December 31, 2017, the reserve with respect to any contract (as determined under § 807(d)) at the end of the preceding taxable year is determined as if the amendments made by section 13517 of the TCJA had applied to such reserve in such preceding taxable year.

(5) Section 13517(c)(3) of the TCJA provides a transition relief rule that requires an insurance company to take into account the difference between (a) the amount of life insurance reserves with respect to any contract as of the close of the taxable year preceding the first taxable year beginning after December 31, 2017, computed using the method prescribed by the TCJA and (b) the amount of such reserves computed using the method prior to the amendments by the TCJA (such difference is the TCJA Transition Adjustment). The TCJA Transition Adjustment for any contract is positive if the amount described in clause (b) of the preceding sentence exceeds the amount described in clause (a) of the preceding sentence and is negative if the amount described in clause (a) of the preceding sentence exceeds the amount described in clause (b) of the preceding sentence. The TCJA Transition Adjustment must be taken into account ratably over each of the eight taxable years following that preceding taxable year under § 803(a)(2) or § 832(b)(1)(C), as applicable, if income,

and under § 805(a)(2) or § 832(c)(4), as applicable, if a deduction.

.02 Section 807(c)(3) Reserves.

(1) Section 807(c) describes items that a life insurance company must account for on a reserve basis and take into account under § 807(a) and (b). Section 807(c)(3) describes amounts (discounted at the appropriate rate of interest) necessary to satisfy the obligations under insurance and annuity contracts if the obligation does not involve (at the time with respect to which the computation is made) life, accident, or health contingencies. Such amount for any contract, however, may not be less than the net surrender value of such contract.

(2) Section 13517(a)(1) of the TCJA amended § 807(c) to provide that the appropriate rate of interest to discount the amounts in § 807(c)(3) is the highest rate or rates permitted to be used to discount the obligations by the National Association of Insurance Commissioners as of the date the reserve is determined. This amendment applies to taxable years beginning after December 31, 2017.

.03 Capitalization of Specified Policy Acquisition Expenses.

(1) Section 848 generally requires specified policy acquisition expenses for a taxable year to be capitalized and amortized over a defined period. Specified policy acquisition expenses are calculated as a certain percentage of net premiums on specified insurance contracts for the taxable year. Special rules may apply if the specified policy acquisition expenses of an insurance company (determined on a controlled group basis) are less than $15,000,000.

(2) Section 13519 of the TCJA amended § 848 by extending the general amortization period from 120 months to 180 months and changing the percentage of net

premiums that are determined to be specified policy acquisition expenses. These amendments apply to net premiums for taxable years beginning after December 31, 2017. A transition rule in section 13519 provides that specified policy acquisition expenses required to be capitalized in a taxable year beginning before January 1, 2018, will continue to be amortized ratably over the 120 month period.

.04 Changes in Method of Accounting.

(1) A change in the method of computing life insurance reserves or amounts under § 807(c)(3) to comply with amendments to § 807 made by the TCJA changes the proper time for the inclusion of the item in income or the taking of the item as a deduction and is a change in method of accounting subject to § 446(e) and § 1.446-1.

(2) A change in the method of calculating the amount of specified policy acquisition expenses to be capitalized and a change in the period over which such capitalized amounts are to be amortized to comply with amendments to § 848 made by the TCJA changes the proper time for taking the item as a deduction and is a change in method of accounting subject to § 446(e) and § 1.446-1.

(3) Section 446(e) and § 1.446-1(e)(2)(i) state that, except as otherwise provided, a taxpayer must secure the consent of the Commissioner before changing a method of accounting for any item for Federal income tax purposes. Under § 1.446-1(e)(3), to obtain the Commissioner's consent to change a method of accounting, a taxpayer generally must file a Form 3115, Application for Change in Accounting Method, during the taxable year for which the taxpayer desires to make the proposed change in method of accounting (year of change). Section 1.446-1(e)(3) provides that the Commissioner may prescribe terms and conditions for effecting a change in method of

accounting. Rev. Proc. 2015-13, 2015-5 I.R.B. 419, as clarified and modified by Rev. Proc. 2015-33, 2015-24 I.R.B. 1067, as modified by Rev. Proc. 2017-59, 2017-48 I.R.B. 543, and as modified by Rev. Proc. 2019-1, 2019-1 I.R.B. 1, provides the current general procedures, including terms and conditions by which an insurance company may obtain consent of the Commissioner to change its method of accounting through the filing of a Form 3115. Unless specifically authorized by the Commissioner or by statute, a taxpayer may not change an established method of accounting by amending any prior Federal income tax return. See Rev. Rul. 90-38, 1990-1 C.B. 57.

(4) Section 481(a) provides that in computing the taxpayer's taxable income for any taxable year, if such computation is under a method of accounting different from the method under which the taxpayer's taxable income for the preceding taxable year was computed, those adjustments that are determined to be necessary solely by reason of the change in order to prevent amounts from being duplicated or omitted must be taken into account. The § 481(a) adjustment is taken into account over the § 481(a) adjustment period provided in the applicable administrative guidance.

(5) In the interest of sound tax administration and in order to reduce the administrative and tax compliance burdens on insurance companies affected by the amendments to § 807 or § 848 made by the TCJA, this revenue procedure provides simplified procedures for an insurance company to obtain consent of the Commissioner to (i) change its methods of computing life insurance reserves to comply with amendments to § 807 made by the TCJA , (ii) change its methods of computing amounts under § 807(c)(3) to comply with amendments to § 807 made by the TCJA, and (iii) change its methods of capitalizing and amortizing specified policy acquisition

expenses to comply with amendments to § 848 made by the TCJA.

.05 Revenue Procedure 2019-10.

On January 7, 2019, the Treasury Department and the IRS published Rev. Proc. 2019-10, 2019-02 I.R.B. 296, which modified Rev. Proc. 2018-31, 2018-22 I.R.B. 637, to provide procedures under § 446 and § 1.446-1(e) for an insurance company to obtain automatic consent of the Commissioner to change its method of accounting to comply with § 807(f), as amended by the TCJA.

SECTION 3. SCOPE

.01 Life Insurance Reserve Method Change. This revenue procedure applies to any insurance company that changes its method of computing life insurance reserves to comply with amendments to § 807 made by the TCJA for the first taxable year beginning after December 31, 2017, provided the insurance company takes into account the § 481(a) adjustment described in section 6.01(1) of this revenue procedure in the manner prescribed in sections 6.02(1) and 6.02(3) of this revenue procedure and follows the procedures prescribed in section 7 of this revenue procedure.

.02 Section 807(c)(3) Method Change. This revenue procedure applies to any insurance company that changes its method of computing amounts under § 807(c)(3) to comply with amendments to § 807 made by the TCJA for the first taxable year beginning after December 31, 2017, provided the insurance company takes into account the § 481(a) adjustment described in section 6.01(2) of this revenue procedure in the manner prescribed in sections 6.02(2) and 6.02(3) of this revenue procedure and follows the procedures prescribed in section 7 of this revenue procedure. However, the portions of this revenue procedure related to § 807(c)(3) do not apply to an insurance company that changes its method of computing amounts under § 807(c)(3) to comply with amendments to § 807 made by the TCJA by complying with the procedures in section 26.04 of Rev. Proc. 2018-31 (as modified by Rev. Proc. 2019-10) (or its successor) to obtain the consent of the Commissioner for such change.

.03 Capitalization of Specified Policy Acquisition Expenses Method Change. This revenue procedure applies to any insurance company that changes its methods of capitalizing and amortizing specified policy acquisition expenses to comply with amendments to § 848 made by the TCJA for the first taxable year beginning after December 31, 2017, provided the insurance company follows the procedures prescribed in sections 6.01(3) and 7 of this revenue procedure.

SECTION 4. CONSENT TO CHANGE

Under § 1.446-1(e)(2)(i), the consent of the Commissioner is hereby granted to any insurance company within the scope of section 3 of this revenue procedure to change its method of accounting for life insurance reserves, amounts under § 807(c)(3), and specified policy acquisition expenses, as applicable, to comply with amendments to §§ 807 and 848, as applicable, made by the TCJA, provided the insurance company complies with the provisions of this revenue procedure and the applicable provisions of Rev. Proc. 2015-13.

SECTION 5. APPLICABILITY OF REV. PROC. 2015-13

.01 Except as otherwise provided in this revenue procedure, the provisions of Rev. Proc. 2015-13 apply to an insurance company within the scope of section 3 of this revenue procedure.

.02 The limitations in section 5 of Rev. Proc. 2015-13 do not apply to a change in method of accounting made under this revenue procedure. Therefore, an insurance company within the scope of this revenue procedure is eligible to make a change in method of accounting under this revenue procedure even if the requested year of change is the final year of the insurance company's trade or business as described in section 5.03(1) of Rev. Proc. 2015-13 or the insurance company engages in a liquidation or reorganization transaction to which § 381 applies as described in section 5.02(1) of Rev. Proc. 2015-13.

SECTION 6. TERMS AND CONDITIONS OF CHANGE

.01 Year of Change and Section 481(a) Adjustment.

(1) Life Insurance Reserve Method Change. For an insurance company described in section 3.01 of this revenue procedure, the year of change is the first taxable year beginning after December 31, 2017, and the § 481(a) adjustment is the sum of the TCJA Transition Adjustments. The insurance company must take the § 481(a) adjustment into account in the manner provided in section 6.02(1) of this revenue procedure.

(2) Section 807(c)(3) Method Change. For an insurance company described in section 3.02 of this revenue procedure, the year of change is the first taxable year beginning after December 31, 2017, and the § 481(a) adjustment is the difference between (a) the amount determined under § 807(c)(3) as of the close of the taxable year preceding the first taxable year beginning after December 31, 2017, determined using the appropriate rate of interest required after the amendments to § 807(c) by the TCJA and (b) such amount determined at such time using the appropriate rate of interest required prior to the amendments to § 807(c) by the TCJA. The § 481(a)

adjustment is positive if the amount described in clause (b) of the preceding sentence exceeds the amount described in clause (a) of the preceding sentence and is negative if the amount described in clause (a) of the preceding sentence exceeds the amount described in clause (b) of the preceding sentence. The insurance company must take the § 481(a) adjustment into account in the manner provided in section 6.02(2) of this revenue procedure.

(3) Capitalization of Specified Policy Acquisition Expenses Method Change. For an insurance company described in section 3.03 of this revenue procedure, the year of change is the first taxable year beginning after December 31, 2017. The change in method of accounting is made using a cut-off method because the TCJA amendments to § 848 apply to net premiums for taxable years beginning after December 31, 2017. Accordingly, a § 481(a) adjustment is neither required nor permitted.

.02 Section 481(a) Adjustment Period.

(1) Life Insurance Reserve Method Change. For an insurance company described in section 3.01 of this revenue procedure, the § 481(a) adjustment period is eight taxable years (the year of change and the seven succeeding taxable years). Any negative § 481(a) adjustment must be taken into account under § 805(a)(2) or § 832(c)(4), as applicable, and any positive § 481(a) adjustment must be taken into account under § 803(a)(2) or § 832(b)(1)(C), as applicable.

(2) Section 807(c)(3) Method Change. For an insurance company described in section 3.02 of this revenue procedure, the § 481(a) adjustment period is one taxable year (the year of change) for a negative § 481(a) adjustment and four taxable years (the year of change and the three succeeding taxable years) for a positive § 481(a)

adjustment. Alternatively, such insurance company may take a positive § 481(a) adjustment into account entirely in the year of change.

(3) General Rules. For purposes of this revenue procedure, with respect to any § 481(a) adjustment described in section 6.01 of this revenue procedure:

(a) The insurance company must take the § 481(a) adjustment into account ratably over the § 481(a) adjustment period specified in this revenue procedure.

(b) If the year of change or any other taxable year during the § 481(a) adjustment period is a short taxable year, the insurance company must take the applicable § 481(a) adjustment described in § 481(a) of this revenue procedure into account as if that short taxable year were a full 12-month year. See Rev. Rul. 78-165, 1978-1 C.B. 276.

(c) The applicable § 481(a) adjustment period described in section 6.02 of this revenue procedure may not be shortened under the provisions of section 7.03(3) of Rev. Proc. 2015-13.

(d) The applicable § 481(a) adjustment period described in section 6.02 of this revenue procedure is accelerated in the situations described in section 7.03(4)(a) and (d) of Rev. Proc. 2015-13.

(e) The applicable § 481(a) adjustment period described in section 6.02(1) of this revenue procedure is accelerated if the insurance company ceases to qualify as an insurance company, and any remaining § 481(a) adjustment must be taken into account in the last year the insurance company qualifies as an insurance company. See section 13517(c)(3)(B) of the TCJA.

SECTION 7. PROCEDURE FOR MAKING THE CHANGE

In accordance with § 1.446-1(e)(3)(ii), the requirement of § 1.446-1(e)(3)(i) to file a Form 3115 is waived for an insurance company making a change in method of accounting under this revenue procedure, provided the insurance company satisfies all of the applicable terms and conditions set forth in section 6 of this revenue procedure; properly reports the amount of any § 481 adjustment described in section 6.01 of this revenue procedure, as applicable, on its Federal income tax returns; and, except as otherwise provided in this revenue procedure, satisfies all of the applicable terms and conditions set forth in Rev. Proc. 2015-13.

SECTION 8. AUDIT PROTECTION

.01 <u>No Audit Protection for Life Insurance Reserve Method Changes</u>. The audit protection in section 8 of Rev. Proc. 2015-13 does not apply to a change in method of accounting that is within the scope of section 3.01 of this revenue procedure.

.02 <u>Audit Protection for Section 807(c)(3) and Capitalization of Specified Policy Acquisition Expenses Method Changes</u>. Except as otherwise provided herein, the IRS will not require an insurance company that makes a change in method of accounting that is within the scope of section 3.02 or section 3.03 of this revenue procedure to change its method of accounting for the same item (that is, for discounting amounts under § 807(c)(3) or capitalizing and amortizing specified policy acquisition expenses under § 848, as applicable) for taxable years prior to the year of change, provided the insurance company complies with the applicable provisions of this revenue procedure. The IRS may change an insurance company's method of accounting for the same item that is the subject of a change in method of accounting described in section 3.02 or section 3.03 of this revenue procedure if the insurance company's method of accounting for the same item (that is, for discounting amounts under § 807(c)(3) or capitalizing and amortizing specified policy acquisition expenses under § 848, as applicable) is an issue under consideration (whether under examination, before an Appeals office, or before a federal court), within the meaning of section 3.08 of Rev. Proc. 2015-13, on August 6, 2019. The exceptions in section 8.02 of Rev. Proc. 2015-13 do not apply to an insurance company within the scope of section 3.02 or section 3.03 of this revenue procedure with respect to the insurance company's method of accounting for the same item that is the subject of a change in method of accounting described in section 3.02 or section 3.03 of this revenue procedure (that is, for discounting amounts under § 807(c)(3) or capitalizing and amortizing specified policy acquisition expenses under § 848, as applicable).

SECTION 9. EFFECT ON OTHER REVENUE PROCEDURES

Section 26.04(1) of Rev. Proc. 2018-31 (as modified by Rev. Proc. 2019-10), is modified by adding a second sentence to read as follows: "However, this section 26.04 does not apply to any change in method of accounting to which Rev. Proc. 2019-30, 2019-33 I.R.B. __ or Rev. Proc. 2019-34, 2019-35 I.R.B. __, applies."

Accordingly, a change in a method of accounting subject to section 26.04 of Rev. Proc. 2018-31 (or its successor) to which this Rev. Proc. 2019-34 does not apply continues to be subject to section 26.04 of Rev. Proc. 2018-31 (or its successor). For example, if in its first taxable year beginning after December 31, 2017, a taxpayer changes its method of computing life insurance reserves in a manner in addition to that required to comply with the amendments to section 807 made by the TCJA, such additional change is not subject to this Rev. Proc. 2019-34 and continues to be subject to section 26.04 of Rev. Proc. 2018-31 (or its successor).

SECTION 10. FORM 3115 TRANSITION RULE

If before August 26, 2019, a taxpayer properly filed a Form 3115 under the non-automatic change procedures in Rev. Proc. 2015-13 requesting the Commissioner's consent for a change in method of accounting described in section 3 of this revenue procedure, and the Form 3115 is pending with the national office on August 26, 2019, the taxpayer may choose to make the change in method of accounting under the automatic change procedures in this revenue procedure and Rev. Proc. 2015-13 if the taxpayer is otherwise eligible to use this revenue procedure and the automatic change procedures in Rev. Proc. 2015-13. The taxpayer must notify the national office contact person for the Form 3115 (if unknown, see section 9.08(6) of Rev. Proc. 2019-1 (or any successor)) of the taxpayer's intent to make the change in method of accounting under the automatic change procedures in Rev. Proc. 2015-13 before the later of (a) September 25, 2019, or (b) the issuance of a letter ruling granting or denying consent for the change. The notification should indicate that the taxpayer chooses to convert the Form 3115 to the automatic change procedures in this revenue procedure and Rev. Proc. 2015-13. If the taxpayer timely notifies the national office that it chooses to convert the Form 3115 to the automatic change procedures in this revenue procedure and Rev. Proc. 2015-13, the national office will send a letter to the taxpayer acknowledging its request and will return the user fee submitted with the Form 3115.

SECTION 11. EFFECTIVE DATE

This revenue procedure is effective for an insurance company’s first taxable year beginning after December 31, 2017.

SECTION 12. DRAFTING INFORMATION

The principal author of this revenue procedure is Dan Phillips of the Office of Associate Chief Counsel (Financial Institutions & Products). For further information regarding this revenue procedure contact Mr. Phillips at (202) 317-6995 (not a toll free call).