Annotate Insurance tax
Ref to STOD

(916) 445-5550

March 24, 1989

Re:

Dear Mr. :

This is in response to your letter dated to Senior Tax Auditor Henry Gordon. In a letter dated January 11, 1989, Mr. Gordon asked you to confirm that the premiums at issue in the above-cited petitions for redetermination satisfied the two requirements for the .50 percent reduced rate of Revenue and Taxation Code section 12202: the premiums were from policies issued to pension or profit-sharing plans; and those plans were exempt or qualified under Internal Revenue Code (IRC) section 401(a), 403(b), 404, 408(b), or 501(a).

You state that your records list the policyholders as "almost exclusively designated as pension or profit-sharing plans, or as individuals." This is not sufficient. All policyholders for which you claim the reduced rate must be pension or profit-sharing plans and, as discussed below, none may be individuals on the basis you assert.

You state that your listings do not disclose whether the subject policyholders were qualified under the Internal Revenue Code. However, you assert that it is an eminently reasonable assumption to conclude that all the pension and profit-sharing plans must have been exempt or qualified under IRC section 401(a) or 501(a) because such qualification was routinely available to any pension or profit-sharing plan and because the advantages of obtaining such qualification were so advantageous that any trustee would have been grossly negligent if the qualification were not obtained.

The reduced rate of section 12202 is a partial exemption from the otherwise applicable rate set by the Constitution at 2.35 percent. (Cal. Const. Art. XIII, Sec. 28 subd. (d) & (i).) You have the burden of establishing that you come clearly within the terms authorizing that exemption. (H.J. Heinz v. State Board of Equalization (1962) 209 Cal.App. 2d 1, 4.) To satisfy this burden, you must confirm that the subject premiums were from policies issued to plans which were actually exempt or qualified under the relevant IRC sections.

Obviously, the most efficient and convincing manner in which to satisfy this burden is done at the time the policies are issued. Many insurers have fully explained their methods to ensure that premiums for which the reduced rate is claimed are from policies meeting both requirements and properly coded in their records as such. Since you have apparently not yet done this, you must do so now. Each qualifying policyholder will have been issued a letter from the IRS. If necessary, you should obtain such letters for the periods in question.

You also state your assumption that premiums from policies originally issued to pension or profit-sharing plans continue to qualify for the reduced rate, even if the premiums are subsequently paid on an individual basis by persons who had been terminated from the plan. We disagree with this assumption. We interpret the language of section 12202 that "gross premiums received upon policies or contracts issued in connection with a pension plan or profit-sharing plan ..." to mean that the reduced rate applies only to premiums from policies that are actually held and paid by pension or profit-sharing plan policyholders. Policies for which premiums are paid by an individual after termination from a pension or profit-sharing plan are no longer regarded as issued to a pension or profit-sharing plan within the meaning of section 12202. Premiums from such policies are taxable at the full rate provided in section 12202.

In summary, the reduced rate applies only to those premiums from policies issued to plans satisfying each of the two requirements set forth in section 12202. The plans may not be "almost exclusively" pension or profit-sharing plans, but must all be pension or profit-sharing plans. You must confirm that each plan is exempt or qualified under one of the listed IRC sections; we will not assume that such is the case. Finally, under your facts, no premiums paid by individual policyholders would qualify for the reduced rate.

Please provide us the specific amounts of premiums, by year, that you can confirm are entitled to the reduced rates as set forth above. Although we would like to act on your petition promptly, we recognize that you have a number of policyholders to contact. If you cannot provide us the requested information within thirty days, please let us know when we can expect this information. If you have any questions, feel free to call me.

Sincerely,

David H. Levine

David H. Levine
Tax Counsel

cc: Mr.

bc: Mr. E. L. Sorensen, Jr.