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## Deferred Compensation Timing Rules, Rather Than Subchapter L, Govern Insurance Company's Deduction for Retiree Medical Benefits

In a Technical Advice Memorandum ([TAM 200939019](#) (June 10, 2009)), the Internal Revenue Service concluded that the deduction timing rules of Internal Revenue Code (IRC) § 404(a)(5) trump Subchapter L in governing a deduction for retiree medical expenses.

On the facts of the TAM, the non-life insurance company parent of an affiliated group that included property and casualty companies reduced the calculation of its taxable income by the discounted present value of future retiree medical benefits to be provided to its claims personnel. Under IRC §§ 831 and 832, non-life insurance companies may reduce their taxable underwriting income by losses and expenses incurred. The amounts taken into account were not contributed to an IRC § 419(e) welfare benefit fund and, accordingly, were not governed by that provision. Any such retiree medical benefits would, however, be received more than 2½ months after the end of the insurance company's tax year to which the employees' related services were provided—the defining characteristic under Treas. Reg. § 1.404(b)-1T, Q&A-2(b)(1) of compensation arrangements subject to the deduction timing rule of § 404(a)(5). Under § 404(a)(5) and related provisions as amended in 1984 and 1986, employer contributions for "nonqualified" plans that provide deferred compensation or other deferred benefits generally are deductible in the year in which the employee includes that compensation or benefit in income (disregarding applicable exclusions).

The insurance company argued that § 404(a)(5) was inapplicable because these tax items were controlled by the loss reserve provisions of Subchapter L. It noted that it was required to include estimates of this liability in determining unpaid loss adjustments on its National Association of Insurance Commissioners (NAIC) annual statement, and that under §§ 832 and 846 the NAIC accounting treatment is controlling for tax purposes. The insurance company further contended that a § 832 unpaid loss adjustment is not a deduction within the purview of § 404(a)(5).

The IRS National Office concluded otherwise, relying primarily on the legislative history of the § 404 amendments in 1984 and 1986 to argue that Congress intended that provision to take precedence over other IRC provisions.



*If you have any questions about this development, please feel free to contact any of the attorneys listed below or the Sutherland attorney with whom you regularly work.*

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