

**DATE:** 07-18-90

**CITATION:** VAOPGCPREC 70-90  
Vet. Aff. Op. Gen. Couns. Prec. 70-90

**TEXT:**

**SUBJECT:**

Countability for Improved Pension Purposes of Interest Accrued on Retirement Annuity Accounts

(This opinion, previously issued as General Counsel Opinion 3-88, dated June 14, 1988, is reissued as a Precedent Opinion pursuant to 38 C.F.R. §§ 2.6(e)(9) and 14.507. The text of the opinion remains unchanged from the original except for certain format and clerical changes necessitated by the aforementioned regulatory provisions.)

**QUESTION PRESENTED:**

Whether interest accrued on an Individual Retirement Annuity owned by a deceased veteran's surviving spouse, who is in receipt of death pension under the improved pension program, is countable as income for pension purposes, and, if so, when and to what extent.

**COMMENTS:**

Such accrued interest should not be counted as income where withdrawal of the interest would result in a substantial penalty to the beneficiary.

The claim file indicates that the pension beneficiary is the owner of two deferred Individual Retirement Annuities maturing in 1994. Interest is credited to these accounts periodically, and the annuity policies may be surrendered in whole or in part at any time. However, full or partial surrender of either policy at present would result in imposition of a substantial penalty, including loss of a large portion of the interest credited to the account.

Statutes governing the improved pension program provide that in determining annual income for pension purposes "all payments of any kind or from any source (including ... annuity payments ...) shall be included" with certain specified exceptions. 38 U.S.C. § 503(a). Similarly, 38 C.F.R. § 3.271(a) provides that "(p)ayments of any kind from any source shall be counted as income in the year in which received unless specifically excluded." Neither the statute nor the regulations contains a provision specifically addressing income accruing to retirement annuities. A review of our precedent files reveals no opinion of the General Counsel authoritatively deciding whether interest of this type falls within the scope of section 503(a). However, an unpublished memorandum dated June 14, 1960, to the Chairman, Board of Veterans Appeals, from the Associate General Counsel for Legal Services, acting for the General Counsel,

dealing with the "old law" pension program, indicates in passing that interest on a retirement annuity is counted as income at the time it is paid to the annuitant as part of the annuity. See also A.D. No. 688 (1946) (implying this result for purposes of "old law" pension). The nature of the annuity contracts, the terms of the applicable statutes and regulations, and the past opinions of this office lead us to conclude that the interest at issue should not be counted as income for improved pension purposes at this time.

An annuity has been described as a right to receive fixed periodic payments for life, or for a specified period. 4 Am. Jur.2d Annuities § 1 (1962). In purchasing an annuity, the purchaser surrenders title to the premiums paid, id. § 2, in exchange for a contractual right to receive specified payments, id. § 4. The annuity contract creates a debtor-creditor relationship, id. § 13, a chose in action for payment of money, id. § 4, rather than an interest in a fund, id. § 1. As noted, in the case of the annuity contracts here at issue, the right to receive the full amount of interest credited to the accounts is conditioned under the contracts on leaving the accounts intact until a specified date. Interest earned on an Individual Retirement Annuity is tax exempt until distribution. 33 Am.Jur.2d Federal Taxation p 3911 (1988). Under the Internal Revenue Code, a ten percent penalty is imposed on withdrawals from such an account prior to the purchaser's reaching age 59 1/2, except in the case of death or disability, id. p 3823, although it appears that in this case the claimant's age places her outside the scope of the penalty provision.

The legislative history of the improved pension program indicates that the term "income," for purposes of determining pension eligibility, was only intended to refer to income available to meet the subsistence needs of the beneficiary and the beneficiary's dependents. The House committee report on legislation which became Pub.L. No. 95-588, 92 Stat. 2497, the Veterans' and Survivors' Pension Improvement Act of 1978, referred to calculation based on "all ... available" non-pension income. H.R. Rep. No. 95-1225, 95th Cong., 2d Sess. 28 (1978), reprinted in 1978 U.S. Code Cong. & Ad. News 5583, 5609. The committee report on the Senate version of the measure contained references to consideration of "the aggregate income available to the household for its basic requirements," "dollars available for ordinary living expenses," and "dollars ... available for maintenance." S. Rep. No. 95-1016, 95th Cong., 2d Sess. 68, 69 (1978). In the subject claim, accrued interest is merely credited to the balance which the grantor of the annuity is legally obligated to pay in accordance with the terms of the contract. The claimant does not receive the benefit of these sums until the annuity matures. Although partial surrender of the policies is possible, the amounts credited are not available to the claimant at this time without imposition of a substantial penalty which would result in loss of much of the accrued interest. We question whether under these circumstances the accrued interest, or any part of it, can be considered available income for pension computation purposes.

Further, section 503(a) defines income in terms of all "payments" of any kind or from any source, including "annuity payments." The VA's implementing regulation at 38 C.F.R. § 3.271(a) contemplates that income will be counted as "received." In Op. G.C. 1-82, holding contributions and interest actually withdrawn from a retirement fund to be

improved-pension income in the year in which received, we stated "Congress intended to include as 'payments' all monies received by the pensioner unless expressly excluded under the law" (emphasis supplied). Interpreting identical language applicable to the section 306 pension program in Op. G.C. 10-62, we stated that retirement benefits would be considered income for pension purposes when "actually received." See also Op. G.C. 20-60 (income "actually received" is considered).

Here, the sums in question were credited to the claimant's annuity accounts for purposes of informing the claimant how much the companies may be required to pay on the annuity contracts under the appropriate circumstances. Mere crediting of interest to such unmaturing annuity accounts cannot be considered actual receipt of payments for purposes of section 503(a) when, in order to actually obtain the funds, the claimant would have to surrender at least a portion of the annuity and incur a substantial penalty. The situation is more analogous to unrealized appreciation of a capital asset than to the crediting of interest to a savings account available in full to the owner upon demand. Accordingly, we conclude that the sums in question have not actually been received by the claimant and may not be considered payments within the meaning of section 503(a). Although the annuity contracts here at issue significantly restrict the current availability of funds to the claimant, the annuity contract nonetheless represents a valuable asset of the claimant. Section 543(a)(1) of title 38, U.S. Code, directs the VA to deny or discontinue payment of death pension to a surviving spouse of a veteran "when the corpus of the estate of the surviving spouse is such that under all the circumstances ... it is reasonable that some part of the corpus of such estate be consumed for the surviving spouse's maintenance." Implementing regulations at 38 C.F.R. § 3.275(b) define "corpus of estate" and "net worth" as the market value of all real and personal property owned by the claimant. A non-assignable annuity does not have a market value in the sense that the contract itself can be sold. Nonetheless, as the contract can be converted to cash through surrender, albeit at a loss, the surrender value may, we believe, be considered in determining net worth. Section 3.275(d) of title 38, Code of Federal Regulations, lists several factors to be considered together in determining whether some part of a claimant's estate should be consumed for the claimant's maintenance. Among these is whether the claimant's property "can be readily converted into cash at no substantial sacrifice." The substantial penalty which would result from surrender of the claimant's annuity policies is relevant to consideration of this factor, as is the option of immediate annuitization, available under one of the policies.

**HELD:**

As it appears that the interest credited to the claimant's annuity accounts cannot currently be obtained without substantial penalty, such interest should not be counted at this time as income for purposes of determining the claimant's entitlement to improved pension. This does not prevent the counting of such interest as income at some future date when it may be considered as having actually been received by the claimant. Further, annuity contracts may be considered under the net-worth factors listed in 38 C.F.R. § 3.275(d) in determining whether it is reasonable that some portion of the claimant's estate should be consumed for the claimant's maintenance.

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