interest to do so. Further, an owner of a variable insurance contract with a declining deferred sales charge, unlike a front-ended contract, does not foreclose his or her opportunity at the end of the first two contract years to receive a refund of monies spent. Not only has such an owner not paid any excess load, but because the deferred charge declines over the life of the Contract, the Contract owner may never have to pay it. Applicants submit that encouraging a surrender during the first two Contracts years could cost a Contract owner more in total sales load (relative to total payments) than he or she otherwise would pay if the Contract, which is designed as a long-term investment vehicle, were held for the period originally intended.

4. Because of the absence of excess sales load, and therefore, the absence of an obligation to assure repayment of that amount, Applicants believe that the Contracts do not create the right in a Contract owner which Form N–271–1 was designed to highlight. In the absence of this right, Applicants submit that the notification contemplated by Form N–271–1 creates an unnecessary and counterproductive administrative burden the cost of which appears unjustified. Any other purpose potentially served by the Form would already be addressed by the required Form N–271–2 Notice of Withdrawal Right, generally describing the charges associated with a Contract, and prospectus disclosure detailing a Contract's sales load structure. Applicants assert that neither Congress, in enacting Section 27, nor the Commission, in adopting Rule 27e–1 and Rule 6e–2, could have contemplated the applicability of Form N–271–1 in the context of a Contract with a declining contingent deferred sales charge.

G. Deduction of Charge for Section 848 Deferred Acquisition Costs

1. Applicants request exemptive relief from Section 27(c)(2) of the 1940 Act to permit the deduction of the 1.0% charge from each Premium Payment received under the Contracts, and from premiums received under Other Contracts to be issued by Guardian through the Future Accounts to reimburse Guardian for its increased federal tax burden resulting from the application of Section 848 of the Code, as amended, to the receipt of those premiums. Applicants also request exemptions from subparagraph (c)(4)(v) of Rules 6e–2 and 6e–3(T) under the 1940 Act to permit the proposed deductions to be treated as other than "sales load," as defined under Section 2(a)(35) of the 1940 Act, for purposes of Section 27 and the exemptions from various provisions of that Section found in Rules 6e–2 and 6e–3(T), respectively.

2. Applicants state that Section 848, as amended, requires life insurance companies to capitalize and amortize over ten years certain general expenses for the current year rather than deduct these expenses in full from the current year's gross income, as allowed under prior law. Section 848 effectively accelerates the realization of income from specified contracts and, consequently, the payment of taxes on that income. Taking into account the time value of money, Section 848 increases the insurance company's tax burden because the amount of general deductions that must be capitalized and amortized is measured by the premiums received under the Contracts.

3. Deductions subject to Section 848 equal a percentage of the current year's net premiums received (*i.e.*, gross premiums minus return premiums and reinsurance premiums) under life insurance or other contracts categorized under this Section. The Contracts will be categorized under Section 848 as life insurance contracts requiring 7.7% of the net premiums received to be capitalized and amortized under the schedule set forth in Section 848(c)(1).

4. The increased tax burden on every $10,000 of net premiums received under the Contracts is quantified by Applicants as follows. For each $10,000 of net premiums received in a given year, Guardian must capitalize $770 (*i.e.,* 7.7% of $10,000), and $38.50 of this amount may be deducted in the current year. The remaining $731.50 ($770 less $38.50) is subject to taxation at the corporate tax rate of 35% and results in $256.03 (.35% × $731.50) more in taxes for the current year than Guardian otherwise would have owned prior to OBRA 1990. However, the current tax increase will be offset partially by deductions allowed during the next ten years, which result from amortizing the remainder of the $770 ($77 in each of the following nine years and $38.50 in year ten).

5. It is Guardian's business judgement that it is appropriate to use a discount rate of 10% in evaluating the present value of its future tax deductions for the following reasons. Guardian has computed its cost of capital as the after-tax rate of return that it seeks to earn on its surplus, which is in excess of 10%. To the extent that surplus must be used by Guardian to pay its increased federal tax burden under Section 848, such surplus will be unavailable for investment. Thus, the cost of capital used to satisfy this increased tax burden essentially will be the after-tax rate of return Guardian seeks on its surplus, which is in excess of 10%. Accordingly, Applicants submit that the rate of return on surplus is appropriate for use in this present value calculation.

6. To the extent that the 10% discount rate is lower than Guardian's actual rate of return on surplus, the calculation of this increased tax burden will continue to be reasonable over time, even if the corporate tax rate applicable to Guardian is reduced, or its targeted rate of return is lowered.

7. In determining the after-tax rate of return used in arriving at the discount rate, Guardian considered a number of factors that apply to itself and to its parent, including market interest rates, anticipated long-term growth rates, the risk level for this type of business that is acceptable, inflation, and available information about the rate of return obtained by other life insurance companies. Guardian represents that these are appropriate factors to consider.

8. First, Guardian projects its future growth rate, including the future growth rate of its parent, based on sales projections, current interest rates, inflation rate and amount of surplus that can be provided to support such growth. Guardian then uses the anticipated growth rate and the other factors to set a rate of return on surplus that equals or exceeds this rate of growth. Of these other factors, market interest rates, acceptable risk level and inflation rate receive significantly more weight than information about the rates of return obtained by other companies.

9. Guardian and its parent seek to maintain a ratio of surplus to assets that is established based on its judgment of the risks represented by various components of its assets and liabilities. Maintaining the ratio of surplus to assets is critical to offering competitively priced products and to maintaining the superior ratings now assigned to Guardian and its parent by various rating agencies. Consequently, Guardian's surplus should grow at least at the same rate as its assets.

10. Using a federal corporate tax rate of 35%, and assuming a discount rate of 10%, the present value of the tax effect of the increased deductions allowable in the following ten years, which partially offsets the increased tax burden, comes to $152.96. The effect of Section 848 on the Contracts is therefore an increased tax burden with a present value of $91.15 for each $10,000 of net premiums (*i.e.*, $244.11 less $152.96).

11. Guardian does not incur incremental federal income tax when it passes on state premium taxes to Contract Owners because state premium