



OFFICE OF
CHIEF COUNSEL

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR JUNE Y. BASS
ASSOCIATE AREA COUNSEL, LMSB

FROM: ASSISTANT CHIEF COUNSEL (ADMINISTRATIVE
PROVISIONS & JUDICIAL PRACTICE) CC:PA:APJP

SUBJECT: Field Service Advice: Section 6041 - Form 1099 Reporting

This Chief Counsel Advice responds to your memorandum dated May 29, 2001. In accordance with I.R.C. § 6110(k)(3), this Chief Counsel Advice should not be cited as precedent.

LEGEND

Taxpayer
Taxable Periods Ended

State
Country
Contract
State's Insurance Code

ISSUES

1. Whether Taxpayer, a title insurance company, is required to issue Forms 1099 for commissions paid to its independent agents?
2. If the answer to Issue 1 is no, whether Taxpayer is nonetheless required to issue Forms 1099 for commissions paid to independent agents who are also attorneys?

CONCLUSIONS

1. Taxpayer is required to issue Forms 1099 for commissions paid to its independent agents.

2. Since we answered to issue 1 affirmatively, the second issue is moot.

FACTS

Taxpayer is a title insurance company incorporated in State A. Taxpayer's policies are sold by its independent agents throughout Country.

The respective rights and obligations of Taxpayer and its agents are governed by Contract. Under Contract, agents are granted the authority to process applications for insurance, perform title searches, issue commitments, issue policies, and collect premiums.

A sale by Taxpayer's agent usually involves a two-step process. The agent first conducts a title search. The agent then issues a title insurance policy. If the terms of the policy are consistent with the title report, and are within the agent's scope of authority, Taxpayer becomes immediately bound by the policy when the policy is delivered and the premiums are paid. As long as Contract remains operative, an agent need not obtain authorization from Taxpayer before issuing a new policy.

Premiums on title insurance policies are collected by the agent, who retains a portion of the premium as his fee before remitting the remainder to Taxpayer. Taxpayer records the entire amount of the premium as income, but at the same time records the associated fee retained by the agent as an expense. Taxpayer does not issue Forms 1099 for commissions retained by its independent agents.

LAW AND ANALYSIS

ISSUE 1

Section 6041(a), requires all persons engaged in a trade or business and making payments in the course of such trade or business to another person, of wages and/or compensation of \$600 or more in any taxable year, to render a return to the Secretary.

Treas. Reg. § 1.6041-3(h)¹, grants an exception to the information return requirement of section 6041 for payments of commissions to general agents by fire insurance companies or other companies insuring property. Thus, for Taxpayer to qualify for the exception under Treas. Reg. § 1.6041-3(h), Taxpayer's agents must qualify as "general agents" and title insurance companies must qualify as "companies insuring property."

General Agents

¹This regulation was subsequently redesignated as Treas. Reg. § 1.6041-3(g) effective January 1, 2001.

The exception under Treas. Reg. § 1.6041-3(h) only applies to general agents.

The term general agent is not defined in the Code or the Regulations. However, in Rev. Rul. 57-747, the Service stated that a general agent:

[I]s authorized to accept risks and settle terms of insurance and to carry them into effect by issuing and renewing policies. He stands in the stead of the company to the insured and may usually bind his principal as to all acts within the scope of his authority. The general agent is responsible for collecting premiums, being obligated under his contract only to submit the difference between the premium collected from the policyholder and the commission owed to him by the insurer. A local soliciting agent without authority to write or issue policies, but who merely procures applications, collects premiums and sometimes delivers policies when payments are made, is not a general agent of the insurer.

Rev. Rul. 57-747, 1957-2 C.B. 841.

Based on the description in Rev. Rul. 57-747, Taxpayer's agents are general agents. Unlike soliciting agents who are only authorized to process applications, Taxpayer's agents are granted the authority to receive and process applications for insurance, perform title searches, settle the terms of insurance based upon those title searches, and issue title insurance policies binding Taxpayer. In addition, agents are authorized to collect premiums, retaining a portion of the premium as a fee and remitting the remainder to Taxpayer. Since Taxpayer's agents retain the qualities described in Rev. Rul. 57-747, Taxpayer's agents qualify as general agents.

Companies Insuring Property

The exception under Treas. Reg. § 1.6041-3(h) only applies to fire insurance companies and other companies insuring property. The term "companies insuring property" is not defined in the Code or the Regulations.

The statutory rule of construction, *ejusdem generis*, provides that "where general words follow a designation of particular subjects or classes or persons, the meaning of the general words will ordinarily be presumed to be restricted by the particular designation, and to include only those things or persons of the same kind, class or nature as those specifically enumerated."

Under Treas. Reg. § 1.6041-3(h), the general words "companies insuring property" follow the specific term "fire insurance companies;" therefore, under *ejusdem generis*, the general words should be restricted to things of the same kind as fire insurance companies.

Fire insurance is defined under State's insurance code as insurance against the loss of property by fire, lightning, windstorm, tornado, or earthquake. Therefore, fire insurance companies insure against the physical loss of property.

Title insurance protects against loss through liens, encumbrances, or other defects in title. King v. Stanley, 32 Cal. 2d 584 (1948); Trisdale, Inc. v. Shasta County Title Co., 146 Cal. App. 2d 831 (1956); Hawkins v. Oakland Title Ins. & Guar. Co., 165 Cal. App. 2d 116 (1958). Defective title is not a physical loss or damage to the property. Nevers v. Aetna Insurance Co., Inc., 14 Wash. App. 906 (1976); HRG Development Corp. v. Graphic Arts Mutual Insurance Co., 26 Mass. App. Ct. 374 (1988); Commercial Union Insurance Co. v. Sponholz, 866 F. 2d 1162 (9th Cir. 1989). Therefore, unlike fire insurance companies which insure against the physical loss of property, title insurance companies insure the owner's legal rights to the property.

Fire insurance and title insurance protect against different losses, and, therefore, are not of the same kind. Because title insurance is not of the same kind as fire insurance, under *ejusdem generis* title insurance should not be included in the term "companies insuring property."

Casualty Insurance Companies

Although the term "companies insuring property" is not defined in the Code or the Regulations, the Service has extended Treas. Reg. § 1.6041-3(h) to casualty insurance companies; thereby including casualty insurance companies within the term "companies insuring property." See, Rev. Rul 57-747, 1957-2 C.B. 841. The extension of the exception to casualty insurance companies is an indicator of the type of insurance companies that should be included within the term "companies insuring property."

Casualty insurance companies insure property against a "fortuitous event – a casualty." HRG Development Corp., 26 Mass. App. Ct. at 376. A casualty has been defined as "losses arising through the action of natural physical forces which occur suddenly and unexpectedly." Mertens, § 28.95. Therefore, casualty insurance companies insure against the physical loss of property due to external and natural causes.

Title insurance companies insure against loss through liens, encumbrances, or other defects in title. King, 32 Cal. 2d at 590; Trisdale, Inc., 146 Cal. App. 2d at 837; Hawkins, 165 Cal. App. 2d at 116. Defective title is not a physical loss or damage to the property. Nevers, 14 Wash. App. at 907; HRG Development Corp., 26 Mass. App. Ct. at 378; Commercial Union Insurance Co., 866 F. 2d at 1163. In addition, the subsequent discovery of a defect in title is not a "casualty" as that term is commonly understood. Modern Home Fire and Casualty Insurance Co. v. Commissioner, 54 T.C. 839, 840 (1970). Therefore, unlike casualty insurance companies which insure against the physical loss of the property due to casualties, title insurance companies insure the owner's legal rights to the property.

Casualty insurance companies and title insurance companies insure against different types of loss. Consequently, the inclusion of casualty insurance companies within the term "companies insuring property" does not encourage the inclusion of title insurance companies within the term "companies insuring property."

Strict Construction

Tax exemptions depend on legislative grace. Luehrmann's Estate v. Commissioner, 287 F.2d 10, 15 (8th Cir. 1961); Cherry-Burrell Corp. v. United States, 367 F.2d 669, 674 (8th Cir. 1966). Tax statutes authorizing special exemptions are to be strictly and narrowly construed against the taxpayer. Helvering v. Northwest Steel Rolling Mills, Inc., 311 U.S. 46 (1940); White v. United States, 305 U.S. 281, 292 (1938); Universal Oil Products Co. v. Campbell, 181 F. 2d 451, 457 (7th Cir. 1950), cert. denied 340 U.S. 850 (1950), reh. denied 340 U.S. 894 (1950).

Treas. Reg. § 1.6041-3(h) grants an exception to fire insurance companies and other companies insuring property. The Service has included casualty insurance companies within the term "other companies insuring property." Consequently, the two types of insurance companies that have been granted the exception both insure against the physical loss of property. As discussed earlier, title insurance companies do not insure against the physical loss of property, title insurance companies insure the owner's legal rights to the property. Therefore, if the statute authorizing the exemption is strictly construed, title insurance companies should not be included within the term "companies insuring property."

Taxpayer is not entitled to the exception under Reg. § 1.6041-3(h), and, therefore, Taxpayer is required to issue Forms 1099 for commissions retained by its independent agents.

ISSUE 2

If the answer to Issue 1 is no, whether Taxpayer is nonetheless required to issue Forms 1099 for commissions paid to independent agents who are also attorneys?

Since we answered issue 1 affirmatively, the second issue is moot.



This writing may contain privileged information. Any unauthorized disclosure of this writing may have an adverse effect on privileges, such as the attorney client privilege. If disclosure becomes necessary, please contact this office for our views.

If you have any further questions, please contact Michelle B. Baxter at (202) 622-7947.

CURTIS G. WILSON
By: JAMES C. GIBBONS
Chief, CC:PA:APJP:1