UIL Code: 501.15-00; 953.06-00

Release Number: **200824029**
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Date November 15, 2005

INTERNAL REVENUE SERVICE

TE/GE TECHNICAL ADVICE MEMORANDUM

Area Manager:

Taxpayer's Name:
Taxpayer's Address:

Taxpayer's Identification Number:

Years Involved:

Conference Held:

LEGEND

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B =
C =
D =
E =
F =
G =
H =
I =
J =
K =
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ISSUES:

1. Whether X qualified as an insurance company under section 501(c)(15) of the Internal Revenue Code for tax years ending December 31 of Year 1 and Date 5 of Year 2.

2. Whether X was entitled to change its taxable year from a calendar taxable year to a Date 5 taxable year pursuant to Revenue Procedure 85-58.

3. Whether the Service should aggregate the premium income earned by X for the period from January 1 of Year 2 through December 31 of Year 2 for purposes of determining whether X exceeded the $350,000 premium limitation set forth in section 501(c)(15) of the Code.

4. Whether X, a foreign company that made an election under section 953(d) of the Code continues to qualify for the election if it is not an insurance company.

5. Whether X can rely on the determination letter granted by the Service allowing it to claim tax exempt status under section 501(c)(15) of the Code.

6. Whether X is entitled to relief pursuant to section 7805(b) of the Code.

7. If X can not rely on its determination letter, what is the effective date of revocation?

FACTS:

X was incorporated in R on Date 1. Effective Date 8, X assumed the assets, liabilities and insurance business of Z, a B State corporation that was a former member of the C.

As of December 31 of Year 1, X had c number of shares of stock issued and outstanding. During Year 1 and Year 2, X was effectively owned and controlled by A directly and through ownership by D or E in which A or D held an interest.

Z, the predecessor to X, filed a Form 1024 Application for Recognition of Exemption under Section 501(a) of the Code, specifically, the exemption provided under section 501(c)(15). In its application, Z described its activities as follows:

> X commenced writing business as a member of the C in Date 9 and continues to write business through the C until it ceased accepting business in Date 10. At that time Z executed an F Agreement with the C and has been running off its business since that time through T.
>
> During the time Z was writing business, they wrote both property and casualty business on a direct/facultative and treaty reinsurance basis.

*   *   *

> Z is committed to remaining as an active writer of insurance business. Z is currently reviewing proposals that will facilitate its withdrawal from the C via an H Agreement which will allow it to move its operations to a new jurisdiction where it can not only run off its C business, but can accept new business for its own account.

The Service granted Z tax exempt status under section 501(c)(15) of the Code in Date 2.

X filed a Form 1024 on Date 3, seeking tax exemption status under section 501(c)(15) of the Code. It described its activities in Form 1024 as follows:

> X is the successor of Z . . . which was an underwriting member of the C. X commenced writing business as a member of the C in Date 9 and continued to write business until it ceased accepting business in Date 10. At that time X executed an F Agreement with the C.
>
> Through a transfer of assets and liabilities on Date 11, X will continue the insurance business of Z from its domicile in R. In the future the company will continue to insure business at a level which will qualify for the tax exemption.
>
> X was formed specifically to continue the operation of Z due to valid business reasons necessitated by the I. Shareholders of X are the same as Z.

In its Form 1024, X stated that its present and future sources of financial support "would be derived from premium income and investments." The Service granted X tax exempt status under section 501(c)(15) on Date 4.

X made the election under section 953(d) to be treated as a domestic corporation for United States income tax purposes. X's copy of the accepted election statement was returned to X on Date 12.

On its Forms 990, X reported "program service revenue" (i.e., insurance premiums) of \$f and \$g for the tax years ending December 31 of Year 1, and Date 5 of Year 2, respectively. X's premiums during the periods ending December 31 of Year 1, and Date 5 of Year 2, were attributable to X's run-off of Z's prior C business, and to a reinsurance contract entered into between X and another company effective Date 13.

R requires that X meet two statutory ratios for regulatory purposes: (1) N, and (2) O. X must maintain enough S to meet the N. For the year ended December 31 of Year 1, X was required to have a minimum S of \$t. During that period, X's aggregate amount of U was \$d. For the year ended December 31 of Year 2, X was also required to maintain a minimum S of \$t. During that period, X's aggregate amount of U was \$e. X met the O in both Year 1 and Year 2.

X provided the Service with a Report from a risk consulting group in Date 14 disclosing an actuarial opinion that the amount of \$h, adjusted to \$i, in loss reserves recorded on the books and records of X was sufficient for all unpaid loss and loss adjustment expenses as of December 31 of Year 1.

From inception through Date 5 of Year 2, X's potential liability for unpaid losses decreased by $j (u%) from $k as of Date 11 to $l as of Date 5 of Year 2. During that same period, X's assets increased by $m (v%), from $n as of Date 11, to $p as of Date 5 of Year 2.

Based on these figures, the amount of investment income in both Year 1 and Year 2 dwarfs the total amount of funds either required by R or needed to resolve all potential insurance claims outstanding in each year. X represents that while in prior and subsequent years its insurance activities were superficially more extensive because of market conditions; the apparent dearth of activity during the years involved does not reflect the true nature and extent of its insurance activities during the years involved.

At the end of Year 1, X owned w% profits, loss and capital interest in V, a domestic partnership. V owned x% of W, a section 501(c)(15) entity incorporated in R. By the end on December 31 of Year 3, V was owned x% by A and X. The substantial asset owned by V was W. X also owns x% of Y, an R corporation that files a Form 1120-PC pursuant to a section 953(d) election. Y and its predecessor have been in run-off status since Date 7. During the relevant time period, W, X and Y had little premium income, significant retained earnings, and assets unrelated to insurance activities.

As of Date 5 of Year 2, X had a y% ownership interest in T. T is a holding company that wholly owns gg U.S. licensed insurance companies. During Year 3, X's interest in P increased to z%.

From its inception through December 31 of Year 1, X filed its returns on a calendar year basis. Effective Date 5 of Year 2, upon X's purchase of Q, X changed from a calendar year to a fiscal year with a Date 5 year end. The purchase of Q resulted in X failing to meet the requirements of exemption under section 501(c)(15) of the Code because X's aggregated premiums exceeded the $350,000 limit. Subsequent to the purchase of Q, X filed a Form 1120-PC return for the period Date 15 through December 31 of Year 2. In subsequent years, X continued to file its Forms 1120-PC returns on a calendar year basis.

LAW AND ANALYSIS:

Issue One: Whether X qualified as an insurance company under section 501(c)(15) of the Code for the years ending December 31 of Year 1 and Date 5 of Year 2.

For years prior to January 1, 2004, an insurance company other than life is exempt pursuant to section 501(c)(15)(A) if the net written premiums for the taxable year do not exceed $350,000. If an entity is a part of a consolidated group, section 501(c)(15)(B) provides that all net written premiums (or direct written premiums) of the members of the group are aggregated to determine whether the insurance company meets the requirements of section 501(c)(15)(A).

X's eligibility for the benefit of section 501(a) of the Code turns on whether it satisfies the criteria for qualification as an insurance company for federal income tax purposes. X's qualification as an insurance company depends on whether its activity constituted issuing an insurance contract or reinsuring the risks underwritten by an insurance company.

For the years involved, for federal income tax purposes, an insurance company is a company whose primary and predominant business activity during the year was the issuing of insurance or annuity contracts or the reinsuring of risks underwritten by insurance companies. In addition, section 1.803-1(a) of the Income Tax Regulations provides that "it is the character of the business actually done in the taxable year which determines whether a company is taxable as an insurance company under the Internal Revenue Code." (Emphasis added.) This language resulted from a series of cases, including Lawyers Mortgage Co., supra, in which the United States Supreme Court established the test that later became incorporated as section 1.803-1(a)of the regulations, as follows:

> While name, charter powers and subjection to state insurance laws have significance as to the business which a corporation is authorized and intends to carry on, the character of the business actually done in the tax years determines whether it is taxable as an insurance company. (Emphasis added.)

285 U.S. at 188.

Although a taxpayer's name, charter powers, and state regulation help to indicate the activities in which it may properly engage, whether the taxpayer qualifies as an insurance company for tax purposes depends on its actual activities during the year. Inter-American Life Ins. Co. Commissioner, 56 T.C. 497, 506-08 (1971), aff'd per curiam, 469 F.2d 697 (9th Cir. 1972) (taxpayer whose predominant source of income was from investments did not qualify as an insurance company); see also Bowers v. Lawyers Mortgage Co., 285 U.S. 182, 188 (1932). To qualify as an insurance company, a taxpayer "must use its capital and efforts primarily in earning income from the issuance of contracts of insurance." Industrial Life Ins. Co. v. United States, 344 F. Supp 870, 877 (D.S.C. 1972), aff'd per curiam, 481 F.2d 609 (4th Cir. 1973). All of the relevant facts will be considered, including but not limited to, the size and activities of any staff, whether X engages in other trades or businesses, and its sources of income. See generally, Lawyers Mortgage Co. at 188-90; Industrial Life Ins. Co., at 875-77; Cardinal Life Ins. Co. v. United States, 300 F. Supp. 387, 391-92 (N.D. Tex. 1969), rev'd on other grounds, 425 F.2d 1328 (5th Cir. 1970); Service Life Ins. Co. v. United States, 189 F. Supp. 282, 285-86 (D. Neb. 1960), aff'd on other grounds, 293 F.2d 72 (8th Cir. 1961); Inter-Am. Life Ins. Co., at 506-08; Nat'l Capital Ins. Co. of the Dist. Of Columbia v. Commissioner, 28 B.T.A. 1079, 1085-86 (1933).

Neither the Code nor the regulations thereunder define the terms "insurance" or "insurance contract." The bedrock for evaluating whether an arrangement qualifies as insurance is Helvering v. LeGierse, 312 U.S 531, 539 (1941), in which the Court stated that "historically and commonly insurance involves risk shifting and risk distributing." The risk transferred must be risk of economic loss. Allied Fidelity Corp. v. Commissioner, 572 F.2d 1190, 1193 (7th Cir.), cert. denied, 439 U.S. 835 (1978). The risk must contemplate the fortuitous occurrence of a stated contingency, Commissioner v. Treganowan, 183 F.2d 288, 290-91 (2d Cir. 1950), and must not be merely an investment or business risk. LeGierse at 542; Rev. Rul. 89-96, 1989-2 C.B. 114.

The commonly accepted sense of insurance derives from all of the facts surrounding each case, with emphasis on the character of X's business "actually done" in the tax years in question. In Year 1 and Year 2, X did not sell or write any insurance

policies. Its insurance activities consisted solely of handling the run-off business of its predecessor that it acquired on Date 11 and to a reinsurance contract entered into between X and another reinsurance company effective Date 13. X's subsequent purchase of insurance companies after the years in question is irrelevant to the present question of whether it qualified for tax exemption as an insurance company under section 501(c)(15) for the years ending December 31 of Year 1 and Date 5 of Year 2. See Lawyers Mortgage, supra, at 188.

Form 990 for each year in question shows premiums and assets as follows: Premium income was $f and $g for Year 1 and Year 2. Assets totaled $o and $p for Year 1 and Year 2.

This information reveals that X's premium income was dwarfed by its investments and other business activities and that its actual insurance expense was minor compared to its other liabilities. X was fully aware that it held investment assets far in excess of what was required by R or what X would need to pay claims. A Report from a consulting group dated Date 16, X obtained an actuarial opinion that the amount of $h, adjusted to $i, in loss reserves recorded on the books and records of X was sufficient for all unpaid loss and loss adjustment expenses as of December 31 of Year 1. However, for that period, X reported assets of $b, an amount that was bb times the amount it needed to pay its insurance obligations. Similarly, by the end of Year 2, X's assets had grown to cc times the amount needed to pay its insurance obligations reporting assets of $p.

X asserts that it "was possible for X to begin to underwrite new business in the Date 17's, but it chose not to do so. From Date 8, when X assumed the assets, liabilities and insurance business of Z through the tax years in question, X devoted no time to developing and marketing its insurance services and had no business plan for the expansion of its insurance business. X had no employees and did not write any new policies. X points to its acquisition of interest in other insurance companies to bolster its assertion that it carried on the business of insurance. X's investment activities are not changed in insurance merely by X's investment in other insurance companies.

X chose not to focus on its insurance business, but rather, chose to pursue its investment activities, including making loans to G and purchasing K in subsequent years. X purchased other noninsurance related assets, such as an interest in an L. X also indirectly owned M from which it received lease income. Based on the above, the activity "actually done" by X during the relevant years proves to be that of investing, not that of insurance.

X asserts that "[i]nvestment of contributed capital and premiums received is an integral and essential activity of an insurance company" and that "[s]ection 501(c)(15) imposes no limitations upon the amount or nature of investments which a tax exempt insurance company may make." However, X's U for the years in question far exceeded both the minimum S of $t required by R and X's unpaid loss reserves, as demonstrated by the financial information supplied by X.

	Date 11	December 31 of Year 1	Date 5 of Year 2
Unpaid loss reserve	$k	$q	$l
Total Assets	n	o	p

Investment Income	N/A	r	s
U	d	e	

Furthermore, from its inception, X's potential liability for unpaid losses decreased by u% to $l as of Date 5 of Year 2, while its assets increased by v% to $m as of Date 5 of Year 2.

In Inter-American Life Insurance Company v. Commissioner, 56 T.C. 497 (1971), aff'd per curiam, 469 F.2d 697 (9th Cir. 1972), the taxpayer was incorporated in Arizona as a limited stock life insurance company. Although the taxpayer alleged that it was an insurance company, over 80 percent of its reported gross income for the years in question consisted of dividends, interest, rents and stock transactions. The court examined the financial data reported by the taxpayer for the years in question and noted that:

> [P]etitioner's primary and predominant source of income was from its investments and not from issuing insurance contracts or reinsuring risks underwritten by insurance companies. During each of the years at issue, petitioner's investment income far exceeded its earned premiums and the amounts of earned premiums were de minimis during those years.
>
> It is equally as clear that petitioner's primary and predominant efforts were not expended in issuing insurance contracts or in reinsurance.

Inter-American at 507.

In holding that Inter-American was not an insurance company for the years in question, the court stated that:

> In deciding this issue, we have given due consideration to the problems indigenous to new life insurance companies...Our decision is ... based upon a finding that ...petitioner was not using its capital and efforts primarily in earning income from the issuance of insurance.

Inter-American at 508.

The court in Cardinal Life Insurance Company v. United States, 300 F. Supp. 387 (N.C. Tex. 1969), was faced with a taxpayer similar to Inter-American and X. Although Cardinal Life Insurance Company was chartered to do business in Texas, the court examined the character of its business activity during the years at issue. The court noted that Cardinal Life did not issue any insurance policies directly to an insured and did not employ a sales force to sell its insurance policies. The court compared Cardinal Life's premium income to its total income, finding percentages of premium income to total income of 0%, 0%, .66%, .87% and 9.11% for the years in question. In holding that Cardinal Life was not an insurance company for the pertinent period, the court stated:

> While Plaintiff's insurance activities were insignificant, it was generating substantial income from dividends on stocks, rental income on real estate, rental income on trailers, interest income and capital gains upon disposal of real estate and stocks. ...The Plaintiff is seeking to remove itself from the grasp of the personal holding company provisions by

> claiming life insurance company status through the issuance of a small and insignificant amount of insurance contracts. ...The question is to be resolved on the basis of the Plaintiff's primary business activity during each of the taxable years. Based upon the undisputed facts, the Court holds that Plaintiff was not a life insurance company during any of the years in question...

300 F. Supp. 387 at 392.

X contends that its fact pattern is more similar to that of Alinco Life Insurance Company v. United States, 373 F.2d 336 (1967). However, the court in Industrial Life Insurance Company v. United States, 344 F.Supp. 870, aff'd 481 F.2d 609 (1973), distinguished Alinco Life Insurance Company and found that Alinco involved the qualification as a life insurance company. It further noted that:

> [T]he risk during the relevant tax year amounted to almost one billion dollars ...and it did not have the majority of its income coming from real estate mortgages, dividends and interest. Alinco was also serving a legitimate business purpose of its owner, a large finance company, since the owner could not engage in the insurance business under the laws of the state under which it was incorporated.

344 F.Supp. at 876.

The Alinco Court was not faced with the question of whether the taxpayer was truly operating as an insurance company. Unlike the facts in X, Alinco's only activity during the years at issue was that of reinsurance. Alinco, 373 F.2d at 340. There was not a disproportionate relationship between Alinco's insurance premiums and its investment income, nor were there significant other investments such as those made by X.

Based on the above, it is clear that X's primary business activity for the years involved were investing its assets, not the business of insurance. Because X is not an insurance company as described in section 1.801-3(a)(1) of the regulations, X would not qualify for recognition of exemption under section 501(c)(15) of the Code.

Issue two: Whether X was entitled to change its taxable year from a calendar taxable year to a Date 5 taxable year pursuant to Revenue Procedure 85-58; AND

Issue Three: Whether the Service should aggregate the premium income earned by X for the period from January 1 of Year 2 through December 31 of Year 2 for purposes of determining whether X exceeded the $350,000 premium limitation set forth in section 501(c)(15) of the Code.

Revenue Procedure 85-58, 1985-1 CB 740 provided, in part, "Section 3.01....organization desiring to change their annual accounting periods (including organizations that come within the exception contained in section 1.442-1(c) of the regulations under which prior approval of the Commissioner to change is not required) may effect the change by timely filing the applicable information return, Form 990 ....with the appropriate Internal Revenue Service Center for the short period for which a return is required. The Form 990 should indicate that a change of accounting period is being

made.

.03. If an organization has previously changed its annual accounting period at any time within the ten calendar years ending with the calendar year that includes the beginning of the short period resulting from the change of an annual accounting period, and if it had a filing requirement at any time during that ten year period, it must file a Form 1128 (Application for Change in Accounting Period) with the appropriate Internal Revenue Service Center with its timely-filed annual information return... The Form 1128 must be filed by the fifteenth day of the fifth month following the close of the short period.

From its inception through December 31 of Year 1, X filed its returns on a calendar year basis. Effective Date 5 of Year 2, upon X's purchase of Q, X changed from a calendar year to a fiscal year with a Date 5 year end. The purchase of Q resulted in X failing to meet the requirements of exemption under section 501(c)(15) of the Code because X's aggregated premiums exceeded the $350,000 limit. Subsequent to the purchase of Q, X filed a Form 1120-PC return for the period Date 15 through December 31 of Year 2. In subsequent years, X continued to file its returns on a calendar year basis.

X argues that it fully complied with Rev. Proc. 85-58 and, therefore, it was entitled to file a return for the short tax year beginning January 1 of Year 2 and ending Date 5 of Year 2. Rev. Proc. 85-58 allows certain exempt organizations to change their annual accounting periods by (i) timely filing their Form 990 for the short period, and (ii) indicating thereon that a change of accounting period is being made. A timely filed Form 990 must be filed by the fifteenth day of the fifth month following the close of the short period. Accordingly, in order to comply with the Revenue Procedure, X needed to file on or before Date 18 either its Form 990, or a Form 8868, Application for Extension of Time To File an Exempt Organization Return, for the short year ending Date 5 of Year 2.

X did not file its Form 990 for the fiscal year ending Date 5 of Year 2 until Date 19. Instead, X is relying on the Form 8868 it filed for Year 2 to argue that its return was timely filed. However, according to the Service's computed records, none of the Forms 8868 at issue were timely filed on or before Date 18.

Attached to X's Form 990 are three Forms 8868. One of the Forms 8868 is a request for an automatic three month extension of time to file. This Form 8868 is dated Date 20 and indicates X is requesting a filing extension for a Year 2 calendar year return. The Service's computer records show that this Form 8868 was not received by the Service until Date 21. Since this extension was clearly filed after Date 18, X can not rely on it for purposes of Rev. Proc. 85-58.

The other two Forms 8868 request a filing extension for a short fiscal year ending Date 5 of Year 2. The first of these Forms 8868 is the automatic three month filing extension request, requesting an extension until Date 22 for filing the short year Return. The second of these forms is an additional three month filing extension request. Neither of these Forms 8868 is dated by X.

The Service's records show the first of these short year filing extensions was not received by the Service until Date 23. Date 23 is dd days after the Date 18 due date for filing a timely return for fiscal year ending Date 5 of Year 2. Accordingly, unless X has evidence that it timely mailed this undated Form 8868, the fact the form was not received

by the Service until dd days after Date 18 is strong evidence it did not timely file an initial extension for its purported return for the short fiscal year ending Date 5 of Year 2.

Moreover, even if X can establish that its initial filing extension for its purported short year return was timely filed, that extension only extended the return filing date until Date 22. The Service's computer records show, however, that X's request for an additional three month extension to file a return for the fiscal year ending Date 5 of Year 2 was not received by the Service until Date 24. This ee day gap between the due date and the date the extension was received by the Service is further evidence X did not timely file a short year return as required by Rev. Proc. 85-58. See JHK Enterprises, Inc., T.C. Memo 2003-79. Accordingly, X did not comply with the timely filing requirement of Rev. Proc. 85-58 and can not rely on the Revenue Procedure as authority for filing a short fiscal year return.

In addition, X is precluded from filing a fiscal year return because it did not maintain its books and records on a fiscal year basis during the taxable Year 2. See section 1.441-1(e)(2) of the regulations. A fiscal year will be recognized only if it is established as the annual accounting period of the taxpayer and only if the books of the taxpayer are kept in accordance with such fiscal year; See, Maclean v. Commissioner, 73 T.C. 1045, 1051 (1980); Brown v. United States, 68-2 USTC 9657 (Fla. D.C. 1968). Section 441 is one of the basic accounting provisions of the Internal Revenue Code (i.e., sections 441, 442 and 443) and it prohibits a taxpayer from filing a fiscal year return when the taxpayer maintains its books and records on a calendar year basis. Although these basic accounting provisions were drafted with a focus on computing taxable income, the provisions have been applied to issues involving tax exempt organizations. See GCM 39864 (Dec. 12, 1991). In fact, Rev. Proc. 85-58 implicitly recognizes the general applicability of these provisions to exempt organizations by setting forth a procedure that allows certain exempt organizations to change their accounting period under section 442. In addition, it should be noted the Revenue Procedure also contains the following recordkeeping requirement consistent with the recordkeeping requirement of section 1.441-1(e)(2) of the regulations: "[r]eturns for subsequent years must be made on the basis of a full 12 months ending on the last day of the last month of the new tax year." Rev. Proc. 85-58, section 5.

Based on Service's records, X did not maintain its books and records on a fiscal year basis during Year 2. Instead, X maintained its books and records as it always had on a calendar year basis and filed two late-filed short year tax returns for the calendar Year 2. The first return for ff months closes X's tax year the day before its premiums would exceed the $350,000 premium limitation of section 501(c)(15) of the Code. The second return covers December of Year 2 and returns X to being a calendar year taxpayer. However, as evidenced by the fact X filed a Form 8868 as late as Date 6 requesting an extension for filing a calendar year Form 990 return for Year 2, X did not maintain its Year 2 books and records on a Date 5 fiscal year basis. Accordingly, X's filing of a short year return claiming a fiscal year ending Date 5 of Year 2 should not be recognized as valid since it did not maintain its books and records as required for filing such a return.

Since X did not comply with the timely filing requirement of Rev. Proc. 85-58, it was not entitled to bifurcate its Year 2 tax year by filing a short year return for the fiscal year ending Date 5 of Year 2. Moreover, since it did not maintain its Year 2 books and records on such a fiscal years basis, X was prohibited from filing a valid fiscal year

return. Accordingly, it is appropriate for the Service to aggregate X's premium income for the entire calendar Year 2.

Issue Four: If it is determined that X no longer qualifies as an insurance company for the Year 1 and Year 2 taxable years, will X's section 953(d) of the Code election be revoked for those years?

Section 953(d)(2)(B) of the Code reads as follows:

> (B) Termination. If a corporation which made an election under paragraph (1) for any taxable year fails to meet the requirements of subparagraphs (A), (B), and (C) of paragraph (1) for any subsequent taxable year, such election shall not apply to any taxable year beginning after such subsequent taxable year.

In addition, Section 4.02 of Rev. Proc. 2003-47, 2003-2 C.B. 55, further clarifies the termination procedures applying to a section 953(d) election as follows:

> .02 Termination or Revocation of Section 953(d) Election
>
> (1) Once approved, the election generally remains effective for each subsequent taxable year in which the requirements of this revenue procedure and section 953(d) of the Code are satisfied unless revoked by the electing corporation with the consent of the Commissioner. However, if the electing corporation fails to timely file a return, pay the tax due as stated on the return, or comply with any other requirement for making the election contained in this revenue procedure and section 953(d), the Commissioner, in his discretion, may terminate the election as of the beginning of the taxable year after the taxable year with respect to which the failure occurs. If an election is terminated or revoked, the foreign corporation and its successors will be barred from making another election under section 953(d) without the consent of the Commissioner.

Section 953(d)(1) of the Code sets forth the requirements for a foreign corporation to elect to be treated as a domestic corporation. One requirement, contained in section 953(d)(1)(B), is that the electing corporation "would qualify under part I or II of subchapter L for the taxable year if it were a domestic corporation." Therefore, a corporation that failed to qualify as an insurance company under part I or II of subchapter L would fail the section 953(d) election requirement contained in section 953(d)(1)(B). In that case, the Commissioner may revoke the corporation's 953(d) election in the year following the year that the corporation failed to qualify as an insurance company.

Thus, if it is determined that X failed to qualify as an insurance company during the Year 1 or Year 2 taxable years, the Commissioner may revoke the section 953(d) of the Code election in the year following the first year in which X failed to qualify as an insurance company. In addition, any revocation of X's section 953(d) election by the Commissioner would bar X from making another section 953(d) election without the consent of the Commissioner. In this respect, since X failed to qualify as an insurance company during Year 1 and subsequent years, X's section 953(d) election is revoked for all tax years after Year 1.

Issue Five: Whether X can rely on the determination letter granted by the Service allowing it to claim tax exempt status under section 501(c)(15) of the Code.

As discussed above, X did not qualify for exemption under section 501(c)(15) of the Code for Year 1 and Year 2 because X's primary business activity for the years involved were investing its assets, not the business of insurance. The facts upon which the exemption was granted to X are not applicable in Year 1 and Year 2. Therefore X cannot rely on its determination letter.

CONCLUSIONS:

1. Because X is not an insurance company as described in section 1.801-3(a)(1) of the regulations, X does not qualify for recognition of exemption under section 501(c)(15) of the Code for tax years ending Year 1 and Year 2.

2. X was not entitled to change its taxable year from a calendar taxable year to a Date 5 taxable year pursuant to Revenue Procedure 85-58.

3. The Service shall aggregate the premium income earned by X for the period from January 1 of Year 2 through December 31 of Year 2 for purposes of determining whether X exceeded the $350,000 premium limitation set forth in section 501(c)(15) of the Code.

4. Since X failed to qualify as an insurance company during the Year 1 or Year 2 taxable years, the Commissioner revokes the section 953(d) election in the year following the first year in which X failed to qualify as an insurance company. In this case, revocation of the section 953(d) election is effective for tax year ending December 31 of Year 2.

5. X is not entitled to relief pursuant to section 7805(b) of the Code for tax years beginning January 1 of Year 1. Therefore, X can not rely on its determination letter effective tax years beginning January 1 of Year 1. For tax years subsequent to Year 2, X filed Forms 1120-PC. This conclusion is responsive to your issues 5, 6 and 7.

A copy of this technical advice memorandum is to be given to the taxpayer. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

- END -