



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

**DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
Attn: Mandatory Review, MC 4920 DAL
1100 Commerce St.
Dallas, TX 75242**

Date: April 22, 2009

Number: **201334042**
Release Date: 8/23/2013

Employer Identification Number:

ORG
ADDRESS

Person to Contact/ID Number:

Contact Numbers:

LEGEND:
ORG = Name of ORGANIZATION
NUM = Identifying Number

UIL: 501.15-01

CERTIFIED MAIL – RETURN RECEIPT REQUESTED

Dear _____ :

In a determination letter dated February 14, 2006, you were held to be exempt from Federal income tax under section 501(c)(15) of the Internal Revenue Code (the Code).

Based on recent information received, we have determined you have not operated in accordance with the provisions of section 501(c)(15) of the Code. Accordingly, your exemption from Federal income tax is revoked effective January 1, 20xx. This is a final adverse determination letter with regard to your status under section 501(c)(15) of the Code.

We previously provided you a report of examination explaining why we believe revocation of your exempt status is necessary. At that time, we informed you of your right to contact the Taxpayer Advocate, as well as your appeal rights. On April 13, 20XX, you signed Form 6018-A, *Consent to Proposed Action*, agreeing to the revocation of your exempt status under section 501(c)(15) of the Code.

You have filed taxable returns on Forms 1120-PC, *U.S. Property & Casualty Insurance Company Income Tax Return*, for the year[s] ended December 31, 20xx with us. For

future periods, you are required to file Form 1120-PC with the appropriate service center indicated in the instructions for the return.

You have the right to contact the Office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal Appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free, 1-877-777-4778, and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please contact the person whose name and telephone number are shown at the beginning of this letter.

Sincerely,

Sunita Lough
Director, EO Examinations



DEPARTMENT OF THE TREASURY

INTERNAL REVENUE SERVICE

1100 Commerce Street

Dallas, TX 75242

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

January 28, 2009

ORG
ADDRESS

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

Dear :

We have enclosed a copy of our report of examination explaining why we believe an adjustment of your organization's exempt status is necessary.

We have also enclosed Publication 892, Exempt Organization Appeal Procedures for Unagreed Issues, and Publication 3498, *The Examination Process*. These publications include information on your rights as a taxpayer, including administrative appeal procedures within the Internal Revenue Service.

If you request a conference with Appeals, we will forward your written statement of protest to the Appeals Office, and they will contact you. For your convenience, an envelope is enclosed. If you and Appeals do not agree on some or all of the issues after your Appeals conference, the Appeals Office will advise you of its final decision

If you elect not to request Appeals consideration but instead accept our findings, please sign and return the enclosed Form 6018-A, *Consent to Proposed Adverse Action*. We will then send you a final letter modifying or revoking your exempt status under I.R.C. § 501(c)(15). If we do not hear from you within 30 days from the date of this letter, we will process your case on the basis of the recommendations shown in the report of examination and send a final letter advising of our determination.

In either situation outlined in the paragraph above (execution of Form 6018-A or failure to respond within 30 days), you are required to file federal income tax returns for the tax period(s) shown above, for all years still open under the statute of limitations, and for all

later years. File the federal tax return for the tax period(s) shown above with this agent within 60 days from the date of this letter, unless a request for an extension of time is granted. File returns for later tax years with the appropriate service center indicated in the instructions for those returns.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance.

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Renee B Wells by *M&B*

Renee B. Wells
Acting Director, EO Examinations

Enclosures:
Publication 892
Publication 3498
Form 6018-A
Report of Examination
Envelope

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG	NUM	Year/Period Ended 12/31/20xx

LEGEND:

ORG = Name of Organization

NUM = Identifying Number

COUNTRY = Name of foreign country

YEAR = xx

PARTNER = Name of ownership partners

ISSUES

1. Does ORG qualify for tax exempt status under Internal Revenue Code (IRC) Section 501(c)(15), for the years beginning January 1, 20xx?
2. If ORG does not qualify for tax exempt status for years beginning January 1, 20xx, what are the tax consequences?
3. If the tax exempt status is revoked, how will it affect future years?

FACTS

ORG was organized in December 20xx in ORG is owned by PARTNER (%) and PARTNER (%).

On March 19, 20xx, ORG filed the election under Internal Revenue Code (IRC) section 953(d). The election stated that PARTNERS were each % shareholders.

Application Form 1024, *Application for Recognition of Exemption under Section 501(a)*, was filed by the organization on August 15, 20xx. The purpose, as stated in the application form, was as follows:

Purpose- small property and casualty insurance company formed under the laws of COUNTRY. Conducts property and casualty related insurance activities on a direct and reinsurance basis.

- Underwriting selected lines of property and casualty insurance coverages for business entities that are both related and unrelated thereto. Categorized-error and omissions insurance, business economic loss, business interruptions, bankruptcy and casualty related risks. Total organizational time devoted is estimated at % to %.
- Accepting and issuing reinsurance coverage for selected lines of property and casualty insurance risks including credit disability insurance and special risks accident medical insurance. No credit life is envisioned. Total organizational time estimated at % to %.
- Activities conducted on COUNTRY.

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After various correspondence between ORG and the Service, the Service, on February 14, 20xx, issued a determination letter granting tax exempt status under IRC 501(c)(15) to ORG.

During the year under examination ORG was involved in the issuance of insurance policies directly and was involved in one reinsurance agreement. The policies issued directly were:

Commercial Crime

- Insured: PARTNERS Company
- Limits: Theft of Money \$; Robbery or safe (inside) \$; Outside of premises \$; Computer fraud \$
- Total Premium: \$

Employee Theft and Forgery Policy

- Insured: PARTNERS Company
- Limits: Employee Theft \$\$; Forgery or Alteration \$\$
- Total Premium: \$

Employee Related Practices

- Insured: PARTNERS Company
- Limit: \$\$
- Premium: \$

Income Replacement- Key Employee

- Insured: PARTNERS Company
- Limit: \$\$ monthly per each key employee; 0 employees listed
- Premium: \$

Tax Audit Expense

- Insured: PARTNERS Company
- Limit: \$\$
- Premium: \$

ORG was involved one reinsurance agreement with Independent Company during 20xx. ORG reinsured credit property insurance and credit disability insurance from Independent Company ORG was one of many organizations involved in reinsuring with Independent Company.

Forms 990 were filed for the 20xx tax year. The following is a breakdown of the Gross Receipts received by ORG for the years ending December 31, 20xx, and the percentage of Gross Premiums to Gross Receipts for the same years per Notice 2006-42.

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG	NUM	Year/Period Ended 12/31/20xx

ORG	20xx
Premiums Written	
Premiums Assumed	
Total Premiums	
Interest Income	
Dividend Income	
Other Investment Income	
Capital Gains	
Total Gross Receipts	
Percentage- Gross Premium/Reinsurance Income to Gross Receipts	%

An election under IRC 831(b) was not made prior to 20xx. Form 1120-PC was filed for year ending December 31, 20xx and an election under IRC 831(b) was attached to it.

ORG was not involved in a court ordered liquidation in 20xx.

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LAW AND ANALYSIS

1. Does ORG qualify for tax exempt status under Internal Revenue Code (IRC) Section 501(c)(15) for the years beginning January 1, 20xx?

Internal Revenue Code section 501(c)(15)(A) exempts from Federal income tax insurance companies (as defined in section 816(a)) other than life (including interinsurers and reciprocal underwriters) if-

- (i.) (I) the gross receipts for the taxable year do not exceed \$600,000, and
(II) more than 50 percent of such gross receipts consist of premiums, or
- (ii.) in the case of a mutual insurance company-
 - (I) the gross receipts of which for the taxable year do not exceed \$150,000 and,
 - (II) more than 35 percent of such gross receipts consist of premiums.

Clause (ii) shall not apply to a company if any employee of the company, or a member of the employee's family (as defined in section 2032(A)(e)(2)), is an employee of another company exempt from taxation by reason of this paragraph (or would be so exempt but for this sentence).

Sec. 206, Clarification of Exemption from Tax for Small Property and Casualty Insurance Companies, of the Pension Funding Equity Act of 2004, P.L. 108-218, amended section 501(c)(15)(A) to change the definition of small property and casualty insurance companies (insurance companies other than life insurance companies) exempt from income taxes to: (1) a company whose gross receipts for the taxable year do not exceed \$600,000, and over half such gross receipts consist of premiums (currently, whose net written premiums (or, if greater, direct written premiums) for the taxable year do not exceed \$350,000); or (2) a mutual insurance company (a) whose gross receipts for the taxable year do not exceed \$150,000 and more than 35 percent of which consist of premiums and (b) none of whose employees (or member of the employee's family) is an employee of another company exempt from tax under section 501(c)(15). These changes were applicable after December 31, 2003.

Notice 2006-42, IRB, 2006-19 provides guidance as to the meaning of "gross receipts" for purposes of section 501(c)(15)(A) of the Internal Revenue Code. This notice advises taxpayers that the Service will include amounts received from the following sources during the taxable year in "gross receipts" for purposes of § 501(c)(15)(A):

- A. Premiums (including deposits and assessments), without reduction for return premiums or premiums paid for reinsurance;

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- B. Items described in § 834(b) (gross investment income of a non-life insurance company); and
- C. Other items that are properly included in the taxpayer's gross income under subchapter B of chapter 1, subtitle A, of the Code.

Thus, gross receipts include both tax-free interest and the gain (but not the entire amount realized) from the sale or exchange of capital assets, because those items are described in § 834(b). Gross receipts do not, however, include amounts other than premium income or gross investment income unless those amounts are otherwise included in gross income. Accordingly, the term gross receipts does not include contributions to capital excluded from gross income under § 118, or salvage or reinsurance recovered accounted for as offsets to losses incurred under § 832(b)(5)(A)(i).

Section 834(b)(1)(D) of the Internal Revenue Code includes under gross receipts the gains from the sale or exchanges of capital assets to the extent provided in subchapter P (section 1201 and following, relating to capital gains and losses).

Section 834(c)(6) of the Internal Revenue Code allows a deduction for Capital Losses to the extent provided in subchapter P (section 1201 and following) plus losses from capital assets sold or exchanged in order to obtain funds to meet abnormal insurance losses and to provide for the payment of dividends and similar distributions to policyholders.

Based on the changes in the limitations under Internal Revenue Code (IRC) Section 501(c)(15)(A), and the operation of ORG during 20xx, it was determined from the chart above that ORG did not qualify for tax exempt status in 20xx. ORG had gross receipts that exceeded the \$600,000 limitation.

Section 206(e) of the Pension Funding Act of 2004, P.L. 118-218 provides the effective date of the new requirements for exemption under IRC 501(c)(15). It states:

EFFECTIVE DATE-

(1) **IN GENERAL-** Except as provided in paragraph (2), the amendments made by this section shall apply to **taxable years beginning after December 31, 2003.**

(2) **TRANSITION RULE FOR COMPANIES IN RECEIVERSHIP OR LIQUIDATION-** In the case of a company or association which--
(A) for the taxable year which includes April 1, 2004, meets the requirements of section 501(c)(15)(A) of the Internal Revenue

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Code of 1986, as in effect for the last taxable year beginning before January 1, 2004, and
(B) on April 1, 2004, is in a receivership, liquidation, or similar proceeding under the supervision of a State court, the amendments made by this section shall apply to taxable years beginning after the earlier of the date such proceeding ends or December 31, 2007.

ORG was not involved in a court ordered liquidation during 20xx. Therefore, Section 206(e)(2) does not apply to this organization.

Therefore, for the years beginning January 1, 20xx, ORG did not qualify for tax exempt status under IRC 501(c)(15).

2. If ORG does not qualify for tax exempt status for years beginning January 1, 20xx, what are the tax consequences?

Since ORG did not qualify for tax exempt status under IRC Section 501(c)(15) for years beginning January 1, 20xx, ORG's filing of the Form 990 was incorrect. ORG should have filed Form 1120-PC.

IRC 831 discusses tax on insurance companies other than life insurance companies.

IRC 831(a) states as a general rule, "Taxes computed as provided in section 11 shall be imposed for each taxable year on the taxable income of every insurance company other than a life insurance company."

IRC 831(b) provides an alternative tax for certain small companies. It states in IRC 831(b)(1) that, in general, "In lieu of the tax otherwise applicable under subsection (a), there is hereby imposed for each taxable year on the income of every insurance company to which this subsection applies a tax computed by multiplying the taxable investment income of such company for such taxable year by the rates provided in section 11(b)."

IRC 831(b)(2) discusses the companies to which this subsection applies.

- (A) In general. This subsection shall apply to every insurance company other than life (including interinsurers and reciprocal underwriters) if-
- (i) the net written premiums (or, if greater, direct written premiums) for the taxable year do not exceed \$1,200,000, and

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- (ii) such company elects the application of this subsection for such taxable year.

The election under clause (ii) shall apply to the taxable year for which made and for all subsequent taxable years for which the requirements of clause (1) are met. Such election, once made, may be revoked only with the consent of the Secretary.

Regulations (Regs.) 301.9100-8(a)(2) discusses the time for making elections. Under (i) it states in general that except as otherwise provided in this section, the elections described in paragraph (a)(1) of this section, must be made by the later of-

- (A) The due date (taking into account any extensions of time to file obtained by the taxpayer) of the tax return for the first taxable year for which the election is effective, or
- (B) January 22, 1990 (in which case the election generally must be made by amended return)

Regs. 301.9100-8(a)(1) mentioned above includes IRC 831(b)(2)(A).

Regs. 301.9100-8(a)(3) describes the manner of making elections. It states, " Except otherwise provided in this section, the elections described in paragraph (a)(1) of this section must be made by attaching a statement to the tax return for the first taxable year for which the election is to be effective."

Based on the Code and Regulation sections above, ORG is not entitled to the relief under 831(b), for the year under examination. An election was made for the 20xx tax year but no election was made for 20xx. The election made in 20xx can not be made retroactive to 20xx. The election made in 20xx is good for the 20xx year and all future years only.

3. If the tax exempt status is revoked, how will it affect future years?

The tax exempt status is being revoked for the years beginning January 1, 20xx. Form 1120-PC is required for 20xx and all future years where ORG does not qualify for exemption. If ORG meets the requirements under IRC 501(c)(15) in future years, it may be allowed to file the Form 990 for each year they qualify, as a self-declared entity. Otherwise, Form 1120-PC would be required. Since ORG made the election in 20xx, it is effective for the year the election was made and for all future years that the Form 1120-PC is required. The election can not be made retroactive.

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TAXPAYER'S POSITION

Unknown at the time of this writing

SUMMARY

It is the Governments position, based on the above facts, law and analysis, that the tax exemption status of ORG for the years beginning January 1, 20xx should be revoked based on not meeting the qualifications for exemption under IRC 501(c)(15). Form 1120-PC would be required to be filed for 20xx and all future years where ORG does not qualify for exemption under IRC 501(c)(15).