



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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Date: March 26, 2009

Release Number: 201341036
Release Date: 10/11/2013

UIL: 501.15-01

LEGEND:

ORG = Name of Organization

Person to Contact/ID Number:

Contact Numbers:

Voice
Fax

CERTIFIED MAIL – RETURN RECEIPT REQUESTED

Dear

In a determination letter dated October 5, 20xx, 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 February 17, 20 , 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 and Casualty Insurance Company Income Tax Return*, for the year ended December 31, 2006 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:

Taxpayer Advocate Service

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 26, 2009

Taxpayer Identification Number:

LEGEND:

ORG = Name of Organization
Address = Address of Organization
Year = xx

Form:
Tax Year(s) Ended:

Person to Contact/ID Number:

ORG
Address

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		Year/Period Ended 12/31/20xx

LEGEND:

ORG = Name of Organization
Country = Name of Foreign Country
Year = xx

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 formed in 19xx in Country. Org filed its Articles of Association under the Country Law of 19xx. Its object as stated in its Articles is to engage in any lawful act or activity for which corporations may be organized under the Law. The Articles also stated that there would be shares with a value of \$.

In August 19xx ORG filed its 953(d) election to be taxed as a domestic organization.

In February 20xx, ORG filed Application Form 1024, *Application for Recognition of Exemption Under Section 501(a)*, with the Internal Revenue Service, seeking exemption under Internal Revenue Code (IRC) section 501(c)(15). Its purpose, as stated in the application form, is to engaged in the reinsurance of credit insurance contracts, vehicle service contracts and GAP Service Contracts. Shareholders listed are Director and His Wife.

On October 5, 20xxx, a determination letter was issued, granting exemption to ORG under IRC 501(c)(15).

Since its inception, ORG has not issued any policies directly. Only insurance business ORG has been involved in has been reinsurance from other insurance and reinsurance

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companies. ORG has reinsurance agreements for Service Contracts, GAP Contracts and Credit Insurance.

- Service Contract: Extended Service Program for Client. Administered by Dealers Services. Repair, replace, or reimburse Purchaser for reasonable costs to repair or replace any of the components listed, if required due to mechanical breakdown. Mechanical breakdown- failure to a faulty part or faulty workmanship by the manufacturer.
- GAP Contract: Agreement with Insurance. Reinsure % of the Client's GAP Service reimbursement liability.
- Credit Insurance: Life Insurance Company. The Life and Health Insurance Company. Coverage- life and health insurance. Maximum- \$. Used in association of a vehicle purchase.

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

ORG	20xx
Premiums Assumed	\$
Total Premiums	\$
Interest Income	\$
Total Gross Receipts	\$
Percentage- Gross Premium/Reinsurance Income to Gross Receipts	0%

The computation under Notice 2006-42 requires "premiums written". In the computation above, the premiums assumed from reinsurance are considered the premiums written.

ORG has two shareholders, Director and his wife. Director and his wife were also sole or partial shareholders of the following organizations:

- Related Ltd. Director %; Wife %

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- Related Ltd. Director %
- LLC Director % (sold in 20xx)
- LLC Director %

A breakdown of other organization's that are sole or partial shareholders, along with the percentages of ownership and gross receipts is below at the end of 20XX

NAME OF ORG.	PERCENT OWNER	20XX
RELATED, LTD	DIRECTOR HIS WIFE	\$
Related, Ltd.	DIRECTOR	\$
, LLC	DIRECTOR	\$
, LLC	DIRECTOR	\$

An election under IRC 831(b) has never been filed. As of the writing of this report, there has never been a filing of the election, either with the filing of the Forms 990 or separately.

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Name of Taxpayer ORG		Year/Period Ended 12/31/20xx

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).

Notice 2006-42 also states that amounts received by all members of the insurance company's controlled group (as defined in section 501(c)(15)(c)) are taken into account for purposes of these tests.

IRC 501(c)(15)(B) states, "For purposes of subparagraph (A), in determining whether any company or association is described in subparagraph (A), such company or association shall be treated as receiving during the taxable year amounts described in subparagraph (A) which are received during such year by all other companies or associations which are part of the same controlled group as the insurance company or association for which the determination is made."

IRC 501(c)(15)(C) states, "For purposes of subparagraph (B), the term "controlled group" has the meaning given such term by section 831(b)(2)(B)(ii), except that in applying section 831(b)(2)(B)(ii) for purposes of this subparagraph, subparagraph (B) & (C) of section 1563(b)(2) shall be disregarded."

IRC 831(b)(2)(B)(ii) states, "Controlled Group. For purposes of clause (i), the term "controlled group" means any controlled group of corporations, (as defined in section 1563(a)); except that-

- (I) "more than 50 percent" shall be substituted for "at least 80 percent" each place it appears in section 1563(a), and
- (II) Subsections (a)(4) and (b)(2)(D) of section 1563 share not apply"

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Section 1563(a)(2) states, "Brother-sister controlled group. Two or more corporations if 5 or fewer persons who are individuals, estates, or trusts own (within the meaning of subsection (d)(2)) stock possessing more than 50 percent of the total combined voting power of all classes of stock entitled to vote or more than 50 percent of the total value of shares of all classes of stock of each corporation, taking into account the stock ownership of each such person only to the extent such stock ownership is identical with respect to each such corporation."

Section 1563(d)(2) states, "Brother-sister controlled group. For purposes of determining whether a corporation is a member of a brother-sister controlled group of corporations, (within the meaning of subsection (a)(1)), stock owned by a corporation means-

- (A) stock owned directly by such corporation, and
- (B) stock owned with the application of paragraphs (1), (2), and (3) of subsection (e)."

Therefore, gross receipts from all other companies or associations that are part of the controlled group with ORG must be included in the gross receipts computation to determine whether ORG qualifies for tax exempt status under IRC 501(c)(15). This includes S Corporations that file Form 1120-S but not organizations that file Form 1065.

Based on the gross receipts of ORG, and the gross receipts of the other organization's listed above that Director and his Wife have more than 50% ownership in, total gross receipts for ORG, per Notice 2006-42, exceeded the \$600,000 limitation as explained in IRC 501(c)(15). The gross receipts of the other organizations of the controlled group were to be considered in the computations starting January 1, 20xx. Therefore, for the years beginning January 1, 20xx, ORG no longer qualified for tax exemption under IRC 501(c)(15).

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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Name of Taxpayer ORG		Year/Period Ended 12/31/20xx

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, 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 the years beginning January 1, 20xx, ORG's filing of the Form 990 was incorrect. For the year beginning January 1, 20xx, 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 years under examination and for any future year, until they decide to file the election. The election has never been filed, either with the Form 990 or separately. Any election filed now or in the future would only be effective for the year the election was filed and all subsequent years. The election can not be made retroactive.

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

The tax exempt status should be revoked for the years beginning January 1, 20xx. Form 1120-PC is required for each year 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. Any year in the future that the Form 1120-PC is required, ORG is allowed to make an election under IRC 831(b). Once the election is made, it is effective for the year the election is made and

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for all future years that the Form 1120-PC is required. The election can not be made retroactive.

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 any year where ORG does not qualify for exemption under IRC 501(c)(15).