



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: Jan. 14, 2009

Number: **201342012**

Release Date: 10/18/2013

Employer Identification Number:

LEGEND:

ORG= Name of Organization

Address= Address of ORG

Date = xx

Person to Contact/ID Number:

Contact Numbers:

ORG

Address

UIL: 501.15-00

CERTIFIED MAIL – RETURN RECEIPT REQUESTED

Dear

In a determination letter dated September 25, 19xx, 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 December 1, 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 Form[s] 1120-PC, *U.S. Property and Casualty Insurance Company Income Tax Return*, for the year[s] ended December 31, 20 20 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,

Renee B. Wells
Acting Director, EO Examinations



DEPARTMENT OF THE TREASURY

INTERNAL REVENUE SERVICE

1100 Commerce Street

Dallas, TX 75242

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

July 8, 2008

Taxpayer Identification Number:

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

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,

Marsha A. Ramirez
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 December 31, 20xx

LEGEND:

ORG = Name of Organization

Date = xx

State = Name of State

ISSUES

1. Does ORG Company qualify for tax exempt status under Internal Revenue Code (IRC) Section 501(c)(15), for the years beginning January 1, 20xx?
2. If ORG Company 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 Company (ORG) was formed In February 19xx in the State. Its purpose according to its Articles of Incorporation at the time of formation was to operate the following types of insurance business as defined in Section 1113(a) of the State Insurance Law:

- Accident and health insurance- insurance against death or personal injury by accident or by any specified kind or kinds of accident and insurance against sickness, ailment or bodily injury, including insurance providing disability benefits pursuant to article nine of the workers' compensation law...
- Fire Insurance- loss or damage to any property resulting from fire, including loss or damage incident to the extinguishment of a fire or to the salvaging of property in connection therewith.
- Miscellaneous Property Insurance- loss of damage to property resulting from lightning, smoke or smudge, windstorm, tornado, cyclone, earthquake, volcanic eruption, rain, hail, frost or freeze, weather or climatic conditions, excess or deficiency of moisture, flood, the rising of waters of the ocean or its tributaries, insects or blights or disease of such property except animals, electrical

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

disturbances causing or concomitant with a fire or an explosion in public service or public utility

In June of 19xx the Articles were amended to add the following types of insurance: water damage, burglary and theft, boiler and machinery, marine protection and indemnity insurance.

ORG was formed and licensed to assume all the assets, liabilities and obligations of Predecessor Corporation which had gone into liquidation in 19xx. Predecessor was dissolved in October 19xx. Ownership of the ORG remained the same as with Predecessor Corporation owning % .

Based on the activities ORG stated they would be conducting, a determination letter was issued by the Service on September 25, 19xx, granting tax exempt status under Internal Revenue Code (IRC) 501(c)(15).

GSC did not accept any new or renewal business from 19xx to its liquidation in 19xx. ORG has not accept any new or renewal business since its formation in 19xx. The only purpose of ORG has been to operate until all claims have been determined and settled. Once all claims have been determined and settled, the organization will liquidate and dissolve.

ORG has been a party to a reinsurance agreement with RE- Insurance Company, which accounts for approximately % of the liability outstanding.

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

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

ORG	20xx	20xx	20xx
Premiums	\$	\$	\$
Total Premiums	\$	\$	\$
Investment Income	\$	\$	\$
Capital Gains	\$		
Other Income			\$
Total Gross Receipts	\$	\$	\$
Percentage- Gross Premium/Reinsurance Income to Gross Receipts	%	%	%

Other income of \$ reported above was an Indemnification Trust Distribution from the State, Inc., for which ORG was a member.

The decision to form ORG, take over the business of Related ORG, and to operate until liquidation and dissolve, has been a voluntary decision and not one decided by the courts.

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.

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

LAW AND ANALYSIS

1. Does ORG Insurance Company 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, 20xx.

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

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
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ORG		December 31, 20xx

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;
- 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 since January 1, 20xx, it was determined from the chart above that ORG did not qualify for tax exempt status for years beginning January 1, 20xx. ORG was not able to meet the \$600,000 Gross Receipts limitation in 20xx & 20xx; and they were unable to meet the greater than 50% requirement of Gross Premiums to Gross Receipts in 20xx, 20xx & 20xx. Since they were unable to meet either or both of the requirements, they did not qualify for tax exemption under IRC 501(c)(15) for years beginning January 1, 20xx.

Since ORG is a stock ownership company, they are not allowed to try to meet the requirements for mutual companies of less than \$150,000 in gross receipts and more than 35% in gross premiums to gross receipts. Even if they could, they would not be able to meet this set of requirements either.

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ORG		December 31, 20xx

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 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 the years ending January 1, 20xx. Therefore, Section 206(e) does not apply to this organization.

2. If ORG Insurance Company 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 was required to file Form 1120-PC for years beginning January 1, 20xx.

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."

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ORG		December 31, 20xx

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
 - (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 year 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 is filed and all subsequent years. The election can not be made retroactive.

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

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 the year ending December 31, 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. 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 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). Forms 1120-PC would be required to be filed for any year where ORG does not qualify for exemption under IRC 501(c)(15).