Internal Revenue Service

Department of the Treasury

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Person to Contact:

Telephone Number:

Refer Reply To:
CC:INTL:Br1-PLR-C-120205-98
Date:
March 25, 1999

LEGEND:

A or Taxpayer A =
B =
Country X =
Country Y =
Date A =
Z =

Dear

This responds to your letter of October 23, 1998, as supplemented by your letter of February 3, 1999. You requested a ruling that premiums received by Taxpayer A on policies of reinsurance of United States risks are exempt from the insurance excise tax imposed by section 4371 of the Internal Revenue Code of 1986.

The Ruling contained in this letter is predicated upon facts and representations submitted by, or on behalf of, Taxpayer A and were accompanied by a penalty of perjury statement executed by the appropriate party. This office has not verified any of the material submitted in support of this request for ruling. Verification may be required as a part of the audit process.

A is incorporated under the laws of Country X, has its home office located within Country X and has been in business in Country X for more than 70 years. A represents that it is entitled to benefits under the United States - Country X Income Tax Treaty (Treaty).

Pursuant to Article of the Treaty, the United States excise tax on premiums paid to foreign insurers is a covered tax but only to the extent that the risks covered by

such premiums are not reinsured with a person who is not entitled to the benefits of the Treaty or the benefits of another treaty with similar provisions.

Article of the Treaty establishes the limitations that determine whether a resident of one of the contracting states is a person entitled to benefits under the Treaty. Taxpayer A represents that it is engaged in an active trade or business in Country X and that the premium income from U.S. insureds is derived in connection with, or incidental to, that trade or business. Accordingly, taxpayer contends that it qualifies for benefits under Article of the United States - Country X Income Tax Treaty.

Rev. Proc. 92-39, 1992-1 C.B. 860, explains the procedure by which a German insurer or reinsurer may request an excise tax closing agreement. While this revenue procedure applies specifically to the United States-Germany Income Tax Convention, sec. 5 of the revenue procedure states that it may be used by insurers or reinsurers claiming benefits under treaties with similar limitations on benefits and excise tax exemption provisions. The United States - Country X Income Tax Treaty has limitations on benefits and excise tax exemption provisions similar to those in the United States - Germany Income Tax Convention. Accordingly, Rev. Proc. 92-39 is also applicable for purposes of the United States - X Income Tax Treaty.

Section 3.06 of the revenue procedure contains a ratio test for determining whether an insurer or reinsurer is engaged in the active conduct of a trade or business in a treaty country and whether premiums received from U.S. insureds are derived in connection with, or incidental to, that trade or business. Section 3.07 of the revenue procedure describes an alternative 11-factor test by which an insurer or reinsurer in a treaty country such as Country X, that cannot meet the ratio test in section 3.06, may establish that it qualifies for benefits under the active trade or business limitation on benefits.

Taxpayer A concedes that it cannot meet the ratio test in section 3.06 of Rev. Proc. 92-39 for 1997. Taxpayer A requests, however, that the Service determine that it is engaged in an active trade or business in Country X, and that the premiums are received in connection with this business, pursuant to the alternative test in section 3.07 of the revenue procedure. The 11-factor test, and taxpayer's representations as to application of the test to its facts for 1997, are as follows:

1. <u>The address of the insurer or reinsurer's office in Country X</u>.

Taxpayer A's address in Country X is Z. This factor supports Taxpayer A's contention that it is engaged in an active trade or business in Country X.

2. <u>The ratio that the insurer or reinsurer's payroll and commission expense paid to employees and agents for services performed in Country X bears to the insurer or</u>

reinsurer's worldwide payroll and commission expense.

Taxpayer A's payroll and commission expense paid to employees and agents for services performed in Country X is 93.9% of Taxpayer A's total worldwide payroll and commission expense. This is 73.9% above the minimum 20% required by section 3.06 of Rev. Proc. 92-39. This factor, therefore, supports Taxpayer A's contention that it is engaged in an active trade or business in Country X.

3. Whether the insurer or reinsurer's employees and agents in Country X have, and habitually exercise, authority to sign policies and to approve payment of claims on the company's behalf.

Taxpayer A's employees and agents in Country X have, and habitually exercise, authority to sign policies and approve payment of claims on the company's behalf. Therefore, this factor supports taxpayer's contention that it is engaged in an active trade or business in Country X.

4. Whether the insurer or reinsurer is subject to the national income tax imposed by Country X on the basis of residence.

Taxpayer A is subject to the national income tax imposed by Country X on the basis of residence. This factor supports taxpayer's contention that it is engaged in an active trade or business in Country X.

5. The ratio that gross premiums received by the insurer or reinsurer for policies on risks situated in Country X bear to total gross premiums received by the insurer or reinsurer.

The ratio that gross premiums received by Taxpayer A on risks situated in Country X bear to total gross premiums is 8.9%. This is 11.1% below the minimum 20% required by section 3.06 of Rev. Proc. 92-39. This factor does not support Taxpayer A's contention that it is engaged in an active trade or business in Country X.

6. The ratio that gross premiums received by the insurer or reinsurer for policies on risks situated in Country X bear to gross premiums received for policies on risks situated in the United States.

The ratio that gross premiums received by Taxpayer A on risks situated in Country X bears to gross premiums received for risks situated in the United States is 900%. Thus, Taxpayer A receives nine times more premiums on risks in Country X than on risks in the United States, and this factor supports Taxpayer A's contention that it is engaged in an active trade or business in Country X.

7. The ratio that the value of the assets of the insurer or reinsurer used or held

for use in the active conduct of a trade or business in Country X at the close of the taxable year bears to the value of all of its assets at the close of the taxable year.

Taxpayer A represents that 98.7% of its worldwide assets are held for use in its business in Country X. This factor supports Taxpayer A's contention that it is engaged in an active trade or business in Country X.

8. Whether the insurer or reinsurer is subject to the Country X government regulations generally applicable to companies authorized to insure or reinsure risks situated in Country X.

Taxpayer A is subject to the Country X government regulation generally applicable to companies authorized to reinsure risks situated in Country X. This factor supports Taxpayer A's contention that it is engaged in an active trade or business in Country X.

9. The percentage of the insurer or reinsurer's shares of outstanding stock of each class not owned by persons entitled to benefits under the Treaty or, in the case of a mutual company, the percentage of the insurer or reinsurer's policies insuring risks of persons not entitled to benefits under the Treaty.

Taxpayer A represents that this ratio is 99.9%. Taxpayer A also represents that the 99.9% is owned by B, a resident of Country Y. The United States - Country Y Income Tax Treaty contains a federal excise tax waiver similar to that of the United States - Country X Income Tax Treaty. Taxpayer A further represents that B has entered into a closing agreement with the Commissioner regarding its entitlement to a federal excise tax waiver. Since Taxpayer A is owned 99.9% by a person not entitled to benefits under the Treaty, this factor does not support Taxpayer A's contention that it is engaged in an active trade or business in Country X.

10. The percentage of the insurer or reinsurer's gross income (including investment income attributable to its insurance business but excluding investment income not attributable to its insurance business) used, directly or indirectly, to meet liabilities to persons not entitled to benefits under the Treaty. For purposes of this test, the term "liabilities" refers to amounts that reduce gross premiums or are deductible

against gross income, including interest, royalties, and premiums paid in connection with reinsuring risks.

Taxpayer A represents that 46.4% of its gross income was used directly, or indirectly, to meet liabilities to persons not entitled to benefits under the Convention. Since less that 50% of Taxpayer A's gross income was used to meet liabilities to persons not entitled to benefits under the Treaty, this factor supports Taxpayer A's contention that it is engaged in an active trade or business in Country X.

11. Other information indicating that the insurer or reinsurer is engaged in the active conduct of a trade or business in Country X.

Taxpayer A represents that it has conducted reinsurance business in Country X since Date A, well before the United States - County X Income Tax Treaty came into force, and that it was not established to take advantage of the excise tax waiver in the Treaty. This factor supports taxpayer's contention that it is engaged in an active trade or business in Country X.

The information submitted by taxpayer indicates that on the basis of the 11-factor test in section 3.07 of Rev. Proc. 92-39, 9 of the factors support taxpayer's contention that it is engaged in an active trade or business in Country X. With the exception of two of the factors , the information submitted by the taxpayer overwhelmingly supports its contention that it is engaged in an active trade or business in Country X. Accordingly, based on the information submitted by Taxpayer A, Taxpayer A is engaged in the active conduct of a trade or business in Country X and the premiums received from U.S. insureds are derived in connection with, or incidental to, this trade or business for purposes of Article of the Treaty.

Pursuant to paragraph (8)(a) of the enclosed Closing Agreement, the liabilities of Taxpayer A for Federal Excise Tax, as agreed upon, including liability resulting from reinsurance of U.S. risks with persons not entitled to exemption under the Treaty or another convention, will commence on October 23, 1998, the date of Taxpayer A's ruling request. The letter of credit required by paragraph (5)(a) of the Closing Agreement, in the amount of , must be in effect within 30 days of the date the Agreement is signed on behalf of the Commissioner.

Any person otherwise required to remit the Federal excise tax on foreign insurance or reinsurance policies issued by Taxpayer A pursuant to section 46.4371-1(a) of the Excise Tax Regulations may rely upon a copy of this letter and/or an executed copy of the Closing Agreement as authority that they may consider premiums paid to you on and after October 23, 1998, as exempt under the United States - X Income Tax Treaty from the federal excise tax.

This ruling does not address the issues of whether Taxpayer A is an insurance

company or whether premiums paid to Taxpayer A are deductible under section 162 of the Internal Revenue Code or any other issue on which there is no explicit holding.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Sincerely,

W. Edward Williams
Senior Technical Reviewer
Branch 1
Associate Chief Counsel
(International)

Enclosures:
Copy of approved Closing Agreement
Copy of letter for Section 6110 purposes
Copy of Closing Agreement for section 6110 purposes

CLOSING AGREEMENT OF FINAL DETERMINATION COVERING SPECIFIC MATTERS

Under section 7121 of the Internal Revenue Code of 1986 ("the Code"), , US Taxpayer Identification Number: Applied for on , and the Commissioner of Internal Revenue ("the Commissioner") make the following closing agreement:

WHEREAS, the business profits article [Article of the United States-Income Tax Convention ("the Convention")] exempts insurance or reinsurance premiums paid to a resident of from the Federal excise tax imposed by section 4371 et seq. of the Code but only to the extent that the insurer or reinsurer does not reinsure such risks with a person not entitled to exemption from such tax under the Convention or another convention [Article] and only if the insurer or reinsurer qualifies under Article of the Convention;

WHEREAS, Section 3.02 of Rev. Proc. 92-39, provides that the person required to remit the tax may consider the premium exempt if, prior to filing the return for the taxable period, such person has knowledge that the insurer or reinsurer has in effect closing agreement to be liable as a United States taxpayer for Federal excise tax due under section 4371 et seq. of the Code on premiums from policies reinsured with reinsurers that are not entitled to exemption from the excise tax under the Convention or any other convention and on premiums paid or accrued when the insurer or reinsurer did not qualify under the Convention for exemption from the excise tax imposed by section 4371 et sea. of the Code;

WHEREAS, represents that it is, and will continue to be, eligible for benefits under the Convention; and

WHEREAS, (hereinafter referred to as "the Taxpayer") wishes to have its policies of insurance or reinsurance considered exempt from tax under the Convention; IT IS HEREBY DETERMINED AND AGREED THAT:

(1) Taxpayer shall, for purposes of this closing agreement, be liable as a United States Taxpayer for the Federal excise tax due under section 4371 et seq. of the Code on premiums from policies reinsured with reinsurers that are not entitled to exemption from the excise tax under the Convention or any other convention and from policies issued or outstanding when Taxpayer did not qualify under the Convention for exemption from the excise tax imposed by section 4371 et seq. of the Code.

(2) (a) Returns of Federal excise tax due under and pursuant to this closing agreement and section 4371 et seq. of the Code shall be made by Taxpayer, or by Taxpayer's

authorized representative on Taxpayer's behalf, by filing Form 720, Quarterly Federal Excise Tax Return, for each return period covered by this closing agreement.

(b) If Taxpayer reinsures, in whole or in part, a policy of insurance or reinsurance with any person(s) not entitled to exemption from the excise tax under the Convention or any other convention or if Taxpayer issues or has outstanding a policy or policies when the Taxpayer did not qualify under the Convention for exemption from the excise tax imposed by section 4371 et seq. of the Code, the tax reportable on the return, Form 720, shall be computed on the basis of the percentage of such policy reinsured or on the basis of premium accrued or received during the time period when Taxpayer did not qualify for exemption under the Convention. For purposes of the preceding sentence, Taxpayer may consider a reinsurer to be entitled to exemption from the excise tax under the Convention or another convention if the reinsurer is a party to a closing agreement with the Internal Revenue Service under this Convention or another convention, or the reinsurer provides evidence that it is a resident of the United States or of a country with which the United States has in effect a convention that waives the excise tax without an explicit "anti-conduit" clause.

(c) Forms 720 shall be filed with the Director, Internal Revenue Service Center, Philadelphia, Pennsylvania 19255, U.S.A.

(d) Taxpayer or Taxpayer's authorized representative, shall make the required Federal tax deposits of the Federal excise tax in such manner and at such times as are prescribed by regulations and explained in the instructions for Form 720.

(3) Taxpayer agrees that, for purposes of determining its Federal excise tax liability pursuant to this closing agreement and for purposes of verifying Taxpayer's entitlement to benefits under the Convention, Taxpayer will maintain for a period of 6 years from the end of each taxable period to which this closing agreement applies accounts and records of items of insurance and reinsurance that will be made available upon written request by the Internal Revenue Service at the place mutually agreed upon by the Service and Taxpayer. Taxpayer will also maintain for 6 years and make available for inspection records to establish eligibility for Convention benefits. Taxpayer will be allowed 60 days, or other period of time (but in no event less than 60 days) determined as reasonable by the Assistant Commissioner (International), within which to make available its accounts and records.

(4) If it is determined that there is an underpayment in respect of any excise tax determined to be due pursuant to this closing agreement and section 4371 et seq. of the Code, the Internal Revenue Service shall issue a statement of notice and demand for the tax due plus any interest and applicable penalties. Notice of any underpayment shall be sent to the Taxpayer at the name and address shown on the Form 720, if a Form 720 was filed for the period for which an underpayment is determined by the

Internal Revenue Service, or otherwise to Taxpayer's registered address in . Payment of all additional amounts due shall be made in accordance with the terms specified in the statement of notice and demand. Collection of such amounts not paid per notice and demand shall be in accordance with paragraph 5 hereof.

(5) (a) As security for payment of tax, Taxpayer shall cause an irrevocable letter of credit to be issued by a United States bank that is a member of the Federal Reserve System, or by a United States branch or agency of a foreign bank that is on the National Association of Insurance Commissioners list of banks from which letters of credit may be accepted, in favor of the Internal Revenue Service in the amount of or such amount as may from time to time be mutually agreed upon by Taxpayer and the Service. Such letter of credit must be in effect within 30 days of the date that the closing agreement is signed for the Commissioner of Internal Revenue.

(b) The Service may issue a statement of notice and demand with respect to:

6. Any tax shown on a Form 720 (original, amended, or substitute for return) that is not paid with such return; or

(ii) Any proposed additional excise tax liability sustained by the Internal Revenue Service Regional Director of Appeals having jurisdiction over such matter, if the time for filing a protest of such proposed liability has expired, provided that the statement of notice and demure has been issued as provided in paragraph 4 hereof.

(c) If, after the conditions in paragraph 5 (b) hereof have been met, the tax, interest, and any applicable penalties, are not paid in accordance with the terms of the statement of notice and demand, collection of such amounts will be made by resorting to such letter of credit, to the extent thereof, before any levy or proceeding in court for collection is instituted against Taxpayer.

(d) If such letter of credit is drawn upon, it must be reinstated to within 60 days after the date drawn upon.

(6) (a) Solely by reason of the execution by Taxpayer and the Commissioner of this closing agreement, any person otherwise required to remit the federal excise tax on foreign insurance or reinsurance premiums pursuant to section 46.4374-1 (a) of the Excise Tax Regulations may consider premiums paid to Taxpayer after the effective date of this agreement as exempt under the Convention from the Federal excise tax.

(b) Taxpayer agrees that the Commissioner, or his or her authorized delegate, may

disclose Taxpayer's name as an insurer or reinsurer that qualifies for exemption from the excise tax under the Convention by publication or otherwise.

(7) (a) This closing agreement shall include, as an attachment hereto, a statement from the local tax office with which Taxpayer files its tax returns, with an English translation, certifying that Taxpayer is a resident of as defined in the Convention and a statement from Taxpayer, with an English translation, that Taxpayer is not disqualified from receiving benefits under the Convention by reason of Article of the Convention. Taxpayer shall submit such information in its statement as will establish its entitlement to benefits under the Convention.

(b) The statement from local tax office shall be effective for a period of 3 calendar years beginning with the year of receipt. Taxpayer agrees to renew the certificate of residency every three years, and its own certification of eligibility for benefits under the Convention every year, on or before the expiration date of the original certificate. Taxpayer agrees to provide an original and one copy of the recertification along with a photocopy of this closing agreement, to:

Internal Revenue Service
1111 Constitution Ave., N.W.
Washington, D.C. 20224, U.S.A.
Attn:CC:INTL:1

Taxpayer also agrees to promptly notify the Competent Authority of and the Internal Revenue Service of any change that may result in its disqualification from receiving Treaty benefits.

(8) (a) This closing agreement shall be effective . This agreement shall thereafter continue in effect unless terminated as provided in subparagraph (b) of this paragraph.

(b) This agreement may be terminated by either Taxpayer or the Commissioner by giving the other written notice of the notifying party's intent to terminate. The decision to terminate is solely at the discretion of the party giving such notice. This agreement shall be terminated on the last day of the return period immediately following the return period within which the written notice of termination is given.

(c) Taxpayer hereby agrees to file a return, Form 720, marked "Final Return" for the taxable period within which this agreement terminates pursuant to paragraph (8) (b) hereof and to furnish a duplicate of such "Final Return" to:

Internal Revenue Service

1111 Constitution Ave., N.W.
Washington, D.C. 20224, U.S.A.
Attn: CC: INTL:1

(d) Taxpayer agrees that the letter of credit issued pursuant to paragraph 5 hereof shall remain in effect for a period of not less than 60 days after the “Final Return" has been filed in accordance with subparagraph (c) hereof, or until the examination of Taxpayer's returns is completed and any additional tax due has been paid, whichever is later.

WHEREAS, the determinations set forth above are hereby agreed to by Taxpayer:

NOW THIS CLOSING AGREEMENT WITNESSETH, that the said Taxpayer and said Commissioner of Internal Revenue hereby mutually agree that the determinations set forth shall be final and conclusive, subject, however, to reopening in the event of fraud, malfeasance, or misrepresentation of material fact, and provided that any change or modification of applicable statutes or tax conventions will render this agreement ineffective to the extent that it is dependent upon such statutes or tax conventions.

IN WITNESS WHEREOF, the above parties have subscribed their names to these presents, in triplicate.

Signed

By
Title

Commissioner of Internal Revenue

By
Associate Chief Counsel (International)

By Assistant Commissioner (International)

_____
Date