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Department of the Treasury
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Person To Contact:
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Date:
July 29, 2024

Legend:

c	=
Date 1	=
Date 2	=
Date 3	=
k	=
Manufacturer X	=
Manufacturer Y	=
Manufacturer Z	=
Parent	=
Prior Parent	=
State	=
Taxpayer	=

Dear :

On April 7, 1999, the Internal Revenue Service (the "Service") issued PLR 199926033 (PLR-122660-98) (the "1999 PLR") to Prior Parent, the parent of the consolidated group of which Taxpayer was a member at the time the 1999 PLR was issued. The 1999 PLR ruled that Taxpayer qualified as an insurance company for federal income tax purposes and was subject to the provisions of parts II and III of Subchapter L of the Internal Revenue Code (the "Code"). This ruling was based on a determination that Taxpayer's 1997 contract with Manufacturer X, as described in the 1999 PLR (the "X Contract"), was an insurance contract for federal income tax purposes.

On Date 1, the Service notified you that it was considering revoking the 1999 PLR because the Service had tentatively concluded that the X Contract was not an insurance

contract for federal income tax purposes. Section 12.04 of Rev. Proc. 99-1, 1999-1 C.B. 6, provides that a letter ruling found to be in error or not in accordance with the current views of the Service may be revoked or modified.

The Service has now concluded that the 1999 PLR's determination that the X Contract was insurance for federal income tax purposes is not in accord with the current views of the Service. As explained below, because this determination was a necessary predicate for the 1999 PLR's ruling that Taxpayer was taxable as an insurance company, the 1999 PLR is hereby revoked, subject to the § 7805(b) relief described below.

FACTS

Taxpayer is a State corporation. When the 1999 PLR was issued, Taxpayer was wholly owned by Prior Parent and joined Prior Parent in filing a consolidated federal income tax return. Currently, Taxpayer is wholly owned by Parent and joins Parent in filing a consolidated federal income tax return.

When the 1999 PLR was issued, Taxpayer contracted with manufacturers of vehicles that offered purchasers of their vehicles a roadside assistance program entitling the purchasers to 24-hour roadside assistance for flat tires, fuel delivery, mechanical breakdowns, dead batteries, and lockouts. Pursuant to the contracts with the manufacturers, Taxpayer arranged for the provision of the roadside assistance to the purchasers of the manufacturers' vehicles. Taxpayer did not perform any of the roadside assistance itself but contracted with many different independent contractors (including, for example, tow truck operators and locksmiths) throughout the United States to provide the actual roadside assistance services.

Taxpayer generally entered into three different types of contracts under which it was obligated to provide roadside assistance: Reimbursement Contracts, Per Vehicle Contracts, and Per Incident Contracts.

Under a Reimbursement Contract, Taxpayer received from the vehicle manufacturer a small fee for each vehicle sold by the manufacturer that was covered by the contract. Taxpayer also charged the manufacturer a dispatch fee plus the actual cost of providing any roadside assistance. Taxpayer's contract with Manufacturer Z, as described in the 1999 PLR, exemplified a Reimbursement Contract.

Under a Per Vehicle Contract, Taxpayer received from the vehicle manufacturer a fee for each vehicle sold by the manufacturer that was covered by the contract. Taxpayer was not further compensated regardless of the number of times roadside assistance was dispatched or the cost of providing such assistance. Taxpayer's contract with Manufacturer Y, as described in the 1999 PLR (the "Y Contract"), exemplified a Per Vehicle Contract.

Under a Per Incident Contract, Taxpayer received from the vehicle manufacturer a predetermined fee each time roadside assistance was provided to a vehicle covered by the contract.

The X Contract was essentially the economic equivalent of a Per Incident Contract combined with a Reimbursement Contract. Under the X Contract, Taxpayer received from Manufacturer X a fee for each covered vehicle, which was a vehicle designated by Manufacturer X as a 1998, 1999, or 2000 model year vehicle for delivery in the United States. Vehicles were provided roadside assistance for a period of 3 years or 36,000 miles, whichever occurred first.

If the cumulative number of dispatches for covered vehicles of a particular model year was below c% of the number of such covered vehicles (the "Model Year Cap"), Taxpayer was to refund to Manufacturer X a certain amount per covered vehicle for each percentage point that the actual usage rate (i.e., the number of dispatches divided by the number of covered vehicles) was below c%. Thus, if the number of dispatches was below the Model Year Cap, the X Contract was generally the economic equivalent of a Per Incident Contract.

However, if the number of dispatches for a given model year exceeded the Model Year Cap, Manufacturer X was required to reimburse Taxpayer for actual payments made to provide roadside assistance for each such additional dispatch. This portion of the contract was the economic equivalent of a Reimbursement Contract because Taxpayer was reimbursed for actual payments made to provide roadside assistance.

When the 1999 PLR was issued, approximately k% of Taxpayer's business was from the X Contract.

LAW AND ANALYSIS

Insurance Risk

Section 831(a) provides that tax is imposed for each taxable year on the taxable income of every insurance company other than a life insurance company. Section 831(c) states that the term "insurance company" is defined in § 816(a). Section 816(a) defines "insurance company" to mean a company more than half of the business of which during the taxable year is the issuing of insurance or annuity contracts or the reinsuring of risks underwritten by insurance companies.

Section 831(c)'s reference to § 816(a) for purposes of defining an insurance company was incorporated into the Code in 2004. Pension Funding Equity Act of 2004, Pub. L. 108-218, § 206(c), 118 Stat. 596, 611 (2004). Prior to that (including when the 1999 PLR was issued) reference was made to Treas. Reg. § 1.801-3(a), which provides:

> The term "insurance company" means a company whose primary and predominant business activity during the taxable year is the issuing of insurance or annuity contracts or the reinsuring of risks underwritten by insurance companies.

Neither the Code nor the Treasury regulations define insurance, but case law has held that to be considered insurance an arrangement must involve risk-shifting, involve risk distribution, involve insurance risk, and meet commonly accepted notions of insurance. See, e.g., Avrahami v. Commissioner, 149 T.C. 144, 177 (2017).

In its discussion of insurance risk, the court in R.V.I. Guaranty Co. v. United States, 145 T.C. 206 (2015), stated:

> We have said that "[i]nsurance risk is involved when an insured faces some loss-producing hazard (not an investment risk), and an insurer accepts a payment, called a premium, as consideration for agreeing to perform some act if and when that hazard occurs."

R.V.I., 145 T.C. at 235 (quoting Black Hills Corp. v. Commissioner, 101 T.C. 173, 182 (1993)).

Central to the notion of insurance is the concept of a "fortuitous event." The court in Commissioner v. Treganowan, 183 F.2d 288 (2d Cir. 1950), wrote: "From an insurance standpoint there is no risk unless there is uncertainty or, to use a better term, fortuitousness. It may be uncertain whether the risk will materialize in any particular case." Id. at 290 (quoting 8 Ency. Soc. Sc. 95). Similarly, the court in AMERCO, Inc. v. Commissioner, 979 F.2d 162 (9th Cir. 1992), explained that "[i]nsurance risk is the possibility that a particular event for which an insured will be held liable will occur." Id. at 167. Thus, a contract that lacks the requisite fortuity does not have insurance risk and is not a contract that constitutes insurance for federal income tax purposes.

Rev. Rul. 2007-47, 2007-2 C.B. 127, involves an arrangement entered into by a taxpayer as it began the operation of a business inherently harmful to people and property. Government regulations required the taxpayer to remediate any harm after the cessation of business. The taxpayer entered into an arrangement with an insurance company under which the insurance company was to reimburse the taxpayer for the remediation costs up to a certain limit. The revenue ruling concluded that the arrangement between the taxpayer and the insurance company lacked insurance risk and was not insurance for federal income tax purposes. In making its determination, the ruling stated that no insurance risk or hazard, such as a hurricane or accident, existed as to whether the taxpayer would have to incur the remediation costs, and it was certain that the insurance company would have to pay for the remediation costs up to the policy limit.

Because of its particular fee refund provision, the X Contract did not have the requisite fortuity to constitute an insurance risk. Accordingly, the X Contract did not constitute insurance for federal income tax purposes. k% of Taxpayer's revenue was from the X Contract. Under the legal standard in effect at the time the 1999 PLR was issued, Taxpayer's "primary and predominant" business activity was not the issuing of insurance or annuity contracts or the reinsuring of risks underwritten by insurance companies. As a result, Taxpayer was not an insurance company for federal income tax purposes when the 1999 PLR was issued. Accordingly, the 1999 PLR is revoked, subject to the § 7805(b) relief described below.

Notwithstanding the revocation of the 1999 PLR, the Service continues to agree with its determination in the 1999 PLR that the Y Contract, a Per Vehicle Contract, was insurance for federal income tax purposes.

Section 7805(b) Relief

Section 7805(b)(8) provides that the Secretary may prescribe the extent, if any, to which any ruling (including any judicial decision or any administrative determination other than by regulation) relating to the internal revenue laws shall be applied without retroactive effect.

Under § 12.07 of Rev. Proc. 99-1, if a letter ruling is issued covering a continuing action or series of actions and the letter ruling is later found to be in error or no longer in accord with the position of the Service, the Service ordinarily will limit the retroactive effect of the revocation or modification to a date that is not earlier than the date on which the letter ruling is revoked or modified.

Under § 12.11 of Rev. Proc. 99-1, a taxpayer may request that the retroactive effect of any revocation or modification of a letter ruling be limited. Parent has made this request on behalf of Taxpayer, and the Service has decided to grant relief under § 7805(b) to limit the effect of the revocation of the 1999 PLR.

The 1999 PLR is revoked as of Date 2. However, Taxpayer may treat Per Incident Contracts (including the X Contract, as amended prior to Date 2) as insurance contracts for purposes of determining whether Taxpayer is an insurance company for federal income tax purposes for Taxpayer's last taxable year ending prior to Date 3. Further, for Taxpayer's taxable year that includes Date 2 and all subsequent taxable years, Taxpayer may treat any Per Incident Contract (including the X Contract, as amended) that was issued before Date 2 as an insurance contract for federal income tax purposes, unless and until such contract is modified or amended (or further modified or amended in the case of a contract that had been previously modified or amended before Date 2).

CONCLUSION

The 1999 PLR is revoked, subject to the § 7805(b) relief described above.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. This letter is directed only to the taxpayer who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter.

In accordance with the power of attorney on file in this office, a copy of this letter is being furnished to your authorized representative.

Sincerely,

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Daniel P. Phillips
Senior Counsel, Branch 4
Office of Associate Chief Counsel
(Financial Institutions & Products)

cc: