

IRC Section 953(c)(3)(C)

Foreign Captive Insurance Company Election

Overview

Generally, "related person insurance income", as defined by IRC §953(c)(2), is considered Subpart F income. Consequently, U.S. shareholders (as defined in §953(c)(1)) of a controlled foreign corporation (as defined in §953(c)(1)) receiving "related person insurance income" are generally taxed on their pro rata share of such income even if the income is not repatriated to the U.S.

A foreign corporation may avoid Subpart F treatment by electing, under §953(c)(3)(C), to treat related person insurance income as effectively connected with a U.S. trade or business. The election permits the foreign corporation to avail itself of tax deferral devices available to U.S. corporations (e.g. net operating loss carrybacks and carryforwards). This election is not available to controlled foreign corporations ("CFCs"), as defined by §957(a).

The foreign corporation must submit to the IRS a signed election statement, a signed closing agreement, and a letter of credit. The purpose of the closing agreement and letter of credit is to secure payment of taxes due from the foreign corporation or its shareholders with respect to "related person insurance income". The amount of the letter of credit, as determined by the IRS, generally must be 10% of the prior year's gross premium income from insuring risks of U.S. shareholders. This amount is usually at least \$75,000, but the corporation may present evidence that the amount determined by the IRS is excessive.

After receipt of the election statement by the IRS, the corporation's representative will receive a closing agreement form. Once executed, a stamped copy of the closing agreement and election statement will be returned to the taxpayer. This confirms the IRS's acceptance of the election. A copy of the agreement and statement should be attached to the taxpayer's timely filed tax return.

Once the election is made, it applies to all subsequent tax years. If an electing corporation fails to file a timely return or to pay the tax due regarding the "related person insurance income", the election will be automatically revoked. An accepted election will also exempt "related person insurance income" from IRC §4371 excise tax, commencing the later of the first day of the taxable year in which election is made or the date the election is accepted.

When to File

The process of making the election is begun by mailing an election statement, in duplicate, signed under penalties of perjury to the Director of the Internal Revenue Service Center, P.O. Box 21086, Philadelphia, PA. The IRS then returns a closing agreement and further instructions. Once the closing agreement has been executed, the Service will return a stamped copy of the election statement and closing agreement, indicating acceptance of the election. These must be attached to the taxpayer's timely filed return.

Where to File

The initial election statement is mailed to the Director of the Internal Revenue Service Center, P.O. Box 21086, Philadelphia, PA. The accepted election statement is attached to the taxpayer's timely filed income tax return, which is mailed to the designated Internal Revenue Service Center.

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1. Code Section: 953
2. Topic: Corporate; Foreign; Insurance
3. Return Type: 1120

Authorities

IRC §953(c)(3)(C); Notice 87-50