Affiliate Reinsurance
SFC Base Erosion Minimum Tax – Alternative Approach

Summary of proposal

Current law:

Under Code Section 832(b)(4), property-casualty insurance companies are permitted to deduct "premiums paid for reinsurance" in calculating their underwriting income.

SFC Proposal – Minimum Tax on Base Erosion Payments

The SFC's version of the Tax Cuts and Jobs Act, as reported on November 16, 2017, includes a proposal whereby reinsurance premiums would be treated as base erosion payments and subject to the proposed base erosion minimum tax. This tax would be computed as the excess of 10% of modified taxable income over regular tax liability. Modified taxable income is defined to be regular taxable income increased by the amount of the base erosion payment (reinsurance premium in this context). As a result, the minimum tax is equal to 10% of the premium payment, offset by the rate differential on otherwise taxable income. The minimum tax operates as an excise tax, as the base against which it's applied does not reflect net income associated with the business, but simply the gross reinsurance premium paid.

Proposed Alternative Approach:

This proposed alternative reflects the fact that reinsurance premium payments differ greatly from typical base erosion payments made with respect to license, trademark or other intangibles. Such payments represent a permanent move of capital from the US. On the other hand, reinsurance payments represent the arms-length price paid to a reinsurer to assume risk from the ceding company. The premium payment funds the risk of loss assumed by the reinsurer. The majority of such payments are paid back to the US ceding company in the form of loss recovery payments, the reinsurer's portion of 3rd party claims. The ceding commissions and loss recovery payments are fully taxable to the US ceding company upon receipt. As such, premium payments do not represent a permanent move of capital offshore and should not be treated in the same manner as typical base erosion payments.

We propose that the definition of base erosion payments be revised to clarify that the premium payment be offset by "*... any return premium, ceding commission, reinsurance recovered, or other amount received by such insurance company with respect to the reinsurance for which such non-taxed reinsurance premium is paid...*".

In addition, the Foreign Excise Tax (FET) that applies to reinsurance premiums pursuant to IRC §4371(3), should not apply to reinsurance premiums taxed pursuant to this section. The FET is intended to be a surrogate for the income tax liability that would have arisen in the US, had the ceded business remained onshore. It was devised as a base erosion measure to achieve tax parity between insurance business wholly conducted in the US and US insurance business ceded offshore. After application of the minimum tax proposal, the US will have eliminated any base erosion concern with respect to the premium ceded. Thus, there is no need for a related FET, as the income has already been taxed in the US. In order to correct this duplicative tax, we propose that a specific reference is added to the Minimum Tax Statute indicating that FET does not apply to amounts taxed under this proposal.

Received by NSD/FARA Registration Unit 11/28/2017 4:20:18 PM

RIMS™
the risk management society

November 28, 2017

The Honorable Tim Scott
Hart Senate Office Building Room 717
Washington, DC 20510-4005

Re: Senate version of H.R. 1, the Tax Cuts and Jobs Act

Dear Senator Scott:

I am writing to you on behalf of Risk and Insurance Management Society, Inc. (RIMS) to express our concern about the economic impact on risk managers of a provision included in the corporate tax reform plan. We support the ongoing work on tax reform, but ask for your consideration in ensuring that this measure related to reinsurance be excluded from this legislation.

The Risk and Insurance Management Society (RIMS) is the world's largest professional organization dedicated to advancing the practice of risk management. We represent more than 600 industrial, service, nonprofit, charitable and government entities in the state of South Carolina. The entities we represent are typically commercial insurance policyholders of all sizes ranging from Fortune 500 companies to small businesses, but also cities, counties and school districts.

Today, premiums paid by a U.S. affiliate to a global affiliate for reinsurance are deductible because they are normal business transactions routinely made by both domestic and global insurers. Affiliate reinsurance enables insurers to diversify risks, lowering costs for policyholders. If the provision in the Senate tax bill to charge an excise tax on transactions within global companies is enacted, it risks cutting off a lifeline to the global insurance capacity that supports so many in coastal states. This provision would also restrict the free flow of capital, concentrate insurance risk, and leave all Americans with higher costs for the same insurance coverage.

As you know, access and availability of property insurance is an issue of great concern. Global insurers will likely pay 50 percent of all claims from Hurricanes Harvey, Maria and Irma, with more than $28 billion already confirmed. An ill-conceived proposal taxing foreign affiliate reinsurance or all international reinsurance would only serve to limit US insurance capacity and drive up the cost of insurance. This would be a major threat to businesses, consumers and homeowners around the country.

A 2017 study released by The Brattle Group, a global economic consulting firm, found that the proposal would decrease the supply of reinsurance by 13 percent nationwide, with an aggregate drop of $18.3 billion in available reinsurance capacity. The result: a steep hike of $5 billion in higher annual premium costs for consumers without any additional benefit.

5 Bryant Park, 13th Floor, New York, NY 10018
t 212.286.9292 ■ f 212.655.5931 ■ www.RIMS.org

Received by NSD/FARA Registration Unit 11/28/2017 4:20:19 PM

RIMS
the risk management society

For the U.S. economy, the Tax Foundation found that eliminating the deduction would reduce gross domestic product by $1.4 billion. In fact, for every dollar raised, the private sector would lose four.

Every year South Carolina is at risk for hurricanes, flooding and earthquakes, among other natural disasters – as exemplified most recently by Hurricane Irma which brought historic flooding to Charleston and $64 billion to $92 billion in damages to Florida, Alabama, Georgia and South Carolina collectively. This comes on the heels of Hurricane Matthew in 2016 which tragically claimed four lives in South Carolina and was the state's deadliest hurricane in more than a decade. Loss estimates from that storm total $2.3 billion with international-based reinsurers expected to cover nearly half.

A robust insurance market, open to as many competitors as possible, is essential for insurance to support economic growth. Global insurers and reinsurers are the bedrock of the insurance and reinsurance market, because they diversify their catastrophic risk globally leading to lower prices and more coverage that benefits the US economy. Global reinsurers play an essential role in stabilizing our insurance marketplace; and without them risk concentrations would make it more difficult for domestic insurance companies to cope with an influx of claims following a disaster.

We need this global insurance and reinsurance capacity, and the proposed discriminatory reinsurance tax would undercut numerous state's economic recovery and increase insurance costs across the board. We ask that you work to keep this proposal out of the final tax reform legislation.

We appreciate your consideration and we thank you for the opportunity to present the concerns and recommendations of risk managers across the country. If you have any questions, please contact RIMS Government Relations Director, Whitney Craig at wcraig@rims.org or 212-655-2699.

Sincerely yours,

Nowell Seaman

Nowell Seaman, RIMS-CRMP, FCIP, CRM
President, RIMS

Received by NSD/FARA Registration Unit 11/28/2017 4:20:19 PM