



March 27, 2014

Honorable Andrew M. Cuomo  
Governor of New York State  
Executive Chamber  
State Capitol  
Albany, NY 12224

**Re: Opposition to Budget Bill's Captive Insurance Company Proposals**

Dear Governor Cuomo:

These comments are submitted on behalf of the Captive Insurance Companies Association ("CICA"). CICA is the leading domicile neutral trade association representing the global captive insurance industry. CICA's members are individual captives, companies that own and utilize captives and service providers (such as actuaries, accountants, attorneys, and insurance consultants).

New York's proposed budget bill (the "Bill") includes several tax reform components, including a mandatory combined reporting methodology. As part of the combined reporting proposal, all captive insurance companies would be included in the combined group — a stark departure from current New York tax law. This proposal represents a significant departure from established tax principles and would make New York an outlier in captive insurance taxation. We strongly oppose this provision, and ask that you support its elimination from the budget bill — which is reflected in the Senate version of the Bill.

Under current New York tax law, captive insurance companies are generally subject to a premium tax instead of a corporate franchise tax, which is consistent with how New York treats other non-life insurance companies and how other states generally treat insurance companies and captive insurance companies.

New York tax law consists of multiple Articles that provide distinct tax regimes for certain types of corporations. New York tax law imposes tax on general business corporations under Article 9-A, and on insurance corporations under Article 33. Specifically, New York tax law imposes a premium tax on captive insurance corporations under New York Tax Law § 1502-b. Under current New York tax law, an insurance corporation cannot be included in an Article 9-A or Article 32 combined return.

The one exception, however, is an overcapitalized (or "stuffed") captive insurance company. New York enacted this provision based on a perception that the state was losing revenue because some captive insurance companies have been overcapitalized and generated significant non-

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premium revenues which would not be taxed. New York tax law considers a captive insurance company to be overcapitalized if fifty percent or less of the company's gross receipts for the taxable year consists of premiums. New York Tax Law essentially disregards an overcapitalized captive insurance company's status as an insurance corporation and imposes tax under Article 9-A as if it were a general business corporation.

The Bill proposes a new Captive Combination Provision that goes well beyond the current law's intent (to combat tax planning) and adversely impacts all captive insurance companies. In the Captive Combination Provision, all "combinable" captive insurance companies would be excluded from Article 33 (so the premium tax under New York Tax Law § 1502-b would not apply), and included in an Article 9-A combined return. New York Tax Law § 2 would include all captive insurance companies, which satisfy the combined reporting requirements, in the definition of a "combinable" captive insurance company. There is no limitation that the captive insurance company be domiciled or licensed in New York State.

If enacted into law, the Captive Combination Provision would likely result in a significant tax increase on captive insurance companies. The Captive Combination Provision also raises several serious constitutional, federal preemption, and tax policy concerns. This letter discusses why the Captive Combination Provision reflects unsound tax and public policy and why it may cause significant unintended consequences.

There are a number of technical arguments against this Bill, to-wit:

- **The Captive Combination Provision violates the tax policy justifications for a separate tax regime for insurance companies.**

Almost every state, including New York, imposes a separate tax regime for insurance companies. A separate tax regime is necessary because the business of insurance companies is so fundamentally different than general corporations. States generally impose a "premium tax" on insurance companies instead of a corporate income or franchise tax. The premium tax is a percentage of the premiums sourced to the taxing state. Generally, states prefer the premium tax because insurance companies often do not have significant taxable income. Thus, the premium tax generates more revenue for the state. The Captive Combination Provision undermines all the justifications for a separate tax regime for insurance companies by disregarding all captive insurance companies' status as insurance companies and taxing them as general business corporations.

- **The current Overcapitalized Captive Combination Provision already remedies New York's perceived tax problem with captive insurance companies.**

The intent of the current Overcapitalized Captive Combination Provision is to combat a perceived tax planning strategy in which some captive insurance companies earned significant non-premium revenues. These non-premium revenues were not subject to the premium tax, so they went untaxed altogether. After significant deliberation, the legislature thoughtfully enacted the Overcapitalized Captive Combination Provision, which remedied this perceived problem. Under current law, captive insurance companies with significant non-premium revenues are subject to the corporate franchise tax. There is no need to subject captive insurance companies that do not have significant non-premium revenues to the corporate franchise tax.

- **The Captive Combination Provision may have unintended consequences.**

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The Captive Combination Provision would not combine captive insurance companies that are alien corporations, assuming they have no effectively connected income with the United States. Therefore, corporations may seek a tax advantage by moving their captive insurance companies offshore. The New York legislature and Department of Financial Services worked very hard to encourage corporations to establish captive insurance companies within New York. These efforts will be completely undermined as a result of the proposed Captive Combination Provision.

- **The Captive Combination Provision would treat captive insurance companies differently than other states treat captive insurance companies, and differently than New York treats other insurance companies.**

The Captive Combination Provision would truly be an outlier in state tax. No other state has a blanket provision that forces all captive insurance companies to be included in a combined group. Many states, such as California, expressly prohibit insurance companies from being included in a combined group. Furthermore, New York would treat similarly situated non-life insurance companies differently than captive insurance companies.

- **The Captive Combination Provision arguably violates the Nonadmitted and Reinsurance Reform Act of Dodd-Frank.**

The Nonadmitted and Reinsurance Reform Act (“NRRA”) is a federal law that preempts states from imposing tax on non-admitted insurance. The NRRA definitions are very broad. If a captive insurance company wrote risk for an insured whose home state was a state other than New York, federal law preempts New York from imposing tax, directly or indirectly, on that premium payment. By including a captive insurance company in a combined group, the captive insurance company’s premium income will be subject to New York corporate franchise tax. This result arguably violates the NRRA, and could generate significant litigation.

**As illustrated in this letter, the Captive Combination Provision raises several serious constitutional, federal preemption and tax policy concerns. The Captive Combination Provision reflects unsound tax and public policy and may cause significant unintended consequences.**

We strongly oppose this provision, and ask that you support its elimination from the budget bill. Therefore, we respectfully request that you accept the amended language proffered by the Senate in its one-house budget proposal concerning the taxation of captive insurance companies.

Very truly yours,



**Dennis P. Harwick**  
**PRESIDENT**

Cc: NYS Assembly Speaker Sheldon Silver  
NYS Senate Majority Coalition Leader Dean Skelos  
NYS Senate Majority Coalition Leader Jeff Klein  
CICA Board of Directors  
Captive Association Leadership Council

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