

Proposed Legislation Targets Related-Party Reinsurance Taxation

BY DAN CRISP

Related-party reinsurance transactions can provide certain tax advantages to offshore-based insurers and their U.S. affiliates. When U.S. risks are transferred to the offshore entity, the U.S. affiliate can generally deduct the premiums ceded from its federal income tax, and the offshore entity pays no U.S. tax on the ceded premiums. Additionally, if the offshore entity is headquartered in a low-tax or no-tax country, the entity could pay little or no tax on the investment income from the ceded premiums. U.S.-based insurers have argued that these tax laws place them at a competitive disadvantage.



Off-shore insurers might not be as tantalizing

On September 18, 2008, Richard Neal (D-MA), Chairman of the Subcommittee on Select Revenue Measures, introduced H.R. 6969. This legislation would amend the U.S. Tax Code to disallow deduction by a company subject to Section 831 of the Code of a certain excess amount of affiliated, non-taxed reinsurance premiums. Based upon

aggregate data from company annual statements, the excess amount would be determined by line of business by reference to an industry average of premiums ceded to unrelated parties. H.R. 6969 was referred to the House Committee on Ways and Means.

On December 10, 2008, the Senate Finance Committee staff released a discussion draft of a bill that is nearly identical to the legislation introduced by Neal. The staff invited public comments until February 28, 2009, on issues such as the possible effect on insurance pricing and capacity, existing treaties and sovereignty rights, and the impact on the

reinsurance market. A European insurance association has responded that such legislation would increase the price of insurance, violate double taxation treaties, and reduce reinsurance capacity. Neal plans to reintroduce this bill in the current session of Congress.

McCarran-Ferguson Does Not "Reverse Pre-empt" International Treaties

BY ROLLIE GOSS



In *Safety National Casualty Corp. v. Certain Underwriters at Lloyd's*, Lloyd's demanded arbitration to settle a dispute under a reinsurance contract, basing its demand on the Convention on the Recognition and Enforcement of Foreign Arbitral Awards. The district court denied a motion to compel arbitration, holding that under the McCarran-Ferguson Act, a Louisiana statute that prohibited arbitration agreements in insurance contracts reverse-preempted the Convention.

The Convention requires that courts of signatory states "shall, at the request of one of the parties, refer the parties to arbitration" McCarran-Ferguson mandates that "No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance" The U.S. Fifth Circuit Court of Appeals in *Safety National* addressed whether the Convention or its enabling legislation was an "Act of Congress" within the meaning of McCarran-Ferguson.

The Fifth Circuit held that treaties are not "Acts of Congress" within the meaning of McCarran-Ferguson, and hence are not reverse-preempted when they conflict with state laws. The court relied upon: (1) an analysis of the language of McCarran-Ferguson; (2) the absence of any indication that Congress, in enacting McCarran-Ferguson, intended to impair the executive power to negotiate treaties; and (3) that treaties are "something more than an act of Congress" due to their being negotiated by the Executive Branch and ratified by the Senate. The court rejected the contention that the Convention was an Act of Congress given that it was not self-executing and required an Act of Congress for its implementation, because that "does not answer the question of what Congress intended when it used the terms '[n]o Act of Congress' and 'such Act' in 1945 or why Congress would have addressed only treaties that required implementation by Congress."