Insurance and Tax Reform

Bruce Ferguson
Senior Vice President, State Relations

May 10, 2018
NCSL Executive Committee Task Force on Insurance
Life insurers are a major source of bond financing for U.S. businesses, holding more than 22% of all U.S. corporate bonds.

90 MILLION
American families rely on life insurers’ products for financial and retirement security.*

More than 16% of Americans’ long-term savings is in permanent life insurance and retirement annuities.

Life insurers have invested $6.4 TRILLION in the U.S. economy.

The life insurance industry generates approximately 2.6 MILLION jobs in the U.S.

Life insurers pay out $1.7 BILLION to families and businesses every day.

Life insurers manage 18% of all defined contribution plan assets and 14% of all IRA assets.
Timeline

▪ Legislation introduced November 2 and signed by President Trump December 22
▪ Passed on a party-line vote by Congressional Republicans through budget reconciliation
▪ Most significant tax legislation enacted since 1986
Key Tax Reform Changes

- Permanently reduces corporate rate from 35% to 21%
- Repeals Corporate Alternative Minimum Tax (AMT)
- Paid for changes through base broadening and $1.5 trillion deficit spending
  - Life insurers subjected to industry-specific revenue raisers & corporate base broadeners
Implications for Life Insurers

- Life insurers will benefit from reduction from 35% to 21%
- However, life insurer-specific revenue raisers & corporate base broadeners offset a significant part of the benefit
  - Industry specific provisions are estimated by JCT to raise approximately $23 billion over 10 years from life insurers
Deduction for Life Insurance Reserves

- Modifies formulaic tax rules for the deduction of life insurance reserves
- Tax rules will more closely track developments with state regulatory reserves like PBR
  - New law defines “tax reserve method” (the basis for a life company’s tax reserve deduction) as the method prescribed by the NAIC
Life Insurance Company Proration

▪ Under prior law, life insurers not allowed full tax benefits available to other corporations regarding tax-exempt interest & dividends received deduction (DRD)

▪ Under new law, proration provision intended to cost the industry additional future federal tax revenue

▪ Law simplifies complex rules for determining an insurer’s DRD & tax exempt interest
Deferred Acquisition Cost (DAC) Tax

- Changes DAC tax capitalization period from 10 to 15 years
- Increases DAC tax capitalization rate, effectively deferring a greater amount of policy acquisition expenses for:
  - Annuity contracts
  - Group life insurance contracts
  - All other specified contracts
Other Notable Changes to Insurer Taxation

- Creates new accounting method rules for changes in reserve basis
- Repeals prior law operation loss deductions for carry backs and carry forwards
- Subjects life insurers to net operating loss (NOL) rules applicable to other corporations
  - Indefinite carry forwards for life companies but limited to 80% of taxable income
Product Taxation & Regulatory Capital

- Tax reform does not directly change taxation of life insurance products
- Estate, individual income, and corporate tax rates could affect market for products
- Changes to life company taxation will hurt risk-based capital (RBC) ratios and may impact the price and/or availability of certain products
State Tax Considerations

- States generally tax insurers on their gross premiums
- Other financial institutions are taxed on corporate net income
- 2014 EY study measured relative state tax burden:
  - 22.1% income tax rate equivalent for insurers
  - 6.5% income tax rate for other corporations
Questions?