March 4, 2009

Via E-Mail

The Honorable Max Baucus
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Senate Finance Committee
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The Honorable Charles Grassley
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Senate Finance Committee
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RE: Comments Draft Senate Anti-Competitive Proposal Regarding Reinsurance Taxation

Dear Chairman Baucus and Senator Grassley:

We are writing on behalf of the *Coalition for Competitive Insurance Rates* to express our concern about draft legislation distributed by the Finance Committee Staff as a discussion draft for comments due by February 28[1]. The draft is substantially the same as HR 6969, introduced last year by Rep. Richard Neal. This legislation is being advocated by a small group of very large US insurers which intend to create a US market advantage for themselves with the enactment of this legislation. We oppose enactment of this proposal.

Background: The Proposal is Bad for Consumers

This legislation would disallow a deduction for certain reinsurance premiums paid by a U.S. insurer to an international affiliate. In effect, this is a proposal designed to be punitive to international insurers by imposing additional taxes on their US operations. This legislation essentially imposes an isolationist tariff on international insurers conducting business in the US. Moreover, this punitive tax regime on international insurers forecloses their use of a business model that will continue to be widely used by US insurers.

Reinsurance is an important tool used by businesses and insurers to control and finance risk. The U.S. requires a large amount of reinsurance capacity, a substantial part of which is supplied by non-U.S. reinsurance companies. Thus, any effort to increase the

[1] Senate Finance Committee Staff Discussion Draft of proposal to modify tax treatment of insurance companies that deduct premiums in excess of the industry average

taxes on international carriers will be counterproductive because it will result in increased costs for US consumers. Furthermore, the increase in taxes could drive out competition which would pressure rates upward. A robust insurance market open to as many competitors as possible is essential to consumers, and particularly understood by those 1) in hurricane exposed states where there has been a crisis of insurance availability and affordability; and 2) buyers of certain classes of commercial insurance that in the past have suffered from contractions in availability of coverage.

The Proposal is Anti-Competitive

The facts do not support the suggestion that international insurance companies have an advantage in raising capital and therefore can outbid U.S. firms in acquisitions, with the potential for the United States to lose its entire property and casualty industry. By all measures (comparative profitability, stock price, and return on equity) the domestic insurance industry is thriving and suggestions of its imminent demise due to competition from foreign insurers are exaggerated and unfounded.

In the September 26, 2007, written statement to the Senate Finance Committee, the advocates for change in the tax treatment for international insurers made it clear that this is all about competition. The statement says: "Historically, offshore reinsurers served a narrow market in the United States, offering primarily catastrophe and high excess reinsurance protection. Today, however, offshore companies have expanded beyond those areas into nearly all lines of the direct insurers…." What those advocates are concerned about is *increased competition*, what they fail to recognize is that this *increased competition is good for consumers*.

The Proposal Raises Serious Issues Under Longstanding U.S. Tax Policy

Not only is their proposal bad for consumers but it also violates long-standing U.S. tax policy that calls for the application of the arms-length standard for related party, cross border dealings. In the insurance business related party transactions are well documented; they are subject to approvals by state insurance regulators and abundant comparative market information is available to use to enforce transfer pricing rules. The proposal being suggested contradicts decades of U.S. tax and trade policy, may be inconsistent with existing U.S. tax treaty obligations and will likely spur retaliatory actions by other countries. Ultimately, the proposal damages relationships with important U.S. trading partners.

Congress Should Look to Make the U.S. System More Competitive, Not Punitive to Some Competitors

Rather than looking to punitive taxes on affiliated reinsurance transactions, Congress should be seeking to make the U.S. system more competitive to attract companies to form and grow in the United States. This is exactly what the United Kingdom, Japan and other European countries are considering so that they remain competitive in the global financial services sector. Europe is also acting to update insurance regulation and make it more uniform, something sorely needed in the United States. Penalizing the efficient economic allocation of capital by internationally diversified companies is not in the best interest of the U.S. economy and will lead to decreased capacity and upward pressure on rates.

Current Economic Conditions

The property and casualty insurance industry has been largely insulated from the 2008 capital markets crisis. Ironically the impact of this legislation may well be to create a capital markets crisis for insurance where none exists today. Reinsurance functions as capital and the impact of this legislation is likely to create a capital shortfall! Moreover, Hurricane Ike reminds all of us that the United States is dependent on the international reinsurance market to pay for U.S. hurricane and earthquake catastrophes. More than 85% of the reinsurance claims of the Texas Windstorm Insurance Association will be paid by reinsurers ultimately controlled by international companies. Hurricane Ike (on an inflation adjusted basis) is now expected to be the third most expensive hurricane in U.S. history. Just as they did following the terrorism attacks of 9/11 and Hurricane Katrina, international reinsurers will pay a very large share of those losses.

We urge you to be skeptical of legislation that is supported by self-interested U.S. insurance companies that offers additional revenue that in the end will be inevitably paid for by U.S. consumers and policyholders. Twice before, U.S. policyholder groups have urged opposition to such proposals because of their effect on the availability and affordability of insurance. We say it again now – these proposals are isolationist measures aimed at benefiting some competitors in the market at the expense of others. Ultimately U.S. consumers will suffer if this proposal is approved.

Sincerely,

Coalition for Competitive Insurance Rates

Florida Consumer Action Network (FCAN)
Consumer Federation of the Southeast
Risk and Insurance Management Society (RIMS)
Organization for International Investment (OFII)
Competitive Enterprise Institute (CEI)
Americans for Tax Reform
Dublin (Ireland) Insurance Markets Association (DIMA)
National Risk Retention Association (NRRA)
Captive Insurance Council of the District of Columbia
Captive Insurance Companies Association (CICA)
American Risk Retention Association
Association of Bermuda Insurers and Reinsurers (ABIR)
Vermont Captive Insurance Association
Fireman’s Fund Insurance Company
Munich Reinsurance America
XL America
Arch Capital Group, Limited

Note: Other insurance groups refer you to their individual comment letters

Attachments: Graphs Illustrating the Role of International Reinsurance in the US cc:

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