The Honorable Kevin Brady
Chairman, House Committee on Ways and Means
1102 Longworth House Office Building
Washington, DC 20515

The Honorable Orrin Hatch
Means Chairman, Senate Committee on Finance
219 Dirksen Senate Office Building
Washington, DC 20510

Dear Chairmen Brady and Hatch,

It has been more than 30 years since tax reform was on the national agenda, so the opportunity for fundamental reform presented during this congress is vital to the future direction of the U.S. economy. Encouragingly, both the House and the Senate have proposed visions for reform that move the nation toward a growth footing. Yet certain specifics of the proposals require further refinement, as both bills include provisions that may inadvertently undermine growth by choking off the supply of internationally sourced risk-transfer capital.

While neither bill specifically mentions reinsurance, both bills, if passed in their current forms, stand to offset many of the salutary impacts of reform. For its part, the House version would levy a 20 percent excise tax on foreign affiliate reinsurance in a manner that, in practice, would operate as a profits tax. Meanwhile, a Senate description of the bill suggests it will include a levy of a 10 percent on affiliate transactions while also potentially including double taxation. If enacted as proposed, each bill would effectively shrink by one eighth the amount of reinsurance capital available to the United States.[1]

Insurance consumers—particularly those in disaster-prone states like those currently recovering from this year's hurricanes—could expect to see their property insurance premiums increase if

[1] Michael Cragg, Jehan de Fonseka, Lawrence Powell, Bi Zhou, "The Impact of Offshore Affiliate Reinsurance Tax Proposals on the U.S. Insurance Market: An Updated Economic Analysis," The Brattle Group, Jan. 23, 2017.
http://www.brattle.com/system/news/pdfs/000/001/172/original/Brattle_Impact_Study_2017.pdf?1485188542

either of these bills become law. That is because such taxes, akin to a tariff, would reduce the supply of internationally sourced reinsurance just as demand for it is increasing.

Specifically, according to studies that we at the R Street Institute completed earlier this year, Louisiana consumers could expect to pay $62 million more each year in property insurance premiums, while Texans and New Yorkers would face $271 million more and $335 million more, respectively.[2] A separate study by Florida TaxWatch showed that Florida consumers would face $259 million in annual increases.[3]

While the consumer-level impact of international risk transfer is significant, it is important to not overlook the systemic benefits the capital provides. Particularly over the last year, the need for international risk-transfer capital has been highlighted by the load international reinsurers have borne in the recovery from Hurricanes Harvey, Irma, Maria and Nate, as well as the record-setting California wildfires. More than half of all insured losses caused this year's storms, which now total more than $100 billion, will be paid by international entities. The proposed excise tax would hamper the ability of regions to recover in the wake of disaster. Public policymakers should be concerned about provisions that would serve to concentrate even more natural disaster risk on American shores, rather than spreading it efficiently and effectively around the globe.

Tax base erosion is, sensibly, a central concern of proposals for reform. However, targeting international risk-transfer mechanisms is, in addition to being harmful to U.S. insurance consumers, unnecessary as a matter of base preservation. International reinsurers already pay substantial U.S. tax. Consider that U.S. subsidiaries pay state gross premium taxes, that international entities pay taxes on each cross-border transaction, in addition to a gross receipts tax, and that they do all of this in addition to taxes paid on their profits in the jurisdiction in which they are earned. In addition, the current tax code mandates an excise tax on premiums paid for foreign reinsurance, including purchases from affiliates. Further tilting the tax code toward the purchase of domestic reinsurance violates a central tenet of sound tax policy – neutral treatment.

In fact, according to the Treasury Department, a tax on affiliate reinsurance transactions would actually be a net base-erosion measure insofar as it harms the ability of risk to be spread around the globe.

The R Street Institute applauds both the House Ways and Means Committee and the Senate Finance Committee for their hard work to make fundamental tax reform more likely today than at

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[2] Lars Powell, Ian Adams, R.J. Lehmann, “Impact of a border-adjustment tax on the Louisiana insurance market,” R Street Institute, May 2017. http://www.rstreet.org/wp-content/uploads/2017/05/94.pdf; Powell, Adams, Lehmann, “Impact of a border-adjustment tax on the Texas insurance market,” R Street Institute, April 2017. http://www.rstreet.org/wp-content/uploads/2017/04/93.pdf; Powell, Adams, Lehmann, “Impact on New York State of taxing reinsurance transactions,” R Street Institute, September 2017. http://www.rstreet.org/wp-content/uploads/2017/09/110.pdf

[3] Florida TaxWatch, “The Effects of a Border-Adjusted Tax on Florida’s Property Insurance Market,” March 2017. http://www.floridataxwatch.org/resources/pdf/BAT-Analysis-FINAL.pdf

any time in the last 31 years. We caution, however, that implementing a significant excise tax on foreign reinsurance affiliates could hamper growth and make recovery from catastrophic events more expensive for Americans.

Sincerely,

R Street Institute