



COMMONWEALTH OF KENTUCKY
DEPARTMENT OF INSURANCE
Frankfort, Kentucky

**ADVISORY OPINION
2011-03**

The following Advisory Opinion is to advise the reader of the current position of the Kentucky Department of Insurance (the “Department”) on the specified issue. The Advisory Opinion is not legally binding on either the Department or the reader.

TO: ALL RISK RETENTION GROUPS, CAPTIVE INSURERS, AND REINSURANCE COMPANIES

FROM: SHARON P. CLARK, COMMISSIONER
KENTUCKY DEPARTMENT OF INSURANCE

DATE: MAY 25, 2011

RE: LOCAL GOVERNMENT PREMIUM TAX COMPLIANCE RELATED TO RISK RETENTION GROUPS, CAPTIVE INSURERS, AND REINSURANCE COMPANIES

Kentucky Revised Statutes 91A.080 through 91A.0812 govern the taxation by local governments on insurance premiums. The Department has received inquiries from representatives of risk retention groups (RRGs), captive insurers, and reinsurance companies seeking clarification regarding the obligations of these entities to comply with the provisions of KRS 91A. The Department also recognizes that, as Department personnel and the provisions of KRS 91A have evolved, these entities may not all be operating in a uniform manner or in accordance with applicable law. This Advisory Opinion is being issued to clarify the obligations of RRGs, captive insurers, and

reinsurance companies regarding compliance with KRS Chapter 91A, the laws governing local government premium taxes.

Risk Retention Groups

A “Risk Retention Group” is defined by KRS 304.45-020(11), in part, as any corporation or other limited liability association whose primary activity consists of assuming and spreading all, or any portion, of the liability exposure of its group members. For the complete definition of a risk retention group please refer to KRS 304.45-020(11).

KRS 304.45-080 provides that all RRGs are subject to taxation and shall be deemed to be insurers for the purpose of assessing and collecting taxes on premiums. The statute further provides that all RRGs shall be subject to the taxes set forth in KRS 91A.080. In accordance with KRS 304.45-080(2), all persons involved in the solicitation, negotiation, or procurement of liability insurance from RRGs are required to cooperate in the reporting and payment of taxes on premiums for risks located in the State of Kentucky. Further, KRS 304.45-080(3) provides that the failure of RRGs to pay taxes or cooperate in accordance with the provisions of KRS 304.45-080 is a ground for suspension or revocation of certificates of authority, licenses, or permission to do business in the State of Kentucky. Lastly, the statute authorizes the Commissioner to take any action necessary to assure that applicable premium taxes are paid to the appropriate taxing authority.

In the past, there has been confusion over whether the federal law, the Product Liability Risk Retention Act and the Liability Risk Retention Act authorized states to impose taxes upon RRGs. 15 U.S.C. Section 3902 exempts certain state laws, rules, regulations, or orders as they may pertain to RRGs but retains the state’s ability to require an RRG to pay, on a nondiscriminatory basis, applicable premium and other taxes which are levied on admitted insurers and surplus lines insurers, brokers, or policyholders under the laws of the state. Based on the language of 15 U.S.C. Section 3902, the Department retains the authority to require compliance by RRGs with the taxation provisions of KRS 91A in accordance with KRS 304.45-080.

Captive Insurers

KRS 304.49-010(3) defines “Captive Insurer” as any pure captive insurer, consortium captive insurer, sponsored captive insurer, special purpose captive insurer formed or issued a certificate of authority under the provisions of KRS 304.49-010 to 304.49-230. For definitions of “pure captive insurer,” “consortium captive insurer,” “sponsored captive insurer,” and “special purpose captive insurer,” please refer to KRS 304.49-010.

KRS 304.49-220 specifies the taxes payable by a captive insurer holding a certificate of authority under KRS 304.49-010 to 304.49-230. The statute establishes taxes on captive insurer premium payable to the Department of Revenue. Further, KRS

304.49-220(7) provides that the tax provided for in KRS 304.49-220 shall constitute all taxes collectible under the laws of Kentucky from any captive insurer, and the taxes imposed under the statute are in lieu of all excise, license, occupational, or other taxes imposed by the state, county, city, or other taxing district. As a result of this statutory language, captive insurers are not subject to the taxes imposed by local governments on premiums pursuant to KRS 91A.

Reinsurance Companies

“Reinsurance” is defined by KRS 304.5-130 as a contract under which an originating insurer (called the “ceding” insurer) procures insurance for itself in another insurer (called the “assuming” insurer or the “reinsurer”) with respect to part or all of an insurance risk of the originating insurer.

It has long been the opinion of the Department that reinsurance contracts are not subject to KRS 91A as this would amount to a double taxation on the underlying risk that is the subject of the reinsurance contract. However, besides the authority to enter into reinsurance contracts, many reinsurance companies are authorized to transact other lines of insurance as well. For instance, a reinsurance company may hold a certificate of authority to transact health, property, surety, casualty, marine and transportation, or other lines of insurance business.

A reinsurance company is not exempt from paying local government premium taxes (KRS 91A) simply because the company engages in reinsuring certain business. If the reinsurance company directly underwrites and insures risks in the State of Kentucky, premiums collected on those risks are subject to local government premium taxes. As an example, a company that primarily engages in reinsurance but is authorized to write malpractice insurance may, under its certificate of authority, directly issue a policy covering physician malpractice. The premiums collected by the reinsurance company on the malpractice policy would be subject to local government premium tax as the policy is not a reinsurance contract.

Lastly, it should be noted that all reinsurance companies holding a certificate of authority with any line of authority are responsible for filing applicable local government premium tax reports. This is true even in the event that the reinsurance company did not directly underwrite any business under the company’s lines of authority. In this case, the reinsurance must file a zero business report to avoid administrative action against non-filers.

Questions regarding this Advisory Opinion may be directed to the Brenda Smith, Local Government Premium Tax, Kentucky Department of Insurance at (502) 564-1649.

/s/ Sharon P. Clark
Sharon P. Clark, Commissioner
Kentucky Department of Insurance
On this 25th day of May, 2011