REPORT OF THE
SENATE STUDY COMMITTEE ON
INSURANCE ECONOMIC DEVELOPMENT

MEMBERS

Senator Eddie Madden
District 47
Chairman

Senator Paul C. Broun
District 46

Senator Robert Brown
District 26

Senator Tim Golden
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1999
THE SENATE STUDY COMMITTEE ON
INSURANCE ECONOMIC DEVELOPMENT

CREATION AND DUTIES

The Senate Study Committee on Insurance Economic Development was created by Lieutenant Governor Mark Taylor pursuant to his authority under Senate Resolution 3. The Study Committee was charged with reviewing ways to reduce the insurance premium tax, encourage insurance companies headquartered in Georgia to remain in the state, and to seek ways to attract the relocation of insurance companies to Georgia.

Senator Eddie Madden was appointed as the Committee's Chairman. The other members appointed to the Committee were: Senator Paul C. Broun, Senator Robert Brown, Senator Tim Golden, Senator Ed Harbison, Senator Rick Price, and Senator Sam C. Roberts. The Study Committee met on September 29, 1999 and October 26, 1999.

The Study Committee heard testimony from the following individuals: Dr. Martin F. Grace of Georgia State University's Fiscal Policy Research Program; Mr. Scott Thompson of American Southern Insurance Company; Mr. Doyle Kelly of CNL/Insurance America, Inc.; Mr. Allen R. Green of Southern Mutual Insurance Company; Mr. Brad Kolter of Cotton States Mutual Insurance Company; Mr. Larry Hilsmier of MAG Mutual Insurance Company; Mr. Jim Grubiak of The Association County Commissioners of Georgia (ACCG); Mr. W. Mark Knowles of The Georgia Municipal Association (GMA); and Mr. Jeffery Skelton of the Insurance Commissioner's Office.

COMMITTEE'S FOCUS

Traditionally, insurance companies are taxed on the premiums they write. Georgia's insurance premium tax rate is currently one of the highest in the nation and over twice the national average. The revenue from the premium tax has proven to be a great windfall for the state and local governments in Georgia. In 1998 alone, the premium tax generated over $211 million for the state and over $232 million for local governments. Critics argue, however, that the tax discourages the development of a strong insurance industry in Georgia. Moreover, because Georgia taxes insurers more than twice the national average, other states penalize Georgia-based insurers by imposing a retaliatory tax on them. Evidence shows that the retaliatory tax has directly forced several Georgia-based insurers to move their headquarters out of Georgia and has discouraged other companies from relocating their corporate headquarters to our state.

INSURANCE PREMIUM TAXATION IN GEORGIA: AN OVERVIEW

The structure of the insurance premium tax in Georgia is quite simple, which is the primary reason why states choose to tax premiums over other taxation methods. Since 1955, there has been no change to the premium tax rate or to the tax base in Georgia. The tax base is simply the gross direct premiums received on policies issued in Georgia. Georgia's tax rate is 2.25 percent. The state also collects an additional tax on premiums and disburses it to the local governments. These local taxes are an additional 1.0 percent of the life premiums, (which are allowed as a deduction against the premium tax) and 2.5 percent of property and casualty (P&C) premiums. Therefore, the true tax rate on P&C premiums is 4.75 percent while Life and Accident and Sickness (A&S) premiums are taxed at 3.25 percent.

The tax due the state of Georgia is simply the tax rate times the tax base, minus any abatements. From premiums received, the taxpayer is allowed to deduct premiums returned to the policyholder and any dividends paid to the policyholder. The resulting taxable premiums are taxed at a rate of 2.25 percent plus the local tax rate.

A number of abatements or deductions exist that affect the taxes due. The first is the investment abatement. If an insurer invests a quarter of its assets in certain qualified Georgia assets, then the State premium tax obligation is reduced from 2.25 percent to 1.25 percent. If the amount of investment by a company equals 75 percent or more of its total assets, then the premium tax is abated one half of one percent.

A second abatement allows for certain Georgia-domiciled insurance companies writing coverage on fire, windstorm, extended coverage, and lightning damage in Georgia to deduct any retaliatory tax paid to another state.

A third abatement allows deductions for license fees paid to local governments by life insurance companies, A&S companies, and Health Maintenance Organizations (HMOs). These license fees vary from municipality to municipality and range from $15 to $150.

The fourth deduction allows HMOs, Life, and A&S companies to deduct payments made to the Georgia Life, Accident and Sickness Guarantee Fund.

A final abatement allows Life, A&S, and HMO companies to deduct the one percent county and municipal taxes. This abatement is not available to the property-liability industry.

For insurance companies domiciled in Georgia, the sum of the abatements is deducted from the total domestic premium tax due to the State of Georgia and its counties and municipalities. Foreign companies (those not domiciled in Georgia) may have a further retaliatory tax imposed depending on the tax policy of their home state. Authorized under O.C.G.A. §33-3-26, the retaliatory tax essentially penalizes a company domiciled in a state with a premium tax rate that is higher than that of Georgia. Likewise, a Georgia company writing in a state with a premium tax rate lower than Georgia's will have to pay the computed difference to that particular state. For example, if a Tennessee property and casualty company writes a policy in Georgia, it pays Georgia's 4.75 percent tax. If a Georgia company sells a policy in Tennessee, which has 2.50 percent rate, Tennessee collects its 2.50 percent plus the 2.25 percent difference from the Georgia-based company. In the simplest of terms, a Georgia-based insurer writing policies in any state with a lower insurance premium tax than Georgia's, will always have to pay Georgia's 4.75 percent rate.

COMMITTEE FINDINGS

On September 29, 1999 and on October 26, 1999, the Committee heard testimony from a broad range of individuals. The insurance industry, Georgia's cities and counties, the Office of the Insurance Commissioner, and academia, all testified before the Committee.

The Committee discovered from Dr. Martin F. Grace of Georgia State University's Fiscal Policy Research Program that the premium tax is a relatively simple tax. In general, a company merely adds up its gross written premiums and applies a tax rate to determine the tax bill. This is a simple process for the company, and a simple tax for the state to administer and audit. However, Dr. Grace clearly illustrated that Georgia's combined state and local premium tax of 4.75 percent is the third highest in the nation. Moreover, the retaliatory tax other states impose against Georgia-based companies is harming Georgia's domestic insurance companies' ability to compete in other states. The majority of states, including Georgia, impose a retaliatory tax on premiums written by non-domestic companies in that state. Although other states' insurers pay the same premium tax that a domesticated company pays when selling policies in Georgia, Georgia's domestic insurers are subject to those states' retaliatory taxes because of this state's excessive premium tax. The method of imposing the retaliatory tax by other states on Georgia's domestic companies requires Georgia companies to pay the Georgia rate of 4.75 percent on premiums written in the foreign state even though the other state has a lower premium tax rate. The result is that foreign insurance companies are discouraged from domesticating in the state of Georgia and existing companies are encouraged to relocate to foreign states.

Witnesses representing several domestic and foreign insurance companies echoed the same concerns. The Committee was informed that the premium tax, in combination with foreign retaliatory taxes, is causing several problems for the insurance industry: foreign insurers are choosing not to locate their corporate headquarters to Georgia; domestic Georgia insurers who have not already relocated to other states, are considering moving their headquarters from

Georgia; and Georgia domestic insurers are forced to operate at a competitive disadvantage in other states. From 1993 through September 1997, eight insurers have relocated their headquarters out of Georgia due primarily to the state's high premium tax.

In 1997, American Southern Insurance Company relocated from Georgia to Kansas. The company cited "the adverse impact from the retaliatory taxes" levied against them as the sole reason for relocating. The company testified that the deciding factor was a dispute over the retaliatory tax with Florida. After rewriting its tax code, Florida disputed American Southern's calculation of its retaliatory tax due to the state. The parties went to trial and American Southern lost. Ultimately, the insurer was forced to pay $1,000,000 in taxes to the state of Florida and $100,000 to its attorneys.

The Committee also discovered that CNL/Insurance America, Inc., headquartered in Macon, may be forced to relocate outside of the state in two or three years if the premium tax is not lowered. The insurer indicated that the retaliatory tax burden it faces when writing policies in other states makes them noncompetitive in most markets. In 1997, over 34% of CNL's policies were written in Tennessee. Since Georgia's premium tax is almost twice as high as Tennessee's 2.5%, CNL was forced to pay Tennessee almost $143,000 in retaliatory tax alone.

The Office of the Commissioner of Insurance indicated that the premium tax affects every aspect of Georgia's economy. Consumers are harmed because insurers pass the tax on to them in the form of higher premiums. Economic growth is obstructed because domesticated companies have moved from Georgia and foreign companies are not willing to relocate to this state. Insurance companies that have chosen to remain in Georgia are burdened by the retaliatory tax that they are required to pay when writing policies in other states. Finally, labor and employment are affected when insurance companies choose not to locate in Georgia, or when Georgia-domiciled insurers are forced to relocate to another state.

Clearly, the premium tax adversely affects the insurance industry. Less clear, however, is just how much the premium tax benefits the state and local governments. In 1998, the tax accounted for over $211 million in revenue for the state, and $232 million for counties and municipalities. The Georgia Municipal Association (GMA) and the Association County Commissioners of Georgia (ACCG) both acknowledged that although the premium tax may be harming the insurance industry, local governments depend on the premium tax as a vital and necessary source of local government revenue. Both associations cautioned the Committee that a repeal of the premium tax without a replacement source would jeopardize local government bond ratings and place a hardship on Georgia's counties and municipalities. In an effort to protect municipal revenue, GMA indicated that it will oppose any legislation that would reduce the amount of local portion of the insurance premium tax.

COMMITTEE RECOMMENDATION

The Committee recognizes that the insurance premium tax adversely affects the insurance industry in Georgia in the following ways:

- The combined state and local premium tax of 4.75% is the second-highest in the nation and is passed on to the consumer through higher premiums.
- When writing premiums in other states, Georgia-domiciled insurers are subject to those states' retaliatory taxes because of the excessive premium tax. Thus placing them at a competitive disadvantage with other insurers.
- Between 1993 and 1997, eight insurance companies relocated their headquarters from Georgia primarily due to the premium tax.
- Insurers are unwilling to relocate their corporate headquarters to Georgia because of the premium tax.

The Committee also recognizes that the county and municipal governments rely on the insurance premium tax for a vital source of revenue.

RECOMMENDATION

In light of these findings, it has been determined that the insurance premium tax must be reduced to the national average. The eventual elimination of the state's portion of the premium tax would significantly reduce, if not eliminate, a Georgia-based insurer's burden of paying the retaliatory tax when writing in other states. A reduced tax would also encourage new insurers to move to Georgia while preventing Georgia-domiciled companies from relocating to other states. Finally, a reduced tax would benefit the consumer by lowering insurance premiums. The Committee therefore recommends that the state's 2.25 percent tax on insurance premiums be phased out permanently over a period of time.

Respectfully Submitted,

THE SENATE STUDY COMMITTEE ON INSURANCE ECONOMIC DEVELOPMENT

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