



Catching Up With U.S. CAPTIVE DOMICILES

By Karrie Hyatt

Three quarters of U.S. states have now enacted captive legislation, but just having legislation on the books is no longer enough to attract new captive business. Captive domiciles have to update their laws regularly to keep on top of industry and market developments and to adjust to developing captive business practices, as well as making the state welcoming to captives.

Since the beginning of 2017, eleven states have updated their captive law, making both minor and major changes to stay competitive captive domicile market. Several more states are in the process of pursuing changes. But why even pursue captives when so many other states already operate as captive domiciles?

As North Carolina can attest to, states that serve as captive domiciles can bring in a significant amount of revenue to the state. North Carolina first passed captive law five years ago and has aggressively been pursuing captive business since then.

At the end of 2017, the state had 248 captive insurers and more than 400 cell and series captives operating in the state. In June, the North Carolina Department of Insurance issued a press release boasting that captives had made a \$30 million fiscal impact on the state during 2017.

According to the statement, “The impact was generated by premium taxes paid to the state by licensed captive insurers as well as service provider and hospitality revenues generated by North Carolina businesses for services they provide to the captive insurance industry.” The department estimates that in the four years between 2013, when the state became a captive domicile, and 2017, that captives made a \$71 million positive fiscal impact on the state.

While North Carolina is an outlier in how quickly and successfully a captive domicile can be established, other newer domiciles are growing at a reasonable and steady rate, reaping the benefits that captive business can bring to a state.

Tightening Up Regulation

In the last two years, the majority of legislative changes in captive law either clarify the existing law, tweak the law to make the it more appealing, or change the financial requirements, fees, or taxes.

A good example is South Carolina, their 2018 update was meant to “clean up” their existing law and one of the modifications made was to redefine a captive’s principal place of business, as well as modifying capital and surplus requirements. Another example is Georgia which removed the stipulation that required captives to use the terminology “captive insurance company” in their name. Texas’s update cleared the way for captives to reinsure with nonadmitted reinsurers.

When it comes the financial side of new captive laws, the changes range from capital requirements to penalties for late premium taxes. The updated law in Connecticut will allow the state insurance commissioner to waive capital and surplus requirements for selected captives and lowers the minimum surplus requirement for sponsored captives.

Kansas, on the other hand, has raised the minimum requirements for capital and surplus that a pure captive must have—from \$100,00 to \$250,000. Kansas has also implemented a fee of \$10,000 for any examinations, investigations, and applications processing conducted by the state.

South Carolina has also made changes regarding examinations for captives. Captives in that domicile must have an examination three years following its start of business, but after that any further examinations will be at the discretion of the regulator.



This year, North Carolina is in the process of trying to pass legislation that will exempt foreign captives doing business in the state from all state taxes. The law was included in a general budget bill this past spring which was vetoed by Governor Roy Cooper for reasons not relating to captives.

Vermont's law made a clarification regarding reinsurance premium tax on loss portfolio transfers. Tennessee's 2017 legislation implemented new penalties for captives that fail to pay their premium taxes on time. The fees consist of \$500 for each month it's late with an interest rate of 10% on the unpaid tax.

New Trends In Captive Law

One of the most common changes that states are making to their captive law these days is to allow captives to go dormant. When a captive decides to cease business and become inactive, under unamended captive law, the captive would have to maintain the capital and surplus requirements that active captives are subject to. States that legislate for dormant captives typically reduce the minimum amount of capital and surplus required and reduce annual fees. Capital and surplus, in most cases, is reduced to \$25,000.

Allowing captives to become inactive, makes it easier for captive owners to react to market changes as needed. Establishing a captive can be a time consuming and onerous undertaking. If a captive is not the best mechanism for insuring risk at the time, a company may choose to put theirs on hold without tying up capital that could be better used elsewhere. Then when the time is right for reactivating their captive, they are a few steps ahead in getting the captive running. The dormancy amendments that states are enacting allow more flexibility for captive owners to make best choices for their risk mitigation.

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In 2017 and 2018, five states updated their captive law to allow for captives to become dormant—Arkansas, Connecticut, Delaware, Montana, and Tennessee. South Carolina and Vermont, both with dormancy legislation on their books, also revised their dormant captive provisions.

Another recent change that domiciles are making is to extend the due dates for premium taxes and/or annual statements. In this year's update to their captive law, Vermont has extended the annual report due date to March 15th for pure, association, sponsored, and industrial insured captives whose fiscal year responds with the calendar year. Other types of captives' annual reports are still due March 1st, unless their fiscal year doesn't correspond to the calendar year. The domicile has also set a hard deadline of March 15th for premium taxes.

In 2018, Both Delaware and South Carolina have also lengthened their due dates. Delaware now gives captives until April 15th to file both their premium taxes and their annual statements. South Carolina will now allow captives (except for risk retention groups) to file their annual reports by July 1—a four month extension from the previous due date of March 1.

Other Ways Domiciles Are Easing the Way for Captives

There is a large variation in the different angles that captive domiciles are taking to make their state more welcoming to captives. Tennessee's latest changes to its law, in 2017, streamlined the process that will allow for a protected cell to become a standalone captive. Arkansas now allows for captives to more easily be merged into another captive.

In 2017, legislation passed in Georgia allows captives to be formed as a limited liability company, rather than as a stock company. Arkansas also amended its captive legislation in 2017 to allow captives to organize and operate in any form of business that is legal in the state, with the permission of the state's insurance commissioner.



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Kansas recently updated its captive law to allow pure captives to insure controlled unaffiliated businesses for up to 5% of the captive's total written premium with approval from the insurance commissioner. While South Carolina has changed its legislation to allow pure captives, special purpose captives, and sponsored captives to make loans to their parent companies or affiliates, with prior approval from the regulator.

Connecticut and Vermont both allow for the formation of agency captives. Agency captives are formed and controlled by licensed insurance agents or brokers. In Kansas's 2018 overhaul of their captive law, they made room for both branch captives and special purpose financial captives. A branch captive is the U.S.-based arm of an offshore domiciled captive and is usually treated as a standalone captive and taxed accordingly. ■

Karrie Hyatt is a freelance writer who has been involved in the captive industry for more than ten years. More information about her work can be found at: www.karriehyatt.com.

In 2017 and 2018, four domiciles updated their law to allow new types of captives to be formed. Arkansas now allows for the formation of incorporated protected cells—cell captives that are established as a legal separate entity from its sponsoring captive.



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