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REINSURANCE TAX ISSUES

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o A discussion of current tax issues dealing with reinsurance

MR. STEVEN W. FICKES: Our session is an open format. This panel is going to talk about the various specific tax issues related to certain aspects of reinsurance. Later we'll open for questions or comments that anybody has from the audience on those topics.

Next, let me introduce the panelists because we'll be skipping around from one to the other. The first panelist is Tom Skillman from Lincoln National. Tom has been with Lincoln National for the last year and a half and prior to that he was with American General for seven years. But before American General, he was with Kentucky Central. Our second speaker is Art Bailey who is a lawyer and a partner at Steptoe & Johnson. Prior to joining Steptoe & Johnson, he was Tax Counsel and General Counsel to Phoenix Mutual and before that he was with the Department of Justice. And lastly, we have Tom Kabele who's been with Guardian since 1979 as a Vice President in the reinsurance area. Finally my name is Steven Fickes. This summer I formed a firm with Al Greenberg called amazingly, Greenberg & Fickes, which shows all of you our creativity.

Our first topic is tax issues as it was defined six months ago. It was a nice catchall because we didn't know what was coming up. But since then there has been a lot of talk about ceding commissions and their deductibility. We'll start with that first because it is probably the major issue in reinsurance now.

MR. THOMAS E. SKILLMAN: Essentially, the ceding commission issue is whether you receive an immediate deduction for the initial relief provided or initial ceding commission paid when you enter into a surplus relief or any other financial reinsurance agreement. The answer to how you treat it depends on the agreement for assumption reinsurance which is a sale of block of business as opposed to indemnity reinsurance where you're just indemnifying the writing company. For assumption reinsurance it's fairly clear that you have to amortize the commissions over the expected life of business. I think there's been one case which decided to the contrary but had a pretty unique fact situation.

Most of the recent court cases have focused on existing issues under indemnity reinsurance and up until about a year and a half ago -- about the time I joined Lincoln -- the industry has been winning fairly consistently. Since then, up

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until the middle of August, the industry has consistently lost. The IRS's position for existing business is that you treat it the same as assumption reinsurance. You set up a ceding commission asset, amortize it over a number of years rather than take an immediate deduction. Not so surprisingly the industry is opposed in that we want to take an immediate deduction.

For new issues, even under the indemnity reinsurance agreement, the industry's position and the IRS's position thus far seems to be much the same. The IRS has permitted an immediate deduction of ceding commissions with respect to new issues. Some of the corollary issues to the ceding commission issue are: If you do have to amortize, over what period of time do you use? In determining the amount of ceding commission, do you determine it with respect to tax basis reserves or statutory basis reserves? Also, the definition of new business: If you enter into a reinsurance agreement now covering 1988 issues, is that new business or not? Very clearly, issues after October 24 would be new issues, but what about issues of September or August -- there's a gray area there. As far as a specific case, cases relating to these various things, we'll let Art discuss that.

MR. ARTHUR L. BAILEY: Let me start off by first saying a little bit about the tax theory that goes behind this issue. There is a long standing principle in the tax laws that if you pay amounts to acquire an asset and that asset has a life expectancy that goes beyond the tax year, the general tax rule would require you at a minimum to amortize that expense over the life of the asset that you acquire. In the case of commissions paid by the direct writer, the current law of the 1984 and 1959 Acts has provided an exception to that rule. When you read the legislative history to both the 1984 and 1959 Acts, it is given to life insurance companies as an exception to this general rule that would normally require you to amortize an expense. What has happened in the tax controversy has been that the Service will acknowledge that the tax laws specifically grant you the deduction for the commission when you pay it as a direct writer. The real dispute is over whether that treatment should carry over into the reinsurance setting where the reinsurers are essentially reimbursing the ceding company for that expense which everybody agrees that the ceding company can currently deduct.

The present controversy can be traced back to the mid-1970s to late 1970s when the Service first in several technical advise memoranda gave indication that they intended to pursue this treatment of amortizing ceding commissions. In 1982, the Service published its position in a ruling that was for general purposes having the issue considered by the courts. Generally taxpayers have a choice of courts after they have completed the administrative process of arguing with the Service. You have a choice of going to one of the federal districts where there is at least one in every state, the Claims Court, located in Washington, D.C., or to the Tax Court which again is a specialized court home-based in Washington, D.C. They may have hearings in various places around the country, but they are specialized courts devoted to the consideration of tax cases. Once you have gone through your trial level, appeals are taken from those decisions to the Circuit Court of Appeals. There are 11 or so Circuit Courts scattered around the country. After that there is the court of last resort -- the Supreme Court.

The ceding commission issue that we're talking about was first considered by the tax court in 1982, in a case entitled "Beneficial Life Insurance Company versus the Commissioner." The tax court in that opinion held in favor of the taxpayer thus permitting the current deduction of the ceding commission paid by the reinsurer. With that decision on the books, it was something of a invitation to other taxpayers who had the same issues. If you could go to the tax court and you knew that they were on your side, it was an open invitation. So what we are seeing in the cases is the tax court considering this issue more than once. It considered the question resolved in favor of the taxpayer in Merit Life, in Colonial American Life, and in a third case, Individual Life Assurance Company that took place over a four year period: 1982-1986.

The next phase in the consideration of this issue by the courts occurs when these cases go up to the Circuit Court of Appeals. The government being the loosing party in the cases I've described is the one taking the appeal and we've had the issue now considered by three Circuits in a case called Prairie States. The eighth Circuit Court's decision was in favor of the government. Again in the case called Colonial American Life Insurance Company, the fifth Circuit Court's decision was in favor of the government. So what we had is the tax courts saying they are in favor of the taxpayer and the Circuit Courts ruling in favor of the government. Now, with the issue postured in that way with the Circuit Courts generally coming down in favor of the government, the chances of going up to the Supreme Court are virtually nil. But then we have a third case called Merit Life Insurance, (that's in the seventh Circuit) and there the Circuit Court rejects the Commissioner's position. So we have three Circuits, two in favor of the government, one in favor of the taxpayer. If there's a conflict within the Circuit, it is not unusual for the Supreme Court to grant a petition to have the case heard.

To put this into context, the Supreme Court considers about ten tax cases a year. It takes them reluctantly because it really doesn't like to look at tax cases. It has been 11 years since it last considered a tax case involving the life insurance tax provisions. Many of you will remember back in 1977, the Supreme Court decided the Standard Life & Accident case involving the treatment of deferred uncollected premiums on individual life insurance. This will be the first federal income tax case involving life insurance that the Supreme Court will have heard, (assuming the case is taken to the Supreme Court). What's the status of the possible consideration of this case by the Supreme Court? There's a case pending now in the ninth Circuit involving a company called Oxford Life that's not yet decided, and late last week, the Justice Department filed a motion to basically suspend proceedings in that case. The reason they gave for asking the court not to consider the issue now was the decision that had been made at the higher levels at the Justice Department to acquiesce in the petition for certiorari that had been filed by the taxpayer, the loosing taxpayer, in the Colonial American Life Insurance Company case. When there is a split in the Circuits and when the government acquiesces, meaning it agrees that the case aught to be considered, it's virtually certain it is strong but very, very likely that the court will consider the case to be considered in its next terms.

Assuming the case is heard we can expect a decision on this issue in the next 9 to 15 months. Will that decision resolve all of our questions? You never know until you see how broadly or narrowly the courts decide on how to draft an opinion. The controversies that may arise here are broad, not just what is the right amortization period if they go that route, but should an exception be made for reinsurance which exists on new business where the reinsurer stands in the shoes of the ceding company from day one in the policy. Should that be treated differently than existing business reinsurance? Should they all be treated the same with the current deduction? We're not going to know until we see the opinion and how broad it is. Whether there's more to do in the Courts on this problem or not we'll have to wait and see.

MR. FICKES: Tom Kabele, if you would now discuss any additions you have on the cases or comments on the issues.

MR. THOMAS G. KABELE: First, I'd like to go over a General Counsel memo that was a precursor of the 1982 and 1969 ruling. I think the logic is quite interesting. The number of the memo for those who are interested is 38833. In the memo of the General Counsel they said "ceding commissions assumption on reinsurance and indemnity reinsurance and on direct business are all start-up costs and we should basically defer all of them." That's including direct business -- they want to defer those too. They also said "assumption we have already won because of the regulations we wrote in 1962." However, direct business they conceded had a weakness because of the legislative history with the 1959 Act and the fact that companies had been deducting them for centuries. However, they said indemnity reinsurance wasn't quite the same as direct business because they claimed a reinsurance treaty was more stable than individual policies. That is, individual policies could lapse and you couldn't predict whether you could recover the acquisition costs, but if the same policy was reinsured somehow the business became more stable. I didn't quite follow the convoluted logic but that's their logic. They also said they shouldn't give indemnity reinsurance the same treatment and suggested an amortization.

Furthermore, they suggested an amortization period. That was the date of the early recapture which in the treaty they were looking at was 20 years. Therefore, you want straight amortization over 20 years. When they got to new business, they were more troubled by that and the General Counsel said "new business should be treated like a pass-through." There were specific comments in the 1959 legislative history that this should be the case -- so they granted a pass-through treatment. The General Counsel memo then became revenue ruling 8269 in which the government just regurgitated the same type of arguments. Then they litigated, as mentioned by Art Bailey. The taxpayer won the Beneficial court case, which was a good court case for us because there was 10 or 12 reinsurance agreements under consideration. Since the court didn't have time to get into each individual one or its accounting, it looked like the company was really in the reinsurances business and not just doing things for tax avoidance. Also, Beneficial had an assumption treaty so the court compromised and gave the IRS a victory in the assumption case to go along with earlier victories. Some partial victories had been given assumption cases but they ruled for the taxpayer on all these indemnity treaties. That went along fairly well as Art mentioned until we got to the Modern American case, and there, the government seemed to distinguish coinsurance versus modified coinsurance. It was a rather strange type of ruling; nobody quite understood it. People were thinking of changing their Modco treaties into coinsurance treaties because it seemed better.

However, in the next court case, Prairie States, they just threw it all aside and they lumped coinsurance and modified coinsurance together. That case was quite interesting. Apparently, there's only one treaty involved. The treaty was signed on December 31, of course, and there was one entry that hit the books. Naturally, that was the ceding commission. They didn't bother to reflect offset premium or Modco reserve adjustments -- it just showed the ceding commission. That didn't look too good. Furthermore, it was paired with another strange issue in which the company would issue par policies. They claimed that the dividends on real par policies were not real dividends. It went to the District

Court where they won that case. It then went to Appeals as a strange dividend issue. As such the government won that case and started what appeared to be a string of victories.

The Oxford Life case held in the District Court had lost an earlier assumption case, but they had received favorable dicta on an indemnity case. However, when it returned to the District Court as an indemnity case involving the same company, the court just said "well look I've got Prairie States Colonial American" and xeroxed them off and said "this is my decision." They went down to the fifth Circuit (the fifth Circuit is right below the eighth Circuit -- the eighth Circuit is essentially Arkansas on up to Minnesota and the fifth Circuit is I believe Louisiana and Texas) and they went with the government as well. It then went to the seventh Circuit and surprise, surprise, we were able to win that one. So, now we have a split in the Circuits. The government's arguments are basically the same as they were in the General Counsel memo. They said "assumption is clear we must amortize." They said indemnity and assumption are really the same thing and in both of them what you're really doing is buying cash flow. I myself think that what you're doing is re-buying liabilities, but they're saying no, you're buying an asset and the asset is cash flow. They also said they are similar enough that they should be treated the same way and cited the general tax laws. Art has already mentioned that you must amortize asset purchases.

The Merit case I thought was well cited because the result was good and because they had analyzed the arguments in great detail. They pointed out the code and regulations and even the legislative histories as being fairly clear and in our favor. Some of the other arguments that have been made in some of the more recent briefs are the so called "negative implication arguments." It has been pointed out by some of our lawyers that indemnity reinsurance is pretty common. That is, about 10 to 20% of all businesses is reinsured under indemnity reinsurance and maybe 25% of all new businesses is reinsured under indemnity reinsurance. However, assumption reinsurance is rare and only an occasional block is ceded off. In fact, it's rather hard to find companies who are willing to sell their blocks of business. So the implication is that the regulations say you must amortize assumption reinsurance. It would seem to be reasonable to many of us that we should get an immediate deduction for indemnity then.

MR. FICKES: Does anybody have any comments they'd like to offer or questions for the panel?

FROM THE FLOOR: I have one for each. First for Art. What happens if the Supreme Court denies certiorari. Do we just live with the split decision then?

MR. BAILEY: In the unlikely event that they deny certiorari, you'll have the result that you have different outcomes for taxpayers in different Circuits on essentially the same facts. The answer is you'd have different results for taxpayers similarly situated which is the reason why normally the Supreme Court would try to resolve this conflict. Let me just amplify and say assuming the Supreme Court does take this case it will be one of those industry events. We'll have lawyers who are representing the taxpayers, lawyers representing the government, lawyers representing the ACLI which is already participating in asking the court to take on the case, and lawyers who are representing individual companies who will be seeking to have their views known to the court. The next year we'll probably see a lot of attention spent watching the various strategies taking shape as the industry and individual companies participate in this process. When Standard Life was decided, a very unusual thing happened in that argument. The Amicus, which was the ACLI who wasn't really a party to legation, was given oral argument time.

FROM THE FLOOR: I guess I'm still confused -- it seems to me that in amortizing if you provided $10 million ceding commission, I thought I understood you to say that we're already amortizing that -- and I don't see how.

MR. SKILLMAN: Direct writers amortize. Suppose a direct writer receives $10 million of premiums and sets up for GAAP purposes a net level benefit reserve of $10 million and deferred acquisition costs of $8 million or for statutory purpose he might set up a CRVM reserve for maybe $3 million. Through the reserve mechanism, direct writers are amortizing acquisition costs.

MR. FICKES: My questions for each of the panelists are first, will the industry win at being able to totally deduct ceding commissions especially on new business? Secondly, if we do not win and we have to go to an amortization basis, isn't that going to open up a whole new can of worms? As I see it, we will get into very intellectual arguments with the IRS as to what the proper amortization period should be.

MR. BAILEY: I won't say that you will win but I think you should win this issue. I think you should win more clearly in the case of reinsurance which starts with the issuance of the policy as opposed to reinsurance that kicks in once you have a block of business in force. The reasons you should win this issue first is this treatment. The allowance of the deduction for the ceding commission has been virtually not in dispute for as long as the income tax laws have had a piece of the tax law based on gainful operations. There is a lot of legislative history that distinguishes indemnity reinsurance from assumption reinsurance, stating with respect to indemnity reinsurance that it is in the nature of a contract of insurance between the ceding company and the reinsurer and then going on to say that assumption reinsurance is like buying a block of business. A further reason that weighs heavily in the favor of the industry on this is that if the Commissioner is right, we, in effect, go from a situation where it's undisputed that the direct writer is supposed to get a deduction for the commission to a situation where nobody gets the deduction for the commission -- certainly not a current deduction. If you don't have reinsurance, the direct writer pays and deducts currently the commission expense. If you have reinsurance that takes place, but the ceding company gets reimbursed for the commission expense which nets out zero as far as the ceding company is concerned, then the reinsurer gets nothing better than an amortized deduction. If you consider that 15% of all insurance in force is subject to reinsurance, and 25% of all new business in force is subject to reinsurance, you see that the necessity for reinsurance comes mostly from the smaller companies. In the context of either the 1959 Act or the 1984 Act which was designed to give special relief to the small companies, the deduction for the commission has a small company explanation for it in legislative history. It would frustrate that intent significantly if the reinsurance business which is serving the smaller companies had this tremendously adverse tax consequence associated with it. So, you should win. What nine members of the Supreme Court (who care very little about taxes or insurance in general) will do with these issues is impossible to predict.

MR. FICKES: That's the first time I've heard a lawyer give an opinion that's one sided and not opinions to both sides.

MR. BAILEY: I just said you should win.

MR. FICKES: Tom, what are your thoughts.

MR. KABELE: I just hope we win at least on the indemnity side. Even if we lose on certain cases, I would hope it would be clear that we could at least deduct the commissions on new business, otherwise the reinsurance business will be doubly taxed versus direct business.

MR. SKILLMAN: From Lincoln's viewpoint because Lincoln's in the seventh Circuit, if the Supreme Court would deny a certiorari, I'm not sure we would view it as being a totally adverse situation. It might reduce competition a little bit, but there's a good chance that if it does go to the Supreme Court that industry will win. The first adverse decisions in the eighth Circuit were, in my lay opinion, very poorly written and very poorly decided. The next adverse decision in the fifth Circuit didn't address the issues, it just piggybacked on the decision in the eighth Circuit. The decision met with was well reasoned, well written, and spoke about the errors in the eighth Circuit's decisions. I think that unless the Supreme Court ignores Merit Life that the industry has a good chance of winning if it does go to the Supreme Court.

MR. SKILLMAN: Just a few passing comments before we leave this topic. My concern speaking from the reinsurance industry's viewpoint, is how would this affect competition between banks and reinsurance companies? I think five years ago the only players in financial reinsurance were reinsurers. Now competition has emerged from banks and investment banks. They can lend money to an insurance company in such a way that the insurance company gets a deduction on the direct business that it wrote and money used to replace it is not taxed because it's a loan. Now if reinsurers have to compete with that, they will be at a definite competitive disadvantage.

FROM THE FLOOR: I have a question for Art. What do you see as a chance that this reinsurance controversy will bring down the house of cards for direct business?

MR. BAILEY: I think the house of cards for direct business is already wobbling. I'm not concerned that the consideration of this issue by the Supreme Court is going to affect that in any way. The treatment of acquisition costs, not just commissions in the regular tax base, is just too much under the spotlight right now. So I'm a little concerned. I'm concerned about the issue but little concerned that ceding commissions are going to change things.

FROM THE FLOOR: I have a question for Art. In our discussions with the Treasury, we brought up the net level reserve issue that for the benefits side, we should be getting a bigger reserve deduction.

MR. BAILEY: This came up first with the movement of minimum tax and when property casualty rules were revised in 1986 -- I don't think anybody in Washington, D.C. believes the industry when it says the commission reserve valuation method (CRVM) reserve in effect is already amortizing this expense. You can make the mathematical comparison, net level versus CRVM and say, that in effect an amortization is occurring, but I think the perspective from people in the staffs both on the hill and the Treasury is that CRVM is too high, that you aught to be on cash value since those are only your "real" liabilities. They're not listening to the same music we are.

OPEN FORUM

MR. FICKES: The next issue with taxes and reinsurance is a holdover from the 1984 Act and that's 845b. I thought we'd first have Tom Skillman speak briefly and give us a little history on that and then Art and Tom Kabele will give their comments.

MR. SKILLMAN: 845b was enacted in part of the 1984 Tax Act as Treasurer's attempt, or rather government's attempt to put an end to the tax motivated reinsurance transactions that had been used prior to that time. 845b is a companion provision to 845a. 845a covers related parties whereas 845b covers unrelated parties. Essentially what it says is that if a reinsurance transaction is deemed to have a significant taxable effect, whether or not it was an arms length transaction, or had a valid business purpose, the IRS can make some changes to the transaction to make it more to their liking. Unfortunately theirs does not have to make it an even-handed reallocation. They can take away the supposed tax avoidance affect of one company but not reverse the taxable income effect that would typically be present for the other company. There are in the committee reports a few "safe harbor" provisions. Although all of them were very intelligently written out with "generally this" or "usually this," there's no hard and fast safe harbor at all. The committee reports did indicate that for a few specific cases, until regulations were developed to the contrary, the tax avoidance treatment would not be permitted and if the regulations were developed, it would be prospective in scope with respect to these particular provisions. This is presumably to avoid any abuses from the IRS. I think from my perception from everyone I talked to is that probably there never will be regulations for 845b.

MR. FICKES: Art, do you want to talk about the fact that it's coming up for autumn?

MR. BAILEY: From a tax lawyer's point of view, and that of an actuary, or somebody in business, it probably sounds astonishing that the Service can take a legitimate transaction and recharacterize it or change the numbers from a real transaction that has gone on between separate entities. Tax lawyers are even more astonished that 845b exists in the context of unrelated parties. 845b exists even if unrelated parties deal at arms length terms. 845b exists even if the transaction has a legitimate business purpose. In the tax laws except for 845b, the existence of a business purpose, arms length terms, and transaction between unrelated parties requires the Service to respect the transaction.

MR. KABELE: As I remember thinking back to when this developed, they had a version in the House and a version in the Senate. It then went into conference, and they usually compromise, and you usually take 50/50 and something reasonable comes out. In this case something worse came out of what was in either the House or Senate bill. It was absolutely dreadful and a total shock. It was apparently written by the staff members. The staff members who wrote it now disclaim authorship. Each keeps pointing to the other one. Apparently, it only applied in 1985 or we get a year's grace because it didn't apply to 1984. The one most interesting thing I find in it is the seventh exception, and that is you can reinsure otherwise insolvent companies. They even mention for surplus relief, for example, surplus reinsurance or otherwise insolvent insurance companies tend to indicate that that transaction may not have a significant tax avoidance affect. I think they even mention that assumption reinsurance may be all right as well.

FROM THE FLOOR: I have a general question. In the United States we allegedly have a kind of self assessment tax system. This is in contrast to the tax system in England where each taxpayer every year meets with the Inland Revenue and they end up with an agreed tax. They sit down and in effect, the government calculates the tax and the taxpayer agrees to that and away they go. It seems to me that at least with the 845b area, we no longer have the self assessment system. We in effect have an effective agreed tax a la the United Kingdom. Would you like to comment as to whether or not this is a major change in the philosophy of taxation, a philosophy here in the United States?

MR. BAILEY: I feel confident in saying that what you see in 845b does not represent a major shift in philosophy in our tax laws as much as it represents a high level of skepticism that people in Washington, D.C., on the hill and the Treasury have towards this industry and its ability to use the rules that are found in Subchapter L to their advantage. That's what I think it is. I mean it's a very unusual provision.

MR. FICKES: One topic I want to touch upon briefly since this panel is a current update on taxes, has to do with the tax treaties that are currently in existence. The reason I'd like to comment on this is I think for many, many companies, offshore reinsurance is becoming more viable if not a necessity. Going to Bermuda is no longer where companies have to go simply because you can dump reserves in the ocean. Bermuda, for example, originally developed an insurance industry primarily for U.S. casualty insurers because of the high surplus to premiums ratios required on onshore. Therefore, a lot of companies went offshore to reinsure their business. Over the years, however, they discovered there were also tax benefits to having business offshore, and as a result a large share of the profits never returned to the United States. When I was in Bermuda last spring, I met with about ten companies who are now writing on a one-to-one surplus to premium basis. So there's a large amount of money offshore that a lot of life insurance companies would like have access to. Although these companies started as casualty companies, there's now a lull in casualty reinsurance, and they're looking for opportunities to invest in other lines such as life reinsurance. Bermuda and more recently Barbados are therefore not countries just for dumping reserves. They're very real. In February of 1987, the Barbados tax treaty came into effect. The reason this is important is that anytime you do reinsurance with a foreign company, you're required by law to pay 1% of premiums excise tax on life insurance business. This is unless, of course, the reinsurer is in a country that is exempt through a tax treaty. The United Kingdom or France are a couple, and there are also a couple of iron curtain countries. The Barbados tax treaty provides Bajun reinsurers with an exemption from the U.S. excise tax. When the Barbados treaty was ratified, it was supposed to be that Bermuda would also receive the same exemption shortly thereafter. All of a sudden the situation changed and it didn't look like Bermuda was going to get their tax treaty. As of late last week, I heard that Bermuda is now on the verge of getting a tax treaty and it will have an exemption to this federal excise tax. If this does happen, then it's a very real issue as far as companies being able to find capacity outside the United States.

MR. BAILEY: I've got a comment from Best Insurance Reports that's quite interesting. It's from the casualty industry and Mendy Polack, Assistant General Counsel of the Reinsurance Association of America claimed that the Bermuda tax treaty was worth 8% of premium. There's that much difference. And in 1986, Congressman Dan Rostenkowski wrote Senate Foreign Relations Chairman, Richard Lugar -- it says "why would any reinsurance activity take place in the United States given the mobility of that activity and thus its extreme sensitivity to tax factors." I know Senator Dodd has been also fighting the tax treaties and I believe that there is a sunset provision in both the Bermuda and Barbados tax treaties.

MR. FICKES: Yes there is, but I think if Bermuda doesn't get their tax treaty, then Barbados is probably doomed. There's some argument that if Bermuda gets theirs, Barbados and Bermuda jointly have a better chance of arguing for an extension of their tax treaties.

FROM THE FLOOR: When is the sunset?

MR. FICKES: End of next year. So hurry up and get down to Barbados while the weather is nice.

Now to conclude, Tom has a real quick comment as to some technical advice memorandums.

MR. KABELE: I thought I would mention a couple of the state tax issues because the memos state that a discussion on current tax issues aren't limited to federal. First, New York and several other states have an income tax and what the IRS does to you gets multiplied by New York state. Next is the super fund tax that is based on the AMTI tax base. Whatever can happen with the AMTI you have to actually pay out money on. You have to do a careful calculation. I find that New York and a few other states base their allocation on net premium, that is, rather than direct premiums based on assumed and ceded premium. Another issue that's not quite a tax issue but an issue where you might pay out money to state governments or similar organizations is the offset issue. Some states have proposed changes in the offset provision in which case they want reinsurers to be financial guarantors of the ceding company. In one paper, I read the lawyer said the reinsurers are somehow able to monitor these companies. One problem being, however, is that we can't monitor more than 50 to 60 years in the future. What is a sound company, 50 years from now it may not necessarily be around; it could be merged several times over. Then there's another state case involving Mississippi in which the court distinguished "coinsurance" from indemnity reinsurance. They decided that coinsurance companies should be financial guarantors and that the individual policyholder should be able to sue them.

MR. FICKES: Are there any further questions on this? I hope you all have enjoyed it and I hope I covered all the bullets that were in the program and didn't leave anything out. I'd like to thank those of you in the audience that participated and especially the panelists. I thought they did a very good job.