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Proposed IASB Discussion Paper Accounting Standard for Insurance—Back to the Future

by Peter H. Winslow

In May 2007, the International Accounting Standards Board (IASB) issued a discussion paper entitled "Preliminary Views on Insurance Contracts." The discussion paper proposes a new accounting model applicable to all insurance contracts including life and non-life. The model for insurance reserve liabilities is "current exit value" (CEV), where CEV is defined as the amount that an insurer would expect to pay to transfer its remaining contractual rights and obligations to another entity. This amount is determined by three building blocks: (1) a probability-weighted best estimate of future cash flows; (2) which is discounted for the time value of money; and (3) to which is added an explicit margin to compensate a potential purchaser for assuming the risk. Remarkably, there is history for a similar market-based approach to reserving in U.S. regulation of property/casualty companies and in the tax law dealing with unearned premium reserves.

The concept of unearned premiums found its origin in the fire insurance business in New York. The comptroller of New York inserted in the 1858 Fire Annual Statement blank a liability item for the "Amount required to safely reinsure all outstanding risks, estimated by the President and Secretary." This liability was later identified as an "unearned premium reserve" in the New York Insurance Law. The primary purpose of the unearned premium reserve was to assure the continuance of coverage in the event the company became insolvent. Insolvency was a particular risk for fire insurers in the mid-1800s due to the predominance of wooden construction and spotty fire protection. As exposure to catastrophic losses from fire lessened and the availability of reinsurance increased, the concept of unearned premium reserves evolved from its original reinsurance-value concept to either the appropriate amount that would be returned to policyholders if the insurer canceled all its policies or the unearned portion of the premium on the unexpired risks under existing policies. Life insurance reserves never followed a similar evolution. At the same time the New York comptroller adopted the original definition of unearned premium reserves, Elizur Wright in Massachusetts was developing a formulaic net premium valuation method which ultimately became the model for the Standard Valuation Law adopted 90 years later.

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Interestingly, the history of unearned premium reserves as a market-based liability has been recognized in the case law in at least one tax case. The Tax Court[1] noted that the reserves for unearned premiums historically included amounts needed for reinsurance in the event of insolvency:

> *The term "unearned premium" is entirely a term of insurance art and can be understood only by reference to industry practice and history. The "unearned premium reserve" (in the words of the Code "unearned premiums on outstanding business") grew up historically as a reserve for insolvency reinsurance, i.e., as the amount required to be set aside out of premiums to compensate some reinsurer if, in the event of insolvency, it should be necessary for the reinsurer to undertake fulfillment of the original insurer's obligations to policyholders for periods subsequent to the date of reinsurance.*

On the basis of this history, the Tax Court concluded that reserves for retrospective rate credits and premium

[1] *Bituminous Casualty Corp. v. Commissioner*, 57 T.C. 58, 81 (1971), acq. 1973-2 C.B. 1.

discounts are deductible as unearned premium reserves because they are the kind of obligations for which a reinsurer would require compensation if it were to take over the future obligations.

Although the CEV model for insurance reserves in the IASB discussion paper may seem new, we may just be going back to our insurance regulatory and tax roots.

Internal Revenue Service Notice 2008-42 Modifications of Split-Dollar Life Insurance Arrangements

by Gary Lee

On March 28, 2008, the Internal Revenue Service issued Notice 2008-42, which is related to modifications made to split-dollar life insurance arrangements. The Notice addresses when an otherwise grandfathered arrangement under IRC §§ 101(j) or 264(f) is treated as a new arrangement for purposes of IRC §§ 101(j) or 264(f).

IRC § 101(j) requires companies to satisfy certain notice and consent requirements when the employer purchases life insurance on the lives of certain employees. If the rules are not satisfied, life insurance proceeds that would otherwise be received tax free upon the death of the employee are taxable income to the extent those proceeds exceed the employer's basis in the policy. In general, the rules apply to policies purchased after Aug. 17, 2006, or to policies issued prior to that date if there is a material change in the contract.

IRC § 264(f) requires taxpayers to reduce their interest expense deduction to the extent the expense is allocable to unborrowed policy cash values that they own on the lives of specified individuals. In general, the rules apply to policies issued after June 8, 1997, or to policies issued prior to that date if there is a material change in the contract.

Notice 2008-42 provides that changes to split-dollar arrangements will not affect the grandfather status of policies purchased prior to the respective effective dates under § 101(j) or § 264(f) if there is no change to the underlying life insurance contract, even if the change is treated as a material modification for purposes of the split-dollar regulations. Thus, a change may be made regarding the terms of the split-dollar arrangement so long as no change is made to the life insurance policy funding the arrangement without jeopardizing the grandfather status of the policy under IRC §§ 101(j) or 264(f). This distinction in treatment arises because § 101(j) and § 264(f) look to modification of the "life insurance contract," whereas the split-dollar regulations look to a modification of the "arrangement" in addressing whether or not a modification results in the loss of grandfather protection. This Notice does not change the income, employment, self-employment, or gift tax rules provided in the split-dollar regulations effective for split-dollar arrangements entered into or materially modified after Sept. 17, 2003.

The Notice was issued in response to accounting changes for post-retiree split-dollar arrangements issued by the Emerging Issues Task Force (EITF) of the Financial Accounting Standards Board in 2006. *See* ETIF 06-04 and ETIF 06-10, which are related to endorsement and collateral assignment arrangements, respectively. In general, the ETIFs require employers to accrue post-retiree split-dollar benefits during a retiree's working years. Such treatment creates an increase in liabilities, reduces net worth and increases the debt-to-equity ratio. In some sectors, such as banking, the requirement could impact the bank's ability to satisfy capital and reserving regulations. Companies can now modify split-dollar arrangements that offer post-retiree benefits to avoid the impact of the ETIFs without subjecting grandfathered policies to the provisions of § 101(j) or § 264(f).

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Proposed Regulations Issued for New Tax Return Preparer Penalty Standards

by John Keenan

The May 2008 edition of *Taxing Times* contained an article that described recent changes relating to the new tax return preparer penalty rules under Internal Revenue Code sections 6694 and 6695, and related Code provisions, and their potential impact on the insurance industry. The return preparer penalty regime had been

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amended pursuant to legislation passed in May 2007 as part of the Small Business and Work Opportunity Act of 2007. Under the amended penalty preparer regime, the standard of care required of the return preparer is greater than the standard of care required of the taxpayer. More specifically, amended section 6694 provides that a paid tax return preparer could be subject to a penalty if the preparer does not have a reasonable belief that the return position for an item would more likely than not be sustained on its merits. Generally speaking, taxpayers can avoid a penalty if substantial authority exists for the return position for the item. This disconnect in the standard of care could create the situation in which a return preparer would require a taxpayer to disclose a tax return position—for which the taxpayer had no penalty exposure—solely to allow the return preparer to avoid a potential penalty.

Under the proposed regulations, the analysis will now focus on the person within the firm who is primarily responsible for the position taken on the return rather than the person with overall supervisor responsibility.

Notice 2008-13, published in December 2007, contained interim guidance on complying with the new section 6694 standards. (*See* John Keenan, "Impact of Tax Return Paid Preparer Penalties on the Insurance Industry," *Taxing Times*, Vol. 4, Issue 2, May 2008.). Around the time of publication, at least one proposal had been submitted in Congress to conform the standard of care required of the return preparer to the "substantial authority" standard of care required of the taxpayer reporting standard for return preparers to that which is applied to taxpayers. There have been no further developments on the legislative front.

On June 16, 2008, however, the Internal Revenue Service (IRS) issued proposed regulations on the tax return preparer penalties. The proposed regulations implement the amendments to the return preparer penalty regime passed in 2007. The proposed regulations retain the disclosure provisions originally set forth in the interim compliance rules of Notice 2008-13. Under these disclosure rules, a signing tax return preparer can, in certain instances, make a disclosure to the taxpayer rather than the IRS in order to avoid a penalty. More specifically, a taxpayer is deemed to have met the requirements of section 6694 for positions with substantial authority if the tax return preparer advises the taxpayer of all of the penalty standards applicable to the taxpayer under section 6662. The signing preparer's files must contain contemporaneous documentation that this advice was provided to the taxpayer.

Another significant change to the return preparer regime contained in the proposed regulations is the change to the "one preparer per firm" rule. Under this rule, if two or more persons with a firm were tax return preparers, ordinarily, the individual with overall supervisor responsibility for the advice given by the firm with respect to the return was considered the return preparer. Under the proposed regulations, the analysis will now focus on the person within the firm who is primarily responsible for the position taken on the return rather than the person with overall supervisor responsibility. Only one person within a firm will generally be considered the person primarily responsible for any one return position.

Other areas addressed in the proposed regulations include rules to compute the amount of the return preparer's income subject to a penalty, the ability of a preparer to rely upon information furnish by others, the reasonable belief of more likely than not standard, the definition of return preparer, and reasonable cause relief from a return preparer penalty.

A public hearing on the proposed regulations was held on Aug. 18, 2008. The IRS has indicated that it intends to finalize the regulations by the end of 2008; but the final regulations will not be applicable to returns and claims for refund filed, and advice given, before Dec. 31, 2008.

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Highest Aggregate Reserves Qualify for Statutory Reserves Cap

by Peter H. Winslow, Lori J. Jones and Samuel A. Mitchell

On June 27, 2008, the Internal Revenue Service (IRS) released Rev. Rul. 2008-37[1] dealing with the application of the statutory cap when a company conducts business in several states with different minimum reserve requirements. The IRS concludes that statutory reserves defined in I.R.C. § 807(d)(6) for purposes of the limitation on tax reserves in I.R.C. § 807(d)(1) is the highest aggregate reserve amount for I.R.C. § 807(c) items actually held and set forth on the annual statement pursuant to the minimum reserve requirements of any state in which the company does business.

The revenue ruling contains two examples. In situation one, the life insurance company (IC) conducts business in 45 states and issues a life insurance contract (Contract A). IC actually holds and reports to each state insurance regulatory authority on its annual statement the highest aggregate minimum amount of reserves required for its insurance and annuity contracts under the rules of any state in which IC does business. As a result, on its 2007 annual statements, IC reported end-of-year aggregate reserves of $405,955,000 which included $9,992 of life insurance reserves with respect to Contract A.

In situation two, IC reported to each state the minimum amount of reserves required for its insurance and annuity contracts under the rules of that state. Following this principle, on its annual statement filed in State X, the state in which IC is chartered, IC reported $402,540,000 of end-of-year aggregate reserves and $9,942 allocable to Contract A. However, in its annual statement filed in State Y, IC reported $405,955,000 and included $9,992 allocable to Contract A. Thus, IC actually held and reported to at least one state the highest aggregate minimum amount of reserves required for its insurance and annuity contracts under any state in which IC does business.

The IRS concluded that in both situations, the statutory reserves as defined in I.R.C. § 807(d)(6) were $405,955,000—the highest aggregate minimum reserve amount for I.R.C. § 807(c) reserve items actually held pursuant to the minimum reserve requirements of any state in which IC does business. Therefore, for purposes of applying the statutory reserves limitation contained in the flush language of I.R.C. § 807(d)(1), the amount of statutory reserves to be taken into account with respect to Contract A is $9,992.

The revenue ruling is interesting in several respects. In a recent *Taxing Times* article,[2] we suggested that the IRS should rely on existing regulations and conclude that "statutory reserves" are the aggregate reserves reported on the annual statement included with the tax return which, at the election of the taxpayer, could be the annual statement reflecting the highest aggregate reserves in any state or jurisdiction in which it transacts business.[3] Rev. Rul. 2008-37 did not base its conclusion directly on these regulations. Instead, it appears to have concluded that statutory reserves are determined by the highest aggregate reserves in any state in which the company does business regardless of the annual statement attached to the return. If this is the correct reading of the ruling, it has several additional implications. For example, it suggests that statutory reserves can be determined by the annual statements of different states depending on which state yields the highest aggregate reserves in the particular tax year. This, in turn, implies that year-by-year changes to the statutory cap caused by changes in the applicable annual statement would not be considered changes in the basis of computing reserves subject to a ten-year spread under I.R.C. § 807(f). That is, any switch to another applicable annual statement yielding higher aggregate reserves would be a mere change in facts.

Another interesting, and somewhat puzzling, aspect of Rev. Rul. 2008-37 is its reference to the "minimum" reserve requirements of the states. In each of the examples, the taxpayer held the minimum aggregate reserves permitted by state law. The facts do not address a situation where the taxpayer holds reserves in excess of all states' minimum reserve requirements. Nevertheless, the actual holding of the ruling appears to state a broader principle than the facts. It defines statutory reserves as "the highest aggregate reserve amount for § 807(c) items actually held and set forth on the annual statement pursuant to the minimum reserve re-

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[1] 2008-28 I.R.B. 77.

[2] Winslow and Mitchell, "IRS to Rule in the Meaning of Statutory Reserves," *Taxing Times* (Feb. 2008).

[3] Treas. Reg. § 1.6012-2(c); § 1.801-5(a).

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quirements of any State in which [the taxpayer] does business." This does not seem to limit statutory reserves to the actual amount of minimum reserves required; instead, it properly focuses on the amount actually reported on the annual statement in satisfaction of state law.

Rev. Rul. 2008-37 is ambiguous in at least one respect. Under I.R.C. § 807(d)(1), the comparison of the actuarially-computed federally prescribed reserve to statutory reserves generally is on a contract-by-contract basis. As a result, it is possible to read the reference to aggregate reserves in the I.R.C. § 807(d)(6) definition of statutory reserves as referring to the aggregate reserves for the contract. Although it is by no means clear, Rev. Rul. 2008-37 appears to measure statutory reserves by the aggregate reserves reported on a single annual statement. Under that reading, multiple annual statements cannot be examined to determine the highest reserves for specific contracts. Despite this ambiguity, the ruling provides useful and timely guidance.

Tax Factors Influence the Viability of NAIC Securitization Initiatives

by Emanuel Burstein

Securitizations and Expanded Insurance Capacity

Congress, state insurance regulators and insurance companies have been examining ways to expand insurance capacity by promoting insurance securitization arrangements. In Congressional hearings on applying certain securitization methods to increase insurance capacity for catastrophe risk coverage, Michael Moriarty,[1] representing the National Association of Insurance Commissioners (NAIC), stated,

> *The NAIC's position is that U.S. regulators should encourage the development of alternative sources of capacity such as insurance securitizations, provided adequate standards governing these transactions are applied. Further deliberations of the [insurance securitization] working group at the NAIC led to a determination that it will be preferable if insurance securitizations could be done here in the United States instead of off-shore.*[2]

He added that "to further that position, the NAIC has adopted separate model acts to facilitate on-shore securitization using two different methods—protected cells and special purpose reinsurance vehicles."[3] Protected cells and special purpose reinsurance vehicles facilitate the transfer of insurance risks to capital markets and enable investors to fund a sizable portion of transferred coverage.

Tax factors, including tax uncertainty, significantly influence the viability of these risk-transfer vehicles. Moriarty stated, "it is our understanding that an important impediment to the utility of both of these options here in the United States is tax uncertainty. Both of these methods depend on certain tax treatment which may require amendments to the tax code." Although Congress has not amended related provisions of the Internal Revenue Code, the Internal Revenue Service (Service) is providing greater tax certainty, at least for protected cell securitizations, by addressing related tax treatment in pronouncements, principally in Rev. Rul. 2008-8[4] and Notice 2008-19,[5] and seeking input from insurance tax

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1 Mr. Moriarty was the director of the Capital Markets Bureau of the New York Department of Insurance.

2 *Catastrophe Bonds: Spreading Risk: Hearing Before the Subcomm. On Oversight and Investigations of the House Comm. On Financial Services*, 107th Cong. (Oct. 8, 2002) at 7.[Hereinafter *Hearing on Catastrophe Bonds*]

3 *Id.* Copies of the NAIC's Protected Cell Company Model Act (1999) and Special Purpose Reinsurance Vehicle Model Act (2001) are respectively included on pages 89-97 and 138-158 of the *Hearing on Catastrophe Bonds.*

4 2008-5 I.R.B. at 340.

5 2008-5 I.R.B. at 366.

professionals. This article summarizes these securitization techniques and related tax issues.

Protected Cell Companies

A protected cell company[6] is a legal entity under applicable state law that is "a domestic insurer that has one or more protected cells."[7] A protected cell is "an identified pool of assets and liabilities of a protected cell company segregated and insulated . . . from the remainder of the protected cell company's assets and liabilities."[8] The Protected Cell Company Model Act provides that the "creation of a protected cell does not create, in respect of that protected cell, a legal person separate from the protected cell company."[9]

The structure and mechanics of a protected cell company (PCC) securitization arrangement are illustrated in Rev. Rul. 2008-8,[10] in which a sponsor forms a PCC and holds its common stock. Each of the PCC's multiple cells is funded from premiums received for the cell's coverage and contributions from participant(s) (investor(s) in the cell), who hold preferred stock in the cell. The non-cellular assets include minimal capital and surplus required under the applicable state law.

Each cell must pay claims under contracts to which it is a party. Each cell also accounts for its income and expenses and is insulated from claims of creditors of other cells or the PCC's general account. In addition, each cell can make distributions to participants with respect to its class of stock without regard to whether any distributions are made with respect to any other class of stock. If a participant terminates its participation in the PCC the participant is "entitled to a return of the assets of the cell in which it participated, subject to any outstanding obligations of that cell."[11]

An insurance securitization using a protected cell company addresses important obstacles to the realization of securitizations by domestic insurers, which was the "central purpose" of the NAIC's Insurance Securitization Working Group.[12] One important obstacle to insurance securitizations by domestic insurers is the relatively high capital requirements imposed on these insurers. Arnold Dutcher, chair of the Insurance Securitization Working Group, stated, "the protected cell concept allows an insurance company to isolate assets and a specific risk exposure in a protected cell with only a marginal risk-based capital requirement."[13]

In addition, each cell can make distributions to participants with respect to its class of stock without regard to whether any distributions are made with respect to any other class of stock.

Tax uncertainly is another important obstacle to domestic insurance securitization transactions.[14] The Service and Treasury Department addressed standards that determine whether and when a protected cell provides insurance in Rev. Rul. 2008-8[15] and proposed standards that determine whether and when a protected cell, separate from the protected cell company that established the cell, would qualify as an insurance company in Notice 2008-19.[16]

In brief, in Rev. Rul. 2008-8 the Service and Treasury apply tax principles that determine whether captive insurance arrangements qualify as insurance to determine whether coverage by the cell qualifies as insurance.[17] Notice 2008-19 addresses when a protected cell is treated as an insurance company, which is addressed below, and requests comments on this and related issues, such as

6 These entities also may be referred to as segregated account companies or segregated portfolio companies. *See* Notice 2008-19, section 2.04, 2008-5 I.R.B. at 367.

7 *See* section 3 of the NAIC's Protected Cell Company Model Act.

8 *Id.*

9 *Id.* section 4.C of the NAIC's Protected Cell Company Model Act.

10 2008-5 I.R.B. 340 (Feb. 4, 2008).

11 *Id.*

12 NAIC Proceedings 1999 3rd quarter vol. 1 at 330 (May 2002).

13 *Id.*

14 *See* notes 4 and 5 and accompanying text.

15 2008-5 I.R.B. 340.

16 2008-5 I.R.B. 366.

17 2008-5 I.R.B. at 341-342. The Ruling and Notice are addressed in Mark H. Kovey, "Protected Cells As Insurance Companies," *Taxing Times* (May 2008) at 37. The tax treatment of captive insurance companies is addressed in detail on pages 16-43 of Emanuel Burstein, *Federal Income Taxation of Insurance Companies* (2nd edition) (2007).

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reporting rules and the treatment of protected cells under consolidated return rules.[18] Rev. Rul. 2008-8 and Notice 2008-19 clarify much of the uncertain tax treatment and arguably indicate that the Service and Treasury are sensitive to the policy goals of Congress and insurance regulators.

A working group of the tax section of the New York State Bar Association argues in a letter to Treasury officials that treating a given cell as an insurance company is the correct tax result.[21]

Is a Protected Cell an Insurance Company for Tax Purposes?

Notwithstanding the characterization of a protected cell in the Model Act as a component of the protected cell company, the Service treats the protected cell as an insurance company in Notice 2008-19[19] if it satisfies the following two requirements,

> (1) "the assets and liabilities of the cell are segregated from the assets and liabilities of any other cell and from the assets and liabilities of the Protected Cell Company such that no creditor of any other cell or of the Protected Cell Company may look to the assets of the cell for the satisfaction of any liabilities, including insurance claims (except to the extent that any other cell or the Protected Cell Company has a direct creditor claim against such cell); and"
>
> (2) "based on all the facts and circumstances, the arrangements and other activities of the cell, if conducted by a corporation, would result in its being classified as an insurance company within the meaning of [sections] 816(a) or 831(c)."[20]

The Service does not elaborate on the basis for this conclusion but a Treasury official indicated at a May 2008 insurance tax conference that treating the protected cell as an insurance company eases the tax administration of these transactions.

A working group of the tax section of the New York State Bar Association argues in a letter to Treasury officials that treating a given cell as an insurance company is the correct tax result.[21] Separate cells should be treated as separate entities under the federal income tax law if the applicable local law requires the "legal separation of the assets and liabilities of each cell from the other cells."[22] The group members recommend that the Treasury issue a safe harbor that provides that a protected cell would be treated as a separate entity under the federal income tax if the protected cell (1) is created under the statute of a state or foreign sovereign jurisdiction and (2) the statute "provides for unambiguous separateness of assets and liabilities of the protected cell company and permits beneficial ownership to be held on a cell by cell basis."[23]

They also argue that the tax principles that the Service applied to characterize separate series when certain conditions were satisfied should apply to treat each cell as a separate entity for federal income tax purposes. A given series had to consist of separate pools of assets and streams of income, the owners could look only to such assets in redemption, liquidation or termination, and creditors' rights were limited to the assets of the series for recovery of expenses, charges or liabilities.[24]

The Service recently concluded in LTR 200803004,[25] for example, that each LLC portfolio of a "series limited

[18] *Id.* at 366-368.
[19] 2008-5 I.R.B. 366. It would require a given cell to acquire a tax identification number. *Id.* at section 3.02(b), 2008-5 I.R.B. at 367.
[20] *Id.* at section 3.01.
[21] Letter from New York State Bar Association: Tax Section, *Re: Notice 2008-19 and Protected Cell Companies Outside of the Insurance Arena*, to Douglas H, Shulman, Commissioner of Internal Revenue and Eric Solomon Assistant Secretary (Tax Policy) Department of the Treasury (May 2, 2008), available at *http://www.nysba.org/AM/Template.cfm?Section=Tax_Section_Reports_2008&TEMPLATE=/CM/ContentDisplay.cfm&CONTENTID=15932.*
[22] *Id.* at 7.
[23] *Id.* at 8-9.
[24] *Id.* at 7.
[25] Oct. 15, 2007.

liability company" that held multiple asset portfolios was treated as a separate entity under the federal income tax. Characteristics of each LLC portfolio that reflected the separate identify of the portfolio included:

- Each portfolio will consist of a separate pool of assets, liabilities and stream of earnings.
- The shareholders of each portfolio may share in the income only of that portfolio.
- The ownership interest of a shareholder in the LLC is limited to the assets of that LLC upon redemption, liquidation or termination of the LLC.
- Payment of the LLC's expenses, charges and liabilities is limited to the LLC portfolio's assets.
- Creditors of an LLC portfolio can access only assets of the LLC portfolio to recover expenses, charges and liabilities.

The letter ruling involved the reorganization of a trust that held separate asset portfolios, each of which was treated as a separate Regulated Investment Company and taxable as a corporation. The Service recognized that each portfolio held by the new LLC was a separate entity because it concluded that each portfolio was classified for tax purposes as either a disregarded entity (which is treated as taxable as part of its owner), a partnership or a corporation depending on the number of the portfolio's owners and whether certain elections were taken.

Special Purpose Reinsurance Vehicles

The other Model Act involves Special Purpose Reinsurance Vehicles (SPRVs). In an SPRV arrangement an insurance (or reinsurance) company transfers certain of its risks, and pays premiums, to an SPRV. The SPRV also is funded by investors. The SPRV transfers the proceeds to a trust that invests in "Treasury securities and other highly rated assets."[26] The investors' security offering "defines a catastrophe that would trigger a loss of investor principal and, if triggered, a formula to specify the compensation level from the investor to the SPRV."[27]

The tax treatment of special purpose reinsurance vehicle arrangements, like that of protected cell securitization arrangements, needs clarification. In the 2002 Hearing on Catastrophe Bonds, a request was made for "pass-through" tax treatment of the SPRV.[28] Officials at the Reinsurance Association of America (RAA), however, were concerned that providing this tax treatment to SPRVs would place reinsurers that assume similar risks at a tax-based competitive disadvantage because the reinsurers are taxable entities.[29]

Conclusion

The NAIC, government agencies and insurance companies seek to increase insurance capacity by promoting insurance securitizations. Tax considerations, including uncertain tax treatment, influence the viability of securitization transactions that transfer risk from insurance companies to investors. The Service is resolving some uncertainties, principally in Rev. Rul. 2008-8 and Notice 2008-19, but tax legislation may be needed to promote certain tax policy goals, such as pass-through treatment for special purpose reinsurance vehicles. Tax and other rules also may have to attempt to minimize adverse consequences including potential competitive disadvantages imposed on other entities that accept similar risks from insurance companies and the possible use of any new rules in "abusive" transactions.

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[26] U.S. General Accounting Office, *CATASTROPHE INSURANCE RISKS: The Role of Risk-Linked Securities and Factors Affecting Their Use,* GAO-02-941 (Washington, D.C.: Sept. 2002) at 20. [Hereinafter cited as GAO report]

[27] *Id.*

[28] *Hearing on Catastrophe Bonds at 7*. Cf. section 860A(a), which provides pass-through tax treatment for qualified mortgage loan securitizations by real estate mortgage investment conduits (REMICs). *But compare* FASIT rules, prior-law section 860H-860L, which were enacted by section 1621 of Pub. L. 104-188, The Small Business Job Protection Act of 1996, 110 Stat. 1858-1868 (August 20, 1996), to promote other qualified securitizations but repealed by section 835(a) of Pub. L. 108-173, The American Jobs Creation Act of 2004, 118 Stat. 1593 (Oct. 22, 2004), because the FASIT rules did not serve the purpose intended by Congress and were "prone to abuse." *See* Joint Committee on Taxation, *General Explanation of Tax Legislation Enacted in the 108th Congress* (JCS-5-05) May 2005 at 396.

[29] *GAO report* at 28. The RAA officials also stated that the SPRV would "act as a reinsurer and yet [would] not be subject to insurance regulation." *Id.*