

**STORAGE NAME:** h4265z.fs  
**DATE:** June 16, 1998

**\*\*FINAL ACTION\*\***  
**\*\*SEE FINAL ACTION STATUS SECTION\*\***

**HOUSE OF REPRESENTATIVES  
COMMITTEE ON  
FINANCIAL SERVICES  
FINAL BILL RESEARCH & ECONOMIC IMPACT STATEMENT**

**BILL #:** HM 4265

**RELATING TO:** Federal tax exemption for joint underwriting associations

**SPONSOR(S):** Representative Safley

**COMPANION BILL(S):** SM 1570 (s)

**ORIGINATING COMMITTEE(S)/COMMITTEE(S) OF REFERENCE:**

- (1) FINANCIAL SERVICES YEAS 12 NAYS 0
- (2)
- (3)
- (4)
- (5)

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**I. FINAL ACTION STATUS:**

HM 4265 passed the House 115-0 on April 16, 1998, and passed the Senate 39-0 on May 5, 1998. It was signed by officers and filed with the Secretary of State's office on May 15, 1998.

**II. SUMMARY:**

Florida's two state-created, nonprofit property insurers of last resort, the Florida Windstorm Underwriting Association (FWUA) and the Residential Property and Casualty Joint Underwriting Association (RPCJUA), are subject to federal income taxation in the same manner as for-profit insurance companies.

This House Memorial urges Congress to enact legislation that would exempt the FWUA and RPCJUA from federal taxation.

III. SUBSTANTIVE RESEARCH:

A. PRESENT SITUATION:

Florida's two state-created nonprofit property insurers of last resort, the Florida Windstorm Underwriting Association (FWUA) and the Residential Property and Casualty Joint Underwriting Association (RPCJUA),<sup>1</sup> are subject to federal taxation in the same manner as insurance companies. In broad terms, the taxable status of the FWUA and RPCJUA means that they must pay taxes on their premium revenues less costs such as operating expenses or claims payments.

Neither the FWUA nor the RPCJUA has requested a tax exemption from the Internal Revenue Service. Although the FWUA and RPCJUA share some characteristics with entities that are exempt from taxation under section 501(c) of the U.S. Internal Revenue Code (nonprofit operation, provision that earnings not inure to the benefit of member insurers), they apparently do not meet all of the requirements for an exemption under any of the subdivisions of section 501(c). Joint underwriting associations have been denied exemptions under section 115 of the Internal Revenue Code, which exempts income accruing to a state from entities that perform essential governmental functions.<sup>2</sup>

The tax exemption of the Florida Hurricane Catastrophe Fund was based on the IRS's determination that the fund was an integral part of state government; the FWUA and RPCJUA, by comparison, are not state agencies and perform functions also performed by taxable private-sector entities.

Until recently, the tax liabilities of the FWUA and RPCJUA were not significant. The RPCJUA showed positive net earnings for the first time in 1996, when it incurred income tax liability of \$17.6 million. The RPCJUA's tax liability for 1997 was \$73.6 million.

For the FWUA, the issue of federal tax liability first arose in 1997. Historically, the IRS had treated the FWUA as a partnership for tax purposes, meaning that the profits and losses distributed to member insurers were reflected in the various members' tax returns. In 1997, the Legislature amended the FWUA law to require the FWUA to retain any earnings as surplus rather than distribute the earnings to member insurers.<sup>3</sup> Because it could no longer be treated as a partnership, the FWUA elected to be treated as a corporation for federal tax purposes beginning April 1, 1997. The FWUA estimates that its federal tax liability for the last nine months of 1997 will be \$14 million to \$15 million.

Legislation is being proposed in the 105th Congress that would amend section 501(c) of the Internal Revenue Code to create a federal income tax exemption for property and casualty joint underwriting associations.

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<sup>1</sup> See section 627.351, F.S.

<sup>2</sup> See, e.g., Letter Ruling LTR 9109031, a 1990 private letter ruling that held a medical malpractice joint underwriting association to be taxable, notwithstanding section 115.

<sup>3</sup> See Chapter 97-55, Laws of Florida.

**B. EFFECT OF PROPOSED CHANGES:**

The Legislature would request that the Florida Congressional delegation, the Congress, and the President act with all deliberate speed to enact legislation that would designate the FWUA and RPCJUA as tax-exempt entities under section 501(c) of the Internal Revenue Code.

**C. APPLICATION OF PRINCIPLES:**

1. Less Government:

a. Does the bill create, increase or reduce, either directly or indirectly:

(1) any authority to make rules or adjudicate disputes?

No.

(2) any new responsibilities, obligations or work for other governmental or private organizations or individuals?

No.

(3) any entitlement to a government service or benefit?

No.

b. If an agency or program is eliminated or reduced:

(1) what responsibilities, costs and powers are passed on to another program, agency, level of government, or private entity?

N/A

(2) what is the cost of such responsibility at the new level/agency?

N/A

(3) how is the new agency accountable to the people governed?

N/A

2. Lower Taxes:

- a. Does the bill increase anyone's taxes?

No.

- b. Does the bill require or authorize an increase in any fees?

No.

- c. Does the bill reduce total taxes, both rates and revenues?

No.

- d. Does the bill reduce total fees, both rates and revenues?

No.

- e. Does the bill authorize any fee or tax increase by any local government?

No.

3. Personal Responsibility:

- a. Does the bill reduce or eliminate an entitlement to government services or subsidy?

N/A

- b. Do the beneficiaries of the legislation directly pay any portion of the cost of implementation and operation?

N/A

4. Individual Freedom:

- a. Does the bill increase the allowable options of individuals or private organizations/associations to conduct their own affairs?

No.

- b. Does the bill prohibit, or create new government interference with, any presently lawful activity?

No.

5. Family Empowerment:

a. If the bill purports to provide services to families or children:

(1) Who evaluates the family's needs?

N/A

(2) Who makes the decisions?

N/A

(3) Are private alternatives permitted?

N/A

(4) Are families required to participate in a program?

N/A

(5) Are families penalized for not participating in a program?

N/A

b. Does the bill directly affect the legal rights and obligations between family members?

N/A

c. If the bill creates or changes a program providing services to families or children, in which of the following does the bill vest control of the program, either through direct participation or appointment authority:

(1) parents and guardians?

N/A

(2) service providers?

N/A

(3) government employees/agencies?

N/A

D. STATUTE(S) AFFECTED:

N/A

E. SECTION-BY-SECTION RESEARCH:

N/A

IV. FISCAL RESEARCH & ECONOMIC IMPACT STATEMENT:

A. FISCAL IMPACT ON STATE AGENCIES/STATE FUNDS:

1. Non-recurring Effects:

None.

2. Recurring Effects:

None.

3. Long Run Effects Other Than Normal Growth:

None.

4. Total Revenues and Expenditures:

None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS AS A WHOLE:

1. Non-recurring Effects:

None.

2. Recurring Effects:

None.

3. Long Run Effects Other Than Normal Growth:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

1. Direct Private Sector Costs:

None.

2. Direct Private Sector Benefits:

If Congress were to enact a tax exemption for the FWUA and RPCJUA, the two insurers of last resort could use the funds that currently are earmarked for federal taxes as contributions to surplus. Additional contributions to the surplus of the FWUA and RPCJUA would improve their ability to pay catastrophic losses without levying assessments on insurance companies and their policyholders.

3. Effects on Competition, Private Enterprise and Employment Markets:

N/A

D. FISCAL COMMENTS:

N/A

V. CONSEQUENCES OF ARTICLE VII, SECTION 18 OF THE FLORIDA CONSTITUTION:

A. APPLICABILITY OF THE MANDATES PROVISION:

N/A

B. REDUCTION OF REVENUE RAISING AUTHORITY:

N/A

C. REDUCTION OF STATE TAX SHARED WITH COUNTIES AND MUNICIPALITIES:

N/A

VI. COMMENTS:

N/A

VII. AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES:

N/A

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VIII. SIGNATURES:

COMMITTEE ON FINANCIAL SERVICES:

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