The Florida Senate

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Committee on Finance and Tax

AN OVERVIEW OF FLORIDA'S INSURANCE PREMIUM TAX

SUMMARY

Insurance premiums have been taxed in Florida since 1895, and the significance of the premium tax to the general revenue Fund has grown in recent years. Insurers are allowed to take several credits against the premium tax, the most important being the credits for Florida salaries, corporate income tax payments, and municipal police officers' and firefighters' pension fund taxes. Every state taxes insurance premiums, and Florida's premium tax rate is lower than the rate in 29 states. Credits against the insurance premium tax allowed by Florida are allowed by some, but not a majority of, other states.

Because of its growing importance as a revenue source, proposals to change this tax warrant careful scrutiny.

BACKGROUND

Insurance premiums have been taxed in Florida since 1895. These are the important developments in the insurance premium tax:

- 1895 – Premiums taxed annually at 1 percent
- 1903 – Premium tax rate increased to 2 percent
- 1949 – Tax exemption created for insurers that maintained home offices in Florida
- 1953 – Tax reduction for foreign insurers with regional offices in Florida
- 1955 – Retaliatory tax on foreign insurers
- 1971 – Estimated tax payments required
- 1971 – Tax credit for corporate income tax payments
- 1979 – Florida Life and Health Insurance Guaranty Association was established and funded by assessments against insurers that are creditable against premium tax
- 1980 - Tax exemption for annuity payments if the resulting tax payments are passed on to annuity holders
- 1987 – Distinction between domestic and foreign insurers is removed and a credit is created for salaries paid to Florida employees
- 1989 – Tax rate is reduced to 1.75 percent
- 1998 – Tax credits are created for child care expenditures, certain capital investments, and investments in Certified Capital Companies.

METHODOLOGY

This project is based on a review of the statutory history of the insurance premium tax and information obtained from the Florida Department of Revenue about how the tax operates and how much revenue it has generated in recent years. Information about the distribution of insurance premium tax revenue to general revenue, trust funds, and local governments is taken from the Florida Revenue Estimating Conference's Revenue Analysis FY 1970-71 Through FY 2014-15, and the fiscal impacts of proposed and enacted changes in the tax comes from the Revenue Estimating Conference's Measures Affecting Revenue and Impact Conference results for the relevant years. Information on other states' insurance premium tax rates and credits came is the CCH State Tax Guide – All States Volume 3, with clarification from state tax administrators, when needed.

FINDINGS

Insurance Premium Tax Rates and Distributions

Insurance premium taxes are imposed on insurance premiums and paid by insurance companies at the following rates: 1.75 percent on gross premiums minus reinsurance and return premiums; 1 percent on annuity premiums; 1.6 percent on self insurers; and 5 percent on surplus lines premiums and independently procured coverage. Exemptions are allowed on annuity premiums paid by annuity policy or contract holders in this state, if the savings are passed on to the consumer. Corporate income tax and the emergency excise tax paid to Florida are credited against premium tax liability. A credit is allowed against the premium tax equal to 15 percent of the amount paid by the insurer in salaries to employees located or based in Florida who are covered by unemployment compensation. This credit, in combination with the corporate income tax credit, may not exceed 65 percent of the tax due for the calendar year. Other credits are available for payments into the Municipal Firefighters' Pension Fund and the Municipal Police Officers' Retirement Fund, certain community contributions, investments in Certified Capital Companies, the capital costs of certain qualifying investments, certain costs associated with providing employee child care services or facilities, workers' compensation assessments and Florida Life and Health Insurance Guaranty Association assessments.

Insurance premium tax revenue is distributed to Municipal Firefighters' Pension Fund and the Municipal Police Officers' Retirement Fund, the Insurance Regulatory Trust Fund, and the General Revenue Fund.

Insurance Premium Tax Revenue History

Since FY1970-71, insurance premium tax revenue has accounted for between 1.45 percent and 2.89 percent of general revenue. Total collections in 2004-05 were 17 times greater than in 1970-71, but the revenue growth has not been consistent. Total collections fell short of the previous year five times during the period.

Changes in the Florida tax base in recent years have increased the importance of the premium tax in general revenue collections. Since 2000, both the estate tax and the annual intangibles tax have been eliminated. Each had contributed more to general revenue than the insurance premium tax, which has risen from the eighth-most important general revenue source to the sixth-ranked source, behind sales tax, corporate income tax, documentary stamp tax, non-recurring intangibles tax, and beverage tax. In the three most recent fiscal years, insurance premium tax has accounted for more than 2 percent of general revenue, and it is forecast to equal 2.4 percent of general gevenue in 2005-06.

Significant Features of the Insurance Premium Tax

Installment Payment (s. 624.5092, F.S.)

The insurance premium tax was paid annually from its inception until 1971, when legislation was enacted to require installment payments on an estimated basis. Section 624.5092, F.S., requires that installment payments are due and payable on April 15, June 15, and October 15 in each year, based upon the estimated gross amount of receipts of insurance premiums or assessments received during the immediately preceding calendar quarter. A final payment and tax return are due on or before March 1, showing, by quarters, the gross amount of receipts taxable for the preceding year and the installment payments made during that year.

A 10 percent penalty is imposed on any taxpayer who fails to report and timely pay any installment of tax, who estimates any installment of tax to be less than 90 percent of the amount finally shown to be due in any quarter, or who fails to report and timely pay any tax due with the final return. This penalty can be avoided by paying, for each installment, 27 percent of the amount of the net tax due for the preceding year.

Retaliatory Tax (s. 624.5091, F.S.)

In 1955 the Florida legislature imposed a retaliatory tax on non-domestic insurance companies doing business in Florida. This tax was included in the Florida Insurance Code adopted in 1959. Retaliatory taxes are determined and assessed on the basis of "what if" a Florida-domiciled insurer were licensed and doing business in the insurer's state of domicile and providing the same insurance products as the foreign insurer is writing in this state. Retaliatory taxes do not apply to surplus lines insurance. All states except Hawaii have retaliatory tax statutes. For calendar year 2004, retaliatory tax revenue was $41.6 million.

Insurance Premium Tax Credits and Exemptions

Tax credits reduce the state premium tax by more than 50 percent.

History of Selected Insurance Premium Tax Credits ($ millions)

Credit	2002	2003	2004	2005
Salary Credit	144.4	176.9	173.9	177.8
Corp Income Tax Credit	103.4	88.6	130.3	188.2
Firefighter's Pension	54.4	60.1	65.9	76.6
Police Officers' Pension	58.9	65.6	67.1	69.4
CAPCO	13.2	12.1	12.4	13.3
Total for Selected Credits	**374.3**	**403.3**	**449.6**	**525.3**

Combined salary credits and corporate income tax credits are limited to 65 percent of the premium tax due after deducting the municipal taxes paid by the insurer to fund police officers' and firefighters' pensions. This limitation results in some credits going unused. This is the recent history of unused credits:

Unused Premium Tax Credits ($ millions)				
Year	Unused CIT Credits	#Taxpayers	Unused Salary Credits	# Taxpayers
2003	26.9	185	78.7	244
2004	46.9	202	91.3	208
2005	72.9	293	85.2	195

Because of limitations on the salary credit, the effective salary credit is less than 15 percent of salary. As the table below shows, the amount of possible salary credit is less than 15 percent of salaries, and the amount of these possible credits that can actually be taken is less than the possible credits. The effective salary credit rate since 2003 has ranged from 5.5 to 6.6 percent of eligible salaries.

Potential and Actual Salary Credits ($ millions)			
	2003	2004	2005
15 Percent of Eligible Salaries	469.5	392.0	481.4
Possible Salary Credits*	255.1	265.2	263.0
Actual Salary Credits Taken**	176.9	173.6	177.8
Effective Salary Credit Rate	5.65%	6.64%	5.54%

*Can be no greater than premiums times 1.75 % less municipal police and firefighters' pension tax payments plus CIT payments.

**Limited by the requirement that combined salary credits and corporate income tax credits cannot exceed 65 percent of the premium tax due after deducting the municipal taxes paid to fund police officers' and firefighters' pensions .

Florida Employees' Salaries Credit (s. 624.509(5), F.S.)

In 1985, the U.S. Supreme Court ruled in *Metropolitan Life Insurance Company v. Ward* that a domestic preference provision in Alabama's insurance tax law similar to the preference provision in Florida at the time violated the Equal Protection Clause. Florida and other states looked for ways to provide tax breaks to their domestic insurance companies that would pass constitutional muster, and the Florida Legislature responded by repealing its own domestic preference provision and replacing it with a Florida employees' salary credit. Chapter 87-99, Laws of Florida, provided a credit against the net insurance premium tax equal to 10 percent of the amount paid by an insurer in salaries to employees located or based within Florida. "Salaries" did not cover amounts paid as commissions, and "employees" did not include independent contractors or persons required to hold a license under the Florida Insurance Code, with certain exceptions. The sum of these credits and the credits against the corporate income tax and emergency excise tax was limited to 50 percent of the tax due, and any group of insurers that qualified as an affiliated group of corporations was allowed to file a consolidated premium tax return for the purpose of claiming salary credits. This law also increased the insurance premium tax rate to 2.25 percent. These changes were effective July 1, 1988.

Before the changes enacted in ch. 87-99, Laws of Florida, took effect, the Legislature enacted ch. 88-206, Laws of Florida, which increased the employees' salary credit to 15 percent, increased the total combined salary and corporate income tax plus emergency excise tax credits to 75 percent of the tax due, and reduced the premium tax rate back to 2 percent. Chapter 89-167, Laws of Florida, limited the employees' salary credit to 65 percent of the tax due, and further reduced the insurance premium tax rate to 1.75 percent.

In FY 2006-07 the salary credit is expected to reduce insurance premium tax revenue by $203.8 million.

Corporate Income Tax Credit (s. 624.509(4) and (6)), F.S.)

Corporate income taxes and emergency excise taxes that are paid by any insurer are credited against the liability for insurance premium tax for the annual period in which such tax payments are made. For any insurer issuing policies insuring against loss or damage from the risks of fire, tornado, and certain casualty lines, the insurance premium tax against which the corporate income tax and emergency excise tax are credited is the net amount of such tax remaining after credits for payments for firefighters' relief and pension funds and police officers' retirement funds have been taken. Payments of estimated income tax under chapter 220 and of estimated emergency excise tax under chapter 221 are deemed paid either at the time the insurer actually files its annual returns under chapter 220 or at the time such returns are required to be filed, whichever occurs first, and not at any earlier time when payments of estimated tax may have been made. The total of the credit granted for corporate income taxes and emergency excise taxes and the Florida employees salary credit may not exceed 65 percent of the insurance premium tax due after deducting the taxes paid by the insurer for the Municipal Firefighters' Pension Fund and the Municipal Police Officers' Retirement Fund and workers' compensation administrative assessments. The 2006-07 value of the corporate income tax credit is estimated to be $151.8 million.

Police and Firefighters' Pension Credits (ss. 175.141 and 185.12, F.S.)

Municipalities and fire control districts are authorized to impose excise taxes on insurers that do business within their jurisdictions for the purpose of funding the pensions of police and firefighters. Police pensions (ch. 185, F.S.) are funded by .85 percent excise taxes on the premiums for casualty insurance on property within the jurisdiction; firefighters' pensions (ch. 175, F.S.) are funded by a 1.85 percent tax on property insurance premiums. These taxes are fully offset by credits against the state insurance premium tax. For 2006-07, the combined impact of these credits is expected to be a $155.8 million, reduction in premium tax that would otherwise be distributed to the General Revenue Fund.

Certified Capital Company Act (s. 288.99, F.S.)

In 1998, the Legislature created the Certified Capital Company Act. The primary purpose of the act was to "stimulate a substantial increase in venture capital investments in this state by providing an incentive for insurance companies to invest in certified capital companies in this state which, in turn, will make investments in new businesses or in expanding businesses." The incentives to insurance companies for investing were in the form of insurance premium tax credits in amounts equal to the investments in the certified capital companies, known as CAPCOs.

Under Program One of the act, the insurance industry was authorized in 2000 to invest up to a maximum of $150 million in CAPCOs and claim insurance premium tax credits totaling $15 million per year for 10 years. Under Program Two, which was never implemented due to lack of funding, an additional $150 million in insurance premium tax credits would have been allocated by the Office of Tourism, Trade, and Economic Development once certain insurance premium tax collection criteria were met as determined by the Revenue Estimating Conference.

Under Program One, there were three certified companies eligible to receive investment funds from insurance companies and to invest these funds as venture capital. Insurance companies invested a total of $150 million in these three CAPCOs.

In 2005 Program Two of the Certified Capital Company Act was repealed because it had not been funded or implemented. Program One was also repealed in 2010 when its insurance premium tax credits are scheduled to expire. The expected value of CAPCO credits for 2006-7 is estimated to be $14.5 million.

Florida Life and Health Insurance Guaranty Association (Section 631.72, F.S.)

Established by ch. 79-189, Laws of Florida, to protect insurance policy holders and providers of services against insurance company failures, the Florida Life and Health Insurance Guaranty Association is funded by assessments imposed upon Florida life and health insurers and annuity contract providers. These insurers may offset these assessments against their premium tax or corporate income tax liabilities at a rate of 0.1 percent of the amount of such assessment, for each assessment levied before January 1, 1997, for each year following the year in which such assessment was paid until such time as the total of all offsets have been claimed for a given year's assessment. For each assessment levied and paid after December 31, 1996, the amount of offset equals 5 percent of the amount of the assessment for each of the 20 calendar years following the year in which the assessment was paid. This offset is expected to reduce insurance premium tax revenue by $3 million in 2006-07.

Workers' Compensation Administrative Assessment Credit (s. 440.51, F.S.)

The administration of Florida's Workers' Compensation program is funded through assessments against workers' compensation insurance carriers and self-insurers. These assessments are authorized by s. 440.51, F.S., which also provides that the assessments shall be allowed as a deduction against any other tax levied by the state upon the premiums, assessments, or deposits for workers' compensation insurance on contracts or policies of any insurance carrier, self-insurer, or commercial self-insurance fund. Any insurance carrier claiming such a deduction against the amount of any such tax is not required to pay any additional retaliatory tax levied pursuant to s. 624.5091, F.S., as a result of claiming such deduction. This credit has an expected value of $58.3 million in 2006-07.

Community Contribution Tax Credit (s. 624.5015, F.S.)

Community contribution tax credits are authorized under s. 624.5105, F.S., equal to 50 percent of the value of a contribution made by an insurer to:

- an activity undertaken by an eligible sponsor that is designed to construct, improve, or substantially rehabilitate housing that is affordable to low-income or very-low-income households; designed to provide commercial, industrial, or public resources and facilities; or designed to improve entrepreneurial and job-development opportunities for low-income persons;

- provide the investment necessary to increase access to high-speed broadband capability in rural communities with enterprise zones, including projects that result in improvements to communications assets that are owned by a business; or

- museum educational programs and materials that are directly related to any project approved between January 1, 1996, and December 31, 1999, and located in an enterprise zone designated pursuant to s. 290.0065, F.S.

Community contribution tax credits were first authorized in 1984. No insurer may receive more than $200,000 in annual tax credits for all approved community contributions made in any one year, and the total amount of tax credit that may be granted for all programs approved under s. 624.5105, F.S. and ss. 212.08(5)(q) and 220.183, F.S., is $10.5 million annually for projects that provide homeownership opportunities for low-income or very-low-income households and $3.5 million annually for all other projects. The value of the credits in 2006-07 is expected to be insignificant because the credits are mostly taken against sales tax or corporate income tax.

Child Care Credit (s. 624.5107, F.S.)

Section 624.5017, F.S. allows a credit of 50 percent of the startup costs of child care facilities operated by an insurer for its employees against any insurance premium tax due for a taxable year. A credit is also allowed for the operation of a child care facility by an insurer for its employees, in the amount of $50 per month for each child enrolled in the facility.

Any insurer that makes payments directly to a child care facility in the name of and for the benefit of an employee of the insurer in this state whose child attends the child care facility during the employee's working hours is eligible for a credit against any insurance premium tax due for a taxable year. The credit shall be an amount equal to 50 percent of the amount of such child care payments.

An insurer may not receive more than $50,000 in annual tax credits for all approved child care costs that the insurer incurs in any one year, and the total amount of tax credits which may be granted for all programs approved under this section and s. 220.19, F.S., is $2 million annually. In 2006-07, these credits are expected to be worth $.9 million.

Capital Investment Tax Credit (s. 220.191(2), F.S.)

Created in 1998, s. 220.191(2), F.S., grants an annual credit against corporate income tax liability or the premium tax liability generated by or arising out of the qualifying project in an amount equal to 5 percent of the eligible capital costs generated by a qualifying project, for a period not to exceed 20 years beginning with the commencement of operations of the project. The sum of all tax credits provided pursuant to this section may not exceed 100 percent of the eligible capital costs of the project. The annual tax credit granted under this section was limited to the following percentages of the annual corporate income tax liability or the premium tax liability generated by or arising out of a qualifying project:

(a) One hundred percent for a qualifying project which results in a cumulative capital investment of at least $100 million.

(b) Seventy-five percent for a qualifying project which results in a cumulative capital investment of at least $50 million but less than $100 million.

(c) Fifty percent for a qualifying project which results in a cumulative capital investment of at least $25 million but less than $50 million.

In 2006-07, the value of this credit is estimated to be $1.1 million.

Chapter 2006-55, Laws of Florida, extended the credit to the lesser of $15 million or 5 percent of the eligible capital costs made in connection with a capital investment of $250 million located in an enterprise zone that creates at least 1500 jobs paying 200 percent of the average annual private sector wage, for a period not to exceed 20 years beginning with the commencement of operations of the project.

Exemption for Annuities (s. 624.509(8), F.S.)

Since 1980, annuity premiums have been exempt from insurance premium tax if the resulting tax savings are credited to the annuity holder, which includes an employer contributing to employees' pension, annuity, or profit-sharing plans. This exemption has an estimated value of $126.9 million in 2006-07.

Recent Legislative Proposals

Title Insurance

In 2004 and 2006, legislation was proposed (SB 2528 and HB 1653 in 2004 and SB 1714 and HB 857 in 2006) that would have reduced the insurance premium tax on title insurance. Under current law, all title insurance premiums are subject to the 1.75 percent premium tax. The 2004 proposals would have exempted up to 70 percent of the gross receipts from title insurance premiums from this tax. The 2006 proposals would have phased in this exemption, with 20 percent of premiums exempt in 2007, 45 percent exempt in 2008, and 70 percent exempt in 2009 and thereafter. The 2006 proposal was amended to reduce the tax rate for title insurance premiums to 0.6 percent. The recurring revenue impact of the 70 percent exemption was estimated to be an $11.3 million reduction in general revenue; reducing the tax rate was estimated to reduce general revenue by $8.4 million on a recurring basis.

In July 2006, the Florida Office of Insurance Regulation (OIR) published *An Analysis of Florida's Title Insurance Market: Three Studies that Provide a Comprehensive, Multifaceted Review of the Florida Title Insurance Industry*. Two of the studies were conducted by academic experts in the fields of Real Estate Insurance, Risk Management and Insurance, and Economics, and the third study was done by an actuary employed in the Department of Financial Services, Office of the Consumer Advocate. <u>All three studies conclude that most Florida consumers of title insurance services appear to be paying more for comparable title insurance than consumers in other states</u>. As a result of these studies, the Office of Insurance Regulation intends to perform an exhaustive analysis of title insurance premiums and related charges. This analysis will provide the basis for setting premiums and limiting related title services charges by OIR.

Salary Credits Issues

In 2001, the Revenue Estimating Conference was asked to estimate the impact of increasing the amount of the insurance premium tax salary credit to be excluded from the retaliatory tax calculation <u>from 80 percent to 100 percent</u>. The annualized reduction in general revenue was estimated to be $4 million. Legislation filed in 2003 included this proposal. Two years later, legislation increased the amount of salary credit excluded from retaliatory tax calculation from 80 percent to 100 percent for employees whose principal place of employment is in a Florida enterprise zone. The fiscal impact of this provision was expected to be an annualized reduction in general revenue of $200,000.

Insurance Premium Taxes in Other States

All states tax insurance premiums and many allow various credits against the tax. Tax rates range from .5 percent (Illinois) to 4.265 percent (Hawaii). While comparisons are complicated by different rates for different types of insurance, 29 states have higher tax rates than Florida for most types of insurance; four other states tax most insurance premiums at 1.75 percent; the rest of the states have lower rates. Oregon does not have a specific insurance premium tax; insurers are subject to a corporate excise tax. Hawaii is the only state whose insurance premium tax that does not include retaliatory taxes.

Seven states in addition to Florida allow credits based on in-state salaries or for maintaining office facilities in the state. Eleven other states have enacted CAPCO-like credits for capital investments intended to encourage specific kinds of development in the state; three of these states, in addition to Florida, have repealed these programs or deauthorized further expansions.

RECOMMENDATIONS

The insurance premium tax has grown in importance as a source of tax revenue in recent years as annual intangibles tax and estate tax revenues have been reduced to zero. Because of its growing importance as a revenue source, proposals to change this tax warrant careful scrutiny. The amount of credits against the insurance premium tax resulting from Florida salary payments, corporate income tax, firefighters' and police officers' pension fund assessments, and CAPCO funding have been about as large as the general revenue contribution of the tax. Proposals to create additional credits or expand existing ones could significantly affect general revenue.

Although the law provides for a credit of up to 15 percent of salaries of eligible Florida employees, actual salary credits are far less than that amount because of other limitations on the credits. The Legislature may want to examine whether the salary credit as it exists is the best tax policy for the insurance industry in Florida.

Florida’s insurance premium tax rate appears to be in line with other states, and Florida offers credits that are available in some, but not the majority of, other states.