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June 12, 2023

CC:PA:LPD:PR (REG-109309-22), Room 5203
Internal Revenue Service
P.O. Box 7604, Ben Franklin Station
Washington, DC 20044
Via Federal eRulemaking Portal

Re: IRS and REG-109309-22

Dear Sir or Madam:

On behalf of the Independent Community Bankers of America (ICBA)¹, I write to express our concerns about your April 10 proposed rulemaking titled Micro-Captive Listed Transactions and Micro-Captive Transactions of Interest. As written, the proposal would make community bank captive insurance arrangements unworkable and thereby expose banks to unreasonable, uninsured risk. We urge Treasury and the IRS to revise the proposal with a view toward narrowly targeting abuses while preserving legitimate captive insurance arrangements.

Community Banks Use Captives to Manage Risk

A captive insurance company is a subsidiary set up by a small or mid-sized business, such as a community bank, to collect premiums, build reserves, and pay claims that protect the insured business from losses. Often, a group of peer business that have formed captives create a reinsurance arrangement for the payment of large claims.

¹ The Independent Community Bankers of America® creates and promotes an environment where community banks flourish. ICBA is dedicated exclusively to representing the interests of the community banking industry and its membership through effective advocacy, best-in-class education, and high-quality products and services. With nearly 50,000 locations nationwide, community banks employ nearly 700,000 Americans and are the only physical banking presence in one in three U.S. counties. Holding \$5.8 trillion in assets, \$4.8 trillion in deposits, and \$3.8 trillion in loans to consumers, small businesses and the agricultural community, community banks channel local deposits into the Main Streets and neighborhoods they serve, spurring job creation, fostering innovation and fueling their customers' dreams in communities throughout America. For more information, visit ICBA's website at www.icba.org.

The Nation's Voice for Community Banks.®

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Community banks form captive insurance companies to cover risks for which coverage is unavailable or is too expensive in the commercial insurance market. Captive insurance is also used to enhance existing commercial coverage. Bank regulators appreciate the buffer provided by captive insurance which protects bank capital from low frequency but high severity losses such as wire fraud, check-kiting fraud and various cyber related fraud.

This is what Congress intended for community banks and other smaller companies when it created Section 831(b) of the tax code in 1986. Section 831(b) provides a tax election for qualified businesses to be taxed as an insurance company that pays tax on investment income only for any year its written premium is at or below a specified threshold, currently \$2.650 million. In 2015, Congress changed 831(b) to establish essential safeguards against the potential use of the code for estate planning and tax avoidance while also tying the premium threshold to inflation to keep up with economic factors in future years.

Captive insurance is a critical tool for the management and distribution of risks that imperil community banks' capital and ability to continue to lend and support their communities. Community banks disproportionately lend to small businesses and farms and thus play a critical role in American economic life. Captive insurance helps community banks remain competitive with large, national banks, most of which have captive insurance structures, as well as nonbank competitors, which enjoy tax and regulatory advantages. A competitive landscape for financial services benefits consumers and small businesses.

The Proposed Rule Is Overreaching and Should Be Revised

The proposed rule provides that an 831(b) captive must have a ratio of claims and expenses paid to premiums collected (a "loss ratio") of at least 65 percent over a period of 10 years. If the captive does not meet or exceed this threshold, it is designated a "listed transaction," which is essentially a tax shelter. We believe this to be an overreach that would make many community bank captive insurance arrangements unworkable.

This arbitrary loss ratio and period do not consider catastrophic risks with low frequency and high potential severity. We believe that a better standard for evaluating whether a captive should be classified as a listed transaction is to assess whether an independent, licensed actuary annually determines the premiums. In addition, we are particularly concerned about a look-back that might trigger prior year tax liability including interest and penalties. Community banks that have complied with the law must not be subject to a punitive retroactive tax liability.

For these reasons, we urge Treasury and the IRS to substantially revise the proposal rule to target abuses while preserving the ability of community banks to insure themselves against catastrophic loss through the use of captive insurance arrangements.

We appreciate the opportunity to comment on the proposed rule. If you have any questions or would like to discuss our letter in further detail, please do not hesitate to contact Alan Keller (alan.keller@icba.org, 202-821-4468) or Steve Keen (steve.keen@icba.org, 202-821-4459).

Thank you for your consideration.

Sincerely,

/s/

Anne Balcer
Senior Executive Vice President
Chief of Government Relations