Senate Fiscal Agency
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BILL ANALYSIS

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Senate Bill 406 (as reported with amendment)
Sponsor: Senator Jon Cisky
Committee: Finance

CONTENT

The bill would amend Section 22a of the Single Business Tax (SBT) Act to provide that the tax base and adjusted tax base of an insurance company would be equal to 25% of the insurer's gross receipts, as apportioned under the Act, excluding receipts on the sale of annuities and receipts on "all reinsurance transactions". Currently, the SBT Act provides that the tax base and adjusted tax base are equal to 25% of the insurer's gross receipts, as apportioned under the Act, excluding receipts on the sale of annuities and receipts on "the sale of reinsurance".

The bill provides that its provisions to amend Section 22a would be retroactive and effective beginning August 3, 1987; Section 22a was first applied to the tax base of insurance companies on that day.

MCL 208.22a Legislative Analyst: G. Towne

FISCAL IMPACT

Department of Treasury audits reveal that insurance companies have not been including reinsurance commissions in their SBT base. If all insurance companies had been paying the SBT on reinsurance commissions, the Department estimates that the total SBT liability on these commissions would have amounted to $4.7 million a year.

Reinsurance occurs when an insurance company buys insurance from another company to help cover the financial risk it has taken in selling policies. For example, if insurance company A sells a policy worth $500,000, but is able to cover only a policy up to $400,000, then company A will buy insurance from company B to cover the last $100,000 of the original policy. The cost of buying this reinsurance is figured in the cost of the original $500,000 policy that company A charges its customer. The premium charged the customer for the $500,000 policy by insurance company A is included in company A's SBT tax base, while the premium for the reinsurance is not included in company B's SBT tax base, because company A already was taxed for the premium. What is at issue, however, is whether the commission payment that company B pays company A under some reinsurance transactions, should be taxed under the SBT. The commission is paid to reimburse company A for part of its expenses incurred in selling and maintaining the original policy to the customer. A major component of this cost is the commission paid to the insurance agent who originally sold the policy to the customer. The Department of Treasury has ruled that reinsurance commissions are income and, therefore, should be included in the tax base. The bill would exempt all reinsurance transactions, including reinsurance commissions, from the SBT.

Date Completed: 5-3-95 Fiscal Analyst: J. Wortley

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