



## WHAT IS A CAPTIVE INSURANCE COMPANY?

The Captive Insurance Company solution has long been utilized by The Fortune 1500 companies. Congress has enacted tax incentives to encourage the formation of captives for the small and medium sized business market. By definition a Captive Insurance Company is a wholly owned company that insures the risks of companies affiliated with the shareholders of the captive.

The origin of the Captive dates back to the 1870s when Protection and Indemnity associations were founded. "Captives", as the term was coined by Fred Reiss, realized growth in the 1960s, primarily in off-shore insurance jurisdictions.

Today there are an estimated 6000 captives worldwide of which Single Parent and Group captives represent 74% of managed captives. Insurance jurisdictions, otherwise known as "Domiciles" located on shore (U.S.) represent over 60% of the captives currently in operation.

## BASIC REQUIREMENTS FOR TAXATION AS AN INSURANCE COMPANY

- ▲ Without a Captive self insurance reserves are not deductible.
- ▲ For premiums to be deductible, the Captive must be recognized as an insurance company for federal income tax purposes.
- ▲ Risk transfer.
- ▲ Risk distribution.
- ▲ Adequately capitalized.
- ▲ Captive conducts itself like an insurance company.
- ▲ Serves a risk management purpose.
- ▲ Captive insurance tax rulings considered for this opinion include: IRC Rev. Rul. 2002-89, 2002-90, 2002-91 and 2005-40
- ▲ Insurance company taxation creates the risk management benefit/cash flow.

## TAX ADVANTAGES OF A CAPTIVE INSURANCE COMPANY

Although tax benefits should not be the primary purpose of forming a captive, the following benefits are available with a properly structured Captive Insurance Company.

- ▲ A properly structured Captive will allow for deductions of premiums.
- ▲ This creates more cash available for risk management.
- ▲ Generally, the Captive can accelerate the deduction for unpaid losses unlike other taxpayers because loss reserves are deductible.
- ▲ Small insurance company provision allows for \$1.2MM annual premium exemption.



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