TAKING NO PRISONERS: CAPTIVE INSURANCE AS AN ALTERNATIVE TO TRADITIONAL OR COMMERCIAL INSURANCE

CONSTANCE A. ANASTOPOULO*

"[P]erhaps no modern commercial enterprise directly affects so many persons in all walks of life as does the insurance business."[1]

I. INTRODUCTION

As Justice Hugo Black stated in 1944, insurance affects most everyone, as it "touches the home, the family and the occupation or the business of almost every person" who wishes to manage risk.[2] Protection is, of course, the primary reason consumers purchase insurance and those purchases are made almost exclusively through traditional insurance companies. However, what if there exists an alternative to the customary forms of insurance and the insurance company in terms of the costs of insuring risks and those associated with paying claims? What if this option provides protection from risk, reduces costs and provides tax benefits, as well as providing non-insurance benefits?

These questions consider the issue of a space that exists between traditional methods of self-insurance and insurance available in the commercial market. Captive insurance companies are a gap-filler between these two common approaches to insurance. This article analyzes captive insurance companies as an alternative to the services provided by established insurance companies, the steps necessary to assess the practicality of a captive and the various choices available to consumers by means of a captive. Captives are not new to the insurance industry, but their creation and use is unfamiliar to many. This article will review the historical creation of captive insurance companies and explore the benefits and risks of this alternative solution to conventional insurance.

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* Associate Professor of Law, Charleston School of Law; J.D., University of North Carolina School of Law. I would like to thank Thomas P. Gressette, Jr. for his helpful comments on earlier drafts of this Article. I would like to thank my law clerk and research assistant, Lane Jefferies, a third-year student at the Charleston School of Law, who was instrumental in the research and writing of this article. In addition, I would like to thank Akim, without whom none of this would be worthwhile.

[1] United States v. Se. Underwriters Ass'n, 322 U.S. 533, 540 (1944).

[2] *Id.*

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Additionally, with access to a large, private closely-held company, this article will analyze the applicability of a captive through a case study using actual data from this company in order to walk the reader through the necessary steps when contemplating and implementing a plan to establish a captive insurance company. Captive insurance companies are not appropriate for every entity or for every risk. However, analyzing real, rather than theoretical data will assist to identify the important areas of consideration to determine if a captive is appropriate in certain situations.

The focus of this paper is not to offer specific insurance or tax advice. Rather, it is to provide a useful tool in determining when and how a captive insurance company is established and what criteria and information are necessary to making that decision. Further, this article reviews a practical example and points out the differences in types of captives, the extent to which states have regulated captives and how various domiciles treat captives differently. Therefore, Part I of this Article focuses on the evolution of the captive insurance company, including the history leading up to and culminating in enabling legislation for the creation of the business. Part II delves into the nature of how captives work in practice and evaluates the benefits and risks associated therewith. This focus permits an objective overview of the advantages and perils associated with captive insurance companies. Part III addresses regulations of captives including statutory provisions, state insurance departments and domicile choice considerations. Part IV examines the various types of captive insurance entities generally. Part V provides an in-depth analysis through case study using a private closely-held company as a business considering the establishment of a captive. This case study will consider the data and steps necessary in evaluating the viability and usefulness of the captive insurance company. Finally, this article concludes that a captive may, in fact, be a practical and feasible solution to rising premiums, control of costs and an opportunity to take advantage of tax savings, while also providing important non-insurance benefits. However, careful consideration must be given before the decision to create a captive is made.

Before discussing captive insurance companies, it is important to understand the state of the insurance industry generally. As insurance contracts and the obligations associated therewith grow more complicated and far-reaching, courts have witnessed an increase in the number of claims being filed and litigated, both nationally and regionally. Insurance companies owe their insureds a duty not to act in bad faith, or a duty to act with good faith and fair dealing towards their insureds.[3] This duty forms the basis of bad faith claims that insureds pursue against their insurers for the

[3] Charleston Dry Cleaners & Laundry, Inc. v. Zurich Am. Ins. Co., 586 S.E.2d 586, 588 (S.C. 2003).

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insurers' failures in treating their insureds with good faith.[4] Bad faith claims arise often in situations where the insurer refuses to indemnify the insured or to pay a first party claim of the insured. In either case, it stems from a break down in the relationship between the insurer and its insured. Innumerable questions abound. Are claims against insurers increasing because insureds continue to be dissatisfied with insurers' services or are other factors at play? What role does the insurance company itself play in the increase in litigation? Importantly, insurance policies are only as good as the insurance company's willingness to pay.[5] An insured's confidence is only as secure as his or her reasonable belief the policy will adequately provide protection. Since the business of insurance affects so many aspects of life and business, it is necessary to consider alternatives to established methods of managing risk. These alternatives include the consideration of the establishment of captive insurance companies.

II. INSURANCE, GENERALLY, AND THE HISTORY OF CAPTIVES

Insurance is most simply defined as a "contract where one undertakes to indemnify another or pay a specified amount upon determinable contingencies."[6] Insurers depend on their ability to calculate the predictability of the loss and their skill at pooling the risk and diversifying the risk to reduce the amount of variance in the loss occurring.[7] This requires predictability in the occurrence and extent of the loss in order to be financially viable at a reasonable premium to the insured and to the insurer. The premium is set to allow the insurer to adequately maintain reserves to pay claims as they occur.[8] Due to keen governmental interest in having its citizens adequately protected, the insurance industry is regulated through state legislatures, regulatory agencies created by statute and the judicial system.[9] Insurance is a trillion-plus dollar a year business.[10] In 2012 the U.S. insurance industry's net premiums written totaled $1.1 trillion.[11] Global insurance premiums in 2009 were $4.1 trillion, with the United

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[4] *See id.* at 588 n.2.
[5] *See* S.C. CODE ANN. § 38-59-20 (2012) (setting forth elements of bad faith refusal to pay).
[6] *Id.* § 38-1-20(25).
[7] *See generally* JUDY FELDMAN ANDERSON & ROBERT L. BROWN, RISK AND INSURANCE (2005), *available at* http://www.soa.org/files/pdf/P-21-05.pdf.
[8] *Id.*
[9] *See generally* Gerald M. Finkel, South Carolina Cases and Materials on Insurance Law 1 (2013) (unpublished course packet) (on file with Charleston School of Law).
[10] *Insurance Industry at a Glance*, INSURANCE INFORMATION INSTITUTE, www.iii.org/facts_statistics/industry-overview.html (last visited Oct. 28, 2013).
[11] *Id.*

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States representing $1.14 trillion of that number.[12] In 2012, there were more than 6000 insurance companies in the United States.[13]

Because of numerous factors, the cost of insurance continues to rise each year.[14] There is the obvious explanation in terms of escalating costs associated with various types of risk. For example, as incidents of piracy have increased on the seas, shipping companies have seen skyrocketing insurance premiums associated with protecting their cargoes and crews.[15] In addition, adding to these increases are rising administrative costs, including the processing and payment of claims, and costs associated with litigation over claims. All of this translates into higher premiums for insureds for the same or less coverage.

As a result, consumers seek other approaches to traditional methods of insurance, including self-insurance and commercial insurance, to control these costs and manage their risks. Insurance remains a flexible and elastic industry transforming different types and methods of insurance to address changing needs. Frederic Reiss, who first introduced the concept of a single client insurer in the 1950s, coined the term "captive" to apply to this new initiative.[16] The idea continued to evolve over the next few years based on several aspects including interpretation of the role and treatment of this entity by the IRS and the courts.[17] Not only is the appropriateness of captives evaluated based on risk management decisions, but also this decision is driven primarily by fact-intensive choices, state regulations and tax consequences. Many jurisdictions license captives with the primary jurisdiction selected for the captive known as the captive's domicile.[18] Many states, for instance, have enacted statutory schemes enabling the establishment of captives.[19] Currently, there are more than twenty states that have enacted legislation to create captives and many offshore domiciles exist as well.[20] Several of these statutes explicitly state that these statutory

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[12] Marko Maslakovic, *Insurance 2010*, THE CITY UK, 3 (Dec. 2010), http://www.thecityuk.com/assets/Uploads/Insurance-2010.pdf.
[13] *Insurance Industry at a Glance*, *supra* note 10.
[14] Phil Gusman, *Recent Reports Outline Stiff Industry Challenges Despite Rising Rates*, PROPERTY CASUALTY 360 (Aug. 16, 2013, 3:22 PM) http://www.propertycasualty360.com/2012/08/16/recent-reports-outline-stiff-industry-challenges-d.
[15] Stella Sakellaridou, *Maritime Insurance & Piracy*, 9 (2009), *available at* http://www.aida.org.uk/AIDAEurop/AIDAStellaspaper.pdf.
[16] CATHERINE R. DUFFY, HELD CAPTIVE, A HISTORY OF INTERNATIONAL INSURANCE IN BERMUDA 39 (2004).
[17] *See generally*, F. HALE STEWART, U.S. CAPTIVE INSURANCE LAW 69–211 (2010).
[18] *Domicile Information*, GLOBAL CAPTIVE INSURANCE AND WEALTH PROTECTION EXPERTS, http://captiveexperts.com/Domicile_Selection.html (last visited Oct. 28, 2013).
[19] *Id.*
[20] *See* Table A.

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provisions provide for general types of captive insurance companies or specialized forms of captives, which may include entities known as cell captives.[21] Whatever form the captive takes, the flexibility as well as other benefits have made captives an attractive alternative to usual and established kinds of insurance.

By way of illustration, states as regionally varied as South Carolina, Colorado and Connecticut have enacted legislation permitting the establishment of captive insurance companies in their states.[22] Additionally, other states as diverse as Hawaii, Utah and Alabama permit captives and cell captives through enabling legislation.[23] States are not the only jurisdictions favorable to the establishment of captive insurance companies, however. An assortment of other jurisdictions permits captives including South America, Europe, the Caribbean Islands, Canada, New Zealand and Asia.[24] The selection of the domicile is an important consideration when deciding whether a captive insurance company is the appropriate vehicle for a particular entity to address their needs. Factors to consider when choosing a domicile will be discussed more fully below.

A company formed to insure the risks of its parent corporation defines a captive insurance company.[25] In other words, the insuring entity is a "captive" of the parent, insuring risks specifically associated with that parent company. A captive is a limited purpose, licensed insurance company, the main business purpose of which is to insure the risks of the captive's owner(s).[26] A pure captive insures only its parent and parent affiliates.[27] It is owned and controlled by one owner and is the most common structure among captives.[28] Historically, two primary motivations guided the creation of the concept of the captive insurance company. These incentives are: (1) when insurance cannot be purchased from commercial insurance companies for a business risk or insurance can be purchased but at a prohibitive cost; and (2) the fact that premiums paid to a captive insurance company are deductible as a business expense for tax purposes

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[21] *Id.*
[22] *Id.*
[23] *Id.*
[24] *Id.*
[25] HARVEY W. RUBIN, BARRON'S DICTIONARY OF INSURANCE TERMS (5th ed. 2008).
[26] Christina Kindstedt, *Non-traditional Insurance Mechanisms: Opportunities, Threat or Both?*, WILLIS (Apr. 11, 2013), http://www.piaa.us/meetings/marketing/pdf_files/Kindstedt.pdf.
[27] S.C. CODE ANN. § 38-90-10(9) (2012).
[28] Shanique Hall, *Recent Developments in the Captive Insurance Industry*, CENTER FOR INS. POL'Y & RES. NEWSL. (Jan. 2012), http://www.naic.org/cipr_newsletter_archive/vol2_captive.htm.

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according to the IRS.[29] The first of these led to the early development of captives in industries involved in diverse and hard to insure activities such as mining,[30] offshore oil development[31] and international shipping.[32] This second consideration provides an attractive alternative to self-insurance, which does not permit the deduction of payments to a reserve fund used to pay a claim as a business expense and therefore these payments are not deductible.[33]

Early on, companies had the idea to establish reserve funds for contingencies associated with these complicated and often hard-to-insure risks, rather than seek to purchase insurance to protect against these types of risks.[34] Additionally, these companies attempted to deduct the payments to the reserve funds as business expenses, believing that the expenses associated with insuring themselves against risk were, in fact, business expenses.[35] However, the IRS challenged the deductibility of these payments based on a strict interpretation of the code and on concerns of earnings manipulation.[36] The Service essentially argued that these payments were not for insurance because there was no shifting of risk and therefore payments made could not be deducted as an insurance or business expense.[37] Even the disallowance of the deductibility of these payments was not enough to offset the necessity to create alternatives to established methods of insurance procurement, however. Therefore, self-insurance remained an option for these hard-to-insure risks. Private insurance providers and companies with these types of risks banded together to continue the push for the development of new and unconventional solutions. This led to the idea of captive insurance companies. Despite objections from the Service, states began to enact enabling legislation to allow the establishment of captives in an effort to attract businesses to their states.[38] By permitting the creation of a captive insurance company by individual companies, states could attract entire industries that faced the same difficulties that led to the creation of captives in the first place. In

[29] Rev. Rul. 2002-89, 2002-2 C.B. 984; Rev. Rul. 2002-90, 2002-2 C.B. 985; Rev. Rul. 2002-91, 2002-2 C.B. 991.
[30] *See, e.g.*, Spring Canyon Coal v. Comm'r, 43 F.2d 78 (10th Cir. 1930).
[31] *See, e.g.*, Ocean Drilling & Exploration Co. v. United States, 988 F.2d 1135 (1933).
[32] *See, e.g.*, The Harper Grp. v. Comm'r, 96 T.C. 45 (1991), *aff'd* The Harper Group v. Comm'r, 979 F.2d 1341 (9th Cir. 1992).
[33] *See* The Harper Grp., 96 T.C. at 47.
[34] *See, e.g.*, Pan-American Hide Co., 1 B.T.A. 1249, 1250 (1925).
[35] *Id.*
[36] Spring Canyon Coal v. Comm'r, 43 F.2d 78, 79 (10th Cir. 1930).
[37] *Id.* at 80; *see also* Carnation Co. v. Comm'r , 71 T.C. 400 (1978); Cougherty Packing Co. v. Comm'r, 84 T.C. 948 (1985); Beech Aircraft Corp. v. United States, CIV. 82-1369, 1984 WL 988, at *1 (D. Kan. July 3, 1984), *aff'd*, 797 F.2d 920 (10th Cir. 1986).
[38] *See e.g.*, S.C. CODE ANN. § 38-90-10 (2012).

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addition, courts began to look more favorably on the use of captives. Cases involving the treatment of captives continued to bubble up through the courts. In *Humana v. Commissioner*,[39] the court ruled for the first time that premiums paid from one subsidiary to another subsidiary for insurance payments were deductible because the subsidiary did not own any of the captive's stock.[40] Following *Humana*,[41] the court in *Harper Group v. Commissioner*[42] established that, in addition to stock ownership, the court would assess "(1) whether the arrangement involves an 'insurance risk'; (2) whether there was both risk-shifting and risk-distribution; and (3) whether the arrangement was for 'insurance' in its commonly accepted sense" in order to determine the deductibility of these payments.[43] These decisions helped lead to the continued development and use of captives.

Ultimately, these court decisions permitted payments made to the captive insurance company to be treated as business expenses under the Internal Revenue Code.[44] As a result, captives offer significant advantages over established methods of insurance or self-insurance often used to address costly or hard to insure risks. Payments made to fund the captive against various or specific risks are significant and their deductibility as expenses is one of the main attractions to the establishment of the captive over self-insurance reserve fund.

In addition to pure captives, there are several other types of captives available and it is useful to be familiar with these other forms. The most common of these forms are discussed below. As insurance needs to change with an ever-changing world, the insurance industry responds with alternative forms of insurance or insurance entities to address this shifting market. Captive insurance companies are just another example of how the insurance industry remains fluid and flexible in adjusting to these changes. The appropriate form is just another consideration in the process of the decision to create a captive insurance company. These various forms permit the parent or parent group to formulate the suitable vehicle necessary to address the need.

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[39] 881 F.2d 247 (6th Cir. 1989); Harper Grp. v. Comm'r, 96 T.C. 45, 58 (1991), *aff'd*, 979 F.2d 1341 (9th Cir. 1992).
[40] *Humana*, 881 F.2d at 253, 257.
[41] *Id.*
[42] *See generally Harper Group*, 96 T.C. 45.
[43] *Id.*
[44] *See* Rev. Rul. 2002-89, 2002-2 C.B. 984; Rev. Rul. 2002-90, 2002-2 C.B. 985; Rev. Rul. 2002-91, 2002-2 C.B. 991.

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III. How Captives Work

A. *Benefits*

Captives offer several benefits over insurance offered through customary insurance companies. Foremost is that captives simplify and reduce costs.[45] There are several ways captives achieve this. Because captives are designed specifically to address the parent's risk needs, they improve coverage availability and afford flexibility.[46] When a company is involved in concerns that are difficult or costly to insure, a captive offers the parent the opportunity to evaluate and assess the risk based on its own experiences as opposed to industry-wide calculations.[47] Therefore, the company is no longer beholden to the standard market and the possible mismanagement by others within the industry that leads to greater risk calculations. Captives thus address risk positions for the parent based solely on the parent's actual risk exposure and history, rather than an industry-wide calculation. This allows the parent the ability to potentially lower the costs associated with insuring the risks because the risk of casualty is determined by its own management decisions. Captives also provide flexibility in that they can be designed to address risks associated with varied lines specific to the parent's business including general liability, professional and products liability, director and officer liability, employment practices liability, environmental liability and workers' compensation, to name a few.[48] This elasticity permits the parent to design the captive in such a way as to address specifically its individual needs or combination of needs without having to swallow an industry-mandated model or risk exposure.

Another advantage of captives is that because the parent owns the captive, there exists a symbiotic relationship. This relationship is premised on the maximization of benefits to the parent. Thus, when the parent incurs a loss within the risk contemplated by the captive, the parent and captive have the same incentive to pay the claim from the captive's reserves. This is uniquely different from the often-adversarial relationship that exists

[45] *Why Form a Captive?*, ALTA HOLDINGS, LLC, http://www.altaholdings.com/why-form-captives/default.aspx (last visited Oct. 28, 2013).
[46] *See, e.g.*, Beech Aircraft Corp. v. United States, CIV. 82–1369, 1984 WL 988 (D. Kan. July 3, 1984), *aff'd*, 797 F.2d 920 (10th Cir. 1986) (involving airplane manufacturer that formed a captive in order to exert greater control over litigation and settlement).
[47] *See, e.g.*, Ocean Drilling & Exploration Co. v. United States, 988 F.2d 1135, 1138 (Fed. Cir. 1993) (involving offshore oil exploration company that formed a captive to avoid paying premiums that were based on the significantly worse loss history of other firms).
[48] Hall, *supra* note 28.

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between insureds and insurers in the commercial market. In the commercial market, the insurer has the incentive to deny claims or delay in paying claims. This allows the commercial insurer to keep premiums paid by insureds while paying as few claims as possible, thereby maximizing its own profits. Therefore, commercial insurance creates contrary purposes between insureds and insurers. None of these concerns exist with the captive insurance companies.

In addition to the monetary advantages regarding deductibility of payments and lowering of costs, another important aspect of captive insurance companies is their ability to provide non-insurance benefits. Foremost among these non-insurance benefits are: (1) estate planning and wealth transfer; (2) asset protection; and (3) taxable income smoothing or shifting.[49] By virtue of the fact that the captive is a wholly-owned entity of the parent, yet a separate and distinct insurance company, the establishment of the captive allows the parent to fund the captive with significant contributions to insure against possible risks, while still remain an asset of the parent. The placement of these funds in the captive is not paid to an outside entity. Thus, when and if the parent decides to discontinue operation, the funds held by the captive continue to belong to the parent as any other asset. The owner(s) of the parent can maintain ownership of the contributions made to the captive. This is distinct from the traditional form of insurance where the owner pays an outside entity the insurance premium, which then belongs to the outside insurer. Therefore, all insurance premiums paid to the captive continue to be assets of the parent and allow the parent to transfer wealth through the captive to the successors of the parent.

While the allure of the captive in permitting premiums to be deductible while remaining an asset of the parent is appealing, captive insurance companies do not come without risks. Contemplation of these risks is necessary in assessing the viability and applicability of the captive insurance company for any entity considering its establishment.

B. *Risks*

While captives offer significant benefits, they also have inherent risks. Primarily, risks associated with captives include: (1) limited risk diversity; (2) costs and capitalization; (3) state regulations; (4) access to re-insurance; and (5) the understanding that establishing a captive insurance company must be undertaken as a long-term strategy.[50]

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[49] *Why Form a Captive?*, *supra* note 45.
[50] *Captive Risks*, GLOBAL CAPTIVE INSURANCE AND WEALTH PROTECTION EXPERTS, http://captiveexperts.com/Captive_Risks.html (last visited Oct. 28, 2013).

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While flexibility and risk management based upon the experiences of the parent are benefits, one of the advantages of traditional insurance is risk pooling or diversification.[51] The concept of insurance is based upon the idea that insurers accept the transfer of risks and then pool them. "By insuring a large number of insureds posing homogeneous and independent risks, an insurer can reduce the amount of variance in its expected losses to a very small range."[52] Thus, insurance by design is a vehicle that allows parties with unrelated risks to spread the risks across large numbers, thereby reducing the exposure of any one event.[53] Obviously, the risk of the captive is that it does not provide for risk-pooling and cost-spreading because it is formed to manage the risks associated only with the parent or relatively small group within an industry such as an association. The potential effect is to obviate the advantage underlying insurance by its nature, which is that of spreading the risk.

As a result, limited risk diversity affects costs and capitalization.[54] The lack of risk-pooling leads to potential greater costs associated with a loss related to the individual risk. This, in turn, results in a necessary greater investment in the captive to insure against that risk, as opposed to the lower cost associated with a risk pool. In order for a captive to have an impact in terms of sufficient reserves to insure against the risk, it requires a material amount of capital/premium funding to offset the limited risk diversity.[55] Thus, there is an opportunity cost associated with the lower yield capital investment in the captive versus investing in higher yielding vehicles available in the market. Consequently, the commercial market may offer lower premiums, at least in the short term, because of its ability to spread the costs associated with risks relative to the initial cost of funding the captive for that same risk.[56]

These are a few of the considerations associated with the risk of establishing a captive. Further evaluation of the risks is contemplated below. It is important to understand both the risks and benefits before a company should undertake to create a captive insurance company.

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[51] KENNETH S. ABRAHAM, INSURANCE LAW AND REGULATION, CASES AND MATERIALS 4 (5th ed. 2010).
[52] *Id.*
[53] *Id.*
[54] *Id.*
[55] Richard Klumpp, *Capitalizing a Startup Captive*, WILMINGTON TRUST (Apr. 18, 2013), http://blog.wilmingtontrustcaptiveinsurance.com/blog/?Tag=capitalizing%20a%20captive.
[56] Richard Klumpp, *5 Key Questions: Is Captive Insurance Right For You?*, WILMINGTON TRUST (Apr. 27, 2011), http://blog.wilmingtontrustcaptiveinsurance.com/blog/bid/48435/5-Key-Questions-Is-Captive-Insurance-Right-For-You.

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IV. Regulation, Generally

A. *Domicile Selection*

Several factors should be contemplated when selecting a domicile, including the regulatory climate of the state or other jurisdiction, the infrastructure of possible offshore domiciles, both in contrast with each other and as opposed to a United States domicile, and tax consequences associated with the jurisdiction.[57] Domiciles such as Bermuda and Vermont have enabled captive formation for over thirty years and the law in these jurisdictions is well settled and stable.[58] Like other insurance companies, captive insurance companies in the United States are created pursuant to the state law of their state of domicile, and must be licensed by the states in which they operate.[59] This is an important factor in the creation of a captive insurance company because registration as an insurance company in the state of domicile has implications for tax treatment of the premiums paid to the captive. In addition, there are a number of federal regulations, to which captives must comply that also effects the ability to deduct premium payments made to the captives as a business expense.[60] Some states continue to fine-tune their statutes that provide for the establishment of captives in the states. For example, Florida completely revised its little-used captive insurance legislation in July 2012 with the intention of competing with more popular domiciles such as Vermont and Delaware in an effort to attract some of the businesses lost to states with more liberal or established legislation.[61] How the Florida courts construe the new legislation remains to be seen, but the state has identified that a favorable captive environment can be attractive to individual companies or industries. In addition to the stability of the regulatory climate, different jurisdictions have different minimum capital requirements for captives.[62] Consequently, in addition to understanding the funding associated with the risk or risks against which the captive is insuring, the parent needs to consider the funding requirements of the jurisdiction of the domicile that may be significant. This too has an impact on the cost of establishing and maintaining the captive.

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[57] William P. Elliott, *A Guide to Captive Insurance Companies (Part 1)*, Apr. 2005, J. INT'L TAX'N, at 28.
[58] *Id.*
[59] *See e.g.*, S.C. CODE ANN. § 38-90-20 (2012) (setting forth statutory requirements for licensing of a captive in South Carolina).
[60] *See generally* Bobbe Hirsh & Alan S. Lederman, *The Service Clarifies the Facts and Circumstances Approach to Captive Insurance Companies*, J. OF TAX'N, Mar. 2004, at 168.
[61] Domenick R. Lioce, *Captive Insurance Companies: Florida Enters the Arena*, FLA. B.J., July–Aug. 2013, at 51.
[62] *See* Gordon A. Schaller & Scott A. Harshman, *The Use of Captive Insurance in Estate and Business Planning*, EST. PLAN., Sept. 2008, at 26.

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Because one of the first decisions for a company to make when deciding whether to create a captive has to do with the choice of domicile in which to establish the captive, the impact of this decision cannot be overstated. Four main areas comprise factors considered in domicile selection: (1) taxes, (2) regulation, (3) infrastructure and (4) perception.[63] Tax issues include choosing a recognized domicile so as not to offend considerations with the IRS.[64] This is an important consideration because the IRS can be suspicious of off shore domiciles and apply strict scrutiny to the treatment of the payments to the captive. Additionally, excise and premium taxes as well as income taxes levied by the domicile must be deliberated.[65] For instance, although many offshore domiciles treat captives favorably, use of such a domicile may trigger U.S. excise or premium taxes that negate the advantage gained by the selection of an offshore domicile.[66] Thus, tax consequences are important considerations when choosing the appropriate domicile.

As to regulation, ownership structure, coverages allowed by the domicile and capitalization options are foremost considerations.[67] Different states as well as offshore domiciles have different capitalization requirements regarding necessary reserves. The amount of reserve requirements affects both the initial establishment of the captive and its funding going forward. With regard to infrastructure, the parent should consider ease of accessibility to the domicile, operating flexibility, as well as the availability, quality and costs associated with service providers.[68] Because establishing and managing a captive requires diverse professionals—attorneys, claims administrators, actuaries, accountants, bankers, etc.—the infrastructure of the selected domicile is also important.[69] Hence, the ability to engage experienced professionals, particularly those familiar with captives specifically, can affect costs, not only in establishing the captive, but also in the managing of claims and costs associated with the administration of the captive. Lastly, the parent should contemplate its perception regarding whether it is appearing to select a "tax haven" if necessary, concerns about corporate governance, shareholder rights if appropriate and again the potential to offend the IRS.[70]

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[63] *Domicile Selection*, ALTA HOLDINGS, LLC, http://www.altaholdings.com/domicile_selection/default.aspx (last visited Oct. 28, 2013).
[64] STEWART, *supra* note 17.
[65] *Id.* at 30.
[66] Elliot, *supra* note 57, at 28.
[67] STEWART, *supra* note 17, at 62–67.
[68] *Id.* at 27–30.
[69] *Id.*
[70] *Id.*

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As a result, important considerations regarding regulation of captives are key factors in determining the efficacy and appropriateness of a captive insurance company for any entity considering it as an alternative to traditional self-insurance or commercial insurance.

B. *State Insurance Departments*

Once the choice of appropriate domicile is made with consideration of the factors above, if the parent chooses a state, the parent must recognize the role of state insurance departments in the regulation of insurance generally and the captive specifically. State insurance commissioners, some of whom are appointed and some of whom are elected, run state insurance departments.[71] Evaluation of the regulatory environment of the state toward the insurance industry generally and toward captives specifically should thus be considered.

V. TYPES OF CAPTIVES

In addition to understanding the treatment of captives generally, it is important to understand the different forms of captive insurance companies. These forms have developed in the same way captives developed generally, in that they are in response to needs of the parent. There are three main forms of captive insurance companies. While this list is not exhaustive, it is important to understand these main forms.

A. *Single Parent*

A "single parent" captive is exactly what its name suggests—a captive insurance company owned entirely by one parent company.[72] For example, an international shipping company might establish a wholly owned insurance company to insure against losses of the packages it ships. Early in the history of captives, the IRS challenged their classification as insurance companies because, the Service argued, there was no shifting of risk between entities and no spreading of risk.[73] Under the Service's theory, there was no shifting of risk because the value of the captive would decrease by the amount of the claims it paid.[74] Because the parent company owned 100% of the captive, its value would decrease by the same amount.[75]

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[71] Ben Nelson, *About the NAIC*, CENTER FOR INS. POL'Y & RES. NEWSL., http://www.naic.org/index_about.htm (last visited Oct. 28, 2013).
[72] Humana Inc. v. Comm'r, 88 T.C. 197, 216 (1987), *aff'd in part, rev'd in part*, 881 F.2d 247 (6th Cir. 1989) (Whitaker, J. concurring).
[73] *Id.*
[74] Beech Aircraft Corp. v. United States, CIV. 82–1369, 1984 WL 988, at *5 (D. Kan. July 3, 1984), *aff'd*, 797 F.2d 920 (10th Cir. 1986).
[75] *Id.*

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As a result, according to the Service, it was as if the parent simply paid for the lost package itself, and thus the captive was just a pass through of the risk to the parent without shifting that risk.[76] If this were the case, the Service argued, premium payments to the captive would not be deductible as insurance expenses.[77]

Fortunately, the deductibility of insurance premiums paid to single parent captives is rarely an issue now because of two relatively recent revenue rulings. The first safe harbor is found in Revenue Ruling 2002-89, 2002-2 C.B. 984.[78] This decision provides a protection where more than 50% of the captive's risk exposure comes from insuring third parties.[79] For instance, in the case of the international shipper mentioned above, in addition to the standard $100-per-package insurance for which the shipper pays, the shipper might offer optional additional insurance to its clients. If more than 50% of the captive's risk is derived from these optional insurance contracts with the clients themselves, then the captive falls within the safe harbor.[80] As a result, premium payments made by the parent to the captive are treated as deductible insurance payments.[81] It is important to keep in mind that the 50% threshold is merely a safe harbor; it is possible to have premium payments paid to a captive with less than 50% outside risk treated as deductible.[82] However, the presumption is against such treatment, which puts the burden on the parent to show why such treatment is appropriate.

Revenue Ruling 2002-90, 2002-2 C.B. 985 provides a second safe harbor where the captive insures at least twelve of its sister entities.[83] This protection applies when: 1) the parent owns 100% of the captive; 2) the parent owns 100% of each of at least twelve other companies; 3) each of the other (brother/sister) companies represents between 5% and 15% percent of the risk that the captive insures; and 4) each of the brother/sister companies is recognized by the IRS as a separate taxable entity.[84] For example, consider a restaurant holding company that owns 100% of twelve separate fast food franchises. Each franchise respects the appropriate corporate formalities and pays its own tax liabilities. As long as each franchise represents between 5% and 15% of the risk exposure of the captive, then

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76 United Parcel Serv. of Am., Inc. v. Comm'r, 78 T.C.M. (CCH) 262 (1999), *rev'd*, 254 F.3d 1014 (11th Cir. 2001).
77 *Id.*
78 Rev. Rul. 2002-89, 2002-2 C.B. 984.
79 *Id.*
80 *Id.*
81 *Id.*
82 Harper Grp. & Includible Subsidiaries v. Comm'r, 96 T.C. 45, 60 (1991), *aff'd sub nom.* Harper Grp. v. Comm'r, 979 F.2d 1341 (9th Cir. 1992) (holding that on this particular set of facts, a 30% unrelated risk was sufficient).
83 Rev. Rul. 2002-90, 2002-2 C.B. 985.
84 *Id.*

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the Service treats premium payments to the captive as deductible insurance expenses.[85]

The single parent captive thus serves the single parent by addressing its specific insurance needs while still maintaining the beneficial tax consequences of captives generally. This is the most familiar form of the captive insurance company.[86]

B. *Group*

Another form of captive is a "group captive."[87] There are several types of group captives.[88] A common type is the "association captive."[89] Companies that insure the risk of the member organizations of an association and their affiliated companies are known as "association captive insurance compan[ies]."[90] Under the association captive, an association of people or businesses forms a captive insurance company to insure against a common risk.[91] Often this is done either because premiums for the type of insurance needed by the association or common to the association are too expensive, or because insurance against the particular risk is simply not available in the commercial market. For example, many life insurance policies do not cover death due to skydiving accidents.[92] Every year about 3,000,000 people jump out of airplanes, and last year nineteen of them died as a result.[93] While the consequences to the families of the deceased are momentous, the chances of dying while skydiving (at about one in 163,000) are extremely low (about a tenth of the risk of dying from the flu).[94] As a result, an association of skydivers could form a captive to offer to its members reasonably priced insurance against the risk of death from skydiving, which is unavailable or prohibitively expensive in the commercial market. The risk of death or injury from skydiving is calculable and is thus an appropriate risk for insurance. However, the commercial

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[85] *Id.*
[86] Hall, *supra* note 28.
[87] *Id.*
[88] S.C. CODE ANN., § 38-90-10(4) (2012) (providing for association captive); Rev. Rul. 2002-91, 2002-2 C.B. 991 (recognizing pool captive); 15 U.S.C. § 3901(a) (1986) (providing for risk retention group captive).
[89] Hall, *supra* note 28.
[90] S.C. CODE ANN., § 38-90-10(4).
[91] *Id.*
[92] *See, e.g.*, Edison v. Reliable Life Ins. Co., 664 F.2d 1130, 1132 (9th Cir. 1981).
[93] *Skydiving Safety*, U.S. PARACHUTE ASS'N, http://www.uspa.org/AboutSkydiving/SkydivingSafety/tabid/526/Default.aspx (last visited Oct. 28, 2013).
[94] *Estimating Seasonal Influenza-Associated Deaths in the United States: CDC Study Confirms Variability of Flu*, CENTERS FOR DISEASE CONTROL & PREVENTION, http://www.cdc.gov/flu/about/disease/us_flu-related_deaths.htm (last visited Oct. 28, 2013).

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market simply does not offer or the cost is prohibitive to insure against this risk.

Revenue Ruling 2002-91, 2002-2 C.B. 991 provides for another type of captive suitable for companies that have fewer than twelve subsidiaries.[95] In what is often called a "pool captive" structure, each company forms its own wholly owned captive.[96] Then, in order to achieve the necessary degree of risk shifting and risk distribution, each of the captives purchases reinsurance from the other captives.[97] For example, an independently-owned restaurant might form a captive from which it buys business interruption insurance. That captive then reinsures the risk with other captives formed by other independent restaurants for the same reason. This vehicle makes captives available to smaller entities with less than twelve subsidiaries while still maintaining the benefits associated with captives generally. Another variety of captive within this group is the "captive re-insurance company." Re-insurance captives are re-insurance companies formed or licensed pursuant to enabling legislation.[98] A qualifying re-insurance parent company wholly owns this type of captive, which accounts for its name.[99] This type of captive may exist and be best suited for an association or group situation as well, where the re-insurance captives address some particular percentage or share of the risk, much as a re-insurer does.

C. *Core-Cell*

Protected Cell Companies, also known as core-cell captives, are a relatively recent innovation.[100] They provide companies with many of the benefits of a captive, without the cost and administrative burden of establishing a single-parent captive.[101] A core-cell captive is an independent legal entity consisting of a core and an indefinite number of cell entities, which are legally separate from each other.[102] The core contains the capital necessary to back up the risk of the cells.[103] Each cell contains dedicated assets and liabilities ascribed to it and are operated as if it were its own

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95 Rev. Rul. 2002-91, 2002-2 C.B. 991.
96 *Id.*
97 *Id.*
98 *Alternative Risk Transfer*, ZURICH, *available at* http://www.zurich.com/NR/rdonlyres/81DF36FA-2F06-45D4-8F31-0E10BB6ED7FE/0/art_fs_001_captive_e.pdf (last visited Oct. 28, 2013).
99 S.C. CODE ANN. § 38-90-10(9) (2012).
100 *Protected Cell Companies*, WILLIS GLOBAL CAPTIVE PRAC. (May 2008), http://www.willis.com/documents/publications/Services/captives/Protected_Cell_Companies_(PCCs)_-_The_present_and_Future.pdf.
101 *Id.*
102 *Id.*
103 *Id.*

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separate insurance company, although it remains part of the larger core-cell corporation.[104] The defining feature of the core-cell captive arrangement is segregation of the cells.[105] As a result, the assets of an individual cell cannot be used to meet the liabilities of any other cell.[106]

The core-cell captive has several advantages for smaller companies—similar to the advantages found in choosing space within a "self storage" warehouse versus building one's own warehouse. First, it is less expensive to form and operate because the costs of doing so are spread across many cell owners.[107] Second, a core-cell captive can be implemented quickly because it is essentially a turnkey operation.[108] Finally, the cell captive uses another company's capital (found in the core) to meet the statutory capital requirements, thus leaving the cell owner's capital available for the operation of the cell owner's own business.[109]

These are but a few of the types of captives available. It is important to understand that one of the clear advantages of captives is their flexibility to address the needs of the parent. Careful analysis of those needs, as well as the regulatory environment, is necessary in determining not only the appropriate domicile, but also the suitable form of captive to address adequately the needs of the parent.

VI. STEPS TO CREATING A CAPTIVE

A. *Case Study: Vandalay Industries, Inc.*[110]

Now that the considerations and types of captives have been explored, it is instructive to consider how a company goes through the process to determining whether the creation of a captive is appropriate for its business operations. To that end, this article examines a real corporate entity and works through the decision-making process. The name of the actual company and individual/family owners are changed to protect the privacy of the corporation. However, the other factors including capitalization and risks are the facts of the company. This data enables a

[104] *Id.*
[105] *Id.*
[106] *Id.*
[107] Ian-Edward Stafrace, *EU Protected Cells: Captives on a Budget*, ATLAS INS. (Mar. 22, 2011), http://irmforum.files.wordpress.com/2011/03/ian-stafrace.pdf.
[108] Arthur D. Perschetz & Melissa A. Hancock, *Segregated Cell Captives – the Law*, CAPTIVE INS. COUNCIL (May 7, 2013), http://www.dccaptives.org/files/2013/May%207/Presentations/Perschetz%20Hancock%20Cell%20Captive%20Seminar%20Presenation1.pdf.
[109] Stafrace, *supra* note 107.
[110] Vandalay Industries, Inc. is a fictitious name used to protect confidential information of the actual company.

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genuine analysis for a case study in the process of determining whether a captive is appropriate.

Vandalay Industries, Inc. is a family-owned, closely held company based in New Orleans, Louisiana with operations worldwide. Its President is Art Vandalay IV, who is the grandson of Vandalay's founder. The majority of its business consists of shipping, manufacturing and mining. In addition, Vandalay has several smaller divisions involved in computer systems and real estate development.

The bulk of Vandalay's business consists of contracts with various government entities, both domestic and foreign. The company provides value to these entities primarily by functioning as a general contractor. As a result, it performs little to none of the line-level work itself. Instead, Vandalay specializes in identifying opportunities, securing government contracts and partnering with companies that can perform the line-level work efficiently and well.

An example serves to illustrate. During a family vacation in western North Carolina in the summer of 2008, Art noticed the increasing number of shuttered sawmills. Research confirmed that this trend was not confined to North Carolina. Across the country, sawmills were closing as the demand for domestically produced lumber decreased. This observation seemed in conflict with a U.S. Department of Agriculture report that Art remembered reading, which indicated that the demand for finished wood products was on the rise. A brief investigation reconciled the two observations; manufacturers of finished wood products had largely moved their operations out of the United States and they were now relying in large part on South American and Indonesian lumber. Vandalay sought out and found an Indonesian state-owned lumber company that exported sustainably harvested hardwood raw lumber to a Chinese manufacturer. The operation was only marginally profitable because of the old and inefficient means it used to transport logs from the point of harvest downriver to the coastal sawmill. Further, the mill itself was also old and inefficient.

Vandalay showed the relevant government officials how the operation could be significantly more profitable by contracting with Vandalay to handle the process from the point of harvest through the loading of ships bound for China. As a result, Vandalay received the contract. Vandalay then formed a partnership with a Brazilian company that had great expertise in this area. Vandalay has majority ownership and executive control, while the Brazilian company has responsibility for operations. Infrastructure was financed through government-backed loans, and labor is provided through a long-term contract with an Indonesian staffing company that may or may not be owned by relatives of the

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government officials who approved the general contract. The joint venture has succeeded beyond its yearly targets and became profitable in 2011.

The lumber company is just one example. By establishing many such businesses in a variety of industries, Vandalay has been able to diversify its sources of income and hedge against political risk in the various countries in which it does business. While the exact number is confidential, Vandalay reports that its income from operations is over $25 million annually. Based on its size, Vandalay would seem to be an ideal candidate for captive insurance. The company has over $25 million in revenue, has thousands of people working in its operations worldwide, has significant property and liability risk exposure and paid over $400,000 annually in insurance premiums in 2012. However, upon closer examination, the expense and administrative burdens of captive insurance appear to outweigh the benefits for this company at this time.

Here is why. The analysis begins by compiling data relevant to the decision. This begins with an understanding of Vandalay's business and sources of income. Vandalay Industries, which began by operating a coastal barge service hauling bulk cargo such as grain and wood chips along the gulf coast, has transitioned almost entirely into joint ventures like those that the Indonesian lumber company as above described. As a result, Vandalay operates very little itself. Additionally, during the course of analysis, in early 2013, Vandalay sold the bulk of its remaining barge operation in Louisiana. During the analysis, it is important to understand Vandalay's current insurance needs and premium amounts. To understand this fully, it is necessary to consult experts, both within the business as well as possibly outside the business. In order to accurately assess whether a captive was appropriate for Vandalay, they allowed the collection of data to include consultation with their insurance brokers and in-house counsel. These discussions were necessary to understand Vandalay's insurance needs as well as to determine exactly the premiums Vandalay was paying. The sale in 2013 of the remaining barge business decreased Vandalay's total insurance premiums for 2013 to just $217,000. Further, this total is composed of premiums for six main types of insurance: $29,000 for hull insurance, $95,000 for marine general liability, $43,000 for property, $32,000 for workers' compensation, $13.000 for general liability, and $5000 for professional liability. Given that the cost of establishing a single-parent captive can easily reach $50,000, none of these components of Vandalay's overall insurance bill were sufficiently large to warrant a transition from traditional insurance with the possible exception of marine general liability.

Vandalay's hull insurance and marine general liability insurance policies cover a single midstream transfer facility in the lower Mississippi River. Midstream transfer facilities are an alternative to shore-based ports.

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Instead of tying to a shore side dock at a midstream transfer facility, bulk cargo ships tie to moorings in the river and their cargo is offloaded onto barges for transportation upriver. Vandalay has an excellent loss history at its Mississippi midstream facility. In fact, it has never had a significant accident there. However, when an accident does occur at its midstream facility, it is generally catastrophic. For instance, in 2011, a ship moored at another midstream facility broke loose from the upriver mooring during a microburst thunderstorm. As it swung around, it hit a number of barges waiting to be loaded as well as several tug boats and a pleasure craft. Six crewmembers on the tugs were injured along with four people on the recreational boat. Property damage alone was in the millions of dollars, but the payments to the injured pleasure boaters were much higher. This type of risk profile is not well suited to a single-parent captive.

For most risks, claims fall into one of three categories.[111] First are predictable losses, those that occur frequently and regularly but are not severe.[112] Second are improbable losses.[113] These do not occur often and when they do they are of moderate severity. Third are catastrophic losses, those that occur extremely rarely but are exceptionally expensive.[114] Loss of a mooring at a midstream facility is a catastrophic claim. Captives work best for their owners when they allow the owner to retain responsibility for all of the predictable losses, as well as some of the improbable losses, while reinsuring against the catastrophic losses.[115] The parent can then minimize the chance of loss in the first two categories (and thus the amount their captive will ultimately need to pay in claims) by instituting safety measures and other procedures to reduce the risk. Where, as with Vandalay's midstream facility, almost the entire risk is that of a catastrophe occurring, there is little opportunity for savings by managing risk. Instead, virtually all of the risk falls within the category against which the captive would need to pay to reinsure. The obvious question then, goes to the feasibility of a captive to address the risk involved with an understanding of the insurance needs. Because of the feasibility analysis, Vandalay found that the premium it would need to pay its captive would be almost identical to the premium it currently pays, and that most of this premium would not be retained by the captive, but would be spent on reinsurance, leaving not enough margin to cover the administrative cost of the captive. Therefore, while on its face, a captive seems to be an appropriate vehicle for Vandalay Industries, after

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[111] *Underlying Principles of Group Captive Risk Management*, ROSENFELD EINSTEIN, http://www.rosenfeldeinstein.com/events/events-captive.php (last visited Oct. 28, 2013).
[112] *Id.*
[113] *Id.*
[114] *Id.*
[115] *Id.*

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careful consideration, it does not appear that the creation of a captive makes financial sense.

If however, the circumstances had not changed and based on the analysis, a captive would have been feasible. Vandalay would then need to select a domicile for its captive. Vandalay would consider the factors and determine the best location for its domicile. Here, since Vandalay already does significant business overseas and since it is privately held, an offshore domicile may make the most sense. Offending shareholders or appearing to seek a tax haven would likely not be a concern for Vandalay. However, Vandalay would still need to consider its relationship with the IRS. Next, Vandalay would select its service partners. This would include agencies capable of handling and paying claims. There are several contractors who provide this service. Vandalay would investigate these vendors and select one that met its needs. Lastly, Vandalay would address the ongoing operation of the captive. Once established and capitalized, even changes in its business would not necessarily make the captive inappropriate because of the flexibility of the vehicle, so long as the captive remains in compliance with the jurisdiction of its domicile.

Therefore, while the establishment of the captive proved not to be feasible for Vandalay Industries, the steps to creating a captive remain the same. The case study of Vandalay describes the necessary considerations when doing the analysis.

VII. CONCLUSION

Captive insurance companies offer important advantages over traditional methods of insurance, including self-insurance or commercial insurance in some instances. These important advantages include flexibility, costs and tax consequences, as well as other non-insurance benefits, especially for privately-held companies. However, captives are not without risks, particularly the start up costs and lack of risk spreading. In order to determine if the captive is the right vehicle for any entity, a careful and deliberate analysis is necessary. Another aspect for future consideration is that of the appropriateness of parent companies the beneficial tax treatment for premiums paid to the captive. As insurance needs change, captives will continue to evolve and develop. How jurisdictions treat captives going forward, and the continued deductibility of premium payments, will also affect the sustainability and progression of captives. The need to balance permitting businesses to use nontraditional means to address their escalating insurance premiums with ensuring that companies are not engaging in activities to avoid simply appropriate tax consequences, will drive this evolution further. As this article has demonstrated, there are

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numerous factors to consider before making the decision to establish a captive. It is significant to understand the impact of these decisions.

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Domicile	Captives	Investment Restrictions	Applicable Acts	Supervisory Juris.
Alabama	17	Cell Captives allowed	2008 Coastal Captive Insurance Company Act	Ala. Dept. of Insurance
Arizona	97	Cell Captives allowed	Title 20, Chapter 4, Article 14	Ariz. Dept. of Insurance
Arkansas	1	Cell Captives allowed	Laws: Licensing and Regulation of Captive Insurers, 2001 Amended '03	Ark. Insurance Dept.
Colorado	5	No Cell Captives	Laws: The Colorado Captive Insuarance Act of 1972	Colorado Division of Insurance
Connecticut	0	No Cell Captives	2011 Economic Development Bill	
Delaware	106	Cell Captives allowed	Title 18, Chapter 69, 1984, 2005, Added Agency & Branch Captive Struction in 2010	Delaware Dept. of Insurance
D.C.	112	Cell Captives allowed	Laws: The Captive Insurance Compnay Act of 2004	Dept. of Insurance, Securities & Banking
Florida	0	-	H.B. 1101	
Georgia	15	-	O.C.G.A. Ttitle 33, Chapter 41, 1989	Georgia Insurance & Fire Safety Comm.
Hawai'i	175	Cell Captives allowed	Chapter 431, Article 19 of Hawai'i's Revised Statutes	Dept. of Commerce & Consumer Affairs, Ins. Division
Illinois	1	Protected Cells under dif. Statute	Article VIIC of the State Insurance Code, 1987	Illinois Insurance Department
Kansas	1	-	K.S.A. 40-4301 et. Seq.	Kansas Dept. of Insurance
Kentucky	137	-	Kentucky Revised Statutes 304.49 & Ken. Admin. Regs. 806 KAR 49 0202-49 040	Kentucky Office of Insurance
Louisiana	1	-	Captive Insurer Law- La. R.S. 22:550.1-550.26	Louisiana Dept. of Insuarace
Maine	2	-	Title 24-A, Chapter 83, Sections 6701-6720, 1997	
Michigan	5	No Cell Captives	Public Act 29 of 2008 adding Chapters 46, 47, & 48 to Michigan Insurance Code	
Missouri	25	-		
Montana	83	Cell Captives allowed	Laws: 33-28-101 to -306 MCA	
Nevada	123	-	Chapter 694C of Nevada Revised Statutes and Nev. Administrative Code	
New Jersey	4	-	Captive Insurers Act	
New York	46	-	Article 70 of New York Insurance Law	New York Insurance Department
Oklahoma	1	Cell Captives allowed		Oklahoma Deparment of Insurance
Oregon	0	-	S.B. 1547	*Russel Latham
South Carolina	157	-	S.C. Code 38-90-10; 38-87-10; 38-10-10 with regulation 69-60	South Carolina Dept. of Insurance
South Dakota	4	No Cell Captives	Laws: Chapter 58-46, 1996, Amended in 2009	South Dakota Division of Insurance
Tennessee	4	-	Tenn. Captive Insurance Company Act, Chapter 13, Title 56, 1978	Department of Commerce and Insurance
Utah	281	Cell Captives allowed	Laws: Captive Insurance Companies Act	Utah Insurance Department
Vermont	590	-	Special Insurers Act of 1981	-
Virginia	0	-	Chapter II, Title 38.2, 1980	Bureau of Insurance
West Virginia	1	-		Leah Cooper- Regulator
South America				
Panama	8	-	Laws: Law 60, 1996	Republic of Panama

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Domicile	Est. Parent #	Est. Group #	Domicile URL	Status	Domiciled	Notes
Alabama	77	0	www.aldoi.gov	Active	2006	
Arizona	74	21	www.id.state.az.us/captives/index.html	Active	2001	30% medical; 22% construction; 16% finance & insurance
Arkansas	-	-		Active	2001	
Colorado	5	-		Active		
Connecticut	0	-		Active		Contact Maura Welch
Delaware	106***	-		Active	Mid-80s	Recently passed Assoication and Branch Captive Law
D.C.	-	-	http://disb.dc.gov/page/captive-insurance-regulations	Active	2000	
Florida	-	-		Active		
Georgia	-	-		Active		
Hawai'i	156	19	www.hawaiicaptives.com	Active	1986	
Illinois	1	0		Active		
Kansas	0	1		Active	1988	
Kentucky	-	-	www.kycaptive.com	Active	2000	
Louisiana	1	-		Active		
Maine	2	-	www.maine.gove/pfr/insurance	Active	1997	
Michigan	5	0		Active	2008	
Missouri	21	1		Active	2007	
Montana	67	18	http://sao.mt.gov/captives/index.asp	Acitve	2001	
Nevada	123	-	www.doi.nv.gov/captive.aspx	Active	1999	
New Jersey	4	-		Active		Crosby Shermar
New York	55	-	www.nycaptives.com	Active	1997	
Oklahoma	1	-		Active	2004	
Oregon	0	-		Active	*	effective July 1, 2012
South Carolina	157	-	http://doi.sc.gov/captives/Pages/index.asp	Active	2000	
South Dakota	3	1		Active		
Tennessee	4	-	www.state.tn.us/commerce/	Active	1978	
Utah	281	-	www.captive.utah.gov	Active	2003	
Vermont	590	-	www.vermontcaptive.com	Active	1981	*952 issued, 590 Active
Virginia	0	-	-	Active	1980	
West Virginia	1	-		Active	2004	
South America						
Panama	-	-		Active		

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Europe				
Denmark	8	-	-	-
Finland	8	-	-	-
Gibraltar	15	-	Laws: Insurance Companies Ordinance of 1987 and associated Regulations	EU Regulations Apply- Comm. Of Insurance
Guemsey	345	-	Laws: Insurance Business (Bailiwick of Geurnsey) Law 2002	Guernsey Financial Services Commission
Ireland	82	-	Laws: Insurance Act of 1989 & 2000; Financial Services Authority of Ireland Act 2003	Irish Financial Services Regulatory Authority
Isle of Man	133	-	Laws: Insurance Act of 1986, Amendments '93, '95, & '04; Protected Cell Companies Act '04	Isle of Man Insurance and Pensions Authority
Liechtenstein	5	-	Insurance Supervision Law of 1 Jan. 1996; Implementing Ordiance of 24 Jan. 1997	Office of National Economy Au Strasse
Lloyd's	1	-	Lloyd's Act	Council of Lloyds
Luxembourg	200	-	Laws: 1991 Insurance Law and Grand Ducal Regulations, amended '94, '01, '04	-
Malta	10	-	Laws: Insurance Business Act	Malta Financial Services Authority
Norway	11	-	-	-
Sweden	50	-	-	-
Switzerland	35	-	Laws: Insurance Supervisory Law, amended 2000; Regulation for the Supervision of Insurance	Swiss Federal Office of Private Insurance
Carribean Islands				
Anguilla	252	-	Section 20, Insurance Act 2004	Anguilla Financial Services Commission
Bahamas	15	-	Laws: The External Insurance Act, '83, Ch. 348; The Subsidiary Legislations/Ch. 348 Ext. Ins. '87	-
Barbados	242	-	Laws: Exempt Insurance Act of 1983	-
Bermuda	862	-	Laws: Amendments to Insurance Act 1978	Bermuda Monetary Authority
B.V.I.	172	-	Laws: The Insurance Act, 1994; more on sheet	Financial Services Commission
Cayman Islands	739	-	Laws: the Insurance Law (2008 Revision)	Cayman Islands Monetary Authority
Curacao	25	-	Special Insurance License Decree National Gazette May 9, 1992, No. 50	Bank Van de Nederlandse Antillen (Central Bank)
Netherland Antilles	13	-	Laws: Special Insurance License Decree, 1992	Central Bank
Nevis	108	-	The Nevis International Insurance Ordinance, 2004; more on sheet	Ministry of Finance
Puerto Rico	3	-	Laws: Puerto Rico Insurance Code, amended by Public Law Nos. 399, 400	Office of the Commisssioner of Insurance
Turks and Caicos	211	-	Turks and Caicos Insurance Ordinance of 1989 and accompanying 1990 regulations	Financial Services Commission
US Virgin Islands	7	-	Virigin Islands International Insurers Act, Title 22, Virigin Islands Code, Ch. 55	Division of Banking and Insurance
Canada				
British Columbia	29	-	The British Columbia Insurance (Captive Company) Act of 1987	Financial Institutions Commissions
Australia				
New Zealand	24	-	Insurance Companies Deposit Act 1953	Public Trust Corporate Trustee Services
Asia				
Hong Kong	2	-	The Insurance Companies Ordinance, Chapter 41 of the laws of Hong Kong	Insurance Authority
Labuan	34	-	The Offshore Insurance Act of 1990, amended in 1997, 2001	Labuan Offshore Financial Services Authority (LOFSA)
Miconesia	3	-	-	-
Singapore	60	-	Insurance Act (Cap. 142), Revised Ed. 2002; Insurance Regulations 2004	Monetory Authority of Singapore

***See sheet for breakdown
*Cell Captives
*SBU= Series Business Units

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Europe					
Denmark	-	-	-	Active	
Finland	-	-		Active	
Gibraltar	15	-	-	Active	
Guernsey	345	-	www.guernseyfinance.com/insurance	Active	
Ireland	154	-	-	Active	
Isle of Man	133	-	www.gov.im/ipa	Active	
Liechtenstein	5	-	www.pgr.li/cd/en/Teil_3/main.html	Active	
Lloyd's	1	-	-	Active	
Luxembourg	200	-	-	Active	
Malta	10	-	www.mfsa.com.mt	Active	
Norway	-	-	-	Active	
Sweden	-	-	-	Active	
Switzerland	48	-	www.bpv.admin.ch	Active	
Carribean Islands					
Anguilla	252	-	www.fsc.org.ai	Active	
Bahamas	15	-	www.bahamas.gov.bs/oric	Active	
Barbados	235	-	-	Active	
Bermuda	862	-	www.bma.bm	Active	
B.V.I.	172	-	BVI Captive Link	Active	2010 Premiums= $8.6B
Cayman Islands	739	-	-	Active	
Curacao	25	-	-	Active	
Netherland Antilles	17	-	-	Active	
Nevis	150	-	www.nevisfinance.com	Active	
Puerto Rico	3	-	www.ocs.gobierno.pr/	Active	
Turks and Caicos	169	-	-	Active	
US Virgin Islands	-	-	-	Active	
Canada					
British Columbia	18	-	-	Active	
Australia					
New Zealand	5	-	www.nzcia.org.nz/	Active	
Asia					
Hong Kong	2	-	www.oci.gov.hk	Active	
Labuan	34	-	-	Active	
Miconesia	-	-	www.mra.fm/dcic.php	Active	
Singapore	60	-	www.mas.gov.sg/masmcm/bin/pt1Home.htm	Active	

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