CICA Statement on 831(b) Captives

Do 831(b)s Right or Don't Do Them at All

CICA, the Captive Insurance Companies Association, is a 42 year old domicile neutral trade association representing the captive insurance industry with members throughout the world. CICA is uniquely situated to address challenges of a national and international nature, including reputational challenges to the industry.

In recent years there has been significant growth in the utilization of small captive insurance companies that use the Internal Revenue Code 831(b) election for small insurance companies. In general terms, if a small property and casualty insurance company with annual gross premium income of $1.2M or less makes an election to use Section 831(b), it is not taxed on its underwriting income, but only on its investment income. However, that insurance company must still meet all the legal requirements established by law, including the US Supreme Court's holding that insurance status generally requires the presence of two elements -- risk shifting and risk distribution.[1]

Unfortunately, these small captive insurance companies (also known as "mini-captives" or "micro-captives") have received considerable attention from the "wealth management" industry and are often "over sold" as a tax shelter without adequate attention to whether these companies are truly insurance companies and meet the requirements of operating as a legitimate insurance company with risk shifting, risk distribution, and arms-length pricing.

The attempt by some to use these small captives primarily as a tax shelter has created a significant reputational challenge to the entire captive insurance industry, which has always focused on the formation of captive insurance companies "to create a risk management program that will proactively anticipate the potential future risks arising in the parent/owner(s) business."[2]

The traditional captive insurance company industry and CICA are extremely concerned about the misuse of small captives utilizing the IRC 831(b) election and the attendant publicity about "captives" being a tax avoidance device. Although there is nothing wrong with the utilization of the 831(b) election when a small captive insurance company is truly engaged in insuring the risk of its parent company/owner(s), the traditional captive insurance industry strongly oppose the utilization of small 831(b) captives primarily for tax sheltering purposes.

In simple language, do 831(b)s right or don't do them at all!

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[1] CICA "Captives: An Overview" publication, page 25.
[2] CICA Best Practices Guidelines, Volume 1. "Business Alignment", page 4.

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