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AN EXAMINATION OF GEORGIA'S PREMIUM TAX

Introduction

This Policy Brief examines a proposed change to the taxation of insurance companies in Georgia. The Brief is organized as follows. First, the structure of the premium tax in Georgia as it currently exists is presented. Secondly, results of a simulation of new proposed tax changes are presented. Finally, some tentative conclusions about what a change in the tax law might do for the Georgia economy are included in the final section.

In sum, a change in the tax law which would eliminate the premium tax on insurers by both the state and local governments would still bring in significant revenues due to the operation of the retaliatory tax. Thus, removing the premium tax in Georgia will yield some $260 million to the state due to the operation of the retaliatory tax, which nearly offsets a loss of $330 million in state level premium insurance revenue. There would be a revenue loss to the local governments, who currently receive insurance premium revenue of over $300 million.

Structure of the Premium Tax in Georgia

Unlike other corporations in the state, insurers are not taxed based on corporate net income, but on gross revenues from insurance premiums. The insurance tax base is premium written in the state of Georgia by domestic (chartered in Georgia) and foreign (chartered in other sates) insurers doing business in Georgia. Both life insurers (which also include accident and health insurers) and property-casualty insurers pay a tax of 2.25 percent of premiums to the state. For life companies there is an additional tax of 1 percent which is collected by the state on behalf of municipalities and county governments. For the property-casualty companies, this local tax rate is 2.5 percent.

The premium tax law also allows for certain deductions from the tax. Life insurers (but not property and casualty insurers) can deduct the local portion of the tax. Secondly, insures investing a significant portion of their investments in qualified Georgia assets can realize a significant reduction in their premium tax liability. If the insurer has 25 percent or more invested in specified Georgia investments, then the state premium tax rate is 1.25 percent rather than 2.25 percent. Further, if the insurer invests 75 percent or more in qualified Georgia assets then the state premium tax rate is 0.5 percent. The general structure of the tax is shown in Table 1.

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There are some additional aspects of the tax. Certain property-casualty insurers are allowed a reduction from their Georgia taxes for certain taxes paid to other states in the form of retaliatory taxes. (These taxes will be discussed further below.) Also, fire insurance is subject to an additional one percent premium tax to cover contributions to fire fighter's pensions. HMO's may deduct license fees paid to local governments and all life insurers are allowed a deduction for any payments made to the life insurance guarantee fund.[1]

A final aspect of the premium tax system in Georgia relates to how other states view Georgia's tax structure. Most states have what is called a retaliatory tax which requires a foreign company to pay the higher of the tax due using its home state's law or the host state's law. For example, suppose a Georgia auto insurer operates in Florida and sells $100 of insurance. Under Georgia law the insurer would have to pay $4.75 (assuming no other credits or abatements) if these premiums were written in Georgia. Under Florida law if the insurer is a Florida domestic company, it is liable for $1.75. The retaliatory tax law calls for the higher of the two tax liabilities to be paid to Florida. Thus, a Georgia insurer writing premiums in Florida pays the higher Georgia rate (4.75%) in every state with a lower tax rate.[2] This can have a negative incentive for Georgia companies to operate outside the state and for potential entrants to move here and apply for a Georgia charter.

What is interesting is that since Georgia has a relatively high premium tax rate (especially for property-casualty companies), Georgia collects little retaliatory tax revenue. However, as the premium tax rate is reduced, Georgia will start collecting significant retaliatory taxes from companies chartered in other states.

Simulation of Tax Changes

One of the proposals is to reduce the premium tax rate to zero. In doing so Georgia companies selling in Georgia would pay no premium taxes on their Georgia premiums—state or local. However, out-of-state companies will use their home state's tax rates to pay taxes to Georgia based on these out of state companies' premiums written in Georgia.

Table 2 shows the results of the simulation. In this simulation it is assumed that Georgia companies would pay zero premium tax and that the out-of-state companies would pay their respective rates on premiums and annuity considerations written in Georgia.[3] We obtained tax rates from the National Association of Insurance Commissioners (NAIC) *Guide to Retaliation* (2004). The *Guide* has state specific rates for life, accident and health (group and individual), annuity considerations, property and casualty, and fire. These tax rates are used to calculate premium tax due based on premiums written in Georgia. The premiums written in Georgia were obtained from the NAIC's annual statement's state pages for both the life and health industry and the property-casualty industry. It is assumed there are no credits or other deductions available to the insurer taxpayer. The weighted average effective tax rate for out-of-state companies is approximately 1.26 percent for property-casualty companies and 1.56 percent for life and health companies, so below those points Georgia starts to collect a larger percentage of its taxes from retaliation.

If the tax rate is reduced to zero, then Georgia is expected to collect some $261 million in premium taxes from the retaliatory tax, but loses its insurance premiums tax of $330 million (2004 levels). In addition, local governments lose somewhat over $300 million in their local insurance premium tax revenue. As the rate is increased the amount of tax revenue collected increases, but what is happening is that a greater share of it comes from the premium tax rather than the retaliatory tax.

Conclusion

Georgia has an insurance tax environment which hinders the development of a domestic insurance industry. This is due to the operation of the other states' retaliatory tax system. Insurers are not likely to locate to Georgia if they are taxed in other states at Georgia's high rates. Removing the premium tax and relying solely on the retaliatory tax can change the overall assessment of Georgia as a place to re-locate insurance operations as tax policy is no longer an impediment to relocation. Thus, removing the premium tax creates an incentive for current Georgia companies to grow as well as an incentive for out-of-state companies to consider re-domestication to Georgia.

Generally, a state's tax policy is not the main reason a company moves its headquarters, but it is an important reason. However, no insurer is likely to move to Georgia without a change in the tax environment. If the environment is altered, then those Georgia characteristics which attract other companies will have a strong influence on insurers.

There are some prospective benefits from encouraging insurers to relocate jobs and corporate headquarters to

TABLE 1. STRUCTURE OF INSURANCE PREMIUM TAX

	Life Insurers	Property Casualty Insurers
State Tax Rate*	2.25 % Premiums	2.25 % Premiums
Local Government Tax Rate	1 %	2.5
Total Premium Tax Rate	3.25%	4.75%
Credits		
Credit for Local Government Tax	1 % of Premiums	None
*Investment Abatement		
If insurer invests 25 percent of it assets in state, the State Premium Tax rate is 1.25%.	Available for Life Insurers	Available for PC Insurers
If the percent of insurer assets invested in Georgia is 75 percent or greater the maximum state premium tax rate is 0.5%		

TABLE 2. TAX SCENARIOS

GA Tax Rate (%)	Total Retaliatory Tax
0	$261,590,338
0.5	$263,378,683
1	$297,937,989
1.5	$333,563,483

Georgia. According to the Bureau of Labor Statistics, insurance jobs average about $59,000 per year[4] while the average job in Georgia pays about $38,000.[5] In addition, there is a multiplier effect for additional insurance jobs. For every one job created in the insurance industry there are about two to three additional jobs created. Further, there is no need to concentrate these positions in congested parts of the state as insurers could operate in almost every part of the state. Finally, a growing insurance industry does not impose significant environmental costs on the state.

In sum, removal of the Georgia premium tax will provide some $261 million in retaliatory tax revenue, which nearly offsets the state's $330 million expected revenue loss from elimination of the tax. If the tax is totally eliminated, local governments will lose approximately $300 million in revenue. Such a change, however, will encourage domestic companies to grow out-of-state which creates headquarters jobs in Georgia and it removes a significant barrier to out-of-state companies re-domesticating to Georgia.

Notes

1 This fund is set up to cover insurance benefits from failed life insurers. Each life insurer can be taxed to support any deficiency due to a failed life insurer. Georgia property-liability companies do not have a similar deduction for amounts paid to the property-liability guarantee fund.

2 This retaliatory tax law, which on the surface appears unconstitutional since is discriminates against foreign companies, has been upheld by the U.S. Supreme Court in *Western & Southern v. California Board of Equalization,* 451 U.S. 648 (1981). A main reason the court upheld the law is the fact that the law is designed to punish other states for having high taxes. Deterring the placement of high taxes on domestic companies is a legitimate state purpose.

3 I did assume that the one percent tax on fire lines to fund fire department pensions is still in existence.

4 http://data.bls.gov/PDQ/servlet/SurveyOutputServlet;jsessionid=f030a540b844$01$2A$3

5 http://data.bls.gov/PDQ/servlet/SurveyOutputServlet;jsessionid=f0302ceb4715u$3F8$03

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