
Federal excise tax: Insurance 'Cascading' FET - Protective refund claims

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In brief

On January 25, 2013 an insurance company domiciled in Bermuda filed a complaint with the US District Court for the District of Columbia challenging the 'cascading' FET. Foreign taxpayers who have paid the cascading insurance excise tax (imposed on foreign to foreign reinsurance of US risks) should evaluate the filing of protective refund claims before the statute of limitation expires.

In detail

Section 4371 of the Internal Revenue Code imposes an excise tax (FET) on each policy of insurance or reinsurance covering US risks issued by any foreign insurer or reinsurer. Section 4371 imposes such excise tax on the gross premiums on contracts covering US risks paid to a foreign insurer or reinsurer at the rate of 4 percent on direct property and casualty insurance business, 1 percent on policies covering life insurance, sickness, or accident insurance, or annuities and 1 percent on reinsurance policies.

On March 7, 2008, the Internal Revenue Service released Revenue Ruling 2008-15 (Ruling), formally adopting the position that the 'cascading' FET will be enforced pursuant to Section 4371. Specifically,

the Ruling stated that premiums paid by a foreign insurer or reinsurer to another foreign reinsurer are subject to the 1 percent excise tax imposed by Section 4371(3). At the same time as the release of the Ruling, the IRS also issued a voluntary compliance initiative in Announcement 2008-18 encouraging foreign persons who failed to pay the cascading excise taxes due or failed to disclose exemptions pursuant to an income tax treaty to become compliant via the filing of FET tax forms along with any amounts due as of the fourth quarter of 2008.

Since the release of the Ruling, many taxpayers and trade associations have questioned the validity of the 'cascading' FET although a formal challenge to the IRS position had not commenced until recently. On January 25, an insurance

company domiciled in Bermuda filed a complaint with the US District Court for the District of Columbia challenging the 'cascading' FET.

The takeaway

Many foreign insurance companies began filing federal excise tax returns for insurance premiums under the voluntary compliance initiative. Additionally, other foreign insurance companies filed delinquent federal excise tax returns as a result of an IRS examination or voluntary filing with the IRS outside of the voluntary compliance initiative. As a result of the recently filed complaint, a favorable outcome for taxpayers with respect to the 'cascading' FET is possible.

Foreign insurance companies that have paid the 'cascading' FET should evaluate the filing of protective refund claims with the IRS. The statute of limitations for excise tax returns timely filed for

the first quarter of 2011 will expire as of April 30, 2013. Those taxpayers who have paid the excise taxes after the due date of the return can submit a refund claim within three years of the date of

payment but can only recover amounts paid in the prior two years from the date the refund claim is filed.

Let's talk

For a deeper discussion of how this issue might affect your practice, please contact:

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