

- Speaker 1: This podcast episode reflects the opinions of the hosts and guests and not of Greenberg Traurig, LLP. This episode is presented for informational purposes only, and it is not intended to be construed or used as general legal advice nor a solicitation of any type.
- John Mangan: And every year in Washington, we pay out \$4.8 billion in just life insurance and annuity payments, and that amounts to \$13 million every day to Washingtonians.
- Nikki Dobay: [00:00:30] Hello and welcome to GeTtin' SALTY State and Local Tax Policy Podcast, hosted by Greenberg Traurig. My name is Nikki Dobay, shareholder in the Portland, Oregon, and Sacramento, California offices. I am very pleased today to be joined by two folks that know way more than me about all things insurance and insurance tax related, and I would consider them both experts in this area. And we are going to have a conversation [00:01:00] about an issue that we've been working through in Washington. And so first, going to introduce my guest. First is Jim Shea. He is the Senior Vice President and Chief Tax Officer at Prudential. Jim, thank you so much for being here.
- Jim Shea: Looking forward to it.
- Nikki Dobay: And joining us also is John Mangan. He is a Vice President and Deputy of State Relations at the American Council of Life Insurers. ACLI, [00:01:30] as many of you have may have heard. John, thank you also for being here.
- John Mangan: Thanks, Nikki. It's great to be working with you again.
- Nikki Dobay: So before we get into the meat of this, I always like to ask newcomers to the podcast how you got into this crazy world. Jim, I know you're not just focused on state tax, so you can take us through a little bit of how'd you get into this insurance tax area.
- Jim Shea: Well, I'm a rare breed, actually. Prudential [00:02:00] was my first job out of college. So I started just walking in doing the low level stuff, but then went to grad school and went to law school. So I've had a really great opportunity at Prudential over the last 38 years and see it go from a slow moving mutual insurance company, basically domestic to a global financial services company, top 10, top 15 asset manager company. And the company's just created me lots [00:02:30] of opportunities to learn and grow. So it has all been insurance, but it's not been a boring ride at all.
- Nikki Dobay: Well, and always tax?
- Jim Shea: Yes.

- Nikki Dobay: Okay. All right. So you are one of those rare ones. John, come on. Now, is this the same story, you just woke up one day as a youngster and thought, I want to do insurance tax?
- John Mangan: Well, not quite. [00:03:00] I had gone to graduate school in comparative literature, if you can believe that, but I ended up working for one of Oregon's great companies, Standard Insurance Company of Oregon, the state's largest life insurer. And about seven years into my career there, I was promoted to be government affairs head and also be our lobbyist in Oregon. And I remember my boss came to me and he said, "Congratulations, John. We really think you can do this job. And by the way, we've got a real problem. We've got [00:03:30] apparently some large companies, MetLife and Prudential in particular have said that they're interested in looking at our tax system here in Oregon. And all you've got to do is meet with those folks and figure out how to change our tax system so that everybody's happy."
- So to be honest, my first assignment was to work on the state tax structure in the state of Oregon, which we did over the next four years, and created what's actually a unique system. But I think [00:04:00] that gives me a little bit of personal perspective, at least on where we're here in the Washington situation.
- Nikki Dobay: And I know you and I first started talking when Oregon had another issue a few years back when they enacted the CAT. And there were some challenges there, especially on the retaliatory tax side. And happily, we were able to work through those as well. And I think we got to a good place.
- John Mangan: Absolutely. And you've got to understand the structure before you start tinkering.
- Nikki Dobay: That's [00:04:30] right. So John, kick us off here and tell us about what is ACLI's mission and how do you all get involved in these type of state tax issues? And then we'll really get into the meat of what's going on in Washington.
- John Mangan: Sure, you bet. The American Council of Life Insurers, we're the National Trade Association of companies like Prudential and all the other major names that you can think of who honestly, we're recovering 90 million American families [00:05:00] for life insurance, but also for annuities, which are individual retirement plans, long-term care insurance, disability income protection, dental vision, and even supplemental benefits. So we have a huge impact on the social safety net in the United States. In Washington in particular, we have, I think 240 licensed companies. They're accounting for about 99% of all annuities sold in the state, [00:05:30] which is obviously a very popular product right now given the fact that so many people are reaching age 65 and looking for retirement security. And so our focus is always on protecting our customers throughout their working and retirement lifetimes. And I think we've done a great job of doing that. And what I like to point out before we start talking about the tax system is what we're doing with the premiums that come into our companies.

And first and foremost, [00:06:00] we use those premiums to make sure that we can put aside reserves and put aside investments that ensure we can pay claims. Some of our products endure for 20, 30, 40, or 50 years or even longer. So we need to make sure that that money is well invested and safely invested. And in the case of Washington, our companies have invested over \$190 billion in the state's economy, a surprising number, [00:06:30] and of course we do that both in the public and private sectors. And nationally, we're the largest investor in corporate bonds. That's the debt structure that most companies use to invest in their companies and create jobs. And in Washington state alone, we have major investments in companies you'd all know. Amazon, T-Mobile, Microsoft, Starbucks, Nordstrom, WeyerHaeuser, et cetera, and provide a meaningful [00:07:00] portion of the corporate bonds that they hold.

But we also invest in public infrastructure and public projects. Some of those highlights that might share, we think have \$300 million in bonds with this University of Washington. We have 117 million invested in the Seattle Convention Center facility, 159 million in the Central Puget Sound Transit Authority. That's mostly light rail. The Snohomish County [00:07:30] PUD, even the Fred Hutch Cancer Center, I think we have more than 20% of their bonds. So those investments are not always well known or connected to our industry, but I think it's really important. Obviously we do that, they'll make those investments so we can make payments to our customers. And every year in Washington, we pay out \$4.8 billion in just life insurance and annuity payments, and that amounts to \$13 million every day to Washingtonians.

[00:08:00] So that's a pretty good baseline of impact for our industry. And of course, we're going to talk about premium taxation, which is the core tax applicable to our companies. And I'm really proud of the contribution we've made to the states in premium tax. It's a unique system. I know Jim's going to fill us in a little bit more about that, but the premium tax generates a very large portion of business taxes in the state of Washington. And what I think is really important is that it's a very [00:08:30] durable, very resilient, very consistent and almost always growing source of revenue for the general fund. So I think that's something that the state can always count on us, and then of course, we're reinvesting that money, as I mentioned. So again, we're pretty proud of that impact.

Nikki Dobay:

Well, thank you for that. I think those are all really important points. And so Jim, now I'm going to give you the incredibly Herculean task of trying to explain state taxation of insurers in about [00:09:00] 90 seconds to two minutes so we can get into what's going on in Washington. If you need a little more time, we could give it. But at a high level, why is insurance in this different category?

Jim Shea:

As John mentioned, we're in a very long-term business model. So when we sell a policy, we have no idea how much money we are eventually going to make on that policy because it could go for 20 to 50 years. Every interval [00:09:30] in the interim is an estimate. You're estimating the reserve liability. There's other estimates involved. So historically what has happened in the case of

Washington, for example, there's been a tax on our premiums since 1891. The federal tax code didn't come into effect in 1913. So we were paying a tax on premiums, which is an easier tax look at a certain percentage of that dollar [00:10:00] premium versus trying to figure out what's the right amount of income that the company earned and what you should tax when the federal tax code was passed and eventually built up.

The life insurance or the insurance industry has its own subchapter in the Internal Revenue code because while a lot of what we do is the same, the investing might be the same. All the employee benefit stuff is the same, the business model itself of taking in money today, knowing that you're going to pay [00:10:30] the vast majority, what you take in today is going to leave as an expense sometime down the road, but you don't know when. So there's a subchapter L that addresses the federal tax income tax, but states almost all of them is a handful of states that we pay premium and an income tax. But generally, the states have stayed with the old approach of, we're going to tax you on your premiums, which we know and not on your income, which is harder to gauge. John said [00:11:00] though, it's a gross receipts tax and it's an onerous one.

We pay in years that we lose money. We're still paying the gross receipts tax in the state of Washington. And this is, I've looked at this across every state. Washington's actually not unusual, but the premium taxes collected by the state are 13% of all of the B&O taxes that are collected. So I don't know what [00:11:30] the insurance industry's percentage of GDP is in the state of Washington. I don't know what our share of corporate profits are, but I am certain that we're not 13% of the business economy in the state of Washington, but we are 13% of the corporate tax receipts will be-

Nikki Dobay: That are coming in to the state.

Jim Shea: ... [inaudible 00:11:50]

Nikki Dobay: Yeah.

Jim Shea: In 90 seconds, which was a little bit longer.

Nikki Dobay: But you did a very good job.

Jim Shea: Every state were taxed on a premiums basis with some [00:12:00] states also taxing us on an income basis. But where they do tax us on income, many of them would give you a credit one way or the other. If you pay a premium tax, they'll give you a credit against the income tax and the income tax, there's only a couple that you end up really paying both.

Nikki Dobay: Okay. Well thank you for that. And you did a very good job. That was very, very, just so our listeners know, there's a whole heck of a lot more two premiums,

taxes of the state and local taxation of insurance companies. But we wanted to set the table. So now let's pivot to [00:12:30] Washington, and I don't know who wants to start on this, but Jim, I think you said Washington has had a premiums tax in the state since 1891. So this is even older than the B&O tax. I think that's a very, very important point. And generally Washington hasn't been an outlier. They've had their premiums tax, they have had an exclusion for purposes of the B&O tax. Of course there is the in lieu of clause, which [00:13:00] we don't have time to get into today, but who wants to kick us off with what is going on? Initially there was a bill that was introduced SB 5949. There's a companion bill HB 2487, what's going on with these bills? And I can also provide some background, but want to let you guys set the stage on this.

Jim Shea: I'll take it.

Nikki Dobay: Okay.

Jim Shea: I got involved in this, not trying to learn this at Washington very late last fall. [00:13:30] So insurance companies have a premium tax, and generally speaking, every time Washington has enacted another tax, they've said no insurance taxes, premium taxes are going to be paid in lieu of these other taxes. So when you look at the insurance, we're paying premium tax. Every other business model in the city of Washington is paying a B&O tax. Within the B&O tax, when you write, there's an exemption for insurance business. So premium taxes [00:14:00] are paid by insurance entities, the B&O tax as an exemption for insurance business, which arguably goes a little farther than just being an insurance entity. So there was a court case that was decided by the Washington Supreme Court that said, an insurance business doesn't have to be inside an insurance company. You need to be related in the value chain of insurance.

So the state of Washington doesn't like the results. They want to say, [00:14:30] we've always intended that insurance companies are in lieu of this other B&O tax not related activities that are outside of the insurance entity. So a bill was put forward very, very late last year, and the wording of it really, really shocked the insurance industry because the exemption would now be only upon premiums upon which you paid a premium tax, Not the other [00:15:00] gross receipts of the insurance company. So we've reacted, no state does that, nobody does all that. And as I said earlier, if you just look at the structure of the premium tax today and what it does pick up, it picks up enough to be 13% of corporate receipts in Washington.

So it's already our fair share, whatever that means at least. So we got involved to say, whoa, whoa, whoa. I think you guys [00:15:30] are overshooting here in the wording of what this says. So in January, there was a hearing in front of the Senate and the Department of Revenue at that hearing said very clearly twice, this bill is intended to change the taxation of insurance affiliates but not change the taxation of insurance companies. So we took a step back and said, good, but [00:16:00] that's not what this bill does at all. And so for the last month we've been trying to work with the legislatures to say, at least Prudential, and at least I

understand what you want to do. I will try and help you get there. But what you have written in front of you does not at all do what the stated intent is.

Nikki Dobay: And John, before we get into the ACLI bill, I know you all have been working very hard internally [00:16:30] with your tax group as well as working with other members of what is now a larger coalition on an amendment. But anything to add to what Jim had to say about the bill and the session and what we've been seeing?

John Mangan: Sure. I'm happy to do that. And just so you understand, my role is to try to translate the incredible expertise of people like Jim and our tax directors from our other companies into hopefully understandable [00:17:00] messages for policymakers. And in my case, I'm not an attorney or a tax expert, but I could read this bill and I could see the very ambiguity that Jim has been talking about. Very clear sense that this language goes way beyond where I think it was intended. So in our initial testimony, we were very clear that we wanted to make sure we could clarify this language to reemphasize and reconfirm that our companies are subject [00:17:30] to a very onerous premium tax in lieu of other taxes, including the B&O tax, and that we are willing to work to clarify that because we don't believe it's your intent as policymakers to impose a tax on things that aren't taxed right now.

For instance, annuities. Annuities have long been exempt from tax in Washington, and I think in the hearings you've heard confirmation of that, and yet the language doesn't say [00:18:00] that. And as you know, Nikki, the language in tax statutes has to be crystal clear because there's just no room for a misunderstanding and we want to make sure that's happening. So that's how we ended up working on some very surgical, very careful amendments to leave the intent of the bill intact, but to confirm its intent not to impose extra taxation on an industry that's already fully taxed.

Nikki Dobay: [00:18:30] Jim, you mentioned the department's testimony, which again, we all listen to. We all agree that we think we understand what they're trying to do with respect to follow up from the Envelope case. And it's great that legislative history is on the record, but John, to your point, we never want to get to a place where we have to get to legislative history. And Jim, you said it earlier, this language is pretty clear when you read it that it could [00:19:00] be interpreted extremely broadly. And so the goal really with the amendment again, was to one, build a coalition of folks that understand the goal and to make it just clarify what the department had put forward, that the intent of the bill is to continue to provide the B&O exclusion for insurance companies and other taxpayers covered under the premiums tax code that are doing the business [00:19:30] of insurance. We probably shouldn't get much more technical with the podcast on that, but do you have any other specific things you'd like to add about the amendment and its role or goal or language there?

Jim Shea: With anytime you get statutory language, it's hard. You want to be precise. We don't want to change taxation pro or con, we no want to give anybody an exemption that they don't already have. So it [00:20:00] takes some-

Nikki Dobay: Takes a village.

Jim Shea: It takes a village. You need a lot of people looking at it. And there's life insurance, there's property casual insurance, there's health insurance, there's title, there's lots of different kinds of insurance. So to get it right, it takes a little bit of time. But the bill that we are proposing as an amendment, I do think accomplishes at least the department stated objective, which I assume can be the legislatives, but if not, we'll work with them to fix it. [00:20:30] But I think it does.

Nikki Dobay: John.

John Mangan: I would just add that this has been really carefully vetted, not only by our life insurance group, which has deep expertise, but also by the property casualty industry as well. They've combed through our language, they agree that it accomplishes the goals we're talking about. And also a company called Primera, which is one of Washington's largest health plans. And the language also we think is protective of, [00:21:00] again, their business model, which has the very same kinds of components that we've been talking about. So as a legislative person, we want to make sure we can make the language clear, make it as minimal as possible to not disturb the overall intent of the legislature, but then also to try to get the parties that are affected to the table and act in some unity or unison about what the solution is. So I think [00:21:30] we're poised to do that and hopefully we can get it accomplished.

Nikki Dobay: Well, thank you both so much for this conversation. It's been a very important one, this legislative session in Washington. Before we get to the real fun, the surprise non-tax question, any final thoughts about Washington and/or state policy related to the taxation of insurance?

Jim Shea: Shouldn't give me an open question like that.

Nikki Dobay: It's a loaded question.

Jim Shea: I do think [00:22:00] most legislatures, I'm going to say all, don't really fully grasp the amount of corporate taxes that are paid through the premium tax. In the last couple of years, there's been a number of states thinking about lowering the corporate income tax rate, and IACL, I say we should be talking about lowering the premium tax rates too. And it's a little complicated, but we pay a very, very high percentage of corporate tax receipts and we shouldn't be forgotten [00:22:30] out there just because it's in terms of premium and non-income.

- John Mangan: Totally agree. And again, Nikki always, I said I was proud of the contribution. We make 2% of gross, again, no offsets, doesn't matter whether we're profitable. And the amount that comes into the State general fund has been growing at a very nice clip that probably exceeds inflation and exceeds the growth of GDP. We're almost estimated to be close to \$2 billion [00:23:00] in premium tax from all insurers in the next biennium. And that's happened through financial downturns, through COVID, and it's something that I think we're all really proud of that contribution in addition to the other things we're doing for consumers.
- Nikki Dobay: Well, thank you both. Just one more thing, one more box to check, surprise non-tax question. So I thought about this one to craft it for both of you because you both spend time, one of you most of your time, one of you, [00:23:30] some of your time in a warmer climate. So my question today and how this works is I ask the question and then I'll answer it first so you can gather your thoughts. Do you prefer socks and sneakers or shoes or barefoot and sandals? I'll go first. I'm definitely a barefoot and flip-flops person whenever I can be. I begrudgingly wear socks when I have to and for professional purposes, but I much prefer to be wearing [00:24:00] flip-flops in a warmer climate. So John, I'll start with you.
- John Mangan: Wow, that is a tough one. I didn't see that coming, but I'm just going to say as an aging male, there's just certain things people shouldn't have to look at. So I would say definitely socks. I really enjoy a cold climate and I grew up in Walla Walla, Washington where it gets cold in the winter and hot in the summer, but you got to have your shoes [00:24:30] on when you're out there, gardening or working in the vineyard. So I'm going to go with socks.
- Nikki Dobay: All right. All right, Jim.
- Jim Shea: I am an old creature of habit, so I wear size 12 Nike basketball shoes since I was 10 years old.
- Nikki Dobay: On the beach.
- Jim Shea: On the beach, everywhere. Size 12 Nike. That's all I wear.
- Nikki Dobay: Wow. I thought I was going to get flip-flops from both of you. We live in these warmer climates, but that's why it's a surprise [00:25:00] non-tax question. It's a surprise for everyone. Well, thank you both for joining me today. I think this is a really important conversation. The Washington Legislature is in session for about another 3 1/2 weeks at the time this airs. So we will perhaps regroup after session, see where it landed. But thank you both for all your work and the contribution you're making this session. Thank you to the listeners information for Jim, John, and I will be in the show notes. If you have any questions or comments, [00:25:30] please leave those there and I will be back with you on another GeTtin' SALTY in a few weeks.