

## CHAPTER 3C

### INSURANCE GROSS PREMIUMS TAX

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#### HIGHLIGHTS

- Purpose In lieu of all other state and local taxes on insurers except, in part, real property taxes and vehicle license fees.
  - Tax Base For insurers other than ocean marine insurers or title insurers, imposed on gross premiums less return premiums. For title insurers, imposed on all income upon business done in California other than interest, dividends, rents from real property, income from investments, gain from disposition of investments.
  - Tax Rate 2.35% on most insurers' gross premiums.  
5% on ocean marine insurers on the share of underwriting profit representing gross premiums of ocean marine insurance written within California to gross premiums of ocean marine insurance written within the United States.
  - Revenue

2002-03	\$1.9 billion
2003-04	\$1.8 billion
2004-05 (estimate)	\$2.2 billion
2005-06 (estimate)	\$2.2 billion
  - Administration Board of Equalization (BOE)  
State Controller  
Department of Insurance
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#### 1. TAX OVERVIEW

Generally, insurers doing business in California are subject to a tax on the **gross premiums** written in the preceding calendar year, less return premiums. Return premiums are premiums paid in part or in full to someone who has canceled their policy before its expiration date. Most insurers pay this insurance tax based on their gross premiums. However, insurers offering certain types of insurance use a different tax base.

**Title insurance** companies are taxed on all income from business done in California, except interest, dividends, rents from real property, profits from sale or disposition of

**CHAPTER 3C  
INSURANCE GROSS  
PREMIUMS TAX**

investments and income from investments. **Ocean marine insurers** are taxed based on their three-year average net profit. Ocean marine insurance is written on hulls, freights, sea-going vessels, and goods and wares transported on the seas.

Each out-of-state insurance company doing business in California is required to pay a retaliatory tax if its California insurance tax liability is less than the tax liability that would be imposed on a California insurance company doing the same level of business in the home state of the out-of-state insurance company.

These taxes are in lieu of all other taxes, except real property taxes.

## **2. CALIFORNIA EARTHQUAKE AUTHORITY**

By law, insurance companies that sell regular homeowners coverage in California are also required to offer earthquake insurance. However, by the mid-1990s, large payouts for the 1989 Loma Prieta and 1994 Northridge quakes resulted in many insurance companies opting out of the California market rather than risking large future losses in the event of another major earthquake. The California Earthquake Authority (CEA) was created by the Legislature in 1996 to help resolve what was then a crisis in the availability of earthquake insurance. The CEA is a privately financed, publicly managed agency that provides limited earthquake insurance coverage for residential property owners, condominium owners, mobile homeowners, and renters. As of February 2001, the CEA has access to \$7.7 billion with which to pay claims, money that was generated from policyholders, participating insurance companies and reinsurance (a form of insurance that insurers purchase to provide additional resources to pay claims).

Insurance companies that sell earthquake insurance through the CEA are not taxed on the value of their earthquake premiums, due to CEA's tax-exempt status. To date, companies that represent 66% of the earthquake insurance market sell through CEA (71% of the homeowner's insurance market). The remaining insurance companies that sell earthquake insurance (which represent 34% of the earthquake insurance market) are taxed on their earthquake insurance premiums at a rate of 2.35%.

## **3. TAX RATE**

Premiums from some pension and profit sharing insurance contracts are taxed at 0.5%. Specialized insurers (surplus lines) and marine insurers are taxed at 3% and 5% respectively. Additionally, "nonadmitted insurers" are subject to a 3% tax on gross premiums less returned premiums. Title insurers and all other insurers are taxed at a rate of 2.35%.

Proposition 103, approved by the voters in November 1988, required the BOE to adjust the rate of the insurance gross premiums tax for 1989 and 1990 to compensate for any

**CHAPTER 3C  
INSURANCE GROSS  
PREMIUMS TAX**

decline in revenue resulting from the initiative's restrictions on premiums. In January of 1991, BOE set the insurance gross premiums tax rate at 2.46% of premiums collected during the 1990 calendar year.

However, BOE's authority under Proposition 103 to administratively set the gross premiums tax rate expired at the end of 1991. Accordingly, the tax rate for premiums collected in subsequent years reverted to the constitutionally specified level of 2.35%.

**4. DEDUCTIONS**

As stated in California Constitution, Article XIII, Section 28, the insurance tax is in lieu of all other state and local taxes and license fees, except real property taxes, motor vehicle license and registration fees, and ocean marine insurance. Insurance companies, therefore, are not subject to the bank and corporation tax, nor do they pay property tax on personal property. Currently, there are no deductions allowed against insurance gross premiums tax.

**5. FEDERAL TAXATION**

Taxation of insurance companies under the federal income tax is consistent with taxation of other companies. There is no federal insurance gross premium tax.

**6. REVENUE**

The insurance gross premiums tax is entirely a General Fund revenue source. Insurance tax revenues for fiscal year (FY) 2002-03 were \$1.9 billion. They are expected to equal \$2.1 billion in FY 2003-04 and \$2.2 billion in FY 2004-06.

**7. ADMINISTRATION**

The insurance tax is jointly administered by three separate state agencies. The Department of Insurance issues permits for each class of insurance, processes returns, and audits taxpayers. California's BOE issues assessments, processes petitions, and hears appeals. The State Controller makes refunds and collects delinquencies and penalties.

Prepayments are required to be made quarterly and returns are required to be filed annually.

**8. CODE**

California Constitution, Article XIII, Section 28

Revenue and Taxation Code Sections 12202-13170