

108TH CONGRESS  
2D SESSION

# H. R. 4186

To amend the Internal Revenue Code of 1986 to provide for the creation of disaster protection funds by property and casualty insurance companies for the payment of policyholders' claims arising from future catastrophic events.

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## IN THE HOUSE OF REPRESENTATIVES

APRIL 21, 2004

Mr. FOLEY (for himself, Mr. MATSUI, Mr. MCINNIS, Mr. HERGER, Mr. ENGLISH, Mr. BOEHNER, and Mr. CHABOT) introduced the following bill; which was referred to the Committee on Ways and Means

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## A BILL

To amend the Internal Revenue Code of 1986 to provide for the creation of disaster protection funds by property and casualty insurance companies for the payment of policyholders' claims arising from future catastrophic events.

1       *Be it enacted by the Senate and House of Representa-*  
2       *tives of the United States of America in Congress assembled,*

3       **SECTION 1. SHORT TITLE.**

4       This Act may be cited as the “Policyholder Disaster  
5       Protection Act of 2004”.

6       **SEC. 2. FINDINGS.**

7       The Congress makes the following findings:

1           (1) Rising costs resulting from natural disasters  
2           are placing an increasing strain on the ability of  
3           property and casualty insurance companies to assure  
4           payment of homeowners' claims and other insurance  
5           claims arising from major natural disasters now and  
6           in the future.

7           (2) Present tax laws do not provide adequate  
8           incentives to assure that natural disaster insurance  
9           is provided or, where such insurance is provided,  
10          that funds are available for payment of insurance  
11          claims in the event of future catastrophic losses from  
12          major natural disasters, as present law requires an  
13          insurer wishing to accumulate surplus assets for this  
14          purpose to do so entirely from its after-tax retained  
15          earnings.

16          (3) Revising the tax laws applicable to the prop-  
17          erty and casualty insurance industry to permit care-  
18          fully controlled accumulation of pretax dollars in  
19          separate reserve funds devoted solely to the payment  
20          of claims arising from future major natural disasters  
21          will provide incentives for property and casualty in-  
22          surers to make natural disaster insurance available,  
23          will give greater protection to the Nation's home-  
24          owners, small businesses, and other insurance con-

1       sumers, and will help assure the future financial  
2       health of the Nation’s insurance system as a whole.

3           (4) Implementing these changes will reduce the  
4       possibility that a significant portion of the private  
5       insurance system would fail in the wake of a major  
6       natural disaster and that governmental entities  
7       would be required to step in to provide relief at tax-  
8       payer expense.

9   **SEC. 3. CREATION OF POLICYHOLDER DISASTER PROTEC-**  
10                   **TION FUNDS; CONTRIBUTIONS TO AND DIS-**  
11                   **TRIBUTIONS FROM FUNDS; OTHER RULES.**

12       (a) CONTRIBUTIONS TO POLICYHOLDER DISASTER  
13   PROTECTION FUNDS.—Subsection (c) of section 832 of  
14   the Internal Revenue Code of 1986 (relating to the taxable  
15   income of insurance companies other than life insurance  
16   companies) is amended by striking “and” at the end of  
17   paragraph (12), by striking the period at the end of para-  
18   graph (13) and inserting “; and”, and by adding at the  
19   end the following new paragraph:

20           “(14) the qualified contributions to a policy-  
21       holder disaster protection fund during the taxable  
22       year.”.

23       (b) DISTRIBUTIONS FROM POLICYHOLDER DISASTER  
24   PROTECTION FUNDS.—Paragraph (1) of section 832(b) of  
25   such Code is amended by striking “and” at the end of

1 subparagraph (D), by striking the period at the end of  
 2 subparagraph (E) and inserting “, and”, and by adding  
 3 at the end the following new subparagraph:

4                   “(F) the amount of any distributions from  
 5                   a policyholder disaster protection fund during  
 6                   the taxable year, except that a distribution  
 7                   made to return to the qualified insurance com-  
 8                   pany any contribution which is not a qualified  
 9                   contribution (as defined in subsection (h)) for a  
 10                  taxable year shall not be included in gross in-  
 11                  come if such distribution is made prior to the  
 12                  filing of the tax return for such taxable year.”.

13           (c) DEFINITIONS AND OTHER RULES RELATING TO  
 14 POLICYHOLDER DISASTER PROTECTION FUNDS.—Section  
 15 832 of such Code (relating to insurance company taxable  
 16 income) is amended by adding at the end the following  
 17 new subsection:

18           “(h) DEFINITIONS AND OTHER RULES RELATING TO  
 19 POLICYHOLDER DISASTER PROTECTION FUNDS.—For  
 20 purposes of subsections (b)(1)(F) and (c)(14)—

21                   “(1) POLICYHOLDER DISASTER PROTECTION  
 22                   FUND.—The term ‘policyholder disaster protection  
 23                   fund’ (hereafter in this subsection referred to as the  
 24                   ‘fund’) means any custodial account, trust, or any  
 25                   other arrangement or account—

1           “(A) which is established to hold assets  
2           that are set aside solely for the payment of  
3           qualified losses, and

4           “(B) under the terms of which—

5                 “(i) the assets in the fund are re-  
6                 quired to be invested in a manner con-  
7                 sistent with the investment requirements  
8                 applicable to the qualified insurance com-  
9                 pany under the laws of its jurisdiction of  
10                domicile,

11               “(ii) the net income for the taxable  
12               year derived from the assets in the fund is  
13               required to be distributed no less fre-  
14               quently than annually,

15               “(iii) an excess balance drawdown  
16               amount is required to be distributed to the  
17               qualified insurance company no later than  
18               the close of the taxable year following the  
19               taxable year for which such amount is de-  
20               termined,

21               “(iv) a catastrophe drawdown amount  
22               may be distributed to the qualified insur-  
23               ance company if distributed prior to the  
24               close of the taxable year following the year  
25               for which such amount is determined,

1 “(v) a State required drawdown  
2 amount may be distributed, and

3 “(vi) no distributions from the fund  
4 are required or permitted other than the  
5 distributions described in clauses (ii)  
6 through (v) and the return to the qualified  
7 insurance company of contributions that  
8 are not qualified contributions.

9 “(2) QUALIFIED INSURANCE COMPANY.—The  
10 term ‘qualified insurance company’ means any insur-  
11 ance company subject to tax under section 831(a).

12 “(3) QUALIFIED CONTRIBUTION.—The term  
13 ‘qualified contribution’ means a contribution to a  
14 fund for a taxable year to the extent that the  
15 amount of such contribution, when added to the pre-  
16 vious contributions to the fund for such taxable  
17 year, does not exceed the excess of—

18 “(A) the fund cap for the taxable year,  
19 over

20 “(B) the fund balance determined as of the  
21 close of the preceding taxable year.

22 “(4) EXCESS BALANCE DRAWDOWN  
23 AMOUNTS.—The term ‘excess balance drawdown  
24 amount’ means the excess (if any) of—

1           “(A) the fund balance as of the close of  
2           the taxable year, over

3           “(B) the fund cap for the following taxable  
4           year.

5           “(5) CATASTROPHE DRAWDOWN AMOUNT.—

6           “(A) IN GENERAL.—The term ‘catastrophe  
7           drawdown amount’ means an amount that does  
8           not exceed the lesser of the amount determined  
9           under subparagraph (B) or (C).

10          “(B) NET LOSSES FROM QUALIFYING  
11          EVENTS.—The amount determined under this  
12          subparagraph shall be equal to the qualified  
13          losses for the taxable year determined without  
14          regard to clause (ii) of paragraph (8)(A).

15          “(C) GROSS LOSSES IN EXCESS OF  
16          THRESHOLD.—The amount determined under  
17          this subparagraph shall be equal to the excess  
18          (if any) of—

19                 “(i) the qualified losses for the taxable  
20                 year, over

21                 “(ii) the lesser of—

22                         “(I) the fund cap for the taxable  
23                         year (determined without regard to  
24                         paragraph (9)(E)), or

1 “(II) 30 percent of the qualified  
 2 insurance company’s surplus as re-  
 3 gards policyholders as shown on the  
 4 company’s annual statement for the  
 5 calendar year preceding the taxable  
 6 year.

7 “(D) SPECIAL DRAWDOWN AMOUNT FOL-  
 8 LOWING A RECENT CATASTROPHE LOSS  
 9 YEAR.—If for any taxable year included in the  
 10 reference period the qualified losses exceed the  
 11 amount determined under subparagraph (C)(ii),  
 12 the ‘catastrophe drawdown amount’ shall be an  
 13 amount that does not exceed the lesser of the  
 14 amount determined under subparagraph (B) or  
 15 the amount determined under this subpara-  
 16 graph. The amount determined under this sub-  
 17 paragraph shall be an amount equal to the ex-  
 18 cess (if any) of—

19 “(i) the qualified losses for the taxable  
 20 year, over

21 “(ii) the lesser of—

22 “(I)  $\frac{1}{3}$  of the fund cap for the  
 23 taxable year (determined without re-  
 24 gard to paragraph (9)(E)), or



1 “(II) 10 percent of the qualified  
 2 insurance company’s surplus as re-  
 3 gards policyholders as shown on the  
 4 company’s annual statement for the  
 5 calendar year preceding the taxable  
 6 year.

7 “(E) REFERENCE PERIOD.—For purposes  
 8 of subparagraph (D), the reference period shall  
 9 be determined under the following table:

<b>“For a taxable year beginning in—</b>	<b>The reference period shall be—</b>
2008 and later .....	The 3 preceding taxable years.
2007 .....	The 2 preceding taxable years.
2006 .....	The preceding taxable year.
2005 or before .....	No reference period applies.

10 “(6) STATE REQUIRED DRAWDOWN AMOUNT.—  
 11 The term ‘State required drawdown amount’ means  
 12 any amount that the department of insurance for  
 13 the qualified insurance company’s jurisdiction of  
 14 domicile requires to be distributed from the fund, to  
 15 the extent such amount is not otherwise described in  
 16 paragraph (4) or (5).

17 “(7) FUND BALANCE.—The term ‘fund balance’  
 18 means—

19 “(A) the sum of all qualified contributions  
 20 to the fund,

21 “(B) less any net investment loss of the  
 22 fund for any taxable year or years, and

1           “(C) less the sum of all distributions under  
2           clauses (iii) through (v) of paragraph (1)(B).

3           “(8) QUALIFIED LOSSES.—

4           “(A) IN GENERAL.—The term ‘qualified  
5           losses’ means, with respect to a taxable year—

6                   “(i) the amount of losses and loss ad-  
7                   justment expenses incurred in the qualified  
8                   lines of business specified in paragraph  
9                   (9), net of reinsurance, as reported in the  
10                  qualified insurance company’s annual  
11                  statement for the taxable year, that are at-  
12                  tributable to one or more qualifying events  
13                  (regardless of when such qualifying events  
14                  occurred),

15                   “(ii) the amount by which such losses  
16                   and loss adjustment expenses attributable  
17                   to such qualifying events have been re-  
18                   duced for reinsurance received and recover-  
19                   able, plus

20                   “(iii) any nonrecoverable assessments,  
21                   surcharges, or other liabilities that are  
22                   borne by the qualified insurance company  
23                   and are attributable to such qualifying  
24                   events.

1           “(B) QUALIFYING EVENT.—For purposes  
2 of subparagraph (A), the term ‘qualifying event’  
3 means any event that satisfies clauses (i) and  
4 (ii).

5           “(i) EVENT.—An event satisfies this  
6 clause if the event is 1 or more of the fol-  
7 lowing:

8           “(I) Windstorm (hurricane, cy-  
9 clone, or tornado).

10          “(II) Earthquake (including any  
11 fire following).

12          “(III) Winter catastrophe (snow,  
13 ice, or freezing).

14          “(IV) Fire.

15          “(V) Tsunami.

16          “(VI) Flood.

17          “(VII) Volcanic eruption.

18          “(VIII) Hail.

19          “(ii) CATASTROPHE DESIGNATION.—  
20 An event satisfies this clause if the event—

21          “(I) is designated a catastrophe  
22 by Property Claim Services or its suc-  
23 cessor organization,

24          “(II) is declared by the President  
25 to be an emergency or disaster, or

1                   “(III) is declared to be an emer-  
2                   gency or disaster in a similar declara-  
3                   tion by the chief executive official of a  
4                   State, possession, or territory of the  
5                   United States, or the District of Co-  
6                   lumbia.

7                   “(9) FUND CAP.—

8                   “(A) IN GENERAL.—The term ‘fund cap’  
9                   for a taxable year is the sum of the separate  
10                  lines of business caps for each of the qualified  
11                  lines of business specified in the table contained  
12                  in subparagraph (C) (as modified under sub-  
13                  paragraphs (D) and (E)).

14                  “(B) SEPARATE LINES OF BUSINESS  
15                  CAP.—For purposes of subparagraph (A), the  
16                  separate lines of business cap, with respect to  
17                  a qualified line of business specified in the table  
18                  contained in subparagraph (C), is the product  
19                  of—

20                       “(i) net written premiums reported in  
21                       the annual statement for the calendar year  
22                       preceding the taxable year in such line of  
23                       business, multiplied by

24                       “(ii) the fund cap multiplier applica-  
25                       ble to such qualified line of business.

1           “(C) QUALIFIED LINES OF BUSINESS AND  
 2           THEIR RESPECTIVE FUND CAP MULTIPLIERS.—  
 3           For purposes of this paragraph, the qualified  
 4           lines of business and fund cap multipliers speci-  
 5           fied in this subparagraph are those specified in  
 6           the following table:

<b>“Line of Business on Annual Statement Blank:</b>	<b>Fund Cap Multiplier:</b>
Fire .....	0.25
Allied .....	1.25
Farmowners Multiple Peril .....	0.25
Homeowners Multiple Peril .....	0.75
Commercial Multi Peril (non-liability portion) .....	0.50
Earthquake .....	13.00
Inland Marine .....	0.25.

7           “(D) SUBSEQUENT MODIFICATIONS OF  
 8           THE ANNUAL STATEMENT BLANK.—If, with re-  
 9           spect to any taxable year beginning after the ef-  
 10          fective date of this subsection, the annual state-  
 11          ment blank required to be filed is amended to  
 12          replace, combine, or otherwise modify any of  
 13          the qualified lines of business specified in sub-  
 14          paragraph (C), then for such taxable year sub-  
 15          paragraph (C) shall be applied in a manner  
 16          such that the fund cap shall be the same  
 17          amount as if such reporting modification had  
 18          not been made.

19          “(E) 20-YEAR PHASE-IN.—Notwith-  
 20          standing subparagraph (C), the fund cap for a  
 21          taxable year shall be the amount determined

1 under subparagraph (C), as adjusted pursuant  
 2 to subparagraph (D) (if applicable), multiplied  
 3 by the phase-in percentage indicated in the fol-  
 4 lowing table:

<b>“Taxable year beginning in:</b>	<b>Phase-in percentage to be applied to fund cap computed under subparagraphs (A) and (B):</b>
2005 .....	5 percent
2006 .....	10 percent
2007 .....	15 percent
2008 .....	20 percent
2009 .....	25 percent
2010 .....	30 percent
2011 .....	35 percent
2012 .....	40 percent
2013 .....	45 percent
2014 .....	50 percent
2015 .....	55 percent
2016 .....	60 percent
2017 .....	65 percent
2018 .....	70 percent
2019 .....	75 percent
2020 .....	80 percent
2021 .....	85 percent
2022 .....	90 percent
2023 .....	95 percent
2024 and later .....	100 percent.

5 “(10) TREATMENT OF INVESTMENT INCOME  
 6 AND GAIN OR LOSS.—

7 “(A) CONTRIBUTIONS IN KIND.—A trans-  
 8 fer of property other than money to a fund  
 9 shall be treated as a sale or exchange of such  
 10 property for an amount equal to its fair market  
 11 value as of the date of transfer, and appro-  
 12 priate adjustment shall be made to the basis of  
 13 such property. Section 267 shall apply to any  
 14 loss realized upon such a transfer.

1           “(B) DISTRIBUTIONS IN KIND.—A transfer  
2           of property other than money by a fund to the  
3           qualified insurance company shall not be treat-  
4           ed as a sale or exchange or other disposition of  
5           such property. The basis of such property im-  
6           mediately after such transfer shall be the great-  
7           er of the basis of such property immediately be-  
8           fore such transfer or the fair market value of  
9           such property on the date of such transfer.

10           “(C) INCOME WITH RESPECT TO FUND AS-  
11           SETS.—Items of income of the type described in  
12           paragraphs (1)(B), (1)(C), and (2) of sub-  
13           section (b) that are derived from the assets held  
14           in a fund, as well as losses from the sale or  
15           other disposition of such assets, shall be consid-  
16           ered items of income, gain, or loss of the quali-  
17           fied insurance company. Notwithstanding para-  
18           graph (1)(F) of subsection (b), distributions of  
19           net income to the qualified insurance company  
20           pursuant to paragraph (1)(B)(ii) of this sub-  
21           section shall not cause such income to be taken  
22           into account a second time.

23           “(11) NET INCOME; NET INVESTMENT LOSS.—  
24           For purposes of paragraph (1)(B)(ii), the net in-  
25           come derived from the assets in the fund for the tax-

1       able year shall be the items of income and gain for  
2       the taxable year, less the items of loss for the tax-  
3       able year, derived from such assets, as described in  
4       paragraph (10)(C). For purposes of paragraph (7),  
5       there is a net investment loss for the taxable year  
6       to the extent that the items of loss described in the  
7       preceding sentence exceed the items of income and  
8       gain described in the preceding sentence.

9               “(12) ANNUAL STATEMENT.—For purposes of  
10       this subsection, the term ‘annual statement’ shall  
11       have the meaning set forth in section 846(f)(3).

12              “(13) EXCLUSION OF PREMIUMS AND LOSSES  
13       ON CERTAIN PUERTO RICAN RISKS.—Notwith-  
14       standing any other provision of this subsection, pre-  
15       miums and losses with respect to risks covered by a  
16       catastrophe reserve established under the laws or  
17       regulations of the Commonwealth of Puerto Rico  
18       shall not be taken into account under this subsection  
19       in determining the amount of the fund cap or the  
20       amount of qualified losses.

21              “(14) REGULATIONS.—The Secretary shall pre-  
22       scribe such regulations as may be necessary or ap-  
23       propriate to carry out the purposes of this sub-  
24       section, including regulations—



1           “(A) which govern the application of this  
2           subsection to a qualified insurance company  
3           having a taxable year other than the calendar  
4           year or a taxable year less than 12 months,

5           “(B) which govern a fund maintained by a  
6           qualified insurance company that ceases to be  
7           subject to this part, and

8           “(C) which govern the application of para-  
9           graph (9)(D).”.

10       (d) EFFECTIVE DATE.—The amendments made by  
11 this section shall apply to taxable years beginning after  
12 December 31, 2004.

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