

OPINION ON IRS NOTICE 2016-66 AND FORM 8886

March 15, 2017

On November 1, 2016, the IRS released Notice 2016-66 which specifies additional disclosure requirements for certain Captive Insurance Companies with regards to Transactions of Interest, transactions that the IRS believes are inconsistent with arm-length transactions and sound business practices. As soon as we were aware of this Notice we began researching its impact on the Reinsurance Companies that we service. This has been a difficult and time-consuming process, to say the least, based in-part on having to review a large collection of opinions on the matter and based in-part on the industry's push to have the IRS slim down the broad scope of the Notice. However, based on our research which included speaking with attorneys, Certified Public Accountants, and industry peers, we are comfortable in our conclusions.

In short, it is our professional opinion that the vast majority of the Reinsurance Companies that we manage *do not* need to file Form 8886 pursuant to Notice 2016-66. In more detail, it is our professional opinion that:

1. An Owner of a Life-based Reinsurance Company *does not* need to file Form 8886.
2. An Owner of a P&C-based Reinsurance Company that has *not* elected 831(b) *does not* need to file Form 8886,
3. An Owner of a P&C-based Reinsurance Company that *has* elected 831(b) and reinsures only Administrator-Obligor products *does not* need to file Form 8886.
4. An Owner of a P&C-based Reinsurance Company that *has* elected 831(b) and reinsures a mix of Administrator-Obligor and Dealer-Obligor products *might* want to protectively file Form 8886, and
5. An Owner of a P&C-based Reinsurance Company that *has* elected 831(b) and reinsures only Dealer-Obligor products *might* want to protectively file Form 8886.

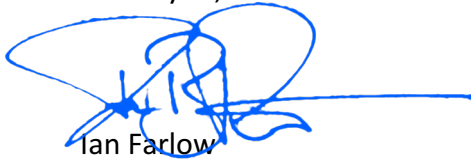
Expanding further on #4 and #5, if during the last five years the Reinsurance Company has not had a loss ratio less than 70% and has not loaned funds to related parties such as shareholders, then it is our professional opinion that the Owner *does not* need to file Form 8886.

It should also be noted that it is our professional opinion that Notice 2016-66 only applies to true Captive Insurance and Captive Reinsurance Companies. Most of the Reinsurance Companies we manage are *not* true Captive Reinsurance Companies. Typical Reinsurance Companies are owned by individual shareholders, and while these individual shareholders may also be shareholders in an associated dealership, the dealership does not own the Reinsurance Company directly. As a result, while there might be a brother-sister relationship between the dealership and the Reinsurance Company, there is not a parent-child relationship which is a critically important distinction.

However, because Dealer-Obligor arrangements are *similar* to Captive arrangements in terms of transfer of risk, we understand a desire to protectively file Form 8886 in response to Notice 2016-66 for those companies that reinsure Dealer-Obligor products.

Please see the next page for a decision tree that we hope will help the Owner determine if we think he or she should file Form 8886 for his or her Reinsurance Company.

Thank you,



Ian Farlow
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DECISION TREE

