



June 13, 2022

Mr. Andres Garcia  
Internal Revenue Service  
Room 6526  
1111 Constitution Avenue, NW  
Washington, D.C. 20224

**Submitted via Email:** [omb.unit@irs.gov](mailto:omb.unit@irs.gov)

***RE: Comment Request on Information Collection for Form 8886 (OMB 1545-1800)***

Dear Mr. Garcia:

The Self-Insurance Institute of America, Inc. ("SIIA") respectfully submits comments related to the ***Comment Request on Information Collection for Form 8886 (OMB 1545-1800)***. SIIA and its members respectfully request the Secretary of the Treasury, Commissioner of the Internal Revenue Service ("IRS"), and Office of Management & Budget ("OMB") to revise and update the filing of the Form 8886 based on the cost and administrative burden imposed by the preparation and filing requirements.

One notable example of this burden is based on the experience of captive managers and owners under IRS Notice 2016-66, Transaction of Interest – Section 831(b) Micro-Captive Transactions ("Notice"). While the preparation and filing of the Form 8886 has changed under the Notice due to recent court decisions, it is nonetheless important to address the ongoing and unnecessary burden that Form 8886 imposes on the U.S. taxpayer, particularly small and medium-sized businesses.

SIIA is a member-based association dedicated to protecting and promoting the business interests of companies involved in the self-insurance and captive industry, especially in the healthcare and workers' comp areas. SIIA's membership includes self-insured businesses, captive insurance managers (who represent thousands of U.S. businesses), industry experts, risk retention groups, third party administrators, excess/stop-loss/reinsurance carriers, and self-insured employers.

Many of our members, particularly those operating captive insurance programs, have faced onerous and ongoing filing requirements related to the Form 8886. Captive

insurance managers, captive owners, and other industry participants have spent innumerable hours, days and often times weeks, and tens of millions of dollars preparing and filing Form(s) 8886. This has been particularly intensive as part of their ongoing compliance with IRS Notice 2016-66, first issued on November 1, 2016 with an initial filing due date of May 1, 2017.

### **Form 8886 Imposes an Undue Financial & Administrative Burden on Taxpayers**

Form 8886 creates an administrative and financial burden on taxpayers due to the following factors: (1) overbroad, (2) duplicative, (3) requires significant financial costs incurred to report, (4) ongoing in nature, (5) creates uncertainty as to how to comply, and (6) demonstrates lack of IRS information access and digital capabilities.

#### **(1) *Overbroad***

When defining which taxpayers need to report information on the Form 8886, the IRS's scope is overbroad. Rather than requiring reporting based on specific fact patterns, the IRS requires reporting by a much broader range of taxpayers without ever going to public comment under requirements outlined in the Administrative Procedures Act ("APA"), which federal courts have found fault with. For example, under Notice 2016-66, captives electing 831(b) tax treatment with less than a 70% loss ratio, or any amount of related party loans or financing, triggers the requirement to file the Form 8886. However, this requirement (which the IRS argued for and lost in two Tax Court cases)<sup>1</sup> captures a number of properly structured insurance transactions simply because the loss ratio is below 70%. As a result, this overly broad criteria subjects large numbers of lawfully-created, lawfully-managed, and state-regulated captives to file a Form 8886.

Participants, many of whom are small business owners already struggling with IRS compliance are also required to disclose their participation with the IRS Office of Tax Shelter Analysis and/or on their individual and business tax returns or be subject to severe penalties,<sup>2</sup> regardless of whether their captive insurance arrangement contained any of the characteristics of concern identified by the IRS in the Notice. This has led to tens of thousands of Form 8886 filings without reason or guidance, and no action on behalf of the IRS to review the broad nature of such filings.

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*See, e.g., In R.V.I Guaranty Co.* Here, the IRS argued that lower loss ratios (e.g. between 2000 and 2006, R.V.I annual loss ratios varied from 0.3% to 64.2%, with an average annual loss ratio of 27.7%) do not reflect a "meaningful risk of loss" and therefore is not insurance, to which the Court responded, "[w]e have no difficulty concluding that ... [the] policies transferred ... a meaningful risk of loss. ... This argument is unpersuasive on both theoretical and evidentiary grounds." The IRS did not appeal the *R.V.I.* case. In *Rent-a-Center*, the IRS argued that the purchase of parent treasury stock constituted an impermissible circular flow of funds, to which the Court responded, "Respondent's expert, however readily acknowledged that he found no evidence of a circular flow of funds, nor have we." While it does not appear that the IRS expressly argued against a low loss ratio (e.g. 10.53% in 2003 and 27.14% in 2004) in *Securitas*, the Court still held that "[c]onsidering all the facts and circumstances, we find that the captive arrangement constituted insurance in the commonly accepted sense." The IRS did not appeal either *Rent-a-Center* or *Securitas*. These examples cast significant doubt on the propriety of the broad net extended by the IRS under the Notice to include captives that have less than a 70% loss ratio or that have had any related party loans or equivalent instruments. These examples cast significant doubt on the propriety of the broad net extended by the IRS under the Notice to include captives that have less than a 70% loss ratio or that have had any related party loans or equivalent instruments.

<sup>2</sup> There are strict liability fines for failing to provide complete and timely filings of up to \$10,000 per individual and \$50,000 per business, in addition to the time and expense involved in individual business compliance.

## (2) *Duplicate Reporting*

Much of the information requested in the Form 8886 is already in the IRS's possession and is filed by taxpayers with their captive's annual tax return, Form 1120-PC. When taking into account the information reporting requirements under Notice 2016-66, the Notice effectively requires at least quadruple reporting of the same transaction. Sometimes hundreds of similar Forms 8886 are required for the same transaction. For example, the following is the minimum number of separately filed Forms required by the Notice for the exact same captive insurance transaction:

- 1) The captive insurance company
- 2) The insured business that paid premium to the captive
- 3) The insured business owner (owners of S-corps and partnerships)
- 4) Any intermediary to the transaction or promoter

The quadruple reporting becomes exponentially higher when you consider that businesses typically have multiple entities, with some having hundreds, and each being required to file a separate Form 8886 with the same information. The same issue arises for business owners. Where the insured business is organized as a partnership or S-corporation for tax purposes (i.e., the most common form for small and medium sized businesses), all owners of such businesses had to file separate Forms or be subject to penalties. Consolidated reporting was not allowed for insured businesses and business owners. The prohibition against consolidated filing greatly increases the IRS's internal cost to process the Forms, in addition to a massive amount of cost and paperwork processing, and results in a tremendous unnecessary cost to taxpayers.

Lastly, an overall insured business could be owned by a large number of passive investors. These investors in many cases have zero ownership in the captive insurance company, receive zero relevant tax benefit from the captive,<sup>3</sup> and typically have no idea of the captive's existence. Yet, they each had to individually file a Form 8886 under the Notice or potentially be subject to onerous penalties.

## (3) *Significant Administrative & Financial Burden on Taxpayers*

As SIIA outlined in comments submitted to the IRS on January 30, 2017, the Form 8886 filing requirements, demonstrated by those mandated under Notice 2016-66, impose an undue financial burden and create undue complexity for small and medium sized businesses, all for little, if any, benefit to the IRS. In contrast, however, the requirements have come at a tremendous cost to many taxpayers.

According to a survey of SIIA members (only a subset of the entire industry), the burden of time and money required to File the Forms 8886 and Forms 8918 required by the Notice alone are as follows:

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<sup>3</sup> If a business buys additional insurance coverage to protect itself from downside risks, it could be argued that the business has less net profit to distribute to investors at the end of the year, which consequently means that these investors pay less federal income tax. However, no passive investor would view this as a tax benefit to themselves any more than viewing a pay cut as a tax benefit to the person who earns less salary.

Total 831(b) captives in survey <sup>4</sup>	2,397
Total number of Forms 8886 and 8918	15,021
Total cost of compliance	\$22,186,800
Average cost per captive to file all Forms 8886 and 8918	\$9,257
Total hours of compliance	121,755
Average hours per captive for compliance	50.97

A few observations regarding the above information may be beneficial to put things into perspective. The annual cost to prepare the Form 1120-PC federal tax return for a captive typically ranges from \$1,000 to \$4,000 a year. *The average cost for a captive to complete reporting requirements under the Notice was \$9,257.* Importantly, the OMB estimated that the burden for individual taxpayers filing a Form 8886 is 10.16 hours for recordkeeping and 6.25 hours for preparation of the Form, for a total of nearly 17 total hours for completion. However, Form 8886 in *actual total incurred time by SIIA members is nearly 51 hours per captive.* This illustrates the unnecessary financial, administrative, and time burdens the IRS is forcing taxpayers to bear for the purposes of receiving information that the IRS already largely has in its possession.

#### (4) *Ongoing Reporting Obligation*

The IRS requires a continuing reporting obligation under the Notice, thus Form 8886 must be filed annually by captives, insureds, and insured owners. Therefore, the IRS will continue to require preparation and submission of duplicative information and will continue to receive thousands of filings from multiple parties for the same exact transaction. This duplicative reporting requirement has never been reviewed by the IRS, nor are its cost and time estimates updated. All the while, the IRS is under no obligation to reconsider, review or offer relief to taxpayers as these requirements go on without a conclusive timeline, or any indication the IRS is reviewing these Form submissions at all. In addition, when the Form 1120-PC is filed, if the taxpayer elected 831(b) treatment with the return, they must “check the box.” Given this, the IRS could simply pull this information from the already filed Form 1120-PCs electing this tax treatment.

#### (5) *Compliance Uncertainty*

In certain cases, IRS Notices can create a great deal of uncertainty for taxpayers due to the lack of detailed instructions provided by the IRS, which can include a lack of clear guidance for filling out the Form 8886. As an example, SIIA and other industry participants made dozens of requests to the IRS for guidance under Notice 2016-66 due to multiple possible interpretations of the Form filing requirements. Furthermore, the potential fines and penalties associated with any mistakes in completing the Form are severe, ranging from \$10,000 to \$50,000. Despite taking every reasonable action to

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<sup>4</sup> These numbers reported do not reflect the entire small captive industry. These numbers are from a subset of the industry that are members of SIIA participating in the survey.

comply, taxpayers are left with significant uncertainty, receiving no guidance from the IRS during the filing process (and in the case of Notice 2016-66, this dates back to 2016).

(6) *IRS Access to Information & Need for Digital Submission*

Under the current IRS process, a great number of taxpayers must submit a Form 8886 in hard-copy form. This hard-copy submission typically requires dozens of boxes of documents to be sent to the IRS every year for each captive client. Since 2017, SIIA members have consistently found, after submitting a Form 8886 for various captive participants, that IRS staff, including field agents, have no ability to access or obtain the Form 8886 already submitted. In a number of cases, IRS staff have asked taxpayers to provide them with copies of the Form 8886 filings that the IRS should already have in their possession. This is after these same taxpayers have complied and sent the Form year after year, at the cost of tens of thousands of dollars.

This also points to the problem and cost of the IRS requiring the submission of the Form 8886 in hard-copy form via the U.S. postal mail. Unfortunately, without the technology or digital capabilities in place by the IRS, this current process not only costs taxpayers additional resources and time, but largely makes these Forms inaccessible to most IRS staff. Further, when asked where IRS staff can access submitted Forms 8886, many have no answer, nor ability, to access them at all. They then must rely on taxpayers, who are already required to submit and mail in these Forms, to supply them yet again.

**Examples of Needed Technical Corrections**

To demonstrate the harm and the overly burdensome paperwork process Form 8886 can be for the IRS and taxpayers, it is helpful to go through a few examples.

*Example #1:* A section 831(b) electing captive is insuring some of the risks of 350 franchise locations throughout the country, each legally formed as a separate entity and each filing its own tax return. There is sufficient common ownership between the franchises that the Notice applies. Because of the 350 entities and the dozens of related and unrelated owners of these entities, there will be over 400 Forms 8886 filed for this one captive insurance arrangement, which the IRS would ostensibly review individually. A more efficient approach would be to allow this captive to file one aggregated report for all insureds and owners. The IRS would receive all of the same information, but it would be organized efficiently on one document.

It is important to highlight that the Form 8886 does not require a signature under penalties of perjury by each filer, as is required on a tax return. It is an information statement that conveys data to the IRS, nothing more. In this Example #1, the same CPA will prepare the 400+ Forms 8886 reporting the same transaction information for each filer, only changing the names and addresses on each hard-copy of the Form 8886. While preparing 400+ similar forms is a financial cost to the taxpayer, it is a greater cost for the

IRS to sort through, organize, and review 400+ paper forms. A single consolidated filing could provide the same information and save IRS resources.

*Example #2:* ABC LLC is a partnership that develops and manages real estate. Person X owns 80% of ABC and person X owns 100% of a captive insurance company that insures certain risks of ABC. There are 20 passive owners of ABC, all are unrelated to Person X and each of these persons' ownership percentages range from 0.1% to 5% of ABC. Each of these 20 passive owners will receive a schedule K-1 showing the income and expenses (including insurance expense) of ABC. Because these 20 owners are shareholders of an insured business, Notice 2016-66 requires that each provides a Form 8886 or be subject to strict liability penalties. None of these 20 small ABC owners are owners of the captive, and so they receive no financial upside from the § 831(b) election of the captive.

In this Example #2, there are 23 Forms 8886 that need to be filed. One by the captive, one by ABC, one by Person X, and 20 by the other investors. The 20 investors are questioning why the IRS is threatening each of them with penalties if they don't file, when they did not benefit financially from the section 831(b) election. The Notice should be modified to require reporting only by those persons that are material owners that benefit from the tax election. These 20 passive investors should not be burdened with this filing.

*Example #3:* An engineering firm owned and utilized a captive insurance company to insure part of its professional liability risk for years, and the captive has been successful in this area. This engineering firm is owned currently by 15 engineers, and another 5 engineers at some time in the last 10 years have been owners that have either retired or moved on to different firms. Since the use of the captive indirectly flowed to each engineer's tax return, all 20 must now file disclosure forms with the IRS or face severe penalties. Without an aggregate filing option, each engineer will be required to file, subject to penalties. Some of these persons may not be locatable or may be deceased. To save the time from having to track down all prior owners, an aggregate filing option is needed.

### **Review the Need for Form 8886 Filings and Modify the Federal Tax Return**

Certain Form 8886 reporting requirements should be reviewed in order to ascertain the need for future filings. For instance, the first filings under Notice 2016-66 (done without following the APA) were completed by May 1, 2017. The IRS now has hundreds, of thousands of filings to review and should be able to glean any information it needs from those. An ongoing filing obligation is not necessary.

The question then remains as to why the IRS is mandating annual filings with the returns, and at such tremendous taxpayer burden, if the IRS does not have a process in place to allow access to filings by IRS personnel. If the taxpayer is expected to undertake the time and resources to comply, the IRS should streamline the process and reduce the overall burden.

If the IRS feels that the information it receives regarding a captive's annual tax return is not sufficient or not organized in the manner it wishes, there is a less burdensome approach to collect this information than the ongoing and duplicative requirement of Form 8886. As SIIA formally requested in 2017, the captive's annual tax return on Form 1120-PC should be modified to ask for the information that the IRS wishes to receive, and should be able to be submitted electronically. The Form 1120-PC already has Schedule B which is dedicated for the filers electing the section 831(b) election. Reorganizing this section or expanding it would be an efficient, low-cost way for the captive insurance industry to report. While we recognize that modifying a tax return is not an easy task for the IRS, in light of the burden this is causing to the industry, this seems like a reasonable and appropriate solution. Incidentally, it will also save the IRS time and resources to have everything organized in one comprehensive filing.

Lastly, the IRS should better put in place a system and procedure in which taxpayers can file concerns and grievances concerning the unnecessary burden and cost the IRS imposes upon them, and have those concerns listened to. This need is further exacerbated when the Service issues Notices to taxpayers that fail to comply with the APA, and does not allow for public comment.

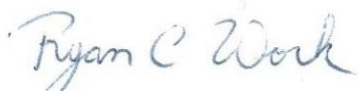
## **Conclusion**

Rather than taking an appropriate and reasoned regulatory course to prevent abuse within the captive space, the ongoing and often unnecessary filing of the Form 8886 imposes a sweeping burden, cost, and complexity on taxpayers, especially small- and mid-sized businesses.

As outlined, the IRS should at the very least review the necessity and compliance burden of Form 8886, particularly considering the lack of access to the filings, as well as the need for additional digital submission capabilities.

We greatly appreciate your review of the compliance burdens imposed by Form 8886 on taxpayers. If you have any additional questions or would like to discuss this further, please do not hesitate to contact me at [rwork@siia.org](mailto:rwork@siia.org).

Sincerely,



Ryan C. Work  
Senior Vice President, Government Relations  
Self-Insurance Institute of America, Inc.