COLORADO
Department of Revenue
Taxation Division

Office of Tax Policy
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PLR-08-001

November 23, 2008

XXXXXXXXXXXXXXX
Attn: XXXXXXXXXXX
XXXXXXXXXXXXXXX
XXXXXXXXXXXXXXX

Re: XXXXXXXXX

Dear XXXXXXXX,

XXXXXXXXXXXXXXXXXXXXXX ("[Company]") submitted a request, dated August 25, 2008,[1] for a private letter ruling pursuant to Department Regulation 24-35-103.5. This letter is the Department's private letter ruling.

Issue

Is the Company exempt from Colorado's corporate income tax because the Company is "subject to" Colorado's gross premium tax, even though the Company is also exempt from the gross premium tax?

Conclusion

The Company is exempt from Colorado's corporate income tax.

Background

The Company asserts the following facts, which the department accepts as complete and accurate only for purposes of this ruling. The Company is a [another state] domiciled insurance company and a wholly owned indirect subsidiary of XXXXXXXXXXXX [another company]. The Company was formed in 2005 for the sole purpose of providing benefits as a prescription drug plan under the federal government's

[1] On August 25, 2008, the Company submitted a request for a "ruling." By letter dated September 16, 2008, the department informed the Company that it had not submitted the base fee with the request as required by Department Regulation 24-35-103.5. The Company submitted that payment by letter dated October 9, 2008.

Medicare Part D program, which is administered by the Centers for Medicare and Medicaid Services (CMS).

From its inception, the Company has offered only Medicare Part D plans and these plans are made available to eligible participants in all 50 states and its territories. The Company is licensed as an insurer in 36 states and has filed expansion applications to become a licensed insurer in states where it is require to do so, and will file applications in the remaining state upon satisfaction of seasoning requirements. The Company operates under a waiver from CMS in states where it is not licensed. In addition to filing license applications, the Company files zero liability gross premiums tax returns in all applicable states, including Colorado.[2]

Discussion

Colorado imposes corporate income tax on domestic and foreign corporations doing business in Colorado in an amount equal to four and sixty-three one-hundredths percent of the net income of such C corporation derived from sources within Colorado. §39-22-301(1)(d)(I), C.R.S. However, Colorado exempts from such tax insurance companies that are "subject to" Colorado's gross premium tax. Colorado's gross premium tax is imposed on insurance companies writing business in this state. The tax is measured by the amount of premiums collected or contracted for on policies or contracts of insurance covering risks in this state during the previous calendar year. §10-3-209, C.R.S.

The Company asserts that federal law prohibits states from imposing a premium tax for the payment CMS makes on behalf of Part D plan or enrollees; or for any payment made to Part D plans by beneficiary or by a third party on behalf of a beneficiary. 42 C.F.R. §423.440(b) ("Medicare exemption").[3]

The resolution of the issue in this case turns on the proper interpretation of the term, "subject to," in the income tax exemption statute. One interpretation would deny the income tax exemption if an insurance company is exempt from the gross premium tax. The Company, on the other hand, asserts that it is "subject to" the gross premium tax because it is an insurance company that falls squarely within the gross premium tax statute,[4] and that it does not matter, for purpose of the income tax exemption, whether some or all of the company's gross premium revenues are exempt from that tax.

We conclude that the income tax exemption applies to an insurance company which is the subject of the gross premium tax statute, regardless of whether the premiums of the insurance company are otherwise exempt from the gross premium tax. We reach this

[2] Our ruling is dependent on the Company holding a license from the Colorado Division of Insurance. If the Company does not have a license or if the Company does not operate in Colorado so as to come within the jurisdiction of the statute and division, we would not conclude that the Company is exempt from Colorado income tax.

[3] The department accepts as complete and accurate the Company's representation that federal law prohibits Colorado from imposing the gross premium tax on the payments described here. However, the department does not administer the gross premium tax and does not offer an opinion regarding the completeness or accuracy of the Company's representation. This ruling does not constitute a determination that any representation of fact or law by the Company is complete and accurate.

[4] As is true of other the Company representations, the department has not independently verified that the company is an insurance company or that it is subject to the gross premium tax. These factual and legal representations are presumed complete and accurate only for purposes of resolving the proper interplay between the income tax exemption and a company exempted from the gross premium tax by reason of the federal prohibition.

conclusion for two reasons. First, and broadly speaking, it is clear that the legislature intended to exclude insurance companies from income taxation even if they are exempt from the gross premium tax. For example, fraternal associations are exempt from the state's income tax because they are specifically referenced in, and are subject to, the gross premium tax statute. These fraternal associations also enjoy a complete exemption from the gross premium tax pursuant to a specific exemption. §10-3-109(1)(d), C.R.S. (fraternal associations are exempt from the gross premium tax).

Similarly, premiums generated by a mutual protective association writing only crop insurance are exempt from the gross premium tax to the extent that revenues are designated for a loss fund. §10-3-209(1)(d)(2), C.R.S. Such companies remain exempt from Colorado's corporate income tax notwithstanding the fact that only a portion of their gross premiums are actually liable for the gross premium tax. Given that the income tax exemption applies regardless of whether one percent or ninety-nine percent of the company's gross premiums are exempt, it is only a matter of degree that, as in this particular case, one-hundred percent of the company's gross premium revenues are exempt from the gross premium tax. [5]

Second, the legislative framework in which these taxes are placed also indicates the legislature intended to "silo" income from premiums, and investment income from those premiums, into its own tax matrix, separate and apart from Colorado income tax, and, importantly, it intended not to reassert Colorado's income tax in cases where the premiums are exempted from the gross premium tax. The gross premium tax statute states that the gross premium tax is the only tax (with certain exceptions not relevant here) that applies to this insurance income. §10-3-209(1)(c), C.R.S. This prohibition applies even though the statute then specifically excludes certain premium revenues (noted above) from the gross premium tax, effectively leaving such premiums exempt from all state taxes. Had the legislature intended to reassert the income tax in situations where the premium tax is exempted from the gross premium tax, it would have included a reference to income tax in §10-3-209(1). This "silo" view of insurance company taxation is consistent with the legislature's general treatment of insurance companies *vis a vis* corporations.[6]

Thus, we have a statutory framework in which insurance companies are excluded from income taxation regardless of whether they actually pay the gross premium tax. In the present case, the exemption from the gross premium tax comes not from state statute, but by virtue of federal legislation and the Supremacy Clause of the United States Constitution. We do not believe, however, that this is a material difference in terms of the interplay between these two statutes. The Company is an insurance company that is the object of §10-3-209, C.R.S. and, therefore, exempt from the income tax statute. The statutory framework makes it clear that an insurance company, which is the object of the

[5] Compare, *L.L.F. Realty Co. v. Fuchs*, 273 A.D. 111, 75 N.Y.S. 2d 356 (N.Y. 1947) (property that was removed from the property that is subject to assessment was nevertheless "subject to" tax and, therefore, properly included in the calculation of budget limitations; there is no requirement that the property actually be taxed).

[6] Compare, *Greiger v. Salzer*, 165 P 240 (Colo 1914), in which the court held that the legislature created a formation process for insurance statutes that is distinct from that process which normally governs corporations.

insurance statute, does not lose the income tax exemption if some or all of its premiums are also exempt from the gross premium tax.

We note, however, that the contrary argument is not without substance. On first blush, one could conclude that the Company is not subject to the gross premium tax because it does not actually owe the tax. However, and for the reasons noted above, the statutory framework indicates that "subject to" does not mean that the company must actually owe the tax.

Similarly, in the area of income tax apportionment under Colorado's multi-state tax compact, income apportioned to another state is "thrown back" to Colorado if the income is not "subject to" taxation in the other state. States, including Colorado for tax years prior to January 1, 2009, have concluded that income is not "subject to" taxation of another state if the income is protected under P.L. 86-272 (a federal prohibition against states taxing income derived solely from solicitation of business in another state). See, e.g., Colorado Regulation IV.3.(c), 1 CCR 201-3. We conclude, however, that the analogy is inapplicable. The multi-state income tax framework is generally interpreted to avoid "nowhere" income – that is, allowing one state, which would otherwise apportion the company's income to another state, to tax the income if the other state is prohibited from taxing the apportioned income. In contrast, the gross premium tax statute and the income tax statute are akin to silos; the income tax exemption applies even though the premium is also exempted under the gross premium statute.

In sum, we conclude that the Company is exempt from Colorado's income tax because it is an insurance company "subject to" the gross premium tax, and this exemption applies regardless of whether the company's premiums are exempt from the gross premium tax by virtue of federal law. A contrary conclusion is inconsistent with the express terms of §10-3-209, C.R.S. and the general statutory framework governing insurance companies.

This ruling is premised on the assumption that the Company has completely and accurately disclosed all material facts. This ruling is further premised on the Company's representation that it is an insurance company within the meaning of §10-3-209, C.R.S. and that, based on the facts set forth in its letter, federal law prohibits the state from applying the gross premium tax. The department reserves the right, among others, to independently evaluate the Company's representations. This ruling is null and void if any such representation is incorrect and has a material bearing on the conclusions reached in this ruling.

Enclosed is a redacted version of this ruling. Pursuant to statute and regulation, this redacted version of the ruling will be made public within 60 days of the date of this letter. Please let me know in writing within that 60 day period whether you have any suggestions or concerns about this redacted version of the ruling.

Sincerely,

Office of Tax Policy
Colorado Department of Revenue