

# SIIA TAKES THE LEAD WITH THE “Captive Code of Conduct”

**I**n January, SIIA released the Captive Manager Code of Conduct—a document meant to guide captive managers to a high standard of ethical conduct and to help strengthen the reputation of the captive industry. With this Code, the association hopes to take a proactive approach to answer any lingering questions about the validity and effectiveness of captives.

In the last five years, the captive industry’s reputation has repeatedly come into question, even as the market has continued to expand. The Internal Revenue Service first began to list captives using the 831(b) tax exemption to the “Dirty Dozen” list—a list of business structures the IRS believes to be tax shelters—in 2014.

That segment of the captive market took another hit in late 2017 when the United States Tax Court

released its decision against the captive owners in the case of *Avrahami v. Commissioner*, a highly anticipated case regarding a captive insurance company using the 832(b) tax code. Several other similar court cases are still pending, due to be decided this year.

One of the central issues surrounding captives using the 831(b) tax designation—these captives are referred to Enterprise Risk Captives (ERC)—is that some captive managers may be promoting their use as a tax scheme.

This issue involving this one segment of the captive industry has created a larger issue of reputation for all captives. There has been much discussion among captive industry professionals about how to deal with managers that are misusing the system while advocating for captives in the larger insurance marketplace, with regulators, and with potential captive owners.

SIIA's Captive Committee decided to meet this issue head on by creating the Captive Manager Code of Conduct as a guideline for the captive industry. The Code is broad enough to encapsulate all types of captives and their managers, not just ERC captives. SIIA sees it as a way to better inform consumers and regulators about how to evaluate captive manager business practices and to help the captive industry in general.



Ryan Work

According to Ryan Work, vice president of Federal Government Relations for SIIA, and staff lead for the working group, "It's important for the industry as a whole that SIIA has taken the lead to establish benchmarks for captive managers—which are a growing part of our membership. It shows that we're serious. From a regulatory and legislative perspective, it shows that we're

not just chasing criticism and having to explain to policymakers what captives are. We're actually getting out there and taking the lead."

### CODE OF CONDUCT

In early 2018, SIIA's Captive Committee formed a working group to address these ongoing issues surrounding captives and captive managers. The group's mission was to look at what the industry needed and to draft ethical guidelines that would help distinguish "best in class" captive managers.

"We realized there was no single source or guideline that managers could commit to as baseline standards," said Jerry D. Messick, CEO of Elevate Captives, who took part in the development of the Code as a member of the working group. "We also appreciate it's a beginning, but everything requires that first step and we feel like we now have a good start."



Jerry Messick

Harry Tipper, III, the Chief Operating Officer - insurance for CaptiveOne Advisors LLC, also a committee member, said,



Harry Tipper

"The captive industry has evolved significantly from its beginnings primarily as a tool of large corporations and to make it down to Main Street America. The members of the SIIA committee wanted to make sure that we as practitioners in the business established a set of standards for our own conduct."

The idea of the Code of Conduct has been in the works for a long time, according to Work. "Over the course of the last couple of years, the idea has matured. One reason is that [SIIA's] captive membership has increased by more than 50% since 2015.

Another reason is everything that has been going on with regulation and tax policy surrounding captives. Our members saw more and more that they needed a tool to help create a better bright line for appropriate captive manager practices, especially as we looked at the repercussions of the IRS activities and recent tax court decisions."

"Personally, I've felt for a long time that we need a standard of conduct that would allow managers to demonstrate a best practice approach to the greater public," added Messick. "I'm in my 35th

## Captive Code of Conduct

year of working with captives and take great pride in our profession. The Code makes us all stronger.”

### THE FIVE CANONS

The Captive Managers Code of Conduct is organized into five canons and meant to be a guideline for captive managers as they navigate through the complicated insurance management and reinsurance business.

The five canons address Integrity, Conflicts of Interest, Confidentiality, Advertising, and Practice Management. The canons on Integrity and Practice Management break-down the expectations into fine detail. The Integrity

section outlines the basics in ethical management for the client and in working with regulators. The Practice Management details good communication, best business practices, and record management.

When asked why the committee chose these five canons, Messick stated, “There are obviously other areas to be considered, but as a starting point, these are foundational.”

The main emphasis of the canons focuses around the day-to-day business of captive managers, but it also reflects the criticism that managers often see from insurance regulators. According to Work, “The canons focus on ethics and transparency, communications, and on administrative procedures. Captive managers have a responsibility to their clients, but they also have a responsibility to the industry and other captive managers.”

On first review, the canons seem to be how any sensible manager would conduct their business. The committee members put a lot of thought into how to create a foundation document and how to state as simply as possible the guidelines the proposed.

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They wanted to start at the very foundation of what good management means and build from there. Jerry Messick describes it this way, “Sensible was a big component of what we were trying for. Our first thought was to provide guidance on the how and why of doing a captive the right way. This would allow the public (as well as new managers) a structure that would help guide them as they considered whether a captive would be an appropriate solution to their risk financing needs. It would help regulators in providing a common-sense approach to those managers that commit to the Code.”

### CODE OF CONDUCT REVIEW TASK FORCE

Now that the Code has been released and is getting positive feedback industry wide, SIIA has commissioned a new working group, the Code of Conduct Review Task Force (CCRTF). This group will be tasked with working with SIIA members and industry professionals to further improve on the Code. The idea is for it to meet at least quarterly, so that committee members can stay on top of changes in the industry.

According to Tipper, the new Task Force, “Grew out of the fact that as we developed the code and worked on getting the whole Captive Committee’s

buy in, we realized the final Code should be a living and breathing document. It’s not a static thing. Circumstances will change. Technology will make circumstances change. So the idea for the new task force was that this should, like most codes of conduct, have a mechanism created to review it periodically so that it’s up-to-date in the current best practices, and that if questions arise [CCRTF] can provide some guidance to people on how to handle situations.”

The CCRTF had its initial meeting on March 1st. The first order of business for the CCRTF will be to review how the dissemination of the Code went and to look for other ways to further communication with stakeholders and regulators.

The working group also wants to investigate how to build other infrastructure around the code—such as adherence requirements or a formalized record of signatories.

Lastly, the group will look at getting industry feedback for changes and updates to the Code. According to Messick, who is chairing the CCRTF, “To that end, we will be establishing a window of time for industry participants, including regulators, captive owners, and others to comment on how to make the Code stronger.”

Messick continued, “The [CCRTF] is designed to continually improve upon the Code and make sure it serves those it’s designed for—regulators, the public, and the managers that commit to it. We hope regulators will adopt the Code as one more standard in reviewing a captive manager’s approach to creating and managing captives. For the public, we hope it provides them with a pathway of how it will be done and what to look for in selecting a manager. We will be looking at improving the canons and determining what the future might hold for a more defined best practice approach for captive managers. We must, and we will continue to, make this Code stronger for everyone in the industry.” ■

Karrie Hyatt is a freelance writer who has been involved in the captive industry for more than ten years. More information about her work can be found at: [www.karriehyatt.com](http://www.karriehyatt.com).

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