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In April 2024, Raymond Ankner and his captive management company RMC Group won an important case against the Internal Revenue Service (IRS) with the assistance of law firm Zerbe, Miller, Fingeret, Frank and Jadav (ZMFF&J).

The jury concluded that the IRS failed to show that the captive manager was liable for Internal Revenue Code Section 6700 penalties, which govern the promotion of abusive tax shelters.

RMC becomes the first micro-captive to prevail against the IRS in court on this issue, marking a big step in the ongoing dialogue surrounding compliance in the management of captive insurance companies.

The Ankner case focused on the IRS's assertion of penalties under IRC Section 6700. Can you provide an overview of the key elements that must be established for the imposition of those penalties, and how the court's analysis of those elements played out in this case?

Under Section 6700, the government must prove: (1) there was a partnership, entity, investment plan, or arrangement; (2) the person (including an employee or agent) must make a false or fraudulent statement; (3) that person must know or have reason to know that the statement is false; (4) the statement must be with respect to a material matter.

Although the definition of the first element, a plan or arrangement, is very broad, case law from other circuits indicates that the plan or arrangement must relate to a tax shelter. That is why we requested the court instruct the jury that they must find that Ankner and his companies — RMC Group — organised a plan or arrangement for the purpose of tax avoidance. The court did not instruct the jury as per our request, and defined the term 'plan or arrangement' very broadly. The Department of Justice (DOJ), on behalf of the IRS, pointed to several instances in the documents where RMC used the term 'programme' in describing their services in connection with the formation and management of 831(b) captives, and tried to equate the use of that term as a stand-in for an admission to plan or arrangement. That fell flat with the jury, and we were able to draw a distinction that appeared to have weight with the jury despite the court not instructing them on the tax shelter element of the plan or arrangement.

The second element consists of a false or fraudulent statement. The DOJ cited various statements from RMC Group's emails and marketing materials, indicating that insurance premiums could be deductible as ordinary and necessary business expenses under Section 162(a), and that Section 831(b) provides an exclusion from taxable income to the captive for premiums paid to the captive, with only investment income subject to taxation. These are generally true statements, but the DOJ asserted that they are false because the companies never actually obtained 'insurance' as defined by the court. The government hired three expert witnesses (an economist, an actuary and an underwriter) to prove to the jury that the captives were not real insurance companies, but then only brought two of the three to the trial.

The experts tried to persuade the jury that RMC's captives were not real insurance companies because they did not meet the insurance's risk distribution element. Shortly before trial, the DOJ conceded that the captives were covering insurable risk, had risk shifting, and were insurance companies in the commonly

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accepted sense — all the other elements of insurance. The government was only challenging risk distribution.

The government's position was that if the captives did not provide risk distribution, then they were not real insurance companies, and the statements regarding deductions by the insured businesses and exclusion of income by the captives would be false. The jury did not find that RMC made false statements.

The third element is that the individual making the purportedly false statement must know the statement is false or fraudulent, or have reason to know. It is this element of a Section 6700 penalty that may have weighed most heavily in the jury's verdict. We showed that the captives managed by RMC did distribute risk through reinsurance agreements, in which they accepted risk from unrelated insureds. We hired Robert Walling of Pinnacle Actuarial, who analysed the programme and concluded that it did distribute risk.

More importantly, RMC's general counsel, Jeffrey Bleiweis, testified that he had engaged in substantial research before RMC began managing captives and had found scant guidance from the IRS about how a small captive insurance company can achieve risk distribution. Bleiweis testified that the only relevant guidance at the time was Revenue Ruling 2002-89 and that the captives were structured in such a way as to comply with the requirements of the revenue ruling.

The fact that the DOJ brought two paid expert witnesses to the trial in 2024, to argue that the the captives did not meet the risk distribution requirement, was a red herring meant to confuse the jury. But the main concern for the jury is what RMC knew in 2010, not what the government's paid experts believed in 2024. The jury seemingly held the view that RMC, having adhered to the IRS's guidance, did not know and had no reason to suspect that the captives did not meet the risk distribution requirement. As a result, the jury likely found that the government did not prove the knowledge element of a Section 6700 penalty.

Finally, the last element that the government had to prove was that any statement was about a material matter or that a reasonable person would have relied on the subject statements. We presented evidence indicating that customers entered the programme solely for risk management purposes. The government did not offer any evidence to counter this point.

The jury determined that the government did not meet its burden to prove each of the four elements of Section 6700 by a preponderance of the evidence.

The court's opinion suggests there were material disputes of fact around whether the plaintiffs' captive management activities constituted a 'plan or arrangement' under the statute. What were the key factual nuances that made this a close and complex question?

The 'plan or arrangement' element has been defined broadly by the courts. The government took this element for granted and tried to equate RMC Group's use of the term 'programme' in various marketing materials to establish a plan or arrangement.

In defence, we argued against the government's partial motion for summary judgement, citing case law from other courts that required the government to demonstrate a connection between the 'plan or arrangement' and a tax shelter, a requirement we believed the government could not meet. We also argued that the captives did not constitute a 'plan or arrangement' because each captive was a separate company with different owners, directors and insureds. The court, in ruling on the government's partial motion for summary judgement, chose not to extend the law as far as we suggested but found that there was a genuine issue of material fact whether the RMC captives constituted a 'plan or arrangement'. The court also ruled that the government had the burden of proving that there was a 'plan or arrangement' and they could not simply rely on the use of the word 'programme' to do that even if the term is broadly defined.

The government sought to preclude the plaintiffs from relying on advice from their general counsel, Jeffrey Bleiweis, to negate the scienter requirement. How did the court analyse the potential conflict of interest issues surrounding Bleiweis' role?

The government's argument on this issue was never clear. Jeffrey Bleiweis is general counsel for RMC Group but also vice president, and he played a key role in determining how RMC should organise and manage captive insurance companies and how the captives could achieve risk distribution. In addition, he drafted most of the marketing materials that the government claimed contained false statements.

He was a key witness for the scienter requirement in this case. Any knowledge imputed to RMC Group was Bleiweis' knowledge or based on memoranda drafted by Bleiweis for the benefit of RMC Group employees. Through summary judgement, the DOJ requested that we refrain from introducing evidence demonstrating RMC Group's reliance on his knowledge and advice. This request is likely due to the fact that many tax code penalties provide exceptions for taxpayers who have relied on professional tax advice, even though the Section 6700 penalty does not contain a reliance exception. The argument by the DOJ never made any sense, and the court pointed that out in its ruling on the government's partial motion for summary judgement. We were not claiming that RMC was immune from penalties under Section 6700 because they relied on Bleiweis' advice. Our argument was that Mr. Bleiweis' knowledge was RMC's knowledge and that the only way for the government to prove the element of knowledge was to prove that he either knew or had reason to know that his advice was false.

Assuming liability, the government sought summary judgement on the full penalty amounts assessed. What were the key disputes around the proper calculation of the penalties, and the burden of proof considerations?

The IRS miscalculated the penalty amounts for one of the corporate plaintiffs as well as for Ankner individually, and we presented evidence to that effect. If the government had been able to meet its burden of proof that the Section 6700 penalty could be assessed, then we would have had to prove that the amounts assessed by the IRS were incorrect. We were able to provide evidence that Ankner did not derive his income directly from RMC's captive management. He provided no direct service to the captives.

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Anything that he did was in his capacity as an officer and employee of the corporate plaintiffs. We also showed the source of all revenue derived from RMC's management of captives and proved that the revenue was paid solely to one or more of the corporate plaintiffs.

The government was, in effect, assessing a double penalty on the same revenue — first when paid to the corporate plaintiffs and then when Ankner was paid a salary by the corporate plaintiffs. Penalties under Section 6700 are already extraordinarily heavy, but it does not allow the government to penalise the same gross income twice, which is what the IRS tried to do here.

For the corporate plaintiff where we claimed that the IRS had miscalculated the penalty, we argued that the IRS had included insurance commissions in RMC income, despite the fact that the insurance companies had paid RMC these commissions, expressly requiring RMC to pay them to a third-party, and that the selling agents who earned these commissions were not RMC employees. Those commissions should not have been included in RMC income because RMC never had the right to those commissions.

The jury did not reach the issue of the amount of the penalties, concluding that the penalties could not be assessed against RMC or Ankner. However, this issue underscores the IRS's heavy-handed approach to these penalties. The IRS clearly took an approach more focused on looking to put RMC Group out of business with such draconian penalties than trying to apply the law appropriately.

In your view, what are the broader doctrinal implications of the court's refusal to grant summary judgement, even on individual elements of the government's case? How does this align with the standards for partial summary judgement?

I think that sometimes the courts (and practitioners) have difficulty extricating the legal arguments that can, and in some cases should, be settled on summary judgement. Dealing with a highly technical and fact-intensive case like captive insurance transactions exacerbates this issue. In retrospect, we would have much rather resolved the case in a pretrial motion and saved our client substantial legal fees and other costs, but at the end of the day, we are happy that the jury came to the conclusion they did. This was one of the first times the District Court has seen a case of this type, so we are hopeful that it provides an avenue for a judge to limit some of these issues via motion for summary judgement when appropriate.

As previously stated, these cases heavily rely on facts, so it is crucial for taxpayers and their legal representatives to present the complete picture and provide the jury with the necessary information to reach a fair decision.

This case has been described as a landmark win for the captive insurance industry. From a policy perspective, what do you think were the most significant aspects of the jury's rejection of the IRS's penalty assertions?

This is the first win for anyone in the 831(b) space. The IRS has notched seven straight wins in the tax court against individual captive insurance companies. The federal government had a lot of momentum prior to this decision, so I am hopeful that this taxpayer-favourable win balances things out a bit.

How do you anticipate this decision may influence the IRS's future enforcement approach in the micro-captive space, both in terms of asserting penalties and the level of scrutiny applied to captive arrangements?

We hope that the IRS is more prone to come to the table and make reasonable considerations on the front end — in audits, appeals and pre-litigation. It is an open secret that the IRS has not provided taxpayers with very many options for resolving a case other than going all the way to litigation or accepting a complete disallowance.

We have seen the IRS make 'settlement offers' consisting of a complete disallowance and penalties before even looking at a copy of the taxpayer's return. We want taxpayers to get a fair shake and an opportunity to be heard.

What lessons can captive insurance providers and their advisors take away from the Ankner case when it comes to navigating the complex regulatory landscape and potential disputes with the IRS?

Facts matter, and records do too. That your captive or your program has operated in a forthright and ethical manner is not something that the IRS, the DOJ or a jury will assume. It is extremely important to (1) comply with the law and (2) keep records demonstrating your due diligence. In many cases, the IRS is asking about things that happened ten-plus years ago.

Being able to access those records and explain your actions to the court is invaluable.

Looking ahead, what outstanding issues or unresolved questions remain in this area of tax law that may be ripe for future litigation or regulatory clarification?

We, like many other practitioners in the area, are waiting for the courts, Treasury, or Congress to provide guidance that illustrates what they want to see in an 831(b) captive programme. Many large corporations have formed captives, so captives are ubiquitous.

Congress has explicitly provided for small insurance companies. Now that smaller entities have taken advantage of Section 831(b) and also formed captives, the IRS has decided that it wants to write Section 831(b) out of the Code.

The IRS should provide guidance to advance Congress' desires rather than frustrate them.

Via the cases that have passed through the courts thus far, we have seen glimpses of things that the IRS does not like, but very little in the way of how they intend to implement Section 831(b) as enacted by Congress.

The IRS often makes out captive providers to be boogeymen, but in our experience, nearly everyone we have worked with is a professional trying to do the best they can for their clients, with very little help from the IRS. ■

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