## Contents

This IPT information booklet covers the following topics:

<table>
<thead>
<tr>
<th>Topic</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>European IPT</td>
<td>2</td>
</tr>
<tr>
<td>Parafiscal Charges</td>
<td>3</td>
</tr>
<tr>
<td>Fiscal Representation</td>
<td>4</td>
</tr>
<tr>
<td>International IPT</td>
<td>5 - 6</td>
</tr>
<tr>
<td>US Direct and Self Procurement Taxes</td>
<td>7 - 8</td>
</tr>
<tr>
<td>IPT Tax authorities</td>
<td>9</td>
</tr>
<tr>
<td>The Kvaerner Case</td>
<td>10 - 11</td>
</tr>
</tbody>
</table>
European IPT

The potential for insurers and captives to write insurance contracts across European borders now extends to over 30 countries. However, European IPT compliance requirements are strict, and often difficult to follow or comply with. TMF IPT Services can help - with professionals in over 30 offices in Europe, and 120+ globally, we have the market reach.

Freedom of Services regime

As part of the free market reforms of the European Union in the early 1990s, the formation of a single European insurance market removes the restrictions on insurers established in an EU Member State providing services in other EU Member States without the establishment of agencies and branches. What is required is permission from the insurer's local regulator, who facilitates the granting of Passporting Rights with other Member States. Under the Freedom of Services regime, direct taxation remains the sole responsibility of Member States. However, insurance companies have to fulfil their duty of compliance (indirect taxes) in other Member States where the risks are covered.

EU Second Non-Life Insurance Directive

For many years, it was assumed by the European insurance industry that any indirect tax was due in the Member State where the insurance contract was concluded. This interpretation was corrected when the EU Second Non-Life Insurance Directive was published, where it defines that taxes are due in the Member State where the insured risk is situated. This definition was again certified by the ruling of the European Court of Justice on the Kvaerner Case (2001).

This means, for example, that an insurer or captive covering risks in 10 European countries would need to comply with the indirect tax rules in each Member State. This can provide many difficulties since the rules and tax rates for the same classes of insurance vary across the EU States.

Insurance Premiums and EU Indirect Tax

The compliance of indirect taxes on European insurance is initially codified by the EU VAT Directive (originally known as the 6th Directive on EU VAT). This Directive provides a common system of VAT for EU Member States, which are required to incorporate the EU VAT Directive into national laws. According to the EU VAT Directive, insurance services are exempt from VAT. However, Member States have the right to impose local taxes (e.g. Insurance Premium Tax) or levies (Parafiscal Charges) on insurance premiums.
Parafiscal Charges

In addition to IPT liabilities, insurers, captives and the insured are also liable to a host of additional Stamp Duties and levies, known as Parafiscal Charges. These diverge hugely in type from country to country, and are often payable to different tax and insurance authorities and to varying deadlines.

A number of Central & Eastern European countries already had Parafiscal Charges in place prior to their recent accession to the EU, e.g. Poland and Hungary. Insurers should be cautious to ensure that there are no such hidden liabilities in these territories. For example, Bulgaria may expect VAT registration for certain types of FOS insurance.

Stamp Duties

An old tax on documents and instruments, Stamp Duty is still commonplace across Europe on insurance premiums. Sometimes it is charged instead of IPT, for example, in Portugal; often it is due on top of IPT, for example, in Greece. It is therefore a further toll on cross-border risk cover.

Typically, Stamp Duty is a small percentage levy or fixed price per contract. It is often separately administered from IPT, in a different division of the tax office. There are also deadline variations. For example, in Greece IPT is due 90 days after the end of the reporting quarter; corresponding Stamp Duty is due 50 days after the quarter end.

Stamp Duty is often calculated on the amount of the Premium plus IPT.

Parafiscal Charges

A bewildering collection of levies, Parafiscal Charges are liable on insurers underwriting in Europe. Common charges include:

- Fire Brigade Charge: payable on policies covering fire protection
- Road Tax: chargeable on motor liability contracts
- Local Insurance Institute: fees for supervising the industry, usu. levied on all classes of insurance.

Beyond this, in a number of countries there are a host of further charges reflecting national priorities. Examples include: Social Security Fund in France on motor insurance, and Fund for Victims of Extortion in Italy on several classes.
Fiscal Representation

Since the inception of Freedom of Services insurance for multi-jurisdiction programmes, the requirement for a local fiscal representative has been a key control for foreign tax authorities. The fiscal representative is usually held jointly liable for insurers' IPT and Parafiscal Charges.

Some tax authorities are beginning to relax the requirements for the appointment of a full fiscal representative, e.g. in Belgium and the UK.

The Role of the IPT Fiscal Representative

Tax authorities look to the local representative to properly calculate record and pay over IPT and Parafiscal Charges. This includes retaining copies of most insurance contracts in-country - the tax authorities have the right to inspect these, and the details of IPT calculations, at short notice.

When questions arise, or if the tax authorities wish to perform an audit, the fiscal representative is the first port of call.

As with other taxes, such as VAT, the fiscal representative is jointly and severally liable for IPT and Parafiscal Charges. In the event of the insurer (or insured) not settling taxes or penalties, the fiscal representative is next in line in terms of liability. There are many cases where the tax authorities have exercised this right, making fiscal representatives sensitive to potential losses when taking on a new insurer. As a result, a fiscal representative will usually insist on a full bank guarantee (or a cash deposit) from a reputable, local bank to cover any potential tax liabilities.

For insurers working in multiple territories, the requirement to appoint fiscal representatives in most territories, and provide local guarantees in each jurisdiction, can be hugely burdensome and expensive.

Relaxation of the Fiscal Rep Requirement

As with VAT, there has been some relaxation in a few countries of the obligation to appoint a fiscal representative. The UK has now dropped the requirement for a fiscal representative. Other countries making similar moves are Germany and Belgium. In the case of the latter, however, there is still the condition that IPT payments are made from a local bank account, making IPT compliance, without the use of some type of local agent, tricky.
International IPT

International Insurance Premium Tax, and variations of it, is an international indirect tax. It is levied on risk contracts issued by insurance companies and captives. IPT covers many insurance classes, although life and ship & hull are often excluded, and reinsurance is not taxed.

Whilst the broad principles for international IPT are similar, the difficulties come down to national variations. In Europe, each state is free to set its own rules. Unlike VAT, there is no central EU co-ordination procedure advising on how IPT should be applied. As a result, uncertainty extends to who is liable to account for IPT - the insurer, the insured or the broker?

As a general rule, the tax is calculated on gross premiums written. There are varying regulations on the inclusion of additional costs such as broker fees.

IPT in Europe

The Freedom of Services regime, established by the EU and EEA, has been the driver for many of the increased IPT liabilities around Europe. FOS permits insurers established in the EU & EEA (including Lichtenstein, Norway and Iceland) to provide risk cover across international borders within the region. All that is required is to seek Passporting Rights from the insurer’s local Regulator and ensure compliance for IPT.

IPT Compliance

The single biggest issue in FOS has been determining where the international IPT is due on multi-jurisdictional programmes. This has been largely reviewed by the Courts in the Kvaerner Case.

Currently, it is only the 'old' European states which have IPT regimes. However, this is changing quickly. For example, Slovenia, one of the group of 10 accession countries which joined in 2004, has already enacted IPT. Others are following. Additionally, a number of countries capture this type of activity in their VAT regimes, e.g. Bulgaria.

European tax authorities have now all adopted the same risk classes. However, significant variations arise in the following areas:

- Treatment of Classes
- Rates
- Reporting deadlines
- Numerous reporting authorities
- Local bank account requirements.
Responsibility for IPT

"Who is responsible for IPT compliance?" is always a key question in determining liability. Broadly, in Europe, the tax authorities pursue any outstanding balances from the following parties, in the following order:

- Insurer
- Policy holder
- Fiscal Representative (assuming correctly appointed)
- Intermediary (only in certain countries).

The party responsible for IPT is required to calculate, collect, keep appropriate accounting records of and pay over to the tax authorities any international IPT due. This also includes Parafiscal Charges.
US Direct and Self Procurement Tax

US self or direct procurement insurance is risk cover purchased in the US directly from a non-admitted insurer. In many US States, direct procurement tax is levied through a separate regime on a number of classes of insurance.

It is arranged by the insured either directly with a non-admitted insurer in the State, or through a non-admitted broker in the territory where the cover extends to.

The alternative route for obtaining non-admitted insurance in the US is through Surplus Lines insurance.

Premium Taxes on Self / Direct Procured Insurance

39 US States charge special tax rates on self-procured insurance, based on the gross premium. These range from 2% to 6%, depending on the State and class of risk. In the remaining states, there is no tax regime – although it is not clear if this means Self Procured Insurance is permitted or regulated.

Nonadmitted and Reinsurance Reform Act (NRRA)

The implementation of Nonadmitted and Reinsurance Reform Act (NRRA) on 11th July 2011 changed the way that Self Procured and Surplus Lines taxes are settled.

Surplus Lines taxes should be settled in the “insured’s home state” by a licensed surplus lines broker and this includes any other taxes, such as stamping fees.

Self Procured taxes should also be settled in the “insured’s home state” by the insured and this includes any other taxes, such as stamping fees. Self Procured taxes follow the same rules as for surplus lines taxes, but consideration of what happens for non-US domiciled buyers of insurance also needs to be taken into account.

The NRRA defines “home state” to mean:

(i) The state in which an insured maintains its principal place of business or in the case of an individual, the individual’s principal residence; or
(ii) If 100% of the insured risk is located out of the state referred to in (i), the state to which the greatest percentage of the insured’s taxable premium for that insurance contract is allocated (this state is referred to as the “principal place of business”).
Definition of “principal place of business” in relation to “insured’s home state”:

(iii) The state where the insured maintains its headquarters and where the insured’s high-level officers direct, control and coordinate the business activities; or

(iv) If the insured’s high-level officers direct, control and coordinate the business activities in more than one state, the state in which the greatest percentage of the insured’s taxable premium for that insurance contract is allocated; or

(v) If the insured maintains its headquarters or the insured’s high-level officers direct, control and coordinate the business activities outside any state, the state to which the greatest percentage of the insured’s taxable premium for that insurance contract is allocated.

Payment of Self / Direct Procurement taxes

The insured party is generally responsible for the settlement of direct procurement taxes. Companies should be careful to pay taxes within one to three months (depending on the State) of the inception of the policy as penalties can be punitive.
IPT Tax Authorities

Initially slow to act on IPT non-compliance by insurers across Europe, the tax authorities are now armed with an array of instruments to detect outstanding liabilities. This has emboldened them to seek out additional IPT revenues.

The following factors are driving the tax authorities' recent interest in IPT:

- The growth of FOS insurance, meaning that potential IPT revenues have become material enough to warrant close scrutiny
- Foreign insurers are seen as a soft target, often unable to launch appeals against foreign tax assessments
- Pressure from national insurance associations whose members are feeling the competitive pressures from foreign FOS insurers.

Mutual Assistance Directive

Introduced to cut tax evasion on direct taxes, the Mutual Assistance Directive gives the powers to national tax authorities to exchange data on the activities of companies operating across their territories. It was extended to IPT recently, and enables tax authorities to question foreign insurers of their activities through their local tax office.

Recent usage of the provision has been growing. Examples include authorities asking for written confirmations of activities from insurers' national tax authorities.

In May 2008, the Mutual Assistance Directive was updated, with the aim of improving co-operation between various Insurance Premium Tax and VAT authorities around Europe.

Help from the Regulators

Many national tax authorities have been asking for assistance from foreign regulators. In particular, there have been exchanges of names of insurers seeking Passporting Rights from the Regulator in the relevant territory. This means the tax office is often aware of an insurer intending to issue cover in-country before any applications for IPT registrations have been made.
Kvaerner Case

The location of risk, and hence of liability for IPT, was initially established by the 2nd Non-Life Insurance Directive. This details guidance for property, vehicle, travel and holiday insurance. However, for many years, exact interpretation and enforcement were patchy in practice - until the 2001 Kvaerner Case.

The outcome of this case, and the will of tax authorities to drag foreign insurers into their tax nets, as seen in the 2007 DSG Case, have focused IPT compliance in the eyes of the insurance community.

**Kvaerner Case**

If there were any lingering doubts on the IPT liability to foreign tax authorities on risks covered in their territories by cross-border insurance, then the 2001 Kvaerner case resolved them.

Kvaerner, a Norwegian engineering and construction service group, took out a global professional indemnity insurance policy for its group companies. This covered a Dutch subsidiary of John Brown plc, which was owned by Kvaerner. The policy was taken out in the UK, and Kvaerner believed it should pay UK IPT on all the coverage.

The Dutch tax authorities raised an IPT assessment on the Dutch element of the policy. The case was eventually referred to the European Court of Justice ('ECJ'). This court ruled that IPT was due where the risk was located - hence Dutch IPT was due on the Dutch subsidiary's element of the policy.

In addition, the ECJ ruling stated that it was not relevant who paid the insurance, or where. It also charged the insured (Kvaerner), and not the insurer.

This landmark decision firmly defined the location of liability for IPT. It also highlighted that cover taken out by parent companies, out of country, will nevertheless be assessed locally by the tax authorities concerned.

**DSG Case**

Following Kvaerner, there seemed to be doubt about whether the tax authorities would pursue non-compliant insurers. However, the DSG case has recently underscored that the authorities are now keen to employ the ruling as one of a number of tools to bring in IPT revenues.

DSG International Insurance Services was part of the old Dixons Group, a household electronics retailer. DSG, an Isle of Man company, was providing appliance breakdown cover for a company offering service cover on appliances in the UK.

The UK tax authorities raised an assessment against DSG for the IPT due on the insurance cover provided in the UK. This implied that DSG should IPT register in the UK, and charge local IPT. DSG took the case to tribunal and won on a complex technicality.
Whilst the UK tax authorities did not win this case, it did show that it was now willing to employ the Dutch Kvaerner ruling to increase its IPT revenue. More similar cases can be expected.

How TMF Group can help

The Kvaerner and DSG cases have firmly established the responsibility of companies and their insurers to properly allocate and report on multi-jurisdictional IPT.

At TMF Group, IPT professionals in 36 offices across Europe, and many more beyond, have been helping insurers and captives with IPT compliance since 1987. This means it has excellent relationships with the local tax authorities, and is often able to come to the best, practical resolution on IPT issues.