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Dutch tax court rules in favor of Dutch tax administration in captive insurance company case

Last year a Dutch lower court issued a ruling relating to the transfer pricing arrangements between a Dutch vacation resort and its Irish captive insurance company. The holiday resort operates a large number of vacation houses. At the time of reservation, tourists can buy cancellation insurance, which the resort subcontracts to its captive insurance company in Ireland.

Facts

Prior to using the services of the captive insurance company, the Dutch resort insured the cancellation insurance itself. The Dutch Insurance Authority warned the resort that such activity was not allowed as the resort did not have a proper license to operate as an insurance company.

Therefore, the Taxpayer argued before the Court, the resort changed its insurance operations. The tourists continued to buy insurance at the resort when making a reservation, but now the resort subcontracted the cancellation risks to an independent Irish insurance company that subsequently re-insured the risks with the Irish captive insurance company, a subsidiary of the resort.

In summary, the contractual agreements between the resort, its captive, and the independent Irish insurance company worked out in such a way that the residual income ended in the captive insurance company while the resort and independent insurance company earned commissions and management fees.

The captive insurance company did not have any staff and its business was managed by the independent Irish insurance company. The captive insurance company had a local license to operate as an insurance company, and its retained earnings were lent to the resort.

The position of the Dutch tax administration

The Dutch tax administrations added the entire profit of the Irish captive insurance company to taxable income of the Dutch resort. In front of the Court, the Dutch tax administration argued that the various agreements between The Netherlands and Ireland were all closely connected and did not really change how the cancellation insurance was operated by the group. It also argued that the Irish organization lacked key elements of (re)insurance, such as diversification, value creation by reducing costs, and costs of capital as well as asset/liability management.

The Court's ruling

The Court followed the argument of the Dutch tax administration that in Ireland only administrative services have been rendered with no insurance or re-insurance activities. It ruled that those services can be rewarded at cost plus a modest mark up. The insurance risk does not require a separate remuneration. The remainder of the Irish insurance profit must be taxed at the Dutch resort.

The Court also held that the investment income (i.e. the interest on the group loan) can be allocated to the Irish captive insurance company. The Court came to this conclusion mainly because the Dutch tax administration had not separately argued why it should have been allocated to the Netherlands.

PwC Observation: For further information, please do not hesitate to contact our colleague in the Netherlands, Hugo Vollebregt @ hugo.vollebregt@nl.pwc.com

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