

# How VAT impacts you

## Insurance sector



### VAT in the GCC

The Gulf Cooperation Council ('GCC') states are gearing toward the introduction of a Value Added Tax ('VAT') in the region, commencing on 1 January 2018. The proposed VAT will tax most goods and services with a limited number of specifically exempt or zero rated supplies.

VAT registered businesses that supply goods and services subject to VAT at standard rate or zero rate are usually entitled to claim a credit for VAT paid on their business expenses (input VAT). However, in the case of supply of exempt goods and services, no input tax credit will be available. Therefore, the VAT cost will be borne by these businesses.

### Complexity for insurers

#### Recovery of input tax

Life insurance is traditionally exempt from VAT and this may be the case in the GCC. Exemption means that no VAT will be charged on the provision of life insurance coverage. For VAT purposes, the definition of 'life insurance' is expected to be confined to insurance against the death of an individual only.

Accordingly, VAT incurred on expenses (known as input tax) cannot be claimed in relation to making these exempt supplies. For example, the VAT on commissions paid to intermediaries will not be recoverable. This VAT will be a cost that must be absorbed by the business.

We observe that other VAT jurisdictions impose VAT on any supply of non-life insurance (such as health, marine cargo and workmen's compensation). Where this is the case, any input tax incurred in making these supplies will be recoverable.

### Bundled insurance products

The provision of any add-on insurance products ('riders') is treated separately from the basic life insurance coverage in certain jurisdictions. This means that if a policyholder takes a life insurance policy and tops this with a health, waiver of premium or critical illness rider under one contract for example, no VAT will apply on the basic life policy but VAT will apply on the riders.

### Cost of outsourcing will increase for insurers under VAT

In other VAT jurisdictions, outsourced services (such as shared accounting or IT services) are subject to VAT at the standard rate. Where these outsourced services are inputs for the provision of both taxable and exempt supplies, there will be a restricted claim of input tax. This will increase your cost of doing business.

It is advisable that a review of current outsourcing policies are performed to ensure correct identification of when input tax will (or will not) be claimable.

The cost efficiencies gained from outsourcing support services for example may be negated if any VAT charged cannot be offset (claimed) in full.

### Zero rating of premiums

Foreign VAT jurisdictions have granted zero rating to certain insurance services. Zero rating means VAT will apply at 0%. Zero rated supplies will still be considered a taxable supply, meaning any input tax which has been directly incurred in the provision of such supplies will be recoverable.

In other jurisdictions, zero rating applies when you are:

- Insuring property or assets outside the country;
- Insuring a person who is not a resident in the country; or
- The risk being insured is wholly outside the country.

## Impact on your business transactions

### Accurate VAT classification of all your business transactions

As mentioned above, some insurance services which you provide, for example, life insurance will be treated as exempt. However non-life insurance may be taxable. You may also zero rate certain insurance premiums.

The correct VAT classification of your insurance services will be crucial as it will dictate if:

- a. VAT has to be charged; and
- b. Establish the base for your claims of input tax on expenses.

Therefore appropriate VAT controls and processes will need to be established to ensure the correct VAT treatment applies on a transaction-by-transaction basis for all your business supplies.

### Systems, procedures and people

An assessment of the capabilities of existing IT systems and re-configurations necessary in order to generate VAT compliant outputs is crucial. In many cases, significant changes will be required to IT platforms and current workflows and processes.

It is essential that your staff and intermediaries are fully cognisant of VAT. It will be difficult to systemise the VAT rules for all supplies made by you: nuances in the VAT law or slight changes in fact scenarios can lead to varying VAT outcomes, as described above.

### Apportionment of overheads

If you provide both taxable (e.g. non-life insurance) and exempt (e.g. life insurance) services, VAT incurred on common overheads (such as marketing and promotional costs, utilities, purchases of office furniture and goods) will not be fully claimable and must be apportioned; meaning you claim only a portion of VAT incurred on such expenses in proportion to the amount of taxable supplies you make over your total supplies.

Costs will increase for insurers providing life insurance. This will further be compounded by the higher compliance costs faced by insurers to ensure correct tracking and attribution of all their inputs and VAT claims.

### Transitional considerations

As in other jurisdictions, the GCC VAT law may make the supplier of goods and services liable to account for VAT. Therefore, if you have entered into insurance contracts which span the VAT start date of 1 January 2018, you need to ensure that there are explicit VAT clauses in your contracts to legally recover the VAT from your policyholder(s).

Otherwise, the VAT cost will be borne by you and impact your bottom-line.

Changes in costs will also impact your pricing policy. An early assessment of the VAT bottom line cost is required in order to rebalance prices in time for 1 January 2018 and maintain current levels of profitability.

### In summary

The above is just a sample of the many issues that will impact insurers under the VAT. Addressing your customers and other stakeholders' concerns in advance of the VAT will be critical.

'Will the cost of my insurance premium rise?' may be one of the questions your customers will ask you. Early preparation is crucial and many of these issues may be resolved and the impact mitigated.

At PwC, we have a strong indirect tax practice with many years of experience in VAT insurance matters both in the Middle East and abroad. We are in an excellent position to help you during this transitional period.

## How we can help – VAT implementation

1

Conduct VAT awareness briefings

2

Assist with classification of your business transactions

3

Review your long term contracts and propose VAT specific changes

4

Undertake a VAT cost financial analysis

5

Provide a VAT implementation plan

6

Advise and support on systems, compliance and training

## Talk to us

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