VAT Deductibility for Life Insurance Companies

This document should be read in conjunction with section 59 and paragraphs 6 and 8 of Schedule 1 of the VAT Consolidation Act 2010 (VATCA 2010)

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Introduction

The purpose of this guidance is to outline the VAT deductibility provisions that apply to life insurance companies.

With developments under International Financial Reporting Standards (IFRS), including IFRS 4, the income of a life insurance company is no longer fully accounted for as insurance income. There is recognition that some savings and investment products offered by life insurance companies carry more financial risk than insurance risk and are, therefore, accounted for as investment products.

There is an acceptance that there are, in fact, two distinct streams, being pure insurance and investment business.

1 VAT deductibility for pure insurance business

Insurance is an exempt activity in accordance with paragraph 8 of the VATCA. However, insurance policies sold to customers located outside of the EU constitute a 'qualifying activity' under section 59(1) (d) for which VAT recovery is available.

Any costs that are directly attributable to the sale of insurance policies to non-EU customers will be eligible for full VAT recovery. Any costs directly attributable to the sale of policies to EU customers will not be eligible for VAT recovery.

Where costs relate to the sale of polices to both EU and non-EU customers, an apportionment of VAT recoverable is required.

2 VAT deductibility for investment business

In respect of the investment business carried out by life insurers, whilst these investments are typically written as a life insurance policy, the fact is that these products contain little or no insurance risk and carry financial risk instead.

These products are in direct competition with other financial products that may be offered by banks, fund managers etc. These products should be treated in the same way from a VAT perspective.

These products involve the collection of subscriptions from investors, and using these funds to buy assets in the hope of generating a return greater than the investment amounts. The assets purchased are typically financial assets of the kind listed in paragraph 6(1) of Schedule 1 of the VATCA. Therefore, the relevant activity for VAT deductibility purposes is the dealing in these financial assets.

Costs that are directly attributable to the dealing in non-EU securities are eligible for full VAT recovery. Costs that are directly attributable to the dealing in EU securities are not eligible for VAT recovery.

Costs that relate to the dealing in both EU and non-EU securities are subject to an apportionment based on the level of non-EU dealing activity to total dealing activity.

3 General overhead costs related to both insurance and investment activity

Where the business incurs costs that relate to both the insurance and investment activities, a methodology will need to be formulated that permits recovery on a basis that correctly reflects the way that such costs are used for the purposes of the deductible activities, and has due regard for the total supplies and activities of the business.

No defined methodology is required to be utilised by any business as each will need to be assessed on its own merits. However, the methodology chosen must be used consistently and must adhere to the principles above.

An example of a method that may fit these criteria is outlined below.

4 Example of VAT deductibility for a life insurance company

A life insurance company has turnover of €500m. €150m is pure insurance income and €350m is related to the investment business. All written premiums are from EU customers and the investments are 60% non-EU, 40% EU.

The company has incurred €5m in VAT. Of this amount; €1m is directly attributable to pure insurance business, €1.5m is attributable to the investment business and the remaining €2.5m relates to both the insurance and investment businesses.

The VAT of €1m directly attributable to the pure insurance business is not recoverable. Of the €1.5m related to the investment business, 60% or €900,000 is recoverable.

In respect of the general overheads of €2.5m, a turnover method can be used to correctly reflect the extent that these costs are utilised for deductible activities. As the only deductible activity is within the investment business, the costs can be allocated to that business as follows; €2.5m x €350m/€500m. Therefore, €1.75m relates to the investment business and 60% or €1.05m is recoverable.