

A practical guideline on the amended savings tax

THE
EU SAVINGS TAX
AMENDMENTS
ON
INSURANCE

*How the
directive affects
life insurance
products*

An indispensable primer for the insurance industry



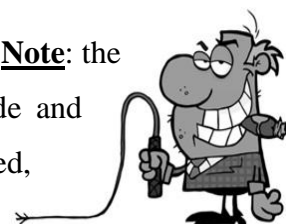
Summary: Key factors

- Life insurance policies issued after June 2010 are in scope if :-
 - a) they provide a guaranteed income, or
 - b) the actual performance contains at least 25% interest.



However, a Member State shall have the option of including in the definition of interest payment benefits regardless of the composition of performance, if paid by or obtained from a life insurer established within that State.

- An insurance benefit is defined as a payment in excess of the premiums paid. **Note:** the entire insurance benefit is deemed to be interest, which will likely include and capital gains and dividends. Unless the calculated benefit is clearly delineated, the entire payment is deemed to be the benefit.



- Pensions and annuities issued by life insurance companies are exempt only if they the contract upon subscription contains a specified condition in that repayments will be made over at least five years.



- If an insurance company is established within the savings tax territory, it is the Paying Agent responsible for applying the savings tax provisions. For interest received from insurers outside the territory, the bank is the Paying Agent.

- If an insurance company has the option to withhold savings tax, then Member States may allow paying agents to levy withholding tax only on the benefits about which the competent authority of the Member State of residence of the beneficial owner has not yet been informed, by the paying agent or its fiscal representatives pursuant to any legislative provision different from those necessary to implement this Directive.



- An insurance company, must report on payments made to any entity or legal arrangement not subject to effective tax and is effectively managed from within another savings tax territory, viz. the name, legal form, place of management and amount of interest. This entity or legal arrangement becomes the Paying Agent Upon Receipt.



Life Insurance Benefits

A life insurance policy is a contract between a policy owner and an insurer where the insurer agrees to pay a beneficiary a sum of money upon the insured individual's death.



Amendment legislative pertaining to life insurance

For the purposes of this Directive, 'interest payment' means benefits from a life insurance contract, if:-

- ♦ the contract contains a guarantee of income return, or
- ♦ the actual performance of the contract is more than 25% linked to **interest**

Exemptions: A benefit from a life insurance contract which:-

- ♦ solely provides for pension or a fixed annuity,
- ♦ paid for at least 5 years

shall be considered as such only if:-

- ✎ it is a **repayment** (*i.e. paid to the individual who subscribed for the policy*), or
- ✎ an assignment to a 3rd party that is made before the end of the 5 year period (*i.e. will be in scope if assigned after 5 years payments has already been made*).

An amount paid out solely in respect of death, disability or illness shall not be considered to be a benefit from a life insurance contract.

Definition of benefit: The excess of any repayment or partial repayment made by the life insurer before the maturity of the life insurance contract as well as the excess of any amount paid out by the life insurer over the sum of the payments made to the life insurer under the same life insurance contract, shall be considered to be a benefit from a life insurance contract.

In the case of assignment, in whole or in part, of a life insurance to a third party, the excess of the value of the contract conferred over the sum of all the payments made to the life insurer shall also be considered to be a benefit from a life insurance contract.

1. What does “actual performance of the contract is more than 25% linked to interest” mean?

It means if the payment excess over cost contains at least 25% interest from:-

- a) Income earned on debt claims
- b) Interest from funds redeemed
- c) Interest distributed from funds
- d) Income from securities that provide a capital guarantee , eg structured products, interest derivatives, etc.

The definition of interest threshold for insurance policies differs significantly from the debt threshold for collective investments. This is because the composition of an insurance policy’s asset classes could change significantly during the policy term.



Difference between Collective investment and insurance policy 25% debt threshold:

	Life Insurance	Collective investments
Debt claim assets held until redemption	Irrelevant	Average 25%
Debt claim assets if income distributed	Irrelevant	Average 15%
Actual interest earned upon payment	At least 25%	Irrelevant

Note: A Member State shall have the option of including in the definition of interest payment benefits regardless of the composition of performance, if paid by or obtained from a life insurer established within that State.

2. Investment type policies

These are within scope if the actual performance of the contract is linked to more than 25% interest:

a. Unit linked insurance policies

With this investment type of life insurance policy, the policyholder bears the entire investment risk. The payout value is linked to a unitised insurance fund. Policies whose performance is linked to more than 25% interest will be in scope.

b. Endowment policies

Under a typical endowment product, a basic guarantee is provided, known as the sum assured, payable at maturity or earlier death. The sum assured generally carries a prudent guaranteed return on the premiums paid and forms the basic guaranteed benefit around which the other benefits are built. As the policy contains a guaranteed income or return, it is in scope.

c. "With profits" policies

An insurance policy issued by a life insurer which has a basic sum assured to which regular bonuses are credited to the policy's value. The basic sum assured is the minimum amount of life assurance payable on death or upon maturity, whichever comes first. The regular bonuses are linked to the profits of the with-profits fund. The policy is not in scope as there is no guarantee of capital, due to a possible Market Valuation Reduction. Nor are annual bonuses credited to the policy classified as interest.

3. Income type policies

An annuity is a regular income paid by a life insurance company to a policyholder, known as an annuitant. The amendment excludes fixed annuities paid over at least 5 years. There are several types of annuities:-

- a. **Fixed Annuities** - is a constant regular payment from a life insurer commencing on a specified date for the rest of the annuitant's life. The insurer incurs longevity risk but no mortality risk. The EU savings tax amendment exempts fixed annuities paid for at least 5 years. As no fixed annuity contract contains a guarantee of payments over five years, all fixed annuities are in scope.
- b. **Temporary Annuities** - are regular constant payments for either a fixed period, or the annuitant's lifetime, whichever is shorter. The insurer incurs longevity risk. If the annuitant survives the fixed period, the annuity ceases, as it does if he dies during that period. Temporary annuities, with a term longer than 5 years, will be exempted.
- c. **Annuities Certain** - The annuitant is guaranteed by the insurance company to receive those payments for the agreed upon time period without exception or contingency. If the annuitant dies before the time period expires, the annuity payments are then made to the annuitant's designated beneficiaries. The insurance company incurs neither longevity nor mortality risk. The EU Commission deems annuities certain as deposits with the payments as "pure income". Therefore annuities certain are in scope.
- d. **Variable Annuities** - The insurer will make future payments to an annuitant, the amount of which is linked to the performance an underlying investment. If the insurer as no mortality or longevity risk, the EU Commission will deem this product as a deposit. and in scope.

4. Other types of insurance policies

- a. **Capital Redemption Bond** - A life insurer promises the policyholder a *certain* redemption value upon maturity.. The beneficiary may surrender early for a *variable* value based on the underlying investment performance held by the policy. A capital redemption bond is therefore a hybrid of two types of annuities:-
- ♦ **Variable Annuity** without life cover if it is surrendered early by the policyholder, or
 - ♦ An **annuity Certain** if kept until maturity.

These policies have no mortality insurance risk, but may incur a financial risk due to its *certain* maturity value. This is therefore more like a deposit. One or more fixed sums are paid to an insurer under a contract pursuant to which one or more specified amounts are paid out at some later time or times, on the basis of an actuarial calculation. Typically the contracts take the form of an annuity certain, where a capital sum is used to buy an annuity for a fixed term not contingent on life, or a sinking fund where regular sums are paid in to secure a capital sum at some later date, for example against the need to find a premium payment to renew a lease. Capital Redemption Bonds should therefore come under the definition of deposits. Capital Redemption Bonds are excluded from the definition of insurances for VAT purposes.

A Capital Redemption Bond is a risky method to avoid the savings tax directive

- If it is deemed as a annuity certain, i.e. an annuity without mortality or longevity risk, then it is deemed a deposit and would be in scope.
- As supported by the EU Commission’s paper on VAT for financial services, if the Member State deems the product is not an insurance policy, then it would be defined as a deposit and hence in scope. Furthermore, the insurer’s guarantee of capital returns brings it within scope.
- The EU Commission is aware of this product and it requires one word amendment in the directive to bring it in scope, i.e. instead of Art 6(1)(e) focusing on “life insurance policies” it could change to “Policies issued by life insurance companies”.

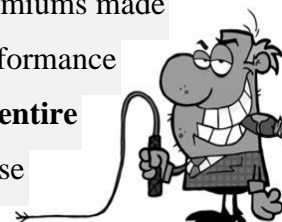
- b. **Non-life unit-linked policies:** Insurance policies whose performance is linked to investments but do not have any component of life cover, are not life insurance policies and are not within scope, such as health unit-linked policies.

5. Insurance Pensions

Technically, an insurance pension policy is identical to a standard unit-linked investment type policy. This type of policy usually pays out a single lump sum upon maturity. The policyholder *usually* has a minimum surrender age to qualify for fiscal benefits but early surrender is possible, albeit with a penalty. Some Member States may mandate that some of the lump sum payout be used to purchase a fixed annuity. A benefit from a life insurance contract which solely provides for pension is out of scope if paid over at least five years. This means if a pension policy will be in scope if it provides a single lump sum payment at maturity.

6. Entire benefit of investment life policies subject to savings tax

Any excess of a repayment made by the life insurer over the sum of the premiums made shall be considered to be a benefit from a life insurance contract if the performance is linked to more than 25% interest or contains a guaranteed income. **The entire benefit is deemed as an interest payment.** This is punitive on those insurers who withhold tax as it will be applied on all the insurance benefits including interest on debt claims plus equity gains and dividends.



7. Grandfathered Exemption

Benefits from a life insurance contract shall be considered to be an interest payment only to the extent that life insurance contract was first subscribed for, after 1 July 2010.

8. Member State retraction of life insurance exemption if performance linked to interest is below 25%:

A Member State shall have the option of including in the definition of interest payment benefits regardless of the composition of performance, if paid by or obtained from a life insurer established within that State.

9. Who is Paying Agent for life insurance policies?

- a) A life insurance company is the Paying Agent responsible for applying the savings tax provisions if:-
- It is established within the savings tax territory, and
 - it makes payments directly to:-
 - a beneficial owner, or
 - an untaxed entity / legal arrangement managed outside the savings tax territory.
- b) If benefits are made to an untaxed entity / legal arrangement managed within the savings tax territory, then the entity / legal arrangement becomes the Paying Agent Upon Receipt. This will occur, for instance, if the policy is held in trust.
- c) If benefits are received from life insurers outside the territory, the bank securing the payment on behalf of the beneficial owner is the Paying Agent. Note that if the external insurer does not enumerate the interest proportion or the cost of the policy, then the entire insurance payment is deemed as interest.

Note: Art 4(2) Par 8 (b) could be a source of confusion regarding if an insurance company is a Paying Agent.

“...This paragraph shall not apply if the entity or legal arrangement provides evidence to the effect that it falls into one of the following cases:

b) it is an institution providing pension or insurance services or an undertaking mandated by such an institution to manage its assets;”

This clause merely affirms that an insurance company is not a Paying Agent Upon Receipt. This means that an insurance company only applies the savings tax upon distribution of the benefit, not upon receipt of the interest.

10. Reporting on payments to Paying Agents Upon Receipt

An insurance company, as economic operator must report on payments made to any entity or legal arrangement not subject to effective tax and is effectively managed from another savings tax territory, viz. the name, legal form, place of management and amount of interest. This entity or legal arrangement becomes the Paying Agent Upon Receipt.

11. Mutual administrative cooperation directive

Pensions and life insurance policies not included in the savings tax is scheduled to be included in the Directive on administrative cooperation in the field of taxation as from 2015.



12. Information to be provided by Paying Agents

In jurisdictions that are mandated or have elected automatic *exchange of information*, the Paying (or Paying Agent Upon Receipt) must provide the following minimum amount of information to the competent authority:

- a. the identity and residence of the beneficial owner established
- b. the name and address of the paying agent;
- c. identification of the life insurance contract;
- d. the total amount of its interest payments received, secured or deemed to accrue to its beneficial owners. The information provided must distinguish and show either the benefit calculated in accordance with that provision or the total amount of the payment. If, in the case of assignment to a third party, the paying agent has no information about the value conferred: the sum of the payments made to the life insurer under the life insurance contract
- e. Notwithstanding the previous Member States may allow Paying Agents (or Paying Agents Upon Receipt) to report only either :-
 - i. the benefits about which the competent authority of the Member State of residence of the beneficial owner has not yet been informed, by the paying agent or its fiscal representative pursuant to any legislative provision different from those necessary to implement this Directive, or
 - ii. the total amount paid out under life insurance contracts generating such payments.
- f. **Paying Agent Upon Receipt:**
 - i. The Paying Agent Upon Receipt shall inform the competent authority of the Member State where it has its place of effective management
 - ii. In the case of shared beneficial ownership, a Paying Agent Upon Receipt shall inform where it has its place of effective management; whether the amount reported for each beneficial owner is the full amount attributable to the beneficial owners collectively; the actual share pertaining to the beneficial owner concerned or an equal share.

13. Withholding Tax

In those jurisdictions which allow withholding tax as an equivalent measure to exchange of information, the Paying Agent (or Paying Agent Upon Receipt) shall levy a withholding tax at a rate of 35 % on :-



- a. the benefit calculated in accordance with that provision.
- b. Member States may allow paying agents to levy withholding tax only on either
 - the benefits about which the competent authority of the Member State of residence of the beneficial owner has not otherwise been informed, by the paying agent, either directly or via its fiscal representative or the competent authority of another Member State, pursuant to any legislative provision different from those necessary to implement this Directive, or
 - the total amount paid out under life insurance contracts generating such payments."
- c. **During the transitional period**, Member States levying withholding tax may provide that an economic operator (insurer) making an interest payment to, or securing such a payment for, an entity or a legal arrangement referred to in Article 4(2), which has its place of effective management in another Member State, shall be considered to be the paying agent in place of the entity or legal arrangement and shall levy the withholding tax on that interest, unless the entity or legal arrangement has formally agreed to its name if any, its legal form, its place of effective management and the total amount of interest paid to it or secured for it being communicated in accordance with the fourth subparagraph of Article 4(2).

EU SAVINGS TAX AMENDMENTS SUMMARY

	Clause	Par		
Beneficial Owner	2.1		Individual	
	2.2		On behalf of someone else	
	2.3		Entity or legal arrangement outside territory for the benefit whose identity shall be according to Art 7 and 8(1)(b) of 2005/60/EC	
	2.4		Paying Agent Upon Receipt shall determine beneficial owner as:-	
	a		Individual entitled to receive	
	b		Individual who directly or indirectly contributed assets	
	c		Individual who later becomes entitled within 10 years - Paying Agent Upon Distribution	
Paying Agent	4.1		Economic operator	
	a		to another another economic operator outside territory	
	b		and knows it is for a beneficial owner	
	4.2		Paying Agent Upon Receipt - an untaxed entity or legal arrangement within the territory	
	8		Exclude collective funds, pension or insurance services, exclusive public charitable purposes, paying agent knows all shared beneficial owners	
	4.3		Paying Agent upon receipt entity opt out to be treated as an undertaking for collective investments	
Interest	6.1	a	interest Paid on debt claims of any kind	
		aa	any income paid, realised or credited on securities of any kind with 95% guarantee or 95% linked to interest	
		b	interest accrued or capitalised at the sale, refund or redemption of the debt claims	
		c	income distributed by undertakings for collective investments within territory, entities in 4(3), collective investment outside territory	
		d	income realised upon the sale, refund or redemption of shares in funds in territory, entities 4(3), funds outside territory if > 25% asserts in debt claims	
		e	benefits (excess over payments) from life insurance if contains a guarantee of income return or performance linked to > 25% interest	
	6.2	1 - 3	For 6(1)(aa), 6(1)(b), 6(1)(c) & 6(1)(d) if no info on amount of income, then total payment is interest	
		4	For 6(1)(e) if no info is avail on the amount is a benefit, then whole payment is interest	
	6.3		For 6(1)(d) if no info on % assets, then assume more than 25%	
			For 6(1)(e) if no info on % of performance linked to insurance, then assume > 25%	
	6.4		if interest paid to entity or legal arrangement as per 4(2) the deemed interest to accrue to person as in 2(4) a - c	
	6.5		For 6(1)(b) & 6(1)(d) MS shall have option requiring Paying Agents annualise interest & deem payments annually, even if no sale / redemption	
	6.6		If Member States apply either par 1 or par 2, then shall be binding on other Member States	
		1		For 6(1)(c) & 6(1)(d) Member States option exclude from interest income distributed whose investments in 6(1)(a) & 6(1)(aa) < 15% of assets
	2		For 6(4) Member States option exclude from interest when entities & arrangements in 4(2) whose investments in 6(1)a & 6(1)(aa) < 15% of assets	
6.7			Debt threshold for 6(1)(d) and 6(1)(e) is reduced from 40% to 25% as from 1 January 2011	
6.8			How debt threshold is calculated for 6(1)(d) and 6(1)(e)	
	a		Fund rules or instrument of incorporation	
	b		Agreement, contract or legal document made avail to economic operator	
	c		Prospectus avail to investors	
	2		If no documentation, then actual composition	
6.9			For 6(1)(aa) - debt claims : capital guarantee - only if issued after 1 July 2010. If before, exclude from 6(1)(d)	
6.10			For 6(1)(e) - insurance benefits - only if subscribed on or after 1 July 2010	
6.11			Member States shall have the option regarding income for 6(1)(d) which are not UCITS authorised, to regard interest accrued only after 1 July 2010	
Identity and residence of beneficial owner	3.1		Each Member State must adopt procedures to identify beneficiaries for the purpose of Articles 8 - 12 in 2003/48/EC	
	3.2	a	If contract before 1 Jan 2004 then name, address according to state regulation and 2005/60/EC	
		b	If no contractual relations or after 1 Jan 2004, name, address, date & place birth, tax identification number per passport / ID card If before 1 Jul 2011 date & place birth only if no tax identification number	
	3.3		Country residence as per tax residence certificate, else permanent address	
	a		If before 1 Jan 2004 address as per state regulations and 2005/60/EC	
	b		If no contractual relation or after 1 Jan 2004, address per 3(2)(b) and updated	
			Tax residence certificate takes precedence over passport for address	
3.4			Each M.S. Issuing tax identification no. must notify Commission of structure and format as well as which official documentation has the no.	
Information reporting by Paying Agent	8.1	1	Where the beneficial owner is resident in a MS other than that in which the paying agent is established, the minimum amount of information:	
	8.1	a	ID and residence of beneficial owner	
		b	Name and address of Paying Agent	
		c	Account number of beneficial owner, if none then identification of debt claim or insurance policy or security or share	
		d	Information concerning the interest payment as per 8(2)	
		2(i)		the total amount of its interest payments received or secured that shall be deemed to accrue to its beneficial owner
		2(ii)		for a beneficial owner according 2(4)(c) the amount that shall be deemed to accrue to that individual and date of accrual
	8.2	a		for 6(1)(a) the amount of interest paid or credited;
		aa		for 6(1)(aa): either the amount of any income paid, realised or credited or the total amount of the payment
		b		for 6(1)(b) or 6(1)(d): either the amount of interest or income or the total amount of the proceeds from the sale, redemption or refund
		c		for 6(1)(c): either the amount of income referred to in that point or the total amount of the distribution
		d		for 6(4): the amount of interest attributable to each of the beneficial owners who fall within
		e		where a Member State exercises the option under 6(5): the amount of annualised interest or other relevant income
		f		for 6(1)(e): the benefit or total payment. If assignment 3rd party and no info on the value conferred: the sum of the payments made to the life insure
8.3			If shared b.o, place of effective management, whether amount reported for each b.o. is full amount attributable to b.os collectively, actual share pertaining to b.o. concerned or an equal share.	
8.4			Member States may allow paying agents to report only : The paying agent shall inform whether it reports the total amounts according to a,b,c	
	a		the total amount of interest or income for 6(1)(a), 6(1)(aa) and 6(1)(c):	
	b		the total amount of the proceeds from the sale, redemption or refund related to such payments for 6(1)(b) and 6(1)(d)	
	c		for 6(1)(e) either the benefit or total payment:	
Withholding tax	11.1		Where the beneficial owner is resident in a MS other than the paying agent is established, where P.A according to 4(2) is established: 35% Withholding tax	
	11.2		The paying agent shall levy withholding tax as follows:	
		a		for 6(1)(a) on the amount of interest paid or credited
		aa		for 6(1)(aa) on the amount of any income paid, realised or credited
		b		for 6(1)(b) or 6(1)(d) on amount of interest or by a levy of equivalent effect on the full amount of the proceeds from the sale, redemption or refund
		c		for 6(1)(c): on the amount of income referred to in that point
		d		for 6(4): amount of interest attributable to each of the beneficial owners who fall within 1(1)
	e		for 6(5): on the amount of annualised interest or other relevant income	
	f		for 6(1)(e) on benefit. MS may tax only benefits the authority M.S. of residence has not yet been informed	
11.5			Economic operators in MS levying WHT shall levy the tax on interest for payments to entities & legal arrangements, unless exchange info	