FROM:	Manager, International Tax
LOCATION:	TAX/58/323
EXTENSION:	6860
DATE:	6 October 2000
REFERENCE:	TAX/MCM/hrc/Y2385
SUBJECT:	SOUTH AFRICAN VAT - UPDATE
ATTACHMENTS:	None
ACTION POINTS:	**Underwriters to note VAT position on premiums and claims relating to South African binding authority business and review pricing**
DEADLINE:	**Immediate**

1. Introduction

1.1 The Market bulletin dated 10 July 2000 advised underwriters and brokers about the removal of the exemption Lloyd's underwriters currently have from Value Added Tax ("VAT") in South Africa. From 1 January 2001, Lloyd's underwriters will be required to register and account for VAT on business written under binding authorities held by South African coverholders. Open market business, including lineslips and business placed under a UK broker's world-wide binding authority, will continue not to be subject to VAT as Lloyd's underwriters are not making a supply in South Africa.

1.2 Section 2 explains when VAT should be charged, section 3 describes the system that will be used to account for VAT and section 4 sets out what Lloyd's Underwriters should take into account when writing binding authority business from 1 January 2001.

2. When VAT should be charged

2.1 There are two rates of VAT, namely the standard rate which is currently 14% and the zero rate. The following are zero-rated: -

(i) The transport of passengers and goods where the transport either begins in South Africa and ends outside South Africa or begins outside South Africa and ends in South Africa.

(ii) The transport of passengers and goods between two ports outside South Africa.

(iii) The transport of passengers by air within South Africa where the transport constitutes “international carriage” as defined.

(iv) Hull and associated liabilities for aircraft and ships which are permanently situated outside South Africa. Temporary presence in South Africa will not affect the zero rating.

(v) Insurance of fixed property or movable goods situated outside South Africa.

(vi) Insurance supplied to non-resident persons outside South Africa for risks outside South Africa. This will include, for example, a policy covering a South African company and its foreign subsidiaries. The premium attributable to the foreign subsidiaries will be subject to VAT at the zero rate unless it covers fixed property or movable goods situated in South Africa.

2.2 Life business written by long term insurers is exempt from VAT but this exemption does not apply to life business written by short term insurers. As Lloyd’s underwriters are only authorised to write short term business in South Africa, the life element of any policy that they write, as defined within the Short Term Insurance Act No.53 of 1998, will be liable to VAT.

3. The system

3.1 A system will be operated centrally to account for VAT, which will initially be operated by Lloyd’s South Africa.

3.2 South African coverholders will be asked to record information about VAT on premiums, claims, commission and expenses on their bordereaux and provide copies each month to Lloyd’s South Africa. This information will be collated by Lloyd’s South Africa and incorporated in a tax return, which will be signed on behalf of Lloyd’s underwriters by their fiscal representative in South Africa. South African coverholders will be asked to pay the VAT they have collected after deducting any input credits due for claims and expenses to Lloyd’s South Africa for onward payment to the tax authorities. If the input credits due on the business written through a coverholder exceed the VAT payable on premiums, Lloyd’s South Africa will arrange for a refund of VAT to be paid to the coverholder.

3.3 Lloyd’s South Africa has recently made presentations to coverholders in Cape Town and Johannesburg about the system and Amit Khilosia, the General Manager of Lloyd’s South Africa, will shortly be writing to all coverholders to let them know what they need to provide and when.

It is important that all coverholders supply copies of bordereaux on a timely basis. Failure to do this may result in an incomplete return and potential interest and penalties.

4. The impact on South African business

4.1 VAT must be charged on all premiums subject to the standard rate of VAT where the policy incepts on or after 1 January 2001. VAT need not be charged on annual policies which incept before 1 January 2001 where the premiums are payable in instalments on or after 1 January 2001. Confirmation of this treatment will be obtained from the South African tax authorities. However, VAT must be charged on additional premiums attaching on or after 1 January 2001 even if the original policy incepted before that date.

A return premium will attract a refund of VAT provided VAT was charged on the original premium.

4.2 Technically, an insurer should differentiate between claims payments made in cash (claims payments) and payments for goods and services (trade payments). An input credit can be claimed on trade payments provided that the supplier has issued a valid tax invoice and VAT has been charged.

An input credit is due for claims paid on or after 1 January 2001 for all policies where the premium is subject to VAT at the standard rate, or would have been subject to VAT at the standard rate if the policy had incepted on or after 1 January 2001. An input credit on claims payments can also be claimed in respect of zero-rated policies unless the insured is not resident in South Africa. Written confirmation of this treatment is being obtained from the South African tax authorities.

If a claim is paid to a South African insured who is required to be registered for VAT and the claim relates to his or her business, the insured must account for VAT on the claims payment. So if, for example, an insured incurs a financial loss of R1,000 the claims payment needs to be inclusive of VAT to fully indemnify the insured, i.e. R1,140 so the insured can account for VAT of R114. Please note that an insured does not have to account for VAT if he or she is not required to be registered for VAT.

This means that input credits will be allowed for all claims paid on or after 1 January 2001 even though they were incurred and/or notified before 1 January 2001 and the policy incepted before that date. Input credits will also be due for goods and services paid for on or after 1 January 2001 provided VAT has been charged by the supplier.

4.3 With effect from 1 January 2001, commission allowed to a South African coverholder will be subject to VAT but as Lloyd's underwriters can claim an input credit, costs will not increase. It is understood that it is local practice to charge commission on the VAT inclusive premium. So if for example the premium is R1,000 plus VAT of R114, commission will be calculated on R 1,114 and be deemed to include VAT of 14%. Where the premium is zero rated the commission may be zero rated depending on the circumstances.

The subject of commissions is, of course, a commercial issue that Lloyd's underwriters need to consider with coverholders.

4.4 Other expenses, such as loss adjusters' fees and legal fees, will be subject to VAT with effect from 1 January 2001 but an input credit will be due for the tax.

4.5 **Lloyd's underwriters should as a matter of urgency consider the impact of VAT with their South African coverholders. It will affect claims costs and Lloyd's underwriters need to consider how this should be reflected in their pricing.**

5. Conclusion

5.1 This bulletin is being sent to all underwriters, managing agents and Lloyd's brokers.

5.2 As South African VAT is a complex subject, Lloyd's Taxation Department and International Department can arrange presentations/workshops which will go into the position in more detail if there is sufficient demand. If you are interested in attending such a presentation or workshop, please contact Helen Clark on Lloyd's extension 6046 or Lynda Newman on Lloyd's extension 6050. If you have any other queries on the bulletin will you please contact me on Lloyd's extension 6860.

Manager, International Tax
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