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This bulletin updates underwriters and brokers on two South African tax issues.

Since 1943 Lloyd's underwriters have had to bear a tax of 2.5% on gross premiums received through intermediaries in South Africa. We have been arguing over the past few years that this puts Lloyd's at a disadvantage, and earlier this year the South African Minister of Finance announced that the tax would be withdrawn with effect from 1 January 2002. The withdrawal has been subject to the Parliamentary process and we are pleased to announce that the legislation has now been passed.

This means that tax will not apply to premiums received by South African intermediaries on or after 1 January 2002 regardless of the date the policy inceptioned. In anticipation of the withdrawal of the tax some premiums for South African business have already been presented to Xchanging Ins-sure Services without the 2.5% tax. However, where a South African intermediary has retained tax it must be paid to underwriters as an additional premium as soon as possible, and in any case no later than 31 October.

Market bulletins dated 10 July 2000 and 6 October 2000 contain information about the way value added tax (VAT) should be applied to South African business. South African coverholders record VAT on premiums, claims, commission and expenses and provide this information to Lloyd's South Africa each month. Lloyd's South Africa operates a central system to account for VAT on behalf of Lloyd's underwriters. KPMG, Lloyd's tax advisers

in Johannesburg, have prepared a manual to help South African coverholders and an electronic version of this manual is provided as an appendix to this bulletin.

If you need a paper copy please contact Lynda Newman in Lloyd's Taxation Department on 020 7327 6050.

This bulletin is being sent to all managing agents, brokers and recognised auditors. If you have any queries please call me on 020 7327 6860 (e:mail : [maureen.c.mcleod@lloyds.com](mailto:maureen.c.mcleod@lloyds.com)) or Roger Ramage on 020 7327 6852 (e:mail : [roger.e.ramage@lloyds.com](mailto:roger.e.ramage@lloyds.com)).

Maureen McLeod  
Taxation Department

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# **Lloyd's**

## **VALUE-ADDED TAX MANUAL**

Tax Services

Lloyds VAT Manual

## **PREFACE**

KPMG has been actively involved in addressing the VAT implications pertaining to the insurance industry since 1990, prior to VAT being introduced on 30 September 1991. KPMG's longstanding involvement in and understanding of the industry has enabled it to develop specific expertise in indirect tax in the field of short term insurance, including Lloyd's business.

This manual was edited by Stéfan Grundlingh (Consultant, Indirect Tax) and André Meyburgh (Director, Indirect Tax) of KMPG. We wish to thank Maureen McLeod and Amit Khilosia of Lloyd's for their valuable input into the document.

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## **INTRODUCTION**

This manual is intended as a guide to illustrate the manner in which value-added tax (“VAT”) has to be accounted for, in respect of insurance business written by Lloyd’s of London (“Lloyd’s”) in the Republic of South Africa (“the RSA”).

The manual is based on the legislation and information available as of 1 January 2001, and endeavors to deal with the industry problems presented by VAT. Unless otherwise indicated, all tax terms quoted and interpretations furnished, are based on the South African Value-Added Tax Act, no 89 of 1991, as amended, hereinafter referred to as “the Act”.

Given the complexity of the application of VAT in the insurance industry and the fairly unique manner in which Lloyd’s conducts its business, it was necessary to obtain directives from the South African Revenue Service (“SARS”) in order to clarify a number of uncertainties which existed. These directives have been incorporated in this manual (refer paragraph [par] 12).

Whilst every effort has been made to ensure that this manual deals with all the issues in a simplistic and practical manner, practices may change from time to time. It is therefore advisable that professional advice is sought where the facts differ from our interpretation thereof.



# **1 TERMINOLOGY**

## **1.1 Open market business**

The unique composition of Lloyd's syndicates and the fact that most of the syndicates specialize in specific types of risks, have ensured that Lloyd's is well known for underwriting almost all types of risks, in particular very high value and highly complex risks, e.g. airline fleets, nuclear plants etc.

Since the arranging of cover for such risks through Lloyd's underwriters requires, *inter alia*, a detailed knowledge of the composition of the various syndicates and their respective specialties, such cover is arranged through Lloyd's brokers in London, who liaise directly with members of the relevant syndicates. Furthermore, the contracts of insurance in respect of such risks are concluded in London.

Lloyd's has independent intermediaries in the RSA who are approved by Lloyd's to introduce certain risks directly to a Lloyd's broker in London. These risks are not placed with Lloyd's underwriters under a binding authority (refer par 1.2). These Lloyd's intermediaries are called open market correspondents.

## **1.2 Coverholder / binding authority business**

As mentioned above, Lloyd's underwrites almost all types of risks, including personal lines such as household content, motor cars, etc. Since these risks are relatively small and simplistic on comparison, it is not cost effective or practical for such risks to be routed directly through Lloyd's brokers in London. Thus, in order to ensure that Lloyd's can underwrite such risks in the RSA in a cost effective and practical manner, Lloyd's has entered into binding authority agreements with certain persons in the RSA. These persons are referred to as coverholders. Coverholders who do not deal directly with policyholders are called wholesale coverholders, whereas coverholders who deal directly with policyholders are called retail coverholders.

The binding authority agreements provide, *inter alia*, that the coverholders can conclude contracts of insurance, collect premiums, and pay out claims on behalf of Lloyd's. All binding authority agreements specify the period for which the binding authority is effective, the classes of business covered, the maximum limits of the sum insured and the rates of premium to be applied, together with the procedures for accounting to underwriters and settling claims.

There are two types of binding authorities – full and limited binding authorities.

### **1.2.1 Full binding authority**

A full binding authority is an agreement under which a coverholder is authorized to accept risks, or to issue insurance documents evidencing the acceptance of risks, on behalf of Lloyd's.

Full binding authority contracts are concluded in the RSA.

## **1.2.2 Limited binding authority**

A limited binding authority is an agreement under which a coverholder is required to refer each risk to the lead underwriter for acceptance, and in some cases rating, prior to the issuing of any documentation. Limited binding authority contracts are concluded either in the RSA or in London, depending on the business process followed (refer par 4.3).

## 2 BASIC PRINCIPLES OF VAT

### 2.1 What is VAT?

VAT is an indirect tax which is designed to be borne by the ultimate consumer or purchaser.

VAT is primarily levied and collected by businesses which are VAT registered vendors, as agents for SARS, throughout the production and distribution chain. Only VAT registered persons or organisations may charge VAT.

Registered vendors collect VAT on an incremental basis by charging VAT on the goods or services supplied by them (**output tax**), and deduct from such VAT, the tax paid in respect of certain goods or services supplied to them or imported by them in the course of their business (**input tax**). The vendor's liability for VAT (which has to be paid to SARS) is calculated as the amount by which the output tax exceeds the input tax. To the extent that a vendor's input tax exceeds his output tax, he will be entitled to claim a refund from SARS.

<i>Output tax</i>	<i>means the VAT that a vendor charges in respect of supplies made by him.</i>
<i>Input tax</i>	<i>means the VAT that a vendor pays in respect of capital goods (for example fixed assets) or other goods (for instance stock) acquired or imported for the purpose of making taxable supplies in the course of his enterprise.</i>
	<i>In terms of the provisions of the Act, vendors are generally not permitted to recover, as input tax, VAT paid in respect of the following expenses:</i>
	<ul style="list-style-type: none"><li>▪ <i>certain entertainment expenses;</i></li><li>▪ <i>membership fees of any sporting or recreational club;</i></li><li>▪ <i>any passenger motor car. Input tax relating to the insurance of or repairs and maintenance of motor cars, may however be claimed; and</i></li><li>▪ <i>medical or dental goods or services acquired by a benefit fund.</i></li></ul>

### 2.2 Imposition of VAT

Section 7(1) of the Act imposes VAT, subject to exemptions (refer par 2.3.3), on:

- the **supply** of **goods** and **services** by a **vendor** in the course of his **enterprise**;
- the importation of goods into the RSA by any **person**; and
- the importation of certain services, referred to in the Act as **imported services** (refer par 2.2.3).

<i>Supply</i>	<i>A supply means 'furnish' or 'provide' and includes supplies which take the form of a sale, rental agreement, barter transactions and includes deemed supplies (refer par 2.3.3).</i>
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<i>Goods</i>	<i>Goods include corporeal moveable things, fixed property and any real right in such thing or property, but excludes services and money.</i>
<i>Services</i>	<i>Services is defined as meaning anything done or to be done, including the supply of insurance, but excludes the supply of goods and money.</i>
<i>Person</i>	<i>A person includes a natural person, a company, a close corporation, any body of persons such as a partnership or a body of syndicates such as Lloyd's, etc.</i>
<i>Vendor</i>	<i>A vendor means any person who is registered for VAT or who is required to be registered for VAT.</i>

## 2.2.1 Supply of goods or services by a vendor (section 7(1)(a))

### 2.2.1.1 Who has to register for VAT?

A person is liable to register as a VAT vendor where such person carries on an **enterprise** or activity in the course of which taxable supplies (refer par 2.3.1 below) are made for a consideration, which exceeds the compulsory VAT registration threshold (currently R300 000, excluding VAT) in any period of twelve months immediately preceding his application, OR whose turnover in respect of taxable supplies is expected to exceed the threshold in the following twelve months.

Registration is voluntary for persons with a taxable income exceeding R20 000, but not exceeding R300 000 a year. Those who do not register for VAT will be treated as final consumers – they may not charge VAT on their sales and are not entitled to claim an input tax credit (refer par 2.1).

Failure to register for VAT where the registration is compulsory, may render the person who carries on an enterprise, liable to account for output tax on past income without the benefit of full input tax credits.

Prior to 1 January 2001, Lloyd's activities in the RSA were specifically excluded from the definition of "enterprise". As a result, Lloyd's could not register as a VAT vendor. However, as from 1 January 2001, Lloyd's is considered to be carrying on an "enterprise" for VAT purposes in respect of insurance contracts concluded in the RSA (i.e. coverholder business only). As a result, Lloyd's has been registered as a VAT vendor in the RSA in respect of its coverholder business only. This has the effect that Lloyd's accounts for output tax on short-term insurance contracts concluded in the RSA and is entitled to claim input tax on costs incurred for purposes of supplying insurance cover under coverholder business.

<i>Enterprise</i>	<p><i>In principle, an enterprise means any enterprise or activity, which is carried on continuously or regularly by any person in the RSA or partly in the RSA, in the course or furtherance of which goods or services are supplied for a consideration</i></p> <p><i>The Act contains various exclusions in respect of what constitutes an enterprise. The definition of 'enterprise', as defined in the Act, has been amended twice to address Lloyd's activities:</i></p> <ul style="list-style-type: none"> <li>▪ <i>Following an amendment to the Act in 1992, the activity of underwriting insurance business by Underwriting Members of Lloyd's of London was</i></li> </ul>
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*deemed not to be the carrying on of an enterprise; and*

- *Following an amendment to the Act in 1999 – which became effective on 1 January 2001 – the activity of underwriting insurance business by Underwriting Members of Lloyd's of London, is deemed to constitute the carrying on of an enterprise, but only to the extent that contracts of insurance are concluded in the RSA.*

### **2.2.1.2 Exclusion from an enterprise**

In terms of the Act, certain activities do not constitute enterprise activities. These include:

- services rendered by any person as an employee for which a salary or wage is earned, unless the employee carries on an enterprise independently from his employer;
- a hobby or recreational pursuit of a natural person;
- activities in respect of exempt supplies (refer par 2.3.3); and
- supplies made outside the Republic by any branch or main business where such branch or main business can be separately identified and has an independent system of accounting. This implies that where an enterprise is carried on in branches or divisions which are located outside the RSA and which keep an independent accounting system, any supplies made by such branch will not constitute an activity carried on by the enterprise in the Republic.

A person who only carries on non-enterprise activities cannot register for VAT and will therefore not be able to charge VAT. Also, any supplies made by a VAT vendor in respect of non-enterprise activities will not attract VAT.

### **2.2.2 Goods imported into the RSA (Section 7(1)(b))**

Where goods are imported into the RSA and those goods are required to be cleared for home consumption, VAT is collected by Customs and Excise, or the postal company, who act as agents on behalf of SARS.

### **2.2.3 Imported services (section 7(1)(c))**

Section 7(1)(c) of the Act imposes VAT on the supply of imported services to any person in the RSA.

The supply of insurance constitutes the supply of a “service” for VAT purposes. In terms of the provisions of the Act, to the extent that services are imported from a non-resident and utilised or consumed by the importer otherwise than in the course of making taxable supplies, said importer is liable to account for VAT on an “imported service”.

*Imported Service* The term “imported services” means a supply of services that is made by a supplier (who is resident or carries on business outside the RSA) to a recipient who is a resident of the RSA to the extent that such services are utilised or consumed in the RSA for the purpose of making non-taxable supplies (refer par 2.3.3).

#### ***Example of an “Imported Service”***

*A RSA homeowner (non-vendor) insures his household content with a non-resident insurance company. Since insurance is a service and since a non-resident supplies the service, the RSA homeowner is liable to pay VAT on the insurance service supplied to him on the basis that he does not apply the household content for purposes of making taxable supplies.*

## **2.3 Types of supplies**

Whether or not a transaction is subject to VAT will depend on whether the transaction is a taxable supply. Supplies can be categorised as follows:

- Taxable supplies; and
- Non-taxable and exempt supplies.

### **2.3.1 Taxable supplies**

Any supply of goods or services made or deemed to be made (refer par 2.3.2) by a VAT vendor in the course of his enterprise (refer par 2.2.1.1), which is chargeable with VAT under the provisions of the Act, is called a taxable supply and attracts VAT (output tax) either at the standard rate or the zero rate.

#### ***Standard-rated supplies***

Supplies of goods and services (which includes the supply of short-term insurance) made by vendors are generally subject to standard rate VAT (currently 14%), where made to persons who consume such goods or services in the RSA.

#### ***Zero-rated supplies***

Section 11 of the Act contains special provisions whereby certain supplies of goods and services are to be taxed at the zero rate (0%). These supplies include:

- The exportation of goods and services from the RSA;
- The supply of certain basic foodstuffs, for example milk and brown bread;
- supplies of services physically rendered outside the RSA; and
- certain supplies made to non-residents.

### **2.3.2 Deemed supplies**

Section 8 of the Act either deems certain activities to be taxable supplies, or deems certain activities to be non-taxable supplies.

In particular, section 8(8) of the Act provides that where a vendor receives an indemnity payment in money, under any contract of short-term insurance (where the premiums payable under the contract are subject to VAT), such vendor is deemed to have made a taxable supply to the insurer to the extent that the payment so received relates to a loss incurred in the carrying on of his enterprise. The indemnity

payment received is therefore considered to include VAT, and the relevant output tax payable by the insured to the Receiver of Revenue, is calculated by applying the tax fraction (14/114) to the amount received by the insured.

Where a vendor is indemnified under a contract of insurance and his insurer pays an amount of money to another person (i.e. the insurer pays a third party on behalf of the vendor), the insured vendor is still deemed to have made a taxable supply to the insurer. The vendor is liable to account for output tax by applying the tax fraction (i.e. 14/114) to the amount paid by the insurer to the third party. The third party (irrespective of whether or not such a person is a vendor) is not deemed to have made a taxable supply and does therefore not have an output tax liability.

The payment received by the vendor will not be deemed to be consideration for a taxable supply should it be received to reinstate the vendor for the total loss or destruction of any goods, in respect of which an input tax was or would have been denied on the initial acquisition thereof, for instance a passenger motor car (refer par 2.1).

This section does not apply in circumstances where the insurer replaces the insured goods or pays, for example a panelbeater, to repair the damaged goods.

Furthermore, where the insured is not a vendor, the deeming provisions of section 8(8) do not apply.

### ***Examples of indemnity payments***

#### ***Example 1***

*Computers are stolen from a registered vendor. The insurer indemnifies the insured by issuing a cheque to the insured for an amount equal to the value of the stolen computers.*

*The payment constitutes an indemnity payment and the vendor has to account for output tax by applying the tax fraction to the indemnity payment received.*

#### ***Example 2***

*A registered vendor's delivery truck is involved in an accident. The insurer pays the panelbeater for the repair services rendered.*

*The payment made to the panelbeater does not constitute an indemnity payment and therefore does not give rise to an output tax liability in the hands of the insured vendor.*

#### ***Example 3***

*One of a vendor's motor cars (on which the vendor was denied an input tax deduction upon acquisition) is involved in an accident and damaged beyond repair. Furthermore, a third party insurance claim is instituted against the vendor following the accident. The insurer indemnifies the vendor by issuing a cheque to the insured for the open market value of the vehicle. In addition, the insurer settles the third party's claim on the vendor's behalf.*

*No output tax liability arises on the indemnity payment which relates to the total reinstatement of the motor car written off. However, the payment made to the third party constitutes an indemnity payment, and the vendor has to account for output tax by applying the tax fraction to the payment*

*made to the third party.*

***Example 4***

*One of a vendor's delivery trucks is stolen. The insurer pays the vendor for the replacement of the truck.*

*The payment made to the vendor constitutes an indemnity payment which gives rise to an output tax liability in the hands of the vendor (the vendor was not denied an input tax deduction upon the acquisition of the truck).*

***Example 5***

*Goods are stolen from a registered vendor and the insurer indemnifies the vendor by replacing the stolen goods.*

*The replacement of goods does not constitute an indemnity payment and therefore does not give rise to an output tax liability in the hands of the vendor.*

### **2.3.3 Non-taxable and exempt supplies**

Supplies which are made by persons or businesses which are not registered for VAT, are commonly referred to as non-taxable supplies and are not subject to VAT. Similarly, supplies which are made by vendors, not being supplies made in the course of their enterprise, do not attract VAT and are also considered to be non-taxable. It follows that businesses which only make exempt supplies, cannot be registered as vendors.

The Act contains special provisions for exempt supplies, which are also non-taxable supplies and therefore not subject to VAT. Exempt supplies largely comprise of, *inter alia*, financial services, (e.g. long-term insurance, rental of residential accommodation, and certain educational services).

A VAT vendor is not entitled to claim input tax in respect of expenses incurred in the course of making non-taxable or exempt supplies. Vendors who, from time to time, make exempt supplies, should take cognisance of the significant difference between zero-rated supplies (which are taxable supplies) and exempt supplies (which are non-taxable). Vendors are not permitted to claim input tax on expenditure incurred for the purposes of making exempt supplies. Input tax may, however, be claimed on expenditure incurred for purposes of making zero-rated supplies.

***Examples of input tax claims***

***Example 1***

*A coverholder (vendor) incurs taxable expenses such as office rent, computer leases etc. He charges commission to Lloyd's in respect of open market business (i.e. zero-rated commissions) and coverholder business. The coverholder is entitled to claim 100% input tax.*

***Example 2***

*A VAT registered insurance broker decides to expand his business by providing cash-loans to clients.*



*He subsequently purchases a computer to be applied wholly for the purpose of managing the loans.*

*The provision of loans constitutes a VAT exempt activity. As the computer was not acquired in the course of making taxable supplies, the vendor is not be entitled to recover the VAT paid on the computer, as input tax.*

## **2.4 Time of supply**

The VAT rules pertaining to “time of supply” determine the date on which a vendor becomes liable to account for the payment of output tax. As it will be totally impractical to expect vendors to pay output tax on a daily basis, the Act makes provision for specific periods, called tax periods, in which vendors are to account for VAT.

### **Monthly tax period**

The monthly tax period is compulsory where the value of a vendor’s annual taxable supplies exceeds R30 million, but is optional where a business’s annual taxable supplies do not exceed R30 million. A monthly tax period is known as a *Category C* tax period.

### **Bi-monthly tax periods**

A vendor may register on a bi-monthly basis either within *Category A* (January, March etc) or *Category B* (February, April etc) where his annual taxable supplies do not exceed R30 million.

A tax period ends on the last day of a particular calendar month. The Act provides that vendors may end their tax periods on a day other than on the last day of a calendar month (within 10 days before or after the last day of the month). Vendors wishing to end their tax periods on such other day are required to submit a written application to their local Receiver of Revenue office and obtain approval from SARS to do so.

Insurers are generally registered on a monthly or bi-monthly basis.

*Lloyd’s is registered on the monthly basis. Lloyd’s tax periods end on the last day of every calendar month. Coverholders should account for Lloyd’s VAT accordingly where they act on behalf of Lloyd’s.*

## **2.5 Basis of accounting**

VAT can be accounted for either on the invoice basis or the payments basis.

### **2.5.1 Invoice basis**

This basis recognises uncollected income, as it only takes account of sales invoices issued. Returns prepared on this basis account for output tax payable at the time of invoice or payment, whichever is the earlier.

Therefore, even if payment has not been received, tax is payable, based on the invoice issued.

## **2.5.2 Payments basis**

In determining a vendor's output tax liability, the payments basis, also commonly known as the cash basis, recognises income actually received (cash received).

Only public authorities, local authorities, associations not for gain and natural persons (who do not make taxable supplies in excess of R2,5 million a year) may apply to the Receiver of Revenue to account for VAT on the payments basis.

## **2.5.3 Accounting basis for Lloyd's**

Lloyd's is registered for VAT on the invoice basis. However, in terms of the Insurance Act, an insurer only supplies insurance cover where the premium has been paid. Given the fact that many insureds cancel their insurance by stopping payment of the premium, insurers can determine the value of insurance cover supplied in any given month, only once they have received premiums. As a result, the local insurance industry agreed with SARS in 1991 that output tax becomes payable in the month in which the premiums are received. Insureds, who are VAT vendors, only become entitled to claim input tax once they have actually paid their insurance premiums.

Furthermore, Lloyd's has specifically received confirmation from SARS that it will only be liable to account for output tax in respect of taxable supplies of insurance in the tax period in which premiums are received by the coverholders. This means that even though Lloyd's is registered on the invoice basis, output tax in respect of insurance premiums will effectively be accounted for on the payments basis.

On the same basis, output tax payable by intermediaries in respect of commissions (deducted by intermediaries from bordereaux payments to Lloyd's), will be accounted for in the tax period that the deductions are made.

## **2.6 Renditions of VAT returns and payment of tax**

### **2.6.1 General**

Vendors are required to submit their VAT returns (a VAT 201 form) and make payment of the tax, if any, within 25 days after the commencement of the month following the relevant tax period. Where the day on which a return has to be submitted (the 25<sup>th</sup>) falls on a Saturday, Sunday or a public holiday, the return, and any payment to be made, have to be submitted on the business day immediately preceding such Saturday, Sunday or public holiday.

A vendor may elect to make payment of his VAT liability by means of an electronic transfer. In such an instance, the electronic transfer will only be effected on the last business day of the month, following the said 25<sup>th</sup> day.

Where a vendor's VAT return shows an amount due to SARS and the vendor either submits the VAT return late, or pays the VAT due late, SARS imposes a penalty of 10 per cent of the tax payable, plus interest at a rate determined by the Minister for every month or part thereof thereafter.

## **2.6.2 Lloyd's VAT returns**

Since Lloyd's VAT returns need to be submitted in accordance with the rules described under par 3.6.1 above, and since all coverholders are required to prepare and submit dummy VAT returns to Lloyd's South Africa's office timeously to ensure that such dummy returns are consolidated into one VAT return, all dummy VAT returns need to reach the offices of Lloyd's South Africa (Pty) Ltd ("Lloyd's South Africa") by no later than the 10<sup>th</sup> business day of the month following the end of each tax period.

## 3 DOCUMENTATION

### 3.1 Documents issued by coverholders as agents for Lloyd's

A significant amount of business in the insurance industry is conducted through intermediaries (insurance brokers). While the contract of insurance is between the insured and the insurer (the principal), section 54(1) of the Act deems a supply made by an agent, to be a supply made by the principal. The agent may, if he is a registered VAT vendor, nevertheless issue a tax invoice in his name on behalf of the principal.

Similarly, section 54(2) of the Act provides that where any vendor makes a taxable supply of goods or services to an agent who is acting for and on behalf of a principal, such supply shall be deemed to be made to the principal and not the agent, provided that the supplier may nevertheless issue a tax invoice in the name of the agent.

As coverholders are agents who act on Lloyd's behalf (the principal) in the RSA and as coverholders issue documents (contracts, tax invoices etc) in respect of taxable supplies made by Lloyd's in the RSA (i.e. coverholder business), it follows that coverholders have to be registered for VAT.

Coverholders are required to maintain separate accounting records in respect of the Lloyd's business conducted by them. This includes:

- collecting premiums and the VAT contained therein from insureds and keeping record of Lloyd's' output tax liability in respect of premiums etc; and
- making payment of claims on behalf of Lloyd's (refer par 8) and the retaining of the relevant documentation which will enable Lloyd's to claim input tax in respect of such supplies.

### 3.2 Documents in respect of premiums

Lloyd's has to account for output tax in respect of the supplies made by coverholders on Lloyd's' behalf. The coverholder (as agent) has to maintain sufficient records to ensure that supplies made by Lloyd's (the principal) are readily identifiable. Any premium notices or policy documents issued by coverholders have to conform to the requirements for **tax invoices**.

#### ***Tax Invoices***

*In terms of section 20 of the Act, a tax invoice for supplies where the consideration exceeds R500 should contain the following details:*

- *the words "tax invoice" in a prominent place;*
- *the name, address, and VAT registration number of the supplier;*
- *the name and address of the recipient;*
- *an individual serialised number and the date upon which the tax invoice is issued;*

- |  |
|--|
| <ul style="list-style-type: none"><li>▪ <i>a description of the goods or services supplied; and</i></li><li>▪ <i>the price excluding tax, the amount of tax, and the amount including tax, or the amount including tax and a statement that the amount includes tax and at which rate tax is included.</i></li></ul> |
|--|

### **3.2.1 Insureds (non-vendors)**

Premiums charged to persons who are not registered vendors (for example the general public) generally do not require any special documentation, as they are generally non-vendors who are not entitled to recover the VAT charged in respect of the premium, as input tax.

### **3.2.2 Insureds (vendors)**

In general, an insurer does not know the VAT status of an insured. Consequently, it is advisable for insurers to always issue a document, which complies with the requirements of a tax invoice, to the insured, in order to ensure that an input tax credit can be claimed by the insured, should he be a vendor.

Insurers are not required to issue tax invoices to registered vendors where the Commissioner is satisfied that there are, or will be, sufficient records available to establish the particulars of the supply in question.

The insurance industry has, in 1991, obtained a directive from SARS which provide, *inter alia*, that where the policy of insurance or the renewal notices, as the case may be, contain the name, address and VAT registration number of the insurer, such policy / renewal notice will become a tax invoice on the date on which the insured pays the premium.

### **3.2.3 SARS dispensation**

Based on the above, coverholders will not be required to issue tax invoices where Lloyd's insurance agreements or renewal notices contain the above details. It is pointed out that the insurance agreements or renewal notices issued by coverholders (vendors) on Lloyd's behalf may either contain Lloyd's name, address and VAT registration number or the coverholder's name address and VAT registration number.

Where an insured, who is a VAT vendor, pays a premium by debit order, he will be entitled to claim input tax based on the debit entry on his bank statement, provided it is supported by a policy agreement or renewal notice containing the information indicated above. Similar circumstances apply where a payment is made through a bond account.

## **3.3 Documentation in respect of commissions**

A significant amount of business in the insurance industry is conducted through intermediaries, for example the rendering of services by a retail broker (not being a coverholder) to a wholesale coverholder. As the intermediaries are generally registered for VAT, documents, which comply with the requirements of the Act, will have to be issued to facilitate the claiming of an input tax credits in respect of commissions payable and claims paid.

### **3.3.1 Self-invoicing**

Where business is conducted through intermediaries (including coverholders), self-invoicing is the most efficient method of generating a tax invoice in respect of premiums received, commissions payable, claims paid etc. Self-invoicing involves the creation of a tax invoice by the recipient of a supply, as opposed to the supplier. The prerequisite for the use of self-invoicing can briefly be summarised as follows:

- the Commissioner has to give his approval prior to the use of such documentation as a valid tax invoice;
- the supplier and recipient agree that the supplier shall not issue a tax invoice; and
- such tax invoice is provided to the supplier and a copy retained by the recipient.

### **3.3.2 Bordereaux as a tax invoice**

In line with the directive issued by SARS to the local insurance industry, coverholders are permitted to use bordereaux for premium payments, claims and commissions paid by insurers etc as valid tax invoices (refer to specimen bordereaux, par 14).



## **4 LLOYD'S VAT IMPLICATIONS**

### **4.1 Open market business**

Open market business contracts are not concluded in the RSA with the result that the supply of insurance by Lloyd's under such contracts fall outside the ambit of the Act, on the basis that Lloyd's activities in respect of open market business do not constitute the carrying on of an "enterprise" in the RSA for VAT purposes (refer par 2.2.1.1).

As Lloyd's does not carry on an enterprise in respect of its open market business, the premiums received in respect of such contracts are not subject to output tax. An imported service VAT charge may, however, apply (refer par 2.2.3). Furthermore, Lloyd's is not entitled to claim input tax in respect of any expenses incurred in the RSA in the course of conducting open market business.

### **4.2 Coverholder / full binding authority business**

Lloyd's insurance contracts in respect of full binding authority coverholder business are always concluded in the RSA, with the result that such contracts fall within the ambit of the Act (refer par 2.2.1.1). In other words, Lloyd's carries on an enterprise in respect of its open market business only. Consequently, the premiums in respect of such contracts comprise consideration for a taxable supply (refer par 2.3.1) and are therefore subject to VAT, either at the standard rate or the zero rate.

It thus follows that Lloyd's is entitled to claim input tax in respect of any expenses incurred in the course of conducting coverholder business in the RSA (refer par 2.1).

### **4.3 Limited binding authority business**

The following business processes may be followed in the concluding of Limited Binding Authority Business.

#### **Contracts concluded in London**

Where a RSA coverholder refers business to the Lloyd's underwriter and the underwriter agrees to go on risk, the contract is considered to be concluded in London and VAT need not be charged on the premium.

#### **Contracts concluded in the RSA**

Where the Lloyd's underwriter (in London) merely quotes terms or provides general advice for a risk, but the coverholder actually binds the risk in the RSA after he has obtained the client's agreement, the contract is considered to be concluded in the RSA and VAT has to be charged on the premium (either at the standard rate or the zero rate).

Where it is difficult for coverholders to differentiate between limited binding authority agreements concluded in the RSA and agreements concluded in London, it is recommended that such contracts rather be treated as being concluded in the RSA. This will result in such agreements being subject to VAT either at the standard or the zero rate.

## **4.4 Imported services and Lloyd's business**

### **4.4.1 Insurance supplied prior to 1 January 2001**

Prior to 1 January 2001, Lloyd's was considered to be a non-resident of the RSA in respect of both open market business and coverholder business (refer par 2.2.1.1). Therefore, where a RSA insured (whether or not registered for VAT) insured goods or services with Lloyd's prior to 1 January 2001 and such goods or services were applied by the vendor for purposes of making non-taxable supplies, such insureds were liable to pay VAT on imported services (refer par 2.2.3).

Similarly, where a RSA resident (vendor) insured his business assets with Lloyd's in circumstances where all the assets were used by the vendor for the purposes of making taxable supplies, the insured did not have to account for VAT in respect of an imported service.

*Resident of the RSA means any person (other than a company) who is ordinarily resident in the RSA or a company, which is a domestic company as defined in the Income Tax Act. Any other person or other company will be deemed to be a resident of the RSA to the extent that such person or company carries on in the RSA any enterprise or other activity and has a fixed or permanent place in the RSA relating to such enterprise or other activity.*

### **4.4.2 Lloyd's business on or after 1 January 2001**

#### **4.4.2.1 Coverholder business**

With effect from 1 January 2001, Lloyd's is considered to be a resident of the RSA to the extent to which it supplies insurance under coverholder business. The imported services provisions do therefore not apply in respect of coverholder business concluded on or after 1 January 2001.

#### **4.4.2.2 Open market business**

Lloyd's will, even after 1 January 2001, continue to be a non-resident of the RSA in respect of its open market business. As a result, individuals and businesses who are not registered for VAT or who are registered for VAT in respect of certain activities will, after 1 January 2001, continue to be liable to account for VAT on imported services in the event where they insure goods or services (which are used for purposes of making non-taxable supplies) under Lloyd's open market business.



## **5 INSURANCE CONTRACTS**

### **5.1 Definition of “insurance”**

Taxable supplies (refer par 3.3.1) include the supply of short-term insurance.

The term ‘insurance’ is defined in the Act to mean insurance or guarantee against loss, damage, injury or risk of any kind whatever, whether pursuant to any contract or law, and includes reinsurance.

The term ‘contract of insurance’ is defined to include a policy of insurance, insurance cover and a renewal of a contract of insurance.

### **5.2 Categories subject to VAT (coverholder business only)**

#### **5.2.1 Standard-rated policies (Section 7(1)(a))**

All categories of short-term insurances are subject to VAT (either at the standard rate or the zero rate) where an insurer who is a VAT vendor supplies the insurance contracts. In the case of Lloyd’s, only coverholder business is subject to VAT.

It is important to note that it is the service consisting of insurance which is subject to VAT and not the underlying subject matter of the insurance. This has the effect that where non-taxable commodities (e.g. money) are insured, the supply of the insurance will remain taxable if supplied by Lloyd’s under coverholder business.

#### **5.2.2 Zero-rated policies (Section 11(2))**

All taxable policies will be subject to VAT at the standard rate, unless where the zero-rating provisions of section 11 of the Act apply.

Section 11(2)(d) provides for the zero-rating of services where they comprise the insuring or the arranging of insurance in respect of:

- the transport of passengers or goods from between places outside the RSA or between the RSA and an export country – (section 11(2)(a)); or
- the transport of passengers by air within the RSA, to the extent that that transport constitutes “international carriage” – (section 11(2)(b)); or
- the transport of goods within the RSA, when being the domestic leg of a foreign journey contemplated in section 11(2)(a), to the extent that the supply of the domestic service is made by the same supplier as for the foreign service – (section 11(2)(c)).

Furthermore, policies in respect of fixed property or movable goods situated outside the RSA during the period of cover, are zero-rated, whether or not supplied to insureds who are residents of the RSA. In particular, hull insurance in respect of foreign-going ships or aircraft is zero-rated, despite the fact that such ships or aircraft may temporarily be in the RSA from time to time.

In addition, policies supplied to non-residents of the RSA are zero-rated, provided the insured is physically outside the RSA and the insurance is not in respect of fixed property or movable goods situated within the RSA.

## **5.3 Categories not subject to VAT**

### **5.3.1 Exempt policies**

The supply of long-term insurance is regarded as a financial service in terms of section 2 of the Act with the result that it is exempt from VAT in terms of section 12 of the Act (refer par 2.3.3).

### **5.3.2 Open market business**

As the supply of insurance under open market business is specifically excluded from the definition of an “enterprise” on the basis that such contracts are concluded outside the RSA, any insurance supplied under open market business is excluded from the ambit of the Act with the result that it is non-taxable (refer par 2.3.3).

## 6 SUMS INSURED

The value of sums insured is normally determined, *inter alia*, with reference to the value of the ultimate loss to be suffered by the insured, taking the VAT effects of section 8(8) into account (refer par 2.3.2). The VAT effects of section 8(8), in turn, are determined with reference to:

- whether the insurance is supplied under open market or coverholder business;
- the purpose for which a vendor insured acquired or applies the subject matter of the policy (i.e. are the goods or services applied in the course of his “enterprise”);
- the VAT status of the insured; and
- the category of business (i.e. whether material damage or consequential loss).

Short-term insurance business can be divided into the following two categories:

- material damage (for example goods such as home content); and
- consequential loss, liability and staff benefit insurance written in the short-term market (for example performance guarantees, personal accident etc).

### ***Examples of sums insured***

#### ***Example 1 - Open Market Business***

*Assume a vendor insured his trading stock with Lloyd’s prior to 1 January 2001, or on or after 1 January 2001 under an open market policy. The value of the sum insured will be the VAT exclusive value of the goods, on the basis that the vendor is entitled to claim the VAT paid on the acquisition of the goods as input tax, thus leaving a VAT exclusive cost and the fact that no section 8(8) liability arises (refer par 2.3.2).*

#### ***Example 2 - Purpose of use of insured property by vendor***

*Assume a vendor insures his trading stock with Lloyd’s after 1 January 2001 under coverholder business, the value of the sum insured is to be determined with reference to the VAT inclusive cost of replacement. This is evidenced since the vendor has a section 8(8) output tax liability in respect of indemnity payments receivable under such contract in respect of his trading stock.*

#### ***Example 3 - VAT status of insured***

*Assume a non-vendor insures his furniture with Lloyd’s under coverholder business. The value of the sum insured is to be determined with reference to the VAT inclusive cost of replacement on the basis that he is not able to re-claim the VAT payable on new furniture, as input tax.*

#### ***Example 4 - Category of business (material damage)***

*A garage owner (vendor) insures his stock of petrol and diesel with Lloyd’s, under coverholder business. Although fuel is subject to VAT at the zero rate, the sum insured is to be determined by*

*adding VAT at the standard rate to the replacement value of the fuel on the basis that the vendor has a section 8(8) liability on indemnities received in respect of zero-rated stock.*

***Example 5 - Category of business (consequential loss)***

*A building contractor (vendor) insures his debtors with Lloyd's under coverholder business. Although the underlying risk consists of money, which is not subject to VAT, and although the value of the debt may include 14% VAT, the value of the sum insured is to be determined by adding VAT at the standard rate to the value of the debt. This is necessary since the indemnity payment receivable is subject to section 8(8) output tax.*

## **7 COMMISSIONS**

Services supplied to Lloyd's by intermediaries (coverholders and brokers) may either constitute taxable supplies where the intermediaries are registered for VAT (taxable at either the standard rate or the zero rate) or non-taxable supplies.

### **7.1 Taxable commission**

Where intermediaries are registered vendors, VAT will be added to the commission.

#### **7.1.1 Standard-rated commission**

Commission in respect of standard-rated coverholder business will be subject to VAT at the standard rate.

#### **7.1.2 Zero-rated commission**

Where the services relate to the arranging of zero-rated policies (refer par 5.2.2), the commission paid on such insurance will be zero-rated. Likewise, commission in respect of insurance services supplied to non-residents (e.g. commissions payable by Lloyd's of open market business) are zero-rated.

#### **7.1.3 Profit Commission**

Wholesale coverholders are, in terms of their binder agreement with Lloyd's underwriters, entitled to receive so-called profit commission in addition to their normal commission. The profit commission becomes payable based on premiums written and claims paid in a twelve month period, reckoned from the date of inception of the coverholder's contract with Lloyd's. However, the commission only become payable after expiry of a pre-determined period, say a four-year period (e.g. commission in respect of the twelve month trading period, commencing say 1 June 1995 to 31 July 1996 will become payable in August 2000).

In order to determine the correct VAT treatment to be applied to profit commission, regard has to be given to the period to which the wholesale coverholder's services refer. This is necessary as the period concerned will determine whether Lloyd's is, for the period concerned, regarded as carrying on an "enterprise" or not (refer par 2.2.1.1). This, in turn, will determine whether Lloyd's is, for the period concerned, regarded as a resident or a non-resident (refer par 4.4).

Lloyd's was not considered to be a resident of the RSA prior to 1 January 2001. Services rendered to Lloyd's prior to 1 January 2001 are therefore considered to have been supplied to a non-resident. It thus follows that the profit commission will, if invoiced or received on or after 1 January 2001, be subject to zero rate VAT where it relates to coverholder contracts incepted prior to this date. Profit commission relating to business written on or after 1 January 2001 will be subject to VAT at the standard rate (refer par 11.4).

#### **7.1.4 Value of Commission**

The value of commission, other than profit commission, is normally determined as a percentage of premium payable. These percentages are capped in terms of the Insurance Act. Premiums, in turn, are normally determined as a percentage of sums insured. Furthermore, where the value of any

consideration (e.g. commission) is determined as a percentage of a VAT inclusive amount (e.g. premium including VAT) the Act provides that the amount calculated is deemed to include VAT, in circumstances where the supplier (i.e. the intermediary) is a VAT vendor. Similarly, where the commission is calculated as a percentage of a VAT exclusive premium, the commission so calculated is also VAT exclusive.

It is pointed out that where a coverholder charged commission, say 15% of premium, prior to 1 January 2001, such commission would have been subject to VAT at the zero rate, with the result that the entire amount would have been income in the hands of the coverholder. However, where the coverholder is a vendor, and he charges 15% commission after 1 January 2001, the commission is to include 14% VAT. This implies that unless the premiums charged after 1 January 2001 are increased by 14%, the coverholders' commissions will effectively reduce by the tax fraction. Thus, in order for a coverholder's (vendor) commission in respect of standard-rated policies to remain unchanged after 1 January 2001, the value of the sums insured needs to be increased by 14%. This will also have the effect that premiums increase by 14%.

## **7.2 Non-taxable commission**

VAT will be not be added to the commission where an intermediary (for instance a non-coverholder retail broker) is not registered for VAT.

## **7.3 Documentation**

Where a coverholder deducts commission from premiums collected by him on behalf of Lloyd's, the premium bordereaux issued by him will become the tax invoice in respect of the VAT charged on the commission and must comply with the necessary requirements (refer par 3.3.2).

## 8 CLAIMS

In processing claims, a distinction needs to be made between so-called ‘trade payments’ and ‘claims payments’. Trade payments are payments made to suppliers of goods or services (for example, where the insured is indemnified by replacing or repairing the goods damaged/destroyed) whereas claims payments are payments of money made to indemnify the insured against the loss suffered.

### 8.1 Trade payments

Where a coverholder indemnifies an insured on behalf of Lloyd’s by way of a trade payment, section 16(3)(a) of the Act provides, *inter alia*, that Lloyd’s is entitled to claim the VAT paid on goods and services as input tax, provided the coverholder is in possession of a valid tax invoice (refer par 3.2).

It thus follows that where Lloyd’s acquires goods or services from non-vendors, in the course of making trade payments, no input tax can be claimed. Furthermore, where the goods or services concerned are exempt or subject to VAT at the zero rate, no input tax can be claimed.

#### 8.1.1 Trade payments in respect of open market business and coverholder business

Section 11(2)(1) of the Act provides for services rendered by residents of the RSA to non-residents to be subject to VAT at the zero rate, but does not include services *directly in connection with movable goods* situated in the RSA at the time the services are rendered.

The view may be held that the term “directly in connection with” implies that the service needs to be rendered on the goods itself, for example the repair of goods.

Therefore, it can be argued that services provided to Lloyd’s by attorneys and assessors in respect of Lloyd’s’ *open market business*, are not supplied directly in connection with movable property and are therefore subject to VAT at the zero rate, irrespective of whether or not the insured is a VAT vendor.

To overcome any confusion whether or not services supplied by attorneys, assessors etc. are supplied in respect of open market business, it is recommended that attorneys, assessors and other vendors who supply services to Lloyd’s, clearly specify on their fee notes/tax invoices, that the services rendered are in respect of open market business or coverholder business. It follows that coverholders will have to timeously inform the attorneys or assessors, as the case may be, whether the services required are for open market business (to be zero-rated) or coverholder business (to be standard-rated).

Certain VAT vendors may supply services to Lloyd’s (in respect of its open market business) consisting of services rendered “directly in connection with movable goods”, for example repair services supplied by a panelbeater on an insured’s motorcar.

Section 11(2)(1)(ii)(bb) of the VAT Act provides that where services (being supplied directly in connection with movable property) are supplied to a non-resident (i.e. Lloyd’s, in respect of open market business) and such services form part of a supply by the non-resident to a *registered* VAT vendor (the insured) and such services are supplied to Lloyd’s for purposes of such supply (which will be the case as the services are supplied in terms of the insurance contract between Lloyd’s and the insured), the services will be zero-rated.

It follows that services (being supplied directly in connection with movable property) provided by Lloyd's to non-vendors (in terms of the insurance contract between Lloyd's) will be subject to VAT at the standard rate. The VAT paid by Lloyd's in this regard may not be recovered as input tax, as it relates to open market business (i.e. Lloyd's non-enterprise activities).

## **8.2 Claims payments made by Lloyd's**

Lloyd's will be entitled to claim an input tax credit based on the tax fraction of indemnity payments made by coverholders on behalf of Lloyd's. This will only apply where the supply of the contract of insurance is a taxable supply or would have been a taxable supply if the supply had taken place on or after 1 January 2001.

Lloyd's will not be entitled to claim an input tax credit where the claims payment relates to a zero-rated policy (refer par 5.2.2) and where the person indemnified is not a vendor and not a resident of the Republic (for example marine claim proceeds paid to a foreigner) at the time of payment.

Lloyd's will also not be entitled to claim an input tax credit where the claims payment results from a supply of goods located outside the Republic or for services performed outside the Republic (for example a reimbursement to the insured for motor vehicle repairs performed in Namibia).

Tax invoices are not required to support Lloyd's input tax claims which relate to claims payments. However, input tax can be claimed as claims payments in the tax period in which the claims are settled.

### **8.2.1 Claims payments to third parties**

Where a coverholder makes claims payments on behalf of Lloyd's to a third party, in the course of indemnifying the insured, and such third party is a vendor, consideration should be given to the nature of the loss in determining whether or not the VAT inclusive value is to be paid.

Claims payments made by coverholders on behalf of Lloyd's to third parties can be summarised as follows:

- Where the nature of the loss is such that the third party (vendor) would, if he were to acquire the goods or services damaged or destroyed, be entitled to claim full input tax, the claims payment may be made for a VAT exclusive value.
- Where the goods or services in respect of which the claim relates, are exempt or subject to VAT at the zero rate, the VAT exclusive amount may be paid.
- Where the third party is not a vendor or a vendor who would not be entitled to claim input tax, the claims payment may be made for a VAT inclusive value.
- Where the third party is a vendor who would, if he were to acquire the goods or services damaged or destroyed, be entitled to a portion of input tax, the claims payment may be made for a value inclusive of VAT only to the extent to which the vendor is not entitled to claim input tax.

It is pointed out that irrespective of whether or not the claim is VAT inclusive or exclusive, Lloyd's will be entitled to claim input tax on the amount paid.



Where an insured claims an indemnity in respect of goods which form the subject matter of a financial agreement with a financier, Lloyd's may, in terms of section 16(3)(c) of the Act, claim input tax on any amount paid towards the financier in the course of indemnifying the insured.

### **8.2.2 Claims payments made to third parties insurer**

Where a coverholder makes payments to other insurance companies on behalf of Lloyd's, other than in terms of a contract of insurance, (e.g. claims for excess payments and other claims where a knock-for-knock agreement does not exist) no input tax may be claimed by Lloyd's.

### **8.3 Claims handling costs**

Claims handling costs such as the payment for police reports, loss adjuster fees, assessors fees etc are to be treated in the same way as trade payments, i.e. input tax can only be claimed if the coverholder received a valid tax invoice from the supplier.

## 9 EXCESSES

### 9.1 Substance of an excess

Generally insureds seek to insure goods or services for its replacement value. However, it is common practice for insurance policies to contain an excess clause in terms of which the insured is required to bear a specified amount in respect of claims. Since the Act does not specifically deal with excess payments, one has to have regard to the general provisions in the Act to determine the VAT treatment, if any, to be applied to excess payments.

Technically, excess payments can only attract VAT if it can be said that such payments constitute the consideration for the supply of services by the insurer to the insured (refer par 2.2.1).

There is an argument that an excess may be viewed as constituting the self-insured portion of the risk insured. As a result, the insurer has no obligation to make good the loss suffered to the extent to which the insured is self-insured. Should this approach be adopted, an argument can be made that an excess is not the consideration for a supply of services by the insurer to the insured, with the result that the excess cannot attract VAT.

However, SARS issued a directive on 11 August 1999, in terms of which the view is expressed that since the value of a loss is inherently VAT inclusive, excess payments will be VAT inclusive. The directive further suggests that an excess payment is the fee which the insured is liable to pay to the insurer for handling an insurance claim.

Lloyd's treats excess payments as VAT sensitive (VAT inclusive), in line with the directive issued by SARS.

#### *Examples of excess payments*

##### *Example 1*

*An insured (VAT vendor) suffers a loss in the amount of R11 400 (VAT inclusive) in respect of a computer destroyed by water damage and has to pay an excess of 10%. The insurer pays the insured an amount of R10 260 (net of excess).*

##### *Position of the insurer*

*The insurer is entitled to claim input tax by applying the tax fraction (14/114) to the indemnity amount paid to the insured; (i.e.  $14/114 \times R10\ 260 = R1\ 260$ ) with the result that the claim net of VAT amounts to R9 000.*

##### *Position of the insured*

*The insured accounts for section 8(8) output tax on the net indemnity payment received (i.e.  $14/114 \times R10\ 260 = R1\ 260$ ). As a result, the amount recovered after VAT amounts to R9 000.*

### *Example 2*

*A home owner (non-vendor) insures his furniture for R114 000, VAT inclusive. His policy provides for a R1 000 excess to be paid on each claim. His house is destroyed by fire and he claims for total loss.*

#### *Position of the insurer*

*The insurer pays the insured the full value of the sum insured less the excess (i.e. R114 000 - R1 000 = R113 000). The insurer claims input tax equal to the tax fraction of the net claims amount paid (i.e.  $14/114 \times R113 000 = R13 877$ ) with the result that the net claim paid amounts to R99 123 in the hands of the insurer.*

#### *Position of the insured*

*Since the insured is not a VAT vendor, he is not liable to account for output tax on the amount received with the result that the net amount received by him is R113 000.*

### *Example 3*

*A vendor insured insures his office furniture for R22 800, VAT inclusive. The insurance policy provides for a 10% excess. The furniture is destroyed by fire and the insured claims for total loss. The insurer decides to replace the furniture and requests the insured to collect the new furniture from the merchant after payment to the merchant of the excess.*

#### *Position of the insurer*

*The insurer receives a tax invoice from the merchant for R22 800, VAT inclusive. Since the insured paid the 10% excess directly to the merchant, the insurer is only liable to pay R20 520, VAT inclusive, to the merchant. The insurer claims the tax charged as input tax (i.e.  $14/114 \times R22 800 = R2800$ ). The insurer issues a tax invoice to the insured for the excess amounting to R2 280, including VAT and the insurer accounts for the output tax (i.e.  $14/114 \times 2 280 = R280$ ). The net cash outflow, after taking input tax and output tax into account, amounts to R18 000 (i.e.  $20 520 - 2 800 + 280$ ).*

#### *Position of the insured*

*The insured receives a tax invoice for the excess of R2 280, VAT inclusive, claims the input tax of R280 leaving a net cash outflow of R2 000 (i.e. 10% of R22 000).*

## **10 RECOVERIES**

### **10.1 Salvage recoveries**

Salvage recoveries are subject to VAT in the same way as any other supply. No VAT is payable until the salvage is sold. Coverholders who sell salvage on behalf of Lloyd's are required to issue a tax invoice at the time of sale.

Where salvage recoveries comprise goods which are exported or salvage sold outside the RSA, such supplies will be subject to VAT at the zero rate (refer par 2.3.1).

### **10.2 Claims recoveries from re-insurers and third parties**

#### **10.2.1 Recoveries from re-insurer**

Where a coverholder makes a claim on behalf of Lloyd's to a re-insurer, the indemnity payment received by the coverholder will be subject to VAT in terms of section 8(8) of the Act, unless the premiums paid to the re-insurer were subject to VAT at the zero rate or were exempt (refer par 2.3.2).

#### **10.2.2 Recoveries from third parties**

Where a coverholder recovers an amount from a third party or from the third party's insurer, the amount received is not subject to VAT on the basis that it does not constitute an indemnity payment received under a contract of insurance as envisaged in section 8(8) of the Act (refer par 2.3.2).

## **11 TRANSITIONAL MATTERS**

SARS has issued a directive which confirms that the following transitional rules will apply:

### **11.1 Premiums to be subject to VAT**

VAT has to be charged at either the standard rate or the zero rate on all premiums in respect of coverholder policies which incept on or after 1 January 2001.

### **11.2 Additional premiums**

Where an insured person wishes to obtain additional insurance cover, for example where an insured person acquires additional assets, the existing policy will be amended and an additional premium will be charged in respect of the additional insured portion. Additional premiums which become payable on or after 1 January 2001 will be subject to VAT.

However, the above treatment does not apply to adjustments to premiums.

#### ***Example of an additional premium not subject to VAT***

*The premium for an annual group personal accident insurance policy is based on the final payroll amount. The premium cannot finally be determined until the end of the insured's financial year-end. Where the policy incepted prior to 1 January 2001, the premium is not subject to VAT. Similarly, any adjustment to such premium will not attract VAT, albeit that the adjustment is an amount payable on or after 1 January 2001. Should the final additional premium become payable on or after 1 January 2001, said additional premium will not be subject to VAT. Should the policy be renewed after this date, the premium will be subject to VAT.*

### **11.3 Credits on policies**

Credits are passed, *inter alia*, where an insured person disposes of insured assets. Credits due on annual policies will be subject to VAT only if the premiums were subject to VAT.

### **11.4 Profit commission**

Profit commission will, if invoiced or received on or after 1 January 2001, be subject to zero rate VAT where it relates to coverholder contracts incepted prior to this date. Profit commission relating to business written on or after 1 January 2001 will be subject to VAT at the standard rate (refer par 7.1.3).

### **11.5 Claims**

Input tax is claimable on claims payable in respect of contracts of insurance which were subject to VAT or contracts of insurance which would have been subject to VAT, had the policies incepted after 1 January 2001 (refer par 8.2).

## 12 ADMINISTRATION OF LLOYD'S VAT

Lloyd's is registered as a vendor with effect from 1 January 2001. Lloyd's VAT accounting system will be operated centrally, initially by Lloyd's South Africa, which will complete and submit Lloyd's VAT returns on a monthly basis.

Lloyd's relies on the South African coverholders in administering its VAT.

### 12.1 Responsibilities of coverholders

Coverholders have the following responsibilities in respect of Lloyd's VAT:

- administer Lloyd's South African VAT (charge output tax, claim input tax) on behalf of Lloyd's;
- maintain separate accounting records in respect of Lloyd's VAT liability (premiums, claims, retain valid VAT documentation etc);
- completing 'dummy VAT returns' (refer par 14); and
- submitting the dummy return, together with the relevant bordereaux, to Lloyd's South Africa by no later than the 10<sup>th</sup> business day of the month following the end of each tax period (refer par 2.6.2).

Lloyd's is entitled to an input tax deduction in respect of commissions paid to wholesale or retail coverholders and retail brokers where such coverholders or brokers are registered VAT vendors. To ensure the consistent treatment of Lloyd's input tax claims in respect of commissions and that input tax claims relating to services provided by retail brokers are treated correctly, the input tax claims of Lloyd's in respect of non-coverholder retail broker commissions will be accounted for by the **wholesale coverholders**.

The information provided to Lloyd's South Africa by coverholders will also need to be reported to the Lloyd's broker so it can be recorded by Lloyd's Policy Signing Office ("LPSO"). Where there is a net credit to be settled to syndicates, the Lloyd's broker will be asked to process a refund against each binding authority block entry or individual claim.

Please refer to the case study in chapter 14.

## **13 LLOYD'S TAX**

The 2.5% Lloyd's tax continues to be chargeable. Please note that this tax should be calculated on the VAT exclusive premium. So if, for example, the premium is R100 plus VAT of R14 the tax due is R2.50, i.e. 2.5% x R100.

## 14 CASE STUDY

<b>1</b>	<b>Premiums – Effective date 1 February 2001</b>	<b>Amount Excl</b>	<b>VAT</b>
	- Hull insurance – foreign going ship	R700 000	Nil
	- Vehicles	R200 000	R 28 000
	- Group accident	R100 000	R 14 000
		<hr/>	<hr/>
		R1 000 000	R 42 000
<b>2</b>	<b>Premiums – Effective prior to 1 January 2001</b>		
	- Household	R300 000	Nil
	- Vehicles	R 50 000	Nil
	- Group accident	R 80 000	Nil
		<hr/>	<hr/>
		R430 000	Nil
<b>3</b>	<b>Claims Paid</b>		
	- Vehicles	R 70 000	R 9 800
	- Group accident	R 20 000	R 2 800
	- Ex gratia	R 50 000	Nil
		<hr/>	<hr/>
		R140 000	R 12 600
<b>4</b>	<b>Recoveries</b>		
	- Salvage sales (local)	R 10 000	R 1 400
	- 3 <sup>rd</sup> Party	R 5 000	Nil
		<hr/>	<hr/>
		R 15 000	R 1 400
<b>5</b>	<b>Commissions Payable</b>		
	- Coverholder (wholesale or retail) iro taxable premium	R 30 000	R 4 200
	- Profit commission iro 1996 business	R 20 000	Nil
	- Retail broker (accounted for by wholesale coverholder)	R 15 000	R 2 100
		<hr/>	<hr/>
		R 65 000	R 6 300
<b>6</b>	<b>Claims handling cost</b>		
	- Assessors (non-vendors)	R 5 000	Nil
	- Loss adjusters (vendors)	R 2 000	R 280
		<hr/>	<hr/>
		R 7 000	R 280



# Specimen Bordereau

Prepared by:  
 Name of Coverholder  
 Address of Coverholder  
 VAT registration number of Coverholder  
 Date  
 Bordereaux number

Issued to:  
 Lloyd's South Africa  
 The Forum 7<sup>th</sup> Floor, Maude Street, Sandton, 2186,  
 South Africa

	PREMIUM (Output)				COMMISSIONS PAYABLE (Input)				RECOVERIES (Output)						
	Standard Rate Excl VAT	VAT	Zero Rate	Non-Taxable	Coverholder Excl VAT	VAT	Zero Rate Commissions	Non-Taxable	Salvage Sales Excl VAT	VAT	Zero Rate Salvage Sales	Third Party Recoveries			
1	R300 000	R 42 000	R700 000	R430 000											
1															
2															
4												R 10 000	R 1 400		
4									R 30 000	R 4 200					R 5 000
5									(I) R 15 000	(I) R 2 100	R 20 000				
5															
5															
	<b>R300 000</b>	<b>R 42 000</b>	<b>R700 000</b>	<b>R430 000</b>	<b>R 45 000</b>	<b>R 6 300</b>	<b>R 20 000</b>	<b>R -</b>	<b>R 10 000</b>	<b>R1 400</b>	<b>R -</b>	<b>R 5 000</b>			

# Specimen Bordereau

Prepared by:  
 Name of Coverholder  
 Address of Coverholder  
 VAT registration number of Coverholder  
 Date  
 Bordereaux number

Issued to:  
 Lloyd's South Africa  
 The Forum 7<sup>th</sup> Floor, Maude Street, Sandton, 2186,  
 South Africa

	CLAIMS (Input)			CLAIMS HANDLING (Input)		
	Claims Paid Excl VAT	VAT	Non-Taxable Claims	Expense Excl VAT	VAT	Non-Taxable Expense
3	R 90 000	R 12 600				
3			R 50 000			
6						R 5 000
6				R 2 000	R 280	
	<b>R 90 000</b>	<b>R 12 600</b>	<b>R 50 000</b>	<b>R 2 000</b>	<b>R 280</b>	<b>R 5 000</b>

# Dummy VAT Return to Lloyd's

Prepared by:  
 Name of Coverholder  
 Address of Coverholder  
 VAT registration number of Coverholder  
 Date

Issued to:  
 Lloyd's South Africa  
 The Forum 7<sup>th</sup> Floor, Maude Street, Sandton 2186,  
 South Africa

	<b>Consideration (Incl VAT)</b>		<b>VAT</b>
<b>CALCULATION OF OUTPUT TAX</b>			
Standard rate (excl capital goods and/or services)	R353 400	x 14/114	R 43 400
Standard rate (only capital goods and/or services)	R -	x 14/114	R -
Zero rate	R700 000		
Exempt and non-supplies	R435 000		
<b>TOTAL OUTPUT TAX</b>			<i>R 43 400</i>
<b>CALCULATION OF INPUT TAX</b>			
Capital goods or services			R -
Other goods or services			R 19 180
<b>TOTAL INPUT TAX</b>			<i>R 19 180</i>
<b>AMOUNT PAYABLE/REFUNDABLE</b>			<i>R 24 220</i>

I certify that the particulars in this return are true and correct.		
_____	_____	_____
Date	Capacity	Signature

