

# MARKET BULLETIN

REF: Y5085

<b>Title</b>	2017 Canadian Income Tax Returns
<b>Purpose</b>	To set out the timetable and procedures for the submission of the Canadian Syndicate Information Statements
<b>Type</b>	Scheduled
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<b>Date</b>	19 April 2017
<b>Deadline</b>	31 May 2017
<b>Related links</b>	Appendix 1: Instructions for Completing the Returns Appendix 2: Table of Canadian FIL Codes

**Please copy this Bulletin and its attachments to those within your organisation that are responsible for reviewing and completing the Canadian Syndicate Information Statements.**

**Additionally, the Head of Tax (or person responsible for taxation within the managing agency) may need to see the section on payments on account and potential liability.**

**Please note that this return must now be made via Core Market Returns.**

## Background

In order that a Canadian income tax return can be filed by Lloyd's on behalf of all non-Canadian resident members, Lloyd's syndicates must complete and submit a Canadian Syndicate Information Statement ("SIS"), for the 2014 Underwriting year of account and the calendar year movement for run offs during 2016. Returns to be received by close of business on the 31 May 2017.

The SIS return is used to determine the Canadian tax liability of all non-Canadian resident members. It also determines the Canadian tax funding requirement from the syndicates, since the Canadian tax liability is funded by the syndicates until the tax is collected from the members via distribution.

### Interaction with discussions in Canada on income tax and HST/GST filings

Lloyd's Tax Team continues to discuss members' tax arrangements with the Canadian Department of Finance ("Finance") and Canada Revenue Agency ("CRA"). Unless and until we have agreed new arrangements the current basis of filing will continue as this is the only basis on which we can file a consolidated income tax return for the market.

### Payments on account and potential liability

Payments on account for the 2014 year of account, which forms the basis of the 2017 return, were made monthly during 2014.

Monthly payments on account have also been made for 2015, 2016 and are being made in 2017.

For 2015 and 2016 the monthly payments were *reduced* to take into account our view of the extent to which members are likely to have a taxable permanent establishment ("PE") under the UK-Canada tax treaty. This reduction was based on several assumptions. First, we had hoped that our discussions with Finance and CRA would be concluded during 2016; second, we took the view that the tax base would significantly reduce under a modern PE analysis of the market's Canadian activity; and finally, we anticipated that the tax due from this reduced base would be much smaller than under the existing agreement with CRA.

While an analysis of the coverholder population for the 2012 year of account does support the conclusion that the tax base at *market-level* would significantly reduce under a modern PE analysis, further analysis of the data suggest that the profits at *member-level* might not necessarily reduce in proportion to the reduction in tax base. Various factors affect this analysis including that many coverholders that one would generally not consider would ever create a PE of members did not, appear to generate much of the profit made by members *in the year of account that we reviewed*. In other words, while premium can be relatively clearly identified as falling outside a members' PE the impact on the taxable profit of the 'remaining' PE is much less certain.

We have taken the decision therefore to restore market-level payments on account for 2017 to their former level from May 2017; the basis of which is the final liability for the 2013 year of account filed in March 2017.

For the 2018 and 2019 returns (the 2015 and 2016 years of account), it is *possible* that payments on account may be inadequate to meet members' final liability. If any member wishes to provide for the potential underpayment we would suggest providing approximately double the payments made for that year. This is on the basis that, across the market, we reduced payments on account for 2015 and 2016 to approximately one-third of the amount paid in 2014.

Any questions regarding the collection of tax from the syndicate should be addressed to Simon Tyler on 01634 392512 or by e-mail: [simon.tyler@lloyds.com](mailto:simon.tyler@lloyds.com).

### **Income tax deduction for HST/GST paid**

The position taken by Lloyd's in its submissions to the Canada Revenue Agency is that any HST/GST liability should only attach to business written through Canadian coverholders.

For the 2014 year of account this aligns with the tax-base for income tax purposes. As such, any additional HST/GST paid for the 2014 year of account (or earlier years and not already deducted for income tax) should be included in Line 8 of the SIS form in Column A (and not allocated across Columns A and B). This will include amounts on the syndicate's GST return for 2015 filed in 2016.

### **Completing the return**

Instructions for completing the return can be found in Appendix 1 and must be followed.

The supporting schedules, such as expenses and closing reinsurance, no longer need to be submitted but you must retain these records until the year of account becomes statute barred for Canadian tax purposes (generally 7 years after a Member receives a Notice of Assessment).

This Bulletin has been sent to all managing agents.

Any queries relating to this Bulletin should be directed to Cheryl Masson on extension 2620 or to me on extension 2433. Alternatively, please contact us by email at [cheryl.masson@lloyds.com](mailto:cheryl.masson@lloyds.com) or [christine.allcott@lloyds.com](mailto:christine.allcott@lloyds.com).

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## Appendix 1

**CANADIAN FEDERAL INCOME TAX 2014 YEAR OF ACCOUNT****Explanatory notes and instructions for the completion of Canadian Syndicate Information Statements (“SIS”)****1. OVERVIEW AND GENERAL INFORMATION**

Canadian tax is payable on the profit arising from business written under both full binding authorities and limited binding authorities held by Canadian coverholders.

Full binding authorities, including those given for reinsurance, are those binding authorities where the Canadian coverholder is authorised to accept risks on behalf of those Underwriters at Lloyd’s, subscribing to the facility, without the prior approval of Underwriters.

A limited binding authority is defined as “an agreement between Underwriters and a coverholder under which the coverholder is authorised to issue documents evidencing that risks have been accepted on behalf of underwriting members only after they have been accepted by the leading Underwriter as provided on the slip”.

The Canadian taxable business is identified using FIL codes. At Appendix 2, there is a list of FIL codes showing which codes relate to taxable Canadian business and which codes relate to non-taxable Canadian business.

The Lloyd’s three year accounting convention is recognised, so the profits of a year of account are taxable in the year of distribution.

Please note the following:

- A return must be completed for every syndicate with Canadian dollar business for the 2014 year of account, even where all such business is non-taxable.
- A separate return must be submitted for years of account that are in run-off during calendar year 2016 reflecting the movement during the year.
- The data needs to be reported in Canadian Dollars, therefore Canadian business written in US dollars should be translated at a rate of Can\$1.34 = US\$1.00.
- All amounts must be shown in Canadian dollars; the rate of exchange to be used is the Lloyd’s audit rate at 31 December 2016 i.e. Can\$1.66 = £1.00.

**DEADLINE:**

The completed forms must be returned to Tax Operations by close of business on 31 May 2017, via Core Market Returns which should be available on 4 May 2017.

**2. UNDERWRITING INCOME****2.1 Allocation between Taxable and Non-Taxable business**

For Canadian taxable underwriting income, please see Appendix 2 for the FIL Codes of items that must be reported in column A.

For Canadian non-taxable underwriting income please see Appendix 2 for the FIL codes of items that should be included in the figures in Column B. Note that this Column should show only **Canadian** business which is not subject to Canadian income tax rather than **all** business which is not subject to Canadian tax.

***N.B: Any Canadian dollar business which does not bear an identifiable taxable or non-taxable code should normally be pro-rated between taxable and non-taxable on the basis of business with identifiable codes.***

Syndicate reinsurances and recoveries bearing old FIL code "JL" or new FIL codes VJ(CDE2), VK(CDE3) and VL(CDE4) should be pro-rated between taxable and non-taxable business.

The figures in Column C represent total world-wide business in all currencies converted to Canadian dollars at Lloyd's audited rate of exchange. **It is not the sum of Columns A and B as on the equivalent US return.**

**2.2 Arriving at underwriting profit/loss**

In arriving at the underwriting profit/loss figure (Line 9) the following items should be included in respect of the 2014 year of account (and all previous years reinsured therein) or the 2016 calendar year movement for a syndicate in run-off:

**2.2.1 Premiums Written (Line 1)**

Premiums must be returned net of commission and brokerage. In calculating these figures, all additional premiums must be included and return premiums should be deducted in full.

Please ensure you report all premiums including those being reported using Lloyd's direct reporting.

**2.2.2 Closing Reinsurance Assumed (Line 2)**

The reinsurance to close premium received by the 2014 year of account from a previous closed year should be included in line 2. This will usually be the reinsurance to close premium for the 2013 year of account.

The amounts shown in Columns A and B should equal the reinsurance to close ceded figures of the previous year of account shown in the 2015 Tax Year SIS. The amount shown in Column C should represent the equivalent worldwide figure but reworked at 31 December 2016 conversion rates.

For years of account which remained open at 31 December 2016, the closing reserve shown on the 2015 SIS should be reported.

**2.2.3 Syndicate Reinsurance Recoveries (Line 3)**

(a) **Facultative Reinsurance**

The FIL coding of the original insurance must be followed, as with reinsurance premiums.

(b) **Whole Account Excess of Loss, Stop Loss, Quota Share etc.**

The general principle is that where a deduction for the reinsurance premium has been taken for Canadian tax purposes, an appropriate proportion of any recovery under the policy must be included in computing the Canadian taxable profit.

Any recoveries on whole account stop loss and excess of loss reinsurance must be allocated to Canadian taxable business and Canadian non-taxable business as follows:

Taxable syndicate reinsurance recoveries =

$$\frac{\text{Canadian taxable premium income}}{\text{Worldwide premium income}} \times \text{Total syndicate reinsurance recoveries}$$

Non-taxable syndicate reinsurance recoveries =

$$\frac{\text{Canadian non-taxable premium income}}{\text{Worldwide premium income}} \times \text{Total syndicate reinsurance recoveries}$$

Where the reinsurance recovery is received in respect of specific sections of the account, the same principle should be applied but instead the Canadian and Worldwide premium income of the original policies protected should be used in each case.

The syndicate may use a more accurate basis e.g. by analysing the coding of the claims contributing to the recovery and then allocating the recovery in line with the proportion of Canadian taxable/non-taxable claims to total worldwide claims. Either basis is acceptable if it is consistently applied.

**2.2.4. Syndicate Reinsurance Ceded (Line 4)**

(a) **Facultative Reinsurance**

The FIL coding of the original insurance must be followed for reinsurance premiums.

(b) **Whole Account Excess of Loss, Stop Loss, Quota Share etc.**

Premiums on whole account stop loss and excess of loss reinsurances must be allocated to Canadian taxable and Canadian non-taxable business as follows:

Taxable syndicate reinsurance ceded =

$$\frac{\text{Canadian taxable premium income}}{\text{Worldwide premium income}} \times \text{Total syndicate reinsurance ceded}$$

Non-taxable syndicate reinsurance ceded =

$$\frac{\text{Canadian non-taxable premium income}}{\text{Worldwide premium income}} \times \text{Total syndicate reinsurance ceded}$$

Where the reinsurance protects specific sections of the account, the same principle should be applied but instead the Canadian and Worldwide premium income of the original policies protected should be used.

**2.2.5. Closing Reinsurance Ceded (Line 5)**

The reinsurance to close premium paid by the 2014 year of account should be reported or, if the year of account did not close, the closing reserve should be reported.

The amount of reinsurance to close premium to be allocated to Canadian taxable business should be calculated on the basis of the taxable outstanding claims, i.e. the claims with a FIL code classed as taxable in Appendix 2. The same principle should be applied to allocate the reinsurance to close premium to Canadian non-taxable business. It is expected that all reinsurance to close will be allocated on an outstanding claims basis. **However, if a syndicate is not able to do this and an alternative method is used, a detailed explanation of the method used must be submitted.**

**2.2.6. Losses Paid (Line 6)**

All claims (less salvages) including settlement costs, fees, etc. debited to the 2014 year of account up to and including 31 December 2016 should be reported.

For years of account in run-off during 2016, only additional claims paid during 2016 should be reported.

**2.2.7 Profit Commission (Line 7)**

A share of profit commission may be included and should be allocated to Canadian taxable and Canadian non-taxable business in the following way:

Taxable profit commission =

$$\frac{\text{Canadian taxable business income before profit commission (Column A Line 12 (before profit commission))}}{\text{Worldwide income (Column C Line 12 (before profit commission))}} \times \text{Total profit commission}$$

Non-taxable profit commission =

$$\frac{\text{Canadian non-taxable business income before profit commission (Column B Line 12 (before profit commission))}}{\text{Worldwide income (Column C Line 12 (before profit commission))}} \times \text{Total profit commission}$$

However, the following limitations and variations apply:-

- (a) If there is a Canadian taxable loss, i.e. Column A Line 12 (before profit commission) is negative, no profit commission must be allocated to Canadian taxable business.
- (b) The amount of profit commission allocated to Canadian taxable business should not create a taxable loss, i.e. it must not exceed Column A Line 12 (before profit commission).
- (c) The amount of profit commission allocated to Canadian taxable business must not exceed the total Worldwide profit commission.
- (d) If the Canadian taxable result (Column A Line 12), is greater than the Worldwide result (Column C Line 12), both before profit commission, the proportion of the profit commission allocated to the Canadian taxable column must be the same as the proportion of the Canadian taxable result compared to the profitable areas of the syndicate's business as a whole.
- (e) If profit commission is calculated by currency rather than on the syndicate's business as a whole, the proportion of the Canadian dollar profit commission allocated to Canadian taxable business must be the same as the proportion

of the Canadian dollar taxable result before profit commission compared to the total Canadian dollar result before profit commission.

- (f) If there is a profit commission refund, this should be allocated to Canadian taxable business on the same basis that the profit commission was originally allocated.

An analysis of the calculations should be attached in all cases.

**2.2.8 Expenses and Other Deductions (Line 8)**

Expenses relating to Canadian dollar business should be allocated across Columns A and B.

The amount to be included in Column A is calculated as follows:

<u>Canadian taxable premium income</u>	X	Expenses relating to Canadian dollar business
Total Canadian business premium income		

It follows that the remaining expenses relating to Canadian dollar business should be allocated to Column B.

If you have written any Canadian business in US dollars, expenses relating to this business may also be allocated across Columns A and B using the above method.

In addition agency salaries, commissions (excluding profit commission) and other expenses (excluding US dollar expenses and any exchange gains and losses) (“Expenses”) should be included as follows:

Amount to be included in Column A

<u>Canadian taxable premium income</u>	X	Expenses
Worldwide business premium income		

Amount to be included in Column B

<u>Canadian non-taxable premium income</u>	X	Expenses
Worldwide business premium income		

**2.2.9 Underwriting Profit or Loss (Line 9)**

This should be the sum of Lines 1-3 minus the sum of Lines 4-8. It will not be possible to submit the return if this check fails.

### 3. **EFFECTIVELY CONNECTED PERCENTAGE (“EC percentage”)**

This percentage is used to apportion investment income and capital gains or losses between Canadian taxable and non taxable income. It is calculated as the ratio of the Canadian taxable premium income over the total premium income in respect of the Canadian business written by the syndicate, or

$$\frac{\text{Line 1, Column A}}{\text{Line 1, (Columns A+B)}} \times 100\%$$

**No variations to this calculation should be made.**

If a return is being made for a year that is running-off, the effectively connected percentage used on the return at 36 months must be used.

### 4. **INVESTMENT INCOME/CAPITAL GAINS**

#### 4.1 **Allocation between Taxable and Non-Taxable business**

The amounts inserted in Column A should be equal to the EC percentage of the income received through the Lloyd’s Canadian Trust Fund (“LCTF”) which has been allocated to 2014 year of account or earlier run-off year of account where appropriate. The EC percentage calculated as per section 2 of this bulletin should be used and no adjustments should be made for variations in the underlying business.

Column B should show the balance of the income received through the LCTF which has been allocated to 2014 year of account or earlier.

Column C should show the total worldwide investment income and capital gains in all currencies converted at Lloyd’s audited rate of exchange (£1.00=Can\$1.66).

#### 4.2 **Investment Income (Line 10)**

All interest and dividends treated as investment income for UK tax purposes should be reported.

#### 4.3 **Capital Gain/Loss (Line 11)**

Capital gains/losses realised and unrealised on the UK basis should be reported.

### 5. **TOTAL INCOME (Line 12)**

This should be the sum of Lines 9 to 11 and is used for verification purposes only. It will not be possible to submit the return if this check fails.

Canadian \$ Taxable Codes (Column A)			Canadian \$ Non-Taxable Codes (Column B)		
Old Codes <sup>2</sup>	2 Digit	4 digit	Old Codes <sup>2</sup>	2 Digit	4 digit
JE	ML	CDC1	JA	VM	CDA1
JM	VB	CDC2	JB	VO	CDA2
	VN	CDF1	JD	VQ	CDA3
	VD	CDF2	JJ	CU	CDA4
	VP	CDG1	JS	VR	CDH2
	VE	CDG2	JN	VS	CDH3
	CW	CMB1	JT	VT	CDH4
	VA	CMB2	JF	VU	CDJ2
	MZ	CMD1	JG	VV	CDJ3
	VC	CMD2	OA <sup>1</sup>	VW	CDJ4
	CS	CMN1		CL	CDK2
	VF	CMN2		CM	CDK3
	CV	CMP1		CN	CDK4
	VG	CMP2		CX	CDQ2
	MI	CMT1		CY	CDQ3
	VH	CMT2		CZ	CDQ4
	MY	CMY1		MC	CDR2
	VI	CMY2		MD	CDR3
				ME	CDR4
				MF	CDS2
				MG	CDS3
				MH	CDS4
				MM	CDU2
				MN	CDU3
				MP	CDU4
				MQ	CDV1
				MR	CDW1
				VX	CML1
				CO	CMM1
				CP	CMM2
				CQ	CMM3
				CR	CMM4
				EL	CMW1
				EM	CMW2
				EJ	CMW3
				EK	CMW4
				EN	CMX1
				EO	CMX2
				EP	CMX3
				ES	CMX4

Canadian \$ Taxable Codes (Column A)			Canadian \$ Non-Taxable Codes (Column B)		
Old Codes <sup>2</sup>	2 Digit	4 digit	Old Codes <sup>2</sup>	2 Digit	4 digit
				5D	YCA1
				7K	YCA2
				7T	YCA3
				7S	YCA4
				1A	YCI1
				4A	YCK1
				5D	YCV1
				VO	CXM2
				VQ	CXM3
				CU	CXM4

Codes to be apportioned between taxable and non-taxable (see appendix 1. 3)

Old Code	2 Digit	4 Digit
JL	VJ VK VL	CDE2 CDE3 CDE4

<sup>1</sup> NB use of the two-character code was wider than the four character codes listed, and includes currencies other than Canadian Dollars. Any use of this two-character code for the purposes of this return must be restricted to Canadian Dollars.

<sup>2</sup> The old tax codes do not necessarily bear any direct relationship to the new codes shown.