



Legal Counsel

Value-Added Tax

VAT 421

Guide for Short-Term Insurance



South African Revenue Service

Preface

This guide is a general guide concerning the application of the VAT Act to short-term insurance transactions in South Africa. Although fairly comprehensive, the guide does not deal with all the legal detail associated with VAT and is not intended for legal reference. Technical and legal terminology has also been avoided wherever possible. For details about the general operation of VAT, see the *VAT 404 – Guide for Vendors* which is available on the South African Revenue Service (SARS) website (www.sars.gov.za).

All references to the “VAT Act” are to the Value-Added Tax Act 89 of 1991 and references to “sections” are to sections of the VAT Act, unless the context otherwise indicates. The Tax Administration Act 28 of 2011 is referred to as the “TA Act”. Any reference to the Short-Term Insurance Act 53 of 1998 and Long-Term Insurance Act 52 of 1998 are referred to as the “STI Act” and the “LTI Act” respectively.

The terms “Republic”, “South Africa” or the abbreviation “RSA”, are used interchangeably in this document as a reference to the sovereign territory of the Republic of South Africa, as set out in the definition of “Republic” in section 1(1). The terms “Commissioner” and “Minister” refer to the Commissioner for SARS and the Minister of Finance respectively, unless otherwise indicated. A number of specific terms used throughout the guide are defined in the Act. These terms and others are listed in simplified form in the **Glossary**, which also includes a selection of terminology used in the insurance industry.

The information in this guide is based on the VAT legislation (as amended) at the time of publishing, up to and including the Taxation Laws Amendment Act 25 of 2015 (as per *Government Gazette (GG)* 39588) and Tax Administration Laws Amendment Act 23 of 2015 (as per GG 39586).

This guide is not an “official publication” as defined in section 1 of the TA Act and accordingly does not create a practice generally prevailing under section 5 of that Act. It is also not a binding general ruling under section 89 of Chapter 7 of the TA Act or a ruling under section 41B of the VAT Act, unless otherwise indicated.

Binding General Ruling (VAT) 14 (Issue 2) “VAT Treatment of Specific Supplies in The Short-Term Insurance Industry” (BGR 14), Binding General Ruling (VAT) 32 “VAT Treatment of Supplies in The Short-Term Reinsurance Industry” (BGR 32) and Binding General Ruling (VAT) 37 “Zero-rating of international travel insurance” (BGR 37), which are included in Annexure A, B and C respectively, deal with some specific aspects of insurance and reinsurance and may be relied upon.

All previous editions of the *VAT 421 – Guide for Short-Term Insurance* will be withdrawn from date of issue of the finalised guide.

There are various other guides available on the SARS website which may be referred to for more information relating to specific VAT topics.

All guides, interpretation notes, binding general rulings, forms, returns and tables referred to in this guide are available on the **SARS website**.

Should there be any aspects relating to VAT which are not clear or not dealt with in this guide, or should you require further information or a specific ruling on a legal issue, you may –

- visit the SARS website at **www.sars.gov.za**;
- contact your local SARS branch;
- contact the SARS National Contact Centre –
 - if calling locally, on 0800 00 7277;
 - if calling from abroad, on +27 11 602 2093 (only between 8am and 4pm South African time);
- submit a ruling application to SARS headed “Application for a VAT Class Ruling” or “Application for a VAT Ruling” together with the VAT301 form by email to **VATRulings@sars.gov.za** or by facsimile on +27 86 540 9390; or
- submit legal interpretative queries on the TA Act by email to **TAAInfo@sars.gov.za**;
or
- contact your own tax advisors.

Comments regarding this guide may be emailed to **policycomments@sars.gov.za**.

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12 December 2016

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Chapter 1

Introduction

1.1 Policy background

When VAT was introduced on 30 September 1991, supplies of short-term insurance became subject to VAT, but long-term insurance was exempt (being “financial services”). At that time, certain other fee-based services, for example, providing financial advice, arranging financial services and debt collection services were also regarded as exempt financial services. However, from 1 April 1995, the VAT Act was amended to exclude such services from the definition of “financial services” from that date. The supply of credit guarantee insurance which was also initially exempt became taxable from 1 October 1996.

1.2 Scope of insurance topics

This guide deals with the VAT implications of transactions related to short-term insurance business in South Africa and the accounting in respect thereof. Included is a discussion on how insurance and related transactions impact on brokers, agents and other intermediaries¹ as they play an important role in the insurance industry. The guide does not deal with long-term insurance services, except to the extent that it serves to clarify the distinction between long-term insurance, short-term insurance and other goods and services supplied in the course of writing short-term insurance business. The guide will focus mainly on the following aspects:

- **The nature and meaning of “insurance”**

Before delving into the application of the VAT law in regard to short-term insurance, we will first establish what is meant by the term “insurance”, which has both an ordinary legal meaning as well as a defined meaning for VAT purposes. The distinction is important in that the VAT treatment of transactions is based primarily on the characterisation of the underlying supplies. We will also mention some of the main legal principles upon which insurance is based, as well as clarify the distinction between long-term and short-term insurance.

- **Supply of short-term insurance²**

Generally, VAT is payable at the standard rate on the supply of risk cover in terms of a short-term insurance policy.³ There are, however, certain instances when the supply of insurance will be subject to VAT at the zero rate. Premiums payable in respect of long-term insurance such as life assurance and endowment policies are generally exempt from VAT. As with any type of legal contract involving supplies, there will be a supplier and a recipient. These two parties will be referred to in this guide as “**the insurer**” or “**reinsurer**” and “**the insured**” or “**cedent**” respectively.

¹ For the purposes of this guide, unless otherwise indicated, the terms “agent”, “intermediary”, “broker” or “independent intermediary” are used interchangeably and indicate the designation of a legal agent of the insurer, reinsurer, cedent or insured (principal).

² The term “insurance” includes reinsurance unless the context indicates otherwise.

³ The term “policy” means a document which is evidence of a contract of insurance, including any renewal notice, premium notification or endorsement in respect thereof.

The explanation of the VAT implications of providing and receiving short-term insurance services includes –

- how and when VAT must be accounted for on transactions and payments;
- the rules regarding the classification of supplies and the issuing of tax invoices; and
- whether output tax must be declared and input tax may be deducted on premiums and other payments associated with insurance contracts.

- **Supplies made by brokers, agents and other intermediaries (agents)**

In the insurance business, agents are often involved in the conclusion of the transaction and the maintenance of the policy. As these agents play an important role in the insurance industry, the guide also deals with the VAT consequences of persons who act as agents and clarifies, amongst others –

- whether these agents are liable to register and account for VAT in respect of the receipt of premiums, commissions, fees and other types of income received;
- whether these agents are regarded as employees or independent contractors; and
- the calculation of commissions.

- **Deemed supplies arising from indemnity payments and third party transactions**

An indemnity payment made under a contract of insurance would not normally be considered to be payment for a supply of goods or services. However, the VAT Act specifically deems such a payment to be in respect of a taxable supply of services made by the insured or cedent to the insurer or reinsurer (subject to a few exceptions). There are also a number of different ways in which insurance claims can be settled. There is also the matter of excess payments to consider. The guide will therefore discuss these different methods to enable vendors to establish whether certain events will trigger a liability for output tax or a right to deduct input tax or any other deduction.

1.3 Approach of the guide

The approach of this guide in dealing with the topics mentioned in **1.2** is set out below.

Chapter 1 – Sets out the policy framework which governs the VAT treatment of insurance in general. It also describes the scope of topics concerning short-term insurance transactions that will be covered in the guide and the approach adopted.

Chapter 2 – Explores some of the principles which underpin the law of insurance in South Africa and the ordinary meaning of the term “insurance”. Included, is a description of what insurance is all about and a discussion of some of the differences between short-term and long-term insurance. This chapter is important in coming to terms with the main principles of insurance law so that the VAT implications of certain insurance-related transactions explained later in the guide can be understood.

Chapter 3 – Introduces the reader to the most important VAT concepts, terms and definitions mentioned in the guide so that the VAT treatment of supplies which are explained in later chapters can be understood. Key points addressed in this chapter include an explanation of the terms “enterprise” and “financial services” in the context of insurance, as well as the meaning of the term “insurance” which is specifically defined for VAT purposes and is wider than the ordinary meaning. The chapter also explains the difference between taxable and non-taxable supplies which is fundamental in establishing whether output tax must be declared and input tax may be deducted.

Chapter 4 – Provides a brief overview of the legal concepts “agent” and “principal”. This is important as the VAT consequences of a transaction cannot be determined until the contractual relationship between the parties is established. These concepts are particularly important with regard to supplies of insurance as agents, brokers and other intermediaries play an important role in the insurance industry in writing and maintaining policies of insurance and providing auxiliary services which are related to the supply of insurance.

Chapter 5 – Deals with how VAT should be accounted for in respect of the different types of supplies made by insurers and intermediaries including the timing rules. The chapter sets out the general rules with regard to classifying supplies, record-keeping, invoicing and documentation required.

Chapter 6 – Focuses on the VAT treatment of specific taxable supplies made by insurers and intermediaries in the short-term insurance industry as well as allowable deductions in respect of these supplies. It discusses the VAT treatment of premium income which may be paid directly to the insurer or collected via intermediaries as well as commissions and fees charged for other types of supplies which are typically found in the insurance industry. Imported services are also dealt with in this chapter.

Chapter 7 – This chapter focuses on the VAT implications of settling claims and the different ways in which this can be done. The most important aspects include how to deal with input tax from the insurer’s perspective when making trade payments and indemnity payments. From the insured’s perspective, the most important aspects include the VAT treatment of the deemed supply which may arise as a result of receiving an indemnity payment, as well as the VAT treatment of excess payments.

Chapter 8 – Deals exclusively with reinsurance and explains the VAT treatment of distinctive aspects of reinsurance, including time of supply, tax invoices, cedent commission, indemnity payments and recoveries.

Chapter 2

What is insurance?

2.1 Legal principles of insurance

Very few reported cases or legal principles were established until the landmark English contract law case of *Carter v Boehm* in 1766, in which the duty of utmost good faith (*uberrimae fidei*) in insurance contracts was established. The judge in *Carter v Boehm* stated as follows regarding this principle:

“Insurance is a contract based upon speculation. The special facts, upon which the contingent chance is to be computed, lie most commonly in the knowledge of the insured only; the underwriter trusts to his representation and proceeds upon the confidence that he does not keep back any circumstance in his knowledge, to mislead the underwriter into a belief that the circumstance does not exist, and to induce him to estimate the risque as if it did not exist. Good faith forbids either party by concealing what he privately knows, to draw the other into a bargain from his ignorance of that fact, and his believing the contrary.”

In addition to the duty to disclose information and generally to act in utmost good faith, other legal principles which are unique to the law of insurance also developed over time. The main legal principles of insurance which were derived mainly from English contract law are:

- Indemnity;
- Insurable interest;
- Duty of disclosure;
- Average;
- Contribution;
- Subrogation; and
- Proximate cause.

More recently, the Supreme Court of South Africa stated in *Mutual and Federal Insurance Company Ltd v The Municipality of Oudtshoorn* (1984) that in our law of insurance there is no need for *uberrimae fides* (utmost good faith) as *bona fides* (good faith) already forms part of contract requirements.

These principles apply in addition to the general principles of the law of contract. More information on these principles as well as other insurance related terminology can be found in **Annexure D** and in the **Glossary: Part 2 – Selected insurance terms**.⁴ The terms and phrases in the **Glossary** are not agreed definitions which have a universal meaning, but are intended merely to provide the reader with a general understanding of insurance terminology which is used in the industry and in this guide.

⁴ These terms have been compiled from a number of sources, but are mainly derived from the information available on the Insurance Gateway website www.insurancegateway.co.za.

2.2 Ordinary meaning and general description of insurance

The term “insurance” has been defined as follows:

“The act or instance of insuring; a sum paid for this; a premium; a sum paid out as compensation for theft, damage, loss, etc., insurance policy; a measure taken to provide for a possible contingency.”⁵

The act, system, or business of providing financial protection for property, life, health, etc., against specified contingencies, such as death, loss, or damage, and involving payment of regular premiums in return for a policy guaranteeing such protection.”⁶

The term “insurance” can also be described as:

“A contract whereby an insurer promises to pay the insured a sum of money or some other benefit upon the happening of one or more uncertain events in exchange for the payment of a premium. There must be uncertainty as to whether the relevant event(s) may happen at all or, if they will occur (for example, death) as to their timing.”⁷

The purpose of insurance is to help businesses and individuals to reduce the financial impact of a risk occurring. While an insurance policy does not remove a risk, it provides the policyholder with some peace of mind that if the insured event should occur, the financial impact on the business or individual will be covered in full, or at least minimised.

A business that provides insurance (known as the “insurer”, or in the case of reinsurance, the “reinsurer”) agrees to take on the risk on behalf of another business or individual (known as the “insured”, or in the case of reinsurance, the “cedent”). It does so through the conclusion of an insurance contract (known as a “policy” or “reinsurance contract”). In the policy, the insurer will state what risks it has agreed to insure against, and how much it will pay if the risk happens so that the insured is restored to the same position as if the risk had not happened. The policy may also include a list of things that are not covered by the policy (known as “exclusions”). In return, the insurer receives a fee from the insured (known as the insurance “premium”).

The insurer collects premiums on a number of policies and pools these funds, which it then invests. Should there be any claim on a policy, the insurer will pay out on that claim from the pool of funds. The insurer is usually in business to make a profit and will be hoping that the total premiums it receives, together with any income it can make by investing the money, will exceed the total claims it has to pay out. It is also a common feature of policies that the insured will be required to contribute financially towards the cost of any claim made in terms of the policy (known as the “excess” amount). “Excess” is regarded as the self-insured or uninsured portion of a risk. Insurers also refer to “excess” as the “deductible” or “first amount payable”.

To be included in an insurance policy, a risk must be capable of being measured in monetary terms, there must be uncertainty as to whether the events concerned will occur, and the insured person must stand to lose something of appreciable value if the thing insured is lost, destroyed or damaged (known as the “insurable interest”).

⁵ The Concise Oxford Dictionary.

⁶ Collins English Dictionary (Desktop edition).

⁷ Lloyd's glossary of insurance-related terms www.lloyds.com/Common/Help/Glossary?page=7.

The insurer will look at all the circumstances surrounding a risk before deciding whether or not to provide insurance cover against it. This process is called “underwriting. This also involves an assessment of the extent to which a particular cause leading to the loss is covered by the policy (known as the “proximate cause”).⁸

From the above, the following characteristics of insurance can be identified:

- The insurer issues a policy to the insured which sets out the contractual conditions under which the risks relating to the insurable interest are covered, and specifies the premium payable.
- There must be an element of uncertainty as to *whether* the insured event will occur or not (or in the case of long-term insurance, the uncertainty relates to *when* the event will occur).
- The policy is based on the transfer of risk from the insured to the insurer. In the event of the risk occurring, the insurer indemnifies the insured, either by making an indemnity payment, or by replacing or repairing the things covered in the policy. The objective being to restore the insured party to the original financial position before the event occurred.
- The consideration in return for the insurance cover in terms of the policy is referred to as a “premium”. The term “premium” in the context of insurance means “the amount paid or payable, usually in regular instalments, for an insurance policy”.⁹ See 3.6 for the relevant time of supply rules.

Insurance business is basically broken down into two main fields, namely, long-term and short-term insurance. The term “assurance” is sometimes confused with “insurance”, and refers to cover that is taken out against something that is certain to happen. The term “assurance” therefore refers to life policies and falls within the field of long-term insurance which will not be discussed in any detail in this guide. The main differences between long-term and short-term insurance are explained in 2.3.

2.3 Long-term vs. short-term insurance

2.3.1 Long-term insurance

Section 1 of the LTI Act contains definitions which describe the ambit of long-term insurance as follows:

- **“Long-term insurance business”** means the business of providing or undertaking to provide policy benefits under long-term policies;
- **“long-term insurer”** means a person registered or deemed to be registered as a long-term insurer under this Act;
- **“long-term policy”** means an assistance policy, a disability policy, fund policy, health policy, life policy or sinking fund policy, or a contract comprising a combination of any of those policies; and includes a contract whereby any such contract is varied; and
- **“reinsurance policy”** means a reinsurance policy in respect of a long-term policy.”

⁸ Passage adapted from www.lloyds.com/Lloyds/About-us/What-we-do/What-is-insurance.

⁹ Collins English Dictionary (Desktop edition).

Long-term insurance (or “assurance”) provides both peace of mind and an investment, because at some time in the future the policy will pay out an amount for the benefit of the insured, or other nominated person. Long-term insurance refers to long-term policies such as life insurance or annuities and the cover relates to death, disablement or old age. The premium is payable for the full term of the contract, which is usually until the death of the insured or a specified future date. Long-term insurance policies usually have a specified term so there is no annual renewal involved, but as the policies usually have an investment component, it cannot be terminated without fairly severe financial consequences for the insured. The supply of long-term insurance and reinsurance written under the LTI Act, being financial services¹⁰ is exempt for VAT purposes.

Examples of long-term insurance:

- Whole or universal life insurance policy. (Provides for payment, upon the death of the insured, of a sum of money to be paid into the insured's estate or to a nominated beneficiary.)
- Retirement annuity fund and endowment policies. (Investment-type policies which pay a lump sum or income stream to the insured upon maturity and may also include cover for death and disability.)
- Funeral policy. (Covers the costs of funerals and burial of the insured or that person's spouse or family.)
- Health policy. (Examples include medical aid or hospital plans to cover medical costs.)
- Accidental death and disability policy. (Covers the death or disability of the insured resulting from the insured being involved in an accident.)

2.3.2 Short-term insurance

Section 1 of the STI Act contains definitions which describe the ambit of short-term insurance as follows:

- **“short-term insurance business”** means the business of providing or undertaking to provide policy benefits under short-term policies;
- **“short-term insurer”** means a person registered or deemed to be registered as a short-term insurer under this Act;
- **“short-term policy”** means an engineering policy, guarantee policy, liability policy, miscellaneous policy, motor policy, accident and health policy, property policy or transportation policy or a contract comprising a combination of any of those policies; and includes a contract whereby any such contract is renewed or varied; and
- **“short-term reinsurance policy”** means a reinsurance policy in respect of a short-term policy.”

Short-term insurance cover relates to loss, damage and liabilities in relation to property and possessions by means of theft, fire or other means of destruction or dispossession. This is referred to as “indemnity insurance”. Premiums may be paid monthly or on an annual basis. Typically, short-term insurance is for a period of one year and is renewable annually at the option of the insured. It can also be for an unspecified (indefinite) period.

¹⁰ Section 12(1) read with section 2(1)(i) of the VAT Act.

Short-term policies do not pay out any investment component at the end of the contract, but may include clauses which provide cover in respect of personal accident, third party liability claims and medical insurance. This is referred to as “non-indemnity insurance”.

The inclusion of a non-indemnity clause in a short-term policy will not affect the VAT treatment of the premium payable or the compensation / indemnity payout made in terms of the policy. The supply of short-term insurance written under the STI Act is a taxable supply for VAT purposes.

Examples of short-term insurance:

- Homeowner's insurance policy. (Cover for the actual building and fixtures.)
- Household insurance policy or all risks policy. (Covering loss, damage or destruction relating to movable contents of a home.)
- Fire policy. (Insures against damage or destruction caused by fire, lightning or explosion.)
- Comprehensive motor vehicle policy. (Covers loss of or damage to an insured vehicle and liability of the insured for damage to property of a third party arising from an accident.)
- Credit-guarantee insurance (Safeguards a business against loss resulting from the supply of goods or services on credit in the event that the customer fails to pay.)
- Marine and aviation insurance, including hull insurance and stock throughput insurance policies.
- Travel insurance policies.

2.3.3 Conclusion and summary

From the above, it is evident that whilst there may be some overlaps, the main difference between long-term and short-term insurance is the type of risks covered. Although the definitions in the LTI and STI Acts do not provide absolute certainty from a VAT perspective, the distinction between the different types of policies should be clear in most cases. Besides the fact that each type of business is covered by a different Act, the distinction is important for the purposes of this guide because only consideration for supplies, (for example, premiums and indemnity / compensation payments) made in terms of short-term insurance policies attract VAT.

2.4 Cross-border short-term insurance

In addition to local short-term insurance, such as car and household insurance, a short-term insurer can also underwrite specialised insurance policies which provide cross-border insurance cover. These include marine, aviation, hull and travel insurance which are discussed below.

2.4.1 Marine and aviation insurance

Marine and aviation insurance policies provide cover against loss, damage or destruction of cargo, freight, merchandise or means of transportation (for example the ship or truck transporting the cargo) whether on land, sea or air. There are various types of insurance policies covering these different risks, including stock throughput, aviation and marine cargo policies.

Marine policies can be underwritten on an annual basis or based on single voyage declarations. In the case of annual policies, the insured pays an annual premium based on the estimated value of goods to be exported or imported during the next twelve months. Once that period has expired, the actual value of goods exported or imported is compared to the estimate—and an adjustment is made for the difference. In the case of policies linked to single voyage declarations, the insurance premium is calculated based on the value of the goods that are exported.

Marine and aviation insurance can be domestic, inbound or outbound. Domestic marine and aviation insurance only relates to goods in South Africa and is therefore not regarded as cross-border short-term insurance. Inbound means that the goods are insured from a place outside South Africa to a place in South Africa whereas outbound insurance covers goods moving from South Africa to a place outside South Africa. Outbound insurance can also cover goods transported from a place outside South Africa to another destination outside South Africa as part of an international voyage. The insurance policy can also provide cover while the goods are stored before or after being transported, including storage at a central warehouse.

2.4.2 Hull insurance

Hull insurance policies provide cover against loss or damage to an aircraft, ship or other air and water borne craft. The insurance policy generally stipulates in which geographical areas cover will be provided and may also include certain limitations, for example, that the ship will not be covered if it docks in a specified country or region. The insurer relies on the warranty given by the insured that the insured ship or aircraft will only be used in the specified areas. The insurer will generally not know the location of the insured goods until a claim is submitted. Once a claim is submitted, the insured needs to prove that the conditions of the policy, including the location of the goods, were met before the claim can be settled.

2.4.3 Stock throughput insurance

Stock throughput policies are designed for companies that import, distribute, or export merchandise. The policy provides cover for all moveable goods (inventory) that are the subject of the insured's trade, including raw materials, semi-finished, and finished products. The goods are covered at all times whether in transit, undergoing process or in storage at owned or third party premises. Damage caused during the manufacturing process is, however, not covered under a stock throughput policy, but can be covered under another type of short-term insurance policy.

Purchasing a separate stock throughput policy rather than basic transit coverage is intended to provide seamless coverage of goods and more control of inventory risks throughout the entire supply chain, from the supplier or point of origin through the goods' final destination.

2.4.4 Travel insurance

Travel insurance policies generally provide for insurance cover whilst the insured is travelling and can include medical cover as well as cover for the insured's possessions and money. In the international context, there are two main types of travel insurance, namely inbound and outbound insurance. From a South African perspective, outbound travel policies provide insurance cover for a person travelling from South Africa to another country, as well as the return journey. Inbound travel policies provide insurance cover for a person travelling from a foreign country to South Africa and returning to a place outside South Africa. Insurers view the supply of insurance as a single supply which provides cover for the whole trip or voyage, including periods during which the insured is not being transported, for example while the insured is staying in a hotel. See **5.3.2**, **6.2.1** and **Annexure C**.

2.5 Reinsurance and retrocession

Reinsurance is an extension of the concept of insurance in that it passes on part of the risk for which the original insurer is liable. Due to the size and complexity of some risks, some insurers take out their own, additional insurance. When insurers insure a risk with another insurer, it is called reinsurance. Reinsurers can also insure their risk with another reinsurer in which case it is known as retrocession. Reinsurance is dealt with in more detail in **Chapter 8**.

Chapter 3

VAT concepts, definitions and terminology

3.1 Enterprise

3.1.1 General

The term “*enterprise*” is one of the tests for determining whether a person is liable to be registered for VAT purposes in the Republic. A person is generally considered to be carrying on an enterprise if all of the following requirements are met:

- An enterprise or activity must be carried on continuously or regularly by a person in the Republic or partly in the Republic.
- In the course of the enterprise or activity, goods or services must be supplied to another person.
- There must be a consideration charged for the goods or services supplied.

A person that conducts an enterprise and the value of taxable supplies made by that person in any 12-month period exceeds, or is likely (as a result of a contractual obligation in writing) to exceed the compulsory VAT registration threshold of R1 million, is obliged to register for VAT. In cases where the value of taxable supplies is less than the compulsory VAT registration threshold, but more than R50 000, a person may apply for voluntary registration. There are also specific instances¹¹ where a person can apply for voluntary registration if the R50 000 threshold is not reached.

3.1.2 Continuously or regularly

The definition also contemplates that the enterprise activity is carried on all the time (continuously), or it must be carried on at reasonably short intervals (regularly). “Continuously” is generally interpreted as ongoing, that is, the duration of the activity has neither ceased in a permanent sense, nor has it been interrupted in a substantial way. The term “regular” refers to an activity that takes place repeatedly. Therefore, an activity can be “regular” if it is repeated at reasonably fixed intervals taking into consideration the type of supply and the time taken to complete the activities associated with making the supply.

3.1.3 Non-enterprise activities

Specifically excluded from the definition of “enterprise” is any activity that involves the making of exempt supplies.¹² A person that only makes exempt supplies will not be able to register for VAT nor deduct input tax on expenses incurred to make the exempt supplies. Similarly, if a person is registered for VAT in respect of a taxable activity and also conducts an exempt activity, output tax cannot be charged on the supplies made in the course of carrying on the exempt activity. In such cases, input tax is only allowed to the extent that any expenses incurred on any goods or services acquired are for the purposes of making taxable supplies, or if it is for mixed purposes (both taxable and non-taxable purposes). The VAT on the allowable portion must be determined by applying the default method of apportionment (that is, the turnover-based method).¹³ The vendor may not use another apportionment

¹¹ Section 23(3)(b)(ii) read with Regulation 447 and section 23(3)(d) read with Regulation 446. (GG 38836 of 29 May 2015).

¹² Refer to section 12.

¹³ For more details on apportionment of input tax, refer to Chapter 8 of the *VAT 404 – Guide for Vendors* and Binding General Ruling (VAT) 16.

method unless the Commissioner has authorised the use of that method in a VAT ruling or VAT class ruling.

The writing of local long-term insurance business is a “financial service” and an exempt supply which constitutes a non-enterprise activity. Commissions for writing long-term insurance business do not fall within “financial services” as defined, and will be subject to VAT at the standard rate (unless the zero rate applies under section 11). Similarly, activities conducted in order to earn investment income in the form of dividends which might be received in the course of carrying on insurance business will also be non-enterprise activities. These payments are sometimes referred to as “out of scope” receipts.

Insurance supplied by the Road Accident Fund (RAF) is another example of a non-taxable supply. The RAF is a State insurer which was set up under the Road Accident Fund Act 56 of 1996 to provide compulsory third party liability insurance to motorists for bodily injury. The “premiums” are paid *via* a levy on fuel purchases such as petrol and diesel. As the RAF is a public authority, its activities are out of scope for VAT purposes and it is not registered as a VAT vendor and does not charge VAT on its premiums. Any claims paid by the RAF to a person will not attract VAT.

3.1.4 Lloyd's of London

Insurance business underwritten by Underwriting Members of Lloyd's of London (Lloyd's) is regarded as the carrying on of an enterprise in the Republic. This applies to the extent that Lloyd's correspondents conclude short-term insurance contracts in South Africa (known as “coverholder business”). Short-term premiums paid in this regard will therefore attract VAT in the same manner as any other supply of short-term insurance in the Republic. Any indemnity payments made in terms of coverholder business contracts will also potentially give rise to a deemed supply and a liability to account for output tax in the hands of the insured under section 8(8).

Lloyd's contracts concluded outside of South Africa which involves the placement of risk by independent intermediaries (known as “open market correspondents”) directly to a Lloyd's broker in London constitutes non-taxable (out of scope) supplies. The insurer will therefore not be liable to levy output tax on the supply of insurance under these policies. Premiums paid by a person in the Republic under an open market business policy may, however, qualify as consideration for taxable “imported services” if it meets the requirements. (See 6.7.)

3.1.5 Self-insurance

The term “self-insurance” refers to a situation where a person may find that insuring a specific risk is too expensive. To mitigate the risk, a person may decide to self-insure by setting up a fund from which losses will be paid. Sometimes very large risks will be insured and smaller losses carried by the business itself, or will be reflected in the acceptance of a higher excess amount in terms of the policy. This form of self-insurance does not involve a supply to any other person and will therefore not constitute an enterprise activity.

Another form of self-insurance is where a company sets up its own insurance company (a so-called “captive insurance company”) to cover losses of the company. Alternatively, the head office or holding company of a group of companies could assume the risk in return for the payment of a premium by its subsidiaries. When self-insurance schemes of this nature are carried on, this will constitute the supply of “insurance”¹⁴ to another person which will be an enterprise activity. Any short-term premiums payable for this type of insurance cover will

¹⁴ As defined in section 1(1) – refer also to 3.8.

consequently attract VAT according to the normal VAT rules and any indemnity payments made in terms of those contractual arrangements will potentially give rise to a deemed taxable supply as envisaged in section 8(8).

3.1.6 Registration of insurers with the Financial Services Board (FSB)

Subject to a few exceptions, a person must be registered with the FSB and be approved as a “short-term insurer” or a “long-term insurer” under the STI or LTI Acts to be able to conduct insurance business legally in South Africa. A person may, however, supply “insurance” from a VAT perspective without being regarded as a “short-term insurer” or a “long-term insurer”. This applies for example where a transporter contractually guarantees the owner of the transported goods against loss or damage whilst the goods are being transported.

A direct insurer may not register with the FSB to conduct both short-term and long-term insurance business under the same legal entity, except in the case of reinsurers. Each type of insurance must therefore be conducted under separate registrations under the relevant Acts. From a VAT perspective, if a person conducts short-term insurance business in South Africa without being registered or approved by the FSB, and the premiums received or receivable from that activity are in excess of the VAT registration threshold, there is a liability to register and account for VAT. This rule applies despite the fact that the activities may be unlawful.

3.2 Supply and taxable supply

The term “supply” is defined very broadly and includes all forms of supply and any derivative of the term, irrespective of where the supply is effected. The term includes performance in terms of a sale, rental agreement, instalment credit agreement or barter transaction as well as supplies which are made voluntarily or by operation of law. Section 8 also provides for certain “deemed supplies”. This provision clarifies, amongst other things, whether certain events or transactions are regarded as being included or excluded from the meaning of “supply”. For example, the receipt of an indemnity payment by the insured in settlement of an insurance claim under a short-term insurance contract would fall outside the scope of the VAT Act if it were not for section 8(8) which deems a taxable supply to take place in certain circumstances.

Supplies can be classified into two main types, namely taxable supplies and non-taxable supplies.

3.2.1 Taxable supplies

A taxable supply is any supply (including a deemed supply) of goods or services made by a vendor in the course or furtherance of an enterprise, which is chargeable with VAT under the Act. Taxable supplies, in turn, are divided into standard-rated supplies which attract VAT at the standard rate (currently 14%) and zero-rated supplies which attract VAT at the zero rate (0%).

3.2.2 Non-taxable supplies

A non-taxable supply is a supply on which no VAT is charged under the Act. There are two types of non-taxable supplies, namely exempt supplies and out of scope supplies. Section 12 contains a list of specific types of supplies of goods and services which are exempt. Examples include the supply of financial services (such as long-term insurance), transport of fare-paying passengers by road or rail, the rental of a dwelling and the supply of certain educational services. Supplies made by persons who are not vendors, and supplies

by vendors not made in the course or furtherance of an enterprise constitute non-taxable supplies which fall outside the scope of the Act.

For example, the *ad-hoc* supply of short-term insurance by a non-resident insurer who is not a vendor to a person in the Republic is an out of scope (non-taxable) supply.¹⁵ Income earned from activities which do not involve a supply to any other person is also non-taxable income.

Although the provision of long-term insurance will usually constitute an exempt financial service, most long-term insurers will also be registered for VAT to the extent that they make taxable supplies. For example if a reinsurer provides both long-term and short-term reinsurance to residents, it will only be making taxable supplies to the extent that it writes short-term reinsurance business. Similarly, if a long-term insurer owns an office block where the offices are rented to businesses, it will be making taxable supplies to the extent that it carries on the letting activity.

3.3 Goods, fixed property and second-hand goods

The term “goods” includes corporeal movable things, fixed property and any real right in such thing or fixed property. The definition basically refers to any tangible property and any real right in such tangible property, but excludes the supply of services and money.

“Fixed property”, in turn, is defined to mean –

- land, including any improvements permanently affixed thereto;
- any sectional title unit;
- any share in a share block company which confers a right to or an interest in the use of immovable property;
- any “time-sharing interest” as defined in section 1 of the Property Time-Sharing Control Act 75 of 1983; and
- any real right in any of the above.

The term “second-hand goods” includes goods which were previously owned and used. As the term “goods” also includes fixed property, if that property has been previously owned and used, it may also constitute second-hand goods. It is necessary to determine whether goods are second-hand because if such goods are acquired by a vendor under a non-taxable supply for the purposes of making taxable supplies, input tax may be deducted on the acquisition. There are however certain goods such as animals, gold and mining rights that are specifically excluded from the definition of “second-hand goods”.

3.4 Services and imported services

The term “services” is defined to mean anything done or to be done, resulting in a definition of “wide inclusion”. Therefore, anything that does not constitute “goods” or “money” may be “services”. The supply of short-term insurance comprises a taxable supply of services if supplied by a vendor.

¹⁵ Refer to 6.7.

The term “imported services” is defined to mean a supply of services that is made by a supplier (who is resident or carries on business outside the Republic) to a recipient who is a resident of the Republic, to the extent that such services are used or consumed in the Republic for non-taxable purposes. Section 7(1)(c) imposes VAT on the supply of imported services under these circumstances. (See 6.7 for more details in this regard.)

3.5 Consideration

The term “*consideration*” in its simplest form means anything that is received in return for the supply of goods or services. It includes, for example:

- A cash payment in respect of the purchase price of goods;
- A debit order payment of a policy premium;
- Commissions earned by agents for concluding contracts and collecting premiums;
- Any barter transaction in terms of which there is an exchange of goods, exchange of services, or any combination thereof, (including any payment in money to account for any differences in the value of goods or services exchanged). In such cases, a value must be attributed to each component of the consideration and aggregated to determine the final VAT-inclusive amount; and
- The amount of any indemnity payment received by the insured in certain circumstances.¹⁶

Some other important features of “consideration” are as follows:

- The term refers to the amount paid for a supply. It does not determine whether the amount received is taxable or not.
- It is a VAT-inclusive concept when the term is used with reference to a taxable supply. VAT is therefore regarded as being included in the payment, whether the parties have regarded it as being inclusive or not. The same rule applies in respect of any part-payment of the consideration.
- The term includes pre-payments for supplies as well as any past payments in the form of instalments, current payments, or payments which are still to be made in the future in respect of any taxable supply.
- Consideration can be received from a third party on behalf of the recipient or beneficiary, or payment of consideration can be made to a third party on behalf of the recipient or beneficiary.

Specifically excluded from the ambit of consideration is a donation made to an association not for gain. Also, a “deposit” payment whether refundable or not, given in respect of a supply of goods or services is not regarded as payment made for the supply unless and until the supplier applies the deposit as consideration for the supply or the deposit is forfeited.

¹⁶ Refer to section 8(8).

3.6 Time of supply

The purpose of the time of supply rules is to establish the date when a supply of goods or services is regarded as being made for VAT purposes. The time of supply therefore establishes the date that the supplier is required to declare the VAT charged on any supply made, and the date that the recipient may be permitted to deduct input tax on goods or services acquired. The output tax and input tax is declared and deducted by the vendor on a VAT 201 return at the end of the applicable tax period covering the time of supply (See **5.3**).

The general rule for the time of supply under section 9(1) is the date when an invoice is issued in respect of a supply or the date that payment of the consideration for the supply is received, whichever date is the earlier. However, some supplies have a special time of supply rule which is set out in section 9.

The parties to an insurance agreement can agree that either no insurance contract will come into being or that the insurer will not be liable to indemnify the insured until a premium is paid.¹⁷ A short-term insurance policy document and a renewal notice will therefore not create an obligation for the insurer to supply any service, or for the insured to make payment in respect of any supply until (and to the extent) the premium is paid. As a result, the time of supply is not triggered by the issuing of the policy document or any renewal notice, but only upon receipt of the premium by the insurer or its intermediary.

For information on the time of supply for reinsurance, see **8.2**.

3.7 Value of supply

The general rule for the value of a supply is that it is equal to the price charged for the supply of goods or services less the VAT included in the price. The value of the supply of goods or services is therefore an amount that excludes VAT. The amount that includes VAT is referred to as “*consideration*”. The calculation of the value of supply and the consideration (including standard-rated VAT charged at 14%) can be illustrated by using the formula:

$$\text{VALUE} + \text{VAT} = \text{CONSIDERATION}$$

Therefore

$$\text{CONSIDERATION} - \text{VAT} = \text{VALUE}$$

There are also special rules which may apply in certain cases for determining the value of the supply or the consideration. For example, where the supplier and the recipient in a transaction are related (connected persons) and the supply is made for no (or below open market value) consideration or the consideration is not determined at the time of the supply, the value of the supply is deemed to be the open market value of the supply.¹⁸ The value of supply rules are set out in section 10.

See the *VAT 404 – Guide for Vendors* for more details on the special time and value of supply rules.

¹⁷ Reinecke, MFB., Van der Merwe, S., Van Niekerk, JP., Havenga, P., 2002, *General Principles of Insurance Law*, LexisNexis, Durban.

¹⁸ Section 10(4).

3.8 Insurance

From the description of insurance and the principles of insurance as discussed in **Chapter 2**, one can get a general sense of what insurance is, and how it works. However, the term “insurance” is also specifically defined for VAT purposes. In order to apply the VAT law correctly, it is necessary to have a proper understanding of the term as defined in the VAT Act as explained below.

Section 1(1) defines “insurance” to mean –

“[i]nsurance or guarantee against loss, damage, injury or risk of any kind whatever, whether pursuant to any contract or law, and includes reinsurance; and “contract of insurance” includes a policy of insurance, an insurance cover, and a renewal of a contract of insurance: Provided that nothing in this definition shall apply to any insurance specified in section 2”.

This definition can be broken down into four main parts as follows:

1. “*Insurance or guarantee against loss, damage, injury or risk of any kind whatever, whether pursuant to any contract or law...*” This statement aligns with the ordinary meaning of insurance as discussed in **2.2**. However, it goes further in that it is not limited to persons (insurers) who are supplying the kind of insurance services which require them to be registered with the FSB. All that is required is for a contract to exist between the parties to transfer the risk from one party to the other in return for the payment of a premium or an obligation in law to cover against loss, damage or any other risk.

Under the STI Act, a guarantee against loss would include a “guarantee policy”, as it is specifically mentioned in the definition of “short-term insurance policy” as defined in section 1 of the STI Act. A “guarantee policy” is further defined in the STI Act to mean –

“a contract in terms of which a person, other than a bank, in return for a premium, undertakes to provide policy benefits if an event, contemplated in the policy as a risk relating to the failure of a person to discharge an obligation, occurs; and includes a reinsurance policy in respect of such a policy”.

2. The second part “... and includes reinsurance...” also aligns with the ordinary meaning and makes the point that “reinsurance” is included within the ambit of the meaning of “insurance”. See **Chapter 8** for more information on reinsurance.
3. The third part “...and ‘contract of insurance’ includes a policy of insurance, an insurance cover, and a renewal of a contract of insurance...” includes a further definition of a “contract of insurance” embedded within the definition of “insurance”. This part clarifies that a policy of insurance, insurance cover and a renewal of a contract of insurance are all included within the ambit of the defined meaning of the term “insurance”. Further, the use of the word “includes” means that the definition is not limited to the insurance cover and contracts mentioned in the definition, but may include other types of contracts and arrangements which have not been specifically mentioned.
4. Lastly, the definition includes a proviso which has the effect of specifically excluding any insurance which is regarded as “financial services” under section 2, for example long-term insurance.

In short, the definition of the term “insurance” in section 1(1) is broader than the ordinary meaning of the term “insurance” as discussed in **Chapter 2** because it includes all contracts, policies or arrangements where risk is transferred from one person to another in return for the payment of a premium or other consideration but excludes any insurance and reinsurance referred to in section 2.

3.9 Financial services

The VAT Act defines the concept “financial services” in section 2 which lists a number of activities which are deemed to be financial services for VAT purposes. The supply of financial services is generally exempt from VAT under section 12(a), but the supply of certain financial services qualify to be charged with VAT at the zero rate under section 11 (in which case the zero rate takes precedence over the exemption).

The following are some examples of financial services:

- The exchange of currency.
- The issue, allotment, drawing, acceptance, endorsement or transfer of ownership of a debt security.
- The issue, allotment or transfer of ownership of an equity security or a participatory security.
- The provision of credit.
- The provision or transfer of ownership of a long-term insurance policy or the provision of reinsurance in respect of any such policy (excluding any activity to the extent that it constitutes the management of a superannuation scheme).
- The provision or transfer of ownership, of an interest in a superannuation scheme.
- The buying or selling of any derivatives.

An important exception, however, is that any consideration payable in the form of a fee, commission, merchant's discount or similar charge, (not being a discounting cost), is generally¹⁹ not deemed to be consideration for a financial service. The definition is therefore intended to exempt, for example, interest and investment growth, but any fee or similar charge in respect of the underlying financial instrument is taxable.

For example, the following services are taxable under section 7(1)(a) and do not constitute exempt financial services:

- A document fee for providing credit in terms of an instalment credit agreement.
- Bank charges (excluding interest) for banking transactions such as debit orders, stop orders and deposits.
- Management fees charged for administering a pension fund.
- Debt collection fees.

Within the definition of “financial services”, certain other terms such as “debt security”, “derivative”, “equity security”, “long-term insurance policy”, “participatory security” and “superannuation scheme” (amongst others) are also defined.

¹⁹ One of the exceptions is long-term insurance in which case fees, commission and similar charges are also regarded as consideration for financial services.

In summary, the most important aspects that need to be noted from the definition of “financial services” in the context of an insurance business are as follows:

- The supply of financial services is exempt from VAT (unless the zero rate applies in certain circumstances);
- The supply of insurance services under a long-term insurance policy constitutes “financial services” and is generally exempt from VAT, whereas this is not the case for insurance services supplied under a policy of short-term insurance.
- Any fee based charges related to the provision of financial services such as advice and broker service, fees, document fees, administrative charges, commission or other charges in relation to short-term insurance policies are not exempt financial services. In the case of long-term insurance, the activity is not deemed to be a financial service to the extent that it includes the management of a superannuation scheme.
- Credit guarantee insurance does not constitute exempt financial services.

Chapter 4

Agent vs principal

4.1 Introduction

Before determining the VAT consequences of a transaction, it is necessary to establish the relationship between the parties. This is to determine if the vendor is acting as an agent on behalf of another person or as principal. Section 54 contains special provisions to deal with the VAT consequences arising from an agency relationship. This chapter aims to provide clarity regarding the VAT treatment of supplies where an agent / principal relationship exists and specific examples are provided to illustrate these concepts.

4.2 Legal principles of agency

In order to correctly apply the VAT legislation to the concept of agents, it is necessary to identify and understand the concept of an “agent” as understood in common law. An agency contract is an arrangement whereby one person (the agent) is authorised and required by another person (the principal) to contract or to negotiate a contract with a third person. In the course of representing the principal, the agent creates, alters or discharges legal obligations of a contractual nature between the principal and the third party. The agent therefore provides a service to the principal and normally charges a fee (generally referred to as “commission” or an “agency fee”) but does not acquire ownership of the goods or services supplied to or by the principal.

This agent / principal relationship may be expressly construed from the wording of a written agreement or contract concluded between the parties. Where a written agreement or contract does not exist, the onus of proof of an implied agency agreement is on the person who seeks to bind the principal in a contract. An understanding of the relationship between the parties is therefore a requirement in understanding the VAT treatment of supplies made by the parties. In essence, the difference is that the principal is ultimately responsible for the commercial risks associated with a transaction whilst the agent takes instruction from the principal and trades for the principal's account.

4.3 Application of agency principles

There are many role players in the insurance industry and it is important to be able to distinguish between them on the basis of their roles so that the VAT consequences of transactions can be determined. One of the difficulties in the insurance industry is that a large number of insurance brokers (also known as intermediaries) appear to act in a dual capacity as agent for both the insurer and the insured parties. The insurance brokers can also act on a principal to principal basis with both the insurer and the insured parties for other activities. In addition to the aforementioned role-players, some of the following parties may also be involved in the conclusion or administration of an insurance contract:

- Underwriting manager;
- Claims or policy administrator;
- Insurance broker;
- Sub-agent;
- Collecting agent; and

- Canvassing agent.

Agency principles are particularly important in the case of insurance as a significant amount of business is conducted through insurance brokers who often carry out a number of functions on behalf of insurers, for example:

- Invoicing;
- The collection of premiums;
- Handling and reporting of claims; and
- Acting as agents for certain supplies of insurance, for example, SASRIA policies.²⁰

4.3.1 Guidance on roles under the STI Act and FAIS Act²¹

The STI Act and FAIS Act contain a number of provisions which govern who may be regarded as an independent intermediary and how that person shall perform functions and charge for services rendered.

For example, the following definitions can be found in section 1 of the FAIS Act:

- **“intermediary service”** means, subject to subsection (3)(b), any act other than the furnishing of advice, performed by a person for or on behalf of a client or product supplier –
 - (a) the result of which is that a client may enter into, offers to enter into or enters into any transaction in respect of a financial product with a product supplier; or
 - (b) with a view to—
 - (i) buying, selling or otherwise dealing in (whether on a discretionary or non-discretionary basis), managing, administering, keeping in safe custody, maintaining or servicing a financial product purchased by a client from a product supplier or in which the client has invested;
 - (ii) collecting or accounting for premiums or other moneys payable by the client to a product supplier in respect of a financial product; or
 - (iii) receiving, submitting or processing the claims of a client against a product supplier;
- **“financial services provider”** means any person, other than a representative, who as a regular feature of the business of such person—
 - (a) furnishes advice; or
 - (b) furnishes advice and renders any intermediary service; or
 - (c) renders an intermediary service;
- **“representative”** means any person, including a person employed or mandated by such first-mentioned person, who renders a financial service to a client for or on behalf of a financial services provider, in terms of conditions of employment or any other mandate, but excludes a person rendering clerical, technical, administrative, legal, accounting or other service in a subsidiary or subordinate capacity, which service—
 - (a) does not require judgment on the part of the latter person; or
 - (b) does not lead a client to any specific transaction in respect of a financial product in response to general enquiries;

Section 1 of the STI Act defines **“Lloyd’s correspondent”** as a person who is approved by Lloyd’s and authorised by a Lloyd’s broker or Lloyd’s underwriter to act in the Republic as an agent for or on behalf of such broker or underwriter.

²⁰ SASRIA stands for the South African Special Risks Insurance Association. SASRIA policies constitute additional insurance for risks that other insurers are not prepared to cover.

²¹ Financial Advisory and Intermediary Services Act 37 of 2002.

Furthermore, under section 8(2) of the STI Act, there is a prohibition against any person rendering services as an independent intermediary in relation to a short-term policy unless –

- (a) short-term insurers are the only underwriters in terms of the short-term policy concerned;
- (b) such person is a Lloyd's correspondent and Lloyd's underwriters are the only underwriters in terms of the short-term policy concerned;
- (c) short-term insurers and Lloyd's underwriters through a Lloyd's correspondent are collectively the only underwriters in terms of the short-term policy concerned; or
- (d) such person does so with the approval of the Registrar.

The term “**insurance agent**” is not defined in the STI or FAIS Acts but is generally used to refer to a person providing intermediary services in respect of the products of a single nominated insurer. Such agent can be an employee of the insurer or an independent contractor.

4.2.2 Employee (“representative”) or independent contractor (“independent intermediary”)

In addition to being able to recognise when there is an agent / principal relationship, and who the agent represents, a further aspect is to be able to distinguish when a person is acting in the capacity of an independent intermediary (that is, as an agent), or as an employee of the insurer (where there is no agency contract) as this determines whether or not the commission received constitutes consideration for a taxable supply. The independent intermediary may need to register as a vendor if an enterprise is carried on and the VAT registration threshold is exceeded or expected to be exceeded. (See 3.1.) For example, an insurance broker is an independent intermediary if the person acts as an agent on behalf of an insurer in concluding insurance business on the insurer's behalf. In this instance, the insurer is the principal for the purposes of the supply. In return for writing the insurance business and maintaining the policy, the broker will earn a commission or brokerage fee.

Insurance brokers may also be involved in making other supplies to insurers and clients in which case fees may be charged separately from commission. For example, an insurance broker may enter into an agreement with an insurer to issue policies or settle claims on behalf of the insurer and to perform other services usually performed by the insurer. Such services are referred to as outsourced services for which the insurance broker charges outsourced service or binder fees. Insurance brokers also provide advice to their clients as well as other services that do not fall within the definition of “intermediary services” for which the insurance brokers charge advice or broker fees.

In instances where the insurance broker is a vendor, VAT must be charged on all forms of consideration received for providing services, whether in the form of a service fee, commission or other charge (subject to the zero-ratings and exemptions contained in sections 11 and 12). Insurance brokers, in their capacity as agents of the insurer will also be responsible to keep the prescribed records on the insurer's behalf as required by section 54(3) and discussed in 4.4. Insurance brokers may also appoint or act as sub-agents in certain instances.

On the other hand, a person known as an insurance agent may often be an employee of the insurer. The term “insurance agent” is however misleading as there is no legal contract of agency with the insurer (the employer) which allows that person to act as an independent intermediary. Insurance agents may be remunerated in the form of a fixed or variable salary, commission or in any other manner.

“Remuneration” paid by the insurer to its employee is not consideration for a taxable supply and will therefore not include any VAT component and the insurer will not be entitled to deduct any input tax thereon. Similarly, the employee will not be entitled or required to register for VAT as a vendor and to account for any output tax on the remuneration received.

Whether a person is an employee or an “independent contractor” will depend on the facts and circumstances of the case. Usually a person cannot be regarded as acting independently if the employer (the insurer) exercises substantial supervision and control over that person’s capacity to earn. The common law dominant impression test for establishing whether an employer and employee relationship exists in any particular case is conclusive as to whether an individual is an employee or independent contractor.

The rules pertaining to whether Pay-As-You-Earn (PAYE) must be deducted from any payments made to the person as set out in the Fourth Schedule to the Income Tax Act 58 of 1962 will also be a useful guideline. For more information in this regard please see Interpretation Note 17 (Issue 3) “Employees’ Tax: Independent Contractors” dated 31 March 2010.

4.2.3 SASRIA

Another example of the agency principle is a SASRIA policy which covers risks associated with riots, public disorder, labour disturbances, civil unrest, strikes and lockouts which are not covered by conventional policies. A SASRIA policy is therefore an optional add-on to a conventional policy already concluded between the insurer and the insured.

SASRIA works through a network of agents (insurers) and insurance brokers so that the person who is the primary insurer for the conventional policy acts as SASRIA’s agent in supplying the special risks cover as well as administering any claims in terms of that policy. It follows that the VAT on the premiums paid in terms of a SASRIA policy, must be declared as output tax by SASRIA (the principal) and not by the primary insurer (the agent).

The primary insurer that acts as the agent in this case may be entitled to a commission on writing the policy on SASRIA’s behalf. The primary insurer will therefore declare output tax on any commission received either directly from SASRIA, or through the deduction of any amount from the premium collected from the insured on SASRIA’s behalf. The primary insurer may also be entitled to a fee for administering any claims in regard to these policies and will therefore also charge VAT on any amount charged for this service. SASRIA, in turn, will be able to deduct input tax on the commission paid to the primary insurer as the expense is incurred in the course or furtherance of its enterprise of providing short-term special risks insurance.

The insured will, in turn, be able to deduct the VAT paid on the premiums for the primary insurance and the SASRIA insurance, provided that the correct documentation is held and the normal rules for deducting input tax have been met.

4.4 Tax invoices, credit notes and debit notes

The normal rule is that any tax invoice, credit note or debit note relating to a supply by, or to the agent, on the principal's behalf should contain the principal's particulars. However, the VAT Act provides that if an agent (being a vendor) makes a supply on behalf of another vendor (the principal), the agent may issue a tax invoice, credit note or debit note relating to that supply as if the supply had been made by the agent. In such instances, the agent's details may be reflected on the tax invoice, credit note or debit note and the principal may not also issue a tax invoice, credit or debit note in respect of that same supply.

The agent must maintain sufficient records so that the name, address and VAT registration number of the principal can be ascertained when a tax invoice, credit note or debit note has been issued by or to an agent in the circumstances described above. Refer also to **4.3**, **5.3.1** and **6.3**, BGR 14 and BGR 32.

In addition, the agent must, under section 54(3), issue a written statement to its principal within 21 days after the end of each month which contains the following information:

- A description of the services supplied; and
- Either –
 - the value of the supply, the amount of tax charged and the consideration for that supply; or
 - where the amount of tax charged is calculated by applying the tax fraction to the consideration, the consideration for the supply and either the amount of tax charged, or a statement that it includes a charge in respect of the tax and the rate at which the tax was charged.

4.4.1 Tax invoices issued to insureds

In the insurance industry, it is common practice not to issue invoices, debit and credit notes in respect of short-term insurance cover. The Commissioner however directed²² under sections 20(7)(a) and 21(5)(a) that the policy document issued by a short-term insurer in respect of insurance constitutes a tax invoice which need not contain the words “tax invoice”, “VAT invoice”, “invoice”, “debit note” or “credit note” provided that –

- the insurer retains proof that the insured paid premiums in accordance with the policy document;
- the policy document reflects all the other information as required by sections 20(4), 21(3)(a) or (b); and
- the document contains the following statement (or substantially similar wording):²³

“In terms of Binding General Ruling No.14, this document constitutes a tax invoice, debit note or credit note as contemplated in sections 20(7) and 21(5) of the VAT Act respectively.”

²² Paragraph 2.12 of BGR 14.

²³ Including the wording contained in paragraph 5.1.1 of the Industry ruling issued to the South African Insurance Association on 10 February 2014.

4.4.2 Tax invoices issued to insurers

In addition to concluding new business, brokers and intermediaries may carry on different functions on behalf of insurers such as collecting premiums and processing claims. In accordance with a decision²⁴ given by the Commissioner under section 20(7)(a) and 21(5)(a), the document (generally known as a bordereau) issued to the insurer by the insurance broker or intermediary in respect of any commission or fees for services is regarded as a tax invoice, credit note or debit note, as the case may be, and need not contain the words “tax invoice”, “VAT invoice”, “invoice”, “credit note” or “debit note”, (as the case may be) provided that the document complies with all the other requirements of section 20(4) and 21(3), whichever are applicable.

In the event that intermediaries also process and pay claims on behalf of insurers, the bordereau should also include the following information:

- In the case of trade payments, the VAT inclusive amount, together with a statement of the rate of VAT included, or the VAT exclusive amount, the VAT amount and the VAT inclusive amount of trade payments made;
- In the case of indemnity payments, the total amount of indemnity claims paid in cash or otherwise.

It should be noted, however, that the bordereau does not have a set format and might not contain sufficient information on its own. In such cases the bordereau should be accompanied by a separate document such as a commission statement containing any further details which may be necessary to meet the requirements of sections 20, 21 and 54(3).

Insurance brokers are required to issue separate tax invoices in respect of any other services supplied to an insurer, such as outsourced services, to the extent that these supplies are not reflected on the bordereau.

4.4.3 Recipient-created tax invoices, credit notes and debit notes

The manner in which the insurance industry operates, lends itself to “recipient-created invoicing” (also known as self-invoicing). Self-invoicing is a process in terms of which the recipient issues the required tax invoices and debit / credit notes for supplies instead of the supplier.²⁵ Insurers and brokers may apply self-invoicing as provided in *Binding General Ruling 15: Recipient-created tax invoices; credit and debit notes* (BGR 15) and paragraph 2.13. of BGR 14. As long as the conditions set out in paragraph 3.3 of BGR 15 are met, a specific ruling to apply self-invoicing procedures does not need to be obtained. According to BGR 14, the requirement to obtain a written agreement between the supplier and recipient of the services will be met if such agreement is contained in the bordereau or other agreement, that is, a separate document containing the agreement is not required.

BGR 15 grants approval to vendors to apply self-invoicing, inter alia, where the recipient determines the consideration for the supply of the goods or services. For more information, see paragraphs 2.12 and 2.13 of BGR 14 as well as BGR 15.

²⁴ Paragraph 2.13 of BGR 14.

²⁵ Refer to sections 20(2) and 21(4).

Chapter 5

Accounting for VAT

5.1 Introduction

The South African VAT is destination based. VAT is therefore paid on the supply of goods or services in South Africa by a vendor as well as on the importation of goods into South Africa by any person. VAT is presently levied at the standard rate of 14% on most supplies and importations, but there is a limited range of goods and services which are either exempt or subject to tax at the zero rate (for example, exports are taxed at 0% in line with the destination principle). The importation of services is only subject to VAT where the importer is not a vendor or where the services are imported for private, exempt, or other non-taxable purposes. Certain imports of goods or services are exempt from VAT.

In this Chapter we will have a look at the general factors that influence the amount of VAT that must be accounted for by a vendor. The focus will be in particular on identifying the different types of supplies and explaining the input tax and output tax implications for the parties. The settlement of claims by way of trade payments and indemnity payments by the insurer and the deemed supplies which may arise in the hands of the insured under section 8(8) will be dealt with separately in **Chapter 7**, whilst reinsurance related supplies are dealt with in **Chapter 8**.

5.2 The mechanics of VAT

The VAT system of taxation is based on a subtractive or credit-input method which allows the vendor to deduct the tax incurred on enterprise inputs (input tax) and other deductions from the tax collected on the supplies made by the enterprise (output tax). Input tax may be deducted subject to the retention of prescribed documentation (for example, tax invoices, debit notes and credit notes, bills of entry etc.) and may not be deducted if the expense was incurred for non-taxable purposes, for example, for the purposes of long-term insurance business. There are also some expenses upon which input tax is specifically denied, such as the acquisition of motor cars and entertainment. Further, since input tax may only be deducted to the extent that goods or services are acquired for taxable “enterprise” purposes, insurers who make both taxable and non-taxable supplies will have to apportion certain of their inputs which cannot be directly attributed to either taxable or non-taxable purposes.²⁶

A vendor must report to SARS at the end of every tax period on a VAT 201 return, where the input tax incurred and other deductions are offset against the output tax levied during the particular tax period and the balance is paid to SARS (usually by no later than the 25th day after the end of the tax period concerned, although e-Filers may pay on the last business day of that month if returns are submitted and payments are made *via* eFiling). Alternatively, if the input tax and other deductions for the tax period exceed the output tax, SARS will refund the vendor. The VAT collected by vendors is usually paid over to SARS every two months, but where the value of taxable supplies in a 12-month period exceeds R30 million, the VAT must be accounted for on a monthly basis.

²⁶ Refer to *Binding General Ruling (VAT) 16 “Standard Apportionment Method”* and paragraph 8.4 of the *VAT 404 – Guide for Vendors*.

Since most short-term insurers will fall into the latter category, for the purposes of this guide it will be assumed that the insurer must –

- account for VAT on a monthly basis;
- account for VAT on the invoice basis of accounting; and
- submit returns and make payment by electronic means (*via e-Filing*).

As mentioned in **3.6**, in the case of short-term insurance, the service is only deemed to be supplied to the extent that the relevant premium is received if no invoice is issued. The liability for the insurer to declare output tax on short-term policy premiums will therefore only arise once payment is received, either directly by the insurer or when the payment is received by the broker or collection agent. For all other supplies, the normal VAT rules will apply in regard to the declaration of output tax and input tax as explained in earlier chapters and in the *VAT 404 – Guide for Vendors*. This is based on the time and value of supply rules applicable to the supplies concerned, as well as the accounting basis (invoice or payments basis) and the tax period which applies to the insurer.

5.3 Application of VAT principles

5.3.1 General tax administration matters

Tax invoices and deduction of input tax

All vendors are, under section 20,²⁷ obliged to issue a tax invoice when the consideration for a taxable supply exceeds R50. See **4.4** for more information on tax invoices. Also, section 16(2) requires that vendors must retain tax invoices and certain other documents to substantiate any input tax or other deductions which are deducted from the output tax liability for any particular tax period.

Retention of records

As VAT is a self-assessment type of tax, a great deal of emphasis is placed on making sure that accurate and complete records of transactions are kept.

Section 55 does not contain a complete list of records relating to all vendors as this would be impractical. However, it prescribes that certain specific records must be kept to satisfy the Commissioner that the vendor has observed the requirements of the Act. Sections 29 and 30 of the TA Act also impose a duty on a person to retain certain records, books of account or other documents in a particular form and manner to comply with a tax Act. The requirements of both Acts must therefore be observed. Failure to retain proper records as required under either Act may trigger administrative non-compliance penalties under Chapter 15 of the TA Act.

The term “records” includes any document or information which a vendor may be required to have in order to justify or confirm, amongst other things, that –

- the value of standard rated, zero-rated and exempt supplies declared on the VAT 201 forms for past tax periods is correct;
- the correct amount of input tax (or other deductions allowed against the output tax liability) has been claimed, including tax invoices, bills of entry and other prescribed documents have been retained which indicate the amount of VAT which may be deducted;

²⁷ Refer to *Binding General Ruling 27: Application of sections 20(7) and 21(5)*.

- VAT at the zero rate was correctly charged on certain supplies of goods or services (or that VAT was not charged because the supply was exempt or out of scope for VAT purposes).

This means that all reasonable accounting documents and records for the particular type of business (or businesses) carried on, should be accessible to enable auditors to establish the nature, time and value of all taxable supplies and the importation of any goods or services. This includes information which assists in reconciling the accounting records and audited financial statements with the VAT returns submitted for at least the past five years from the date the returns were submitted. Details of any exempt supplies, other non-taxable activities, adjustments and any method of apportionment used should also be available.

See the *VAT 404 – Guide for Vendors* for more information as well as the *Short Guide on the TA Act, 2011* for more information on record-keeping and tax administration matters in general.

5.3.2 Output tax

Most of the supplies made by short-term insurers and intermediaries will generally attract VAT at the standard rate as the definition of “enterprise” is wide and not restricted only to the main business activity of insurance services. For example, if an insurer owns a commercial building which it rents to tenants as offices, it must charge VAT on the supply of the offices leased and short-term insurance for which premium income is received.

No output tax is declared on the supply of financial services²⁸ (such as the provision of long-term insurance), as the supply of financial services are generally exempt from VAT. However, certain other fee-based services in connection with the provision of the underlying financial service are subject to VAT at the standard rate. See **3.9**.

As the VAT calculation for any particular tax period depends on accurate record-keeping and documentation, due care should be taken to ensure that the different types of supplies are properly described, classified, and entered in the accounting records as either –

- standard-rated supplies;
- zero-rated supplies;
- non-taxable supplies, or receipts not in respect of any supply (exempt or out of scope); or
- not a receipt belonging to the insurer, but an amount received (or paid) as agent for another person.

Zero-rated supplies

Insurers and their agents and intermediaries should also take care to establish which supplies of insurance and associated services qualify for the zero rate. Not all intermediary services associated with zero-rated supplies of insurance qualify to be charged with VAT at the zero rate. Below is a summary of the most common zero-rating provisions relating to short-term insurance premiums:

- Section 11(2)(d) – insurance services in regard to the international transport of passengers and goods (including the arranging of that insurance).
- Section 11(2)(f) – insurance services provided directly in connection with fixed property (land and improvements) situated outside the Republic.

²⁸ As defined in section 2.

- Section 11(2)(g) – insurance services provided in certain circumstances which are directly in connection with –
 - goods (movable property) situated outside the Republic;
 - goods exported to foreign-going ships and aircraft;
 - certain goods temporarily imported for processing or repair before being exported again; and
 - foreign-going ships and aircraft that are temporarily in the Republic.

BGR 14 provides further details on the different kinds of insurance cover and the conditions under which those supplies will be subject to VAT at the zero rate. This includes international transport policies, hull and associated liability policies and stock throughput policies. The supply of international travel insurance may, subject to certain conditions, be zero-rated under section 11(2)(d). See 2.4.4, 6.2.1 and BGR XX for more information on the zero rating of international travel insurance.

With regard to zero-rated supplies, see *Interpretation Note 31 “Documentary Proof Required for the Zero-Rating of Goods and Services”* (IN 31) to ensure that the appropriate documents as prescribed have been obtained and retained as part of the accounting records. In instances where a declaration or confirmation is required to substantiate the supplier's entitlement to charge VAT at the zero rate on a supply, the supplier may accept the declaration in good faith. The declaration or confirmation can form part of the insurance policy or it may be a separate document.

In instances where the relevant documentation is not obtained within the prescribed period, certain output tax or input tax adjustments may be applicable.²⁹ See Chapters 6 and 12 of the *VAT 404 – Guide for Vendors* for more details in regard to zero-rated supplies, exports and the documentation required.

Exempt and out of scope supplies

Insurers should ensure that exempt or out of scope supplies are not incorrectly recorded as zero-rated supplies. A note should also be made in the records as to why no VAT was charged. For example, if an insurer wins a settlement in court when pursuing its subrogated rights under a contract of insurance due to a claim by the insured, the court documentation should be retained as part of the records to verify the non-taxable treatment of the amount received.

Similarly, it should also be clear from the records which sub-paragraph of section 12 applies in the case of any amount received in respect of an exempt supply. In particular, for vendors like reinsurers and long-term insurers that make a mixture of taxable and non-taxable supplies, the provisions of section 2 (financial services) must be read together with sections 11 and 12 to establish whether the supply is exempt or zero-rated. For example, the supply of long-term insurance to a South African resident is exempt from VAT but can qualify as a zero-rated supply in certain limited instances when the policy is concluded with a non-resident.

5.3.3 Input tax

Generally, the VAT charged by a vendor to another vendor on any goods or services acquired for the business will qualify as input tax in the hands of the recipient. However, it is

²⁹ Refer to BGR 14 regarding the records required for the application of the zero rate under section 11(2)(d) and the consequential adjustments which will be required in the event of the incorrect application of that provision.

important that input tax is only deducted insofar as the goods or services acquired are used for the purposes of making taxable supplies in the course or furtherance of the enterprise.

Brokers and intermediaries usually do not have to apportion their input tax as the commissions which they earn will constitute consideration for taxable supplies, whether they are in respect of short-term or long-term insurance policies. However, insurers sometimes make both taxable and non-taxable supplies and will be required to apportion the input tax when an expense is incurred for both taxable and non-taxable purposes. Before apportioning an expense, the first step is to determine if the expense can be directly attributed. Direct attribution means that the VAT expense must be attributed or allocated according to the intended purpose for which it will be used or consumed in the business.

The application of direct attribution means that the expense is incurred either –

- wholly for making taxable supplies, in which case input tax can be deducted in full; or
- wholly for making exempt supplies or for other non-taxable purposes, in which case no input tax can be deducted.

For example, if a VAT-inclusive expense is incurred exclusively for conducting long-term insurance business, no input tax may be deducted. This is because the expense is directly attributable to exempt supplies. It is only when the expense cannot be directly attributed because it relates to **both** taxable supplies and exempt supplies (or other non-taxable purposes), that the expense must be apportioned. Expenses which have to be apportioned are usually in the nature of general overheads which relate to all parts of the business.

Once it is clear that the expense must be apportioned, the next step is to calculate the proportion of input tax which may be deducted. This is referred to as the apportionment ratio and is expressed as a percentage. The vendor can then deduct input tax on the expenses which are incurred for both taxable and non-taxable purposes (also referred to as “mixed purposes”), but only to the extent that those expenses relate to making taxable supplies as determined in terms of the apportionment calculation. However, where the intended use relating to taxable supplies is 95% or more of the total intended use, the input tax may be deducted in full. The apportionment ratio must be determined by using an approved method so that only a fair and reasonable proportion is deducted as input tax.³⁰

The only approved method which may be used to apportion input tax without specific prior written approval from the Commissioner is the turnover-based method, provided the outcome is fair and reasonable. A record must be kept of how the apportionment percentage was calculated in terms of the turnover-based method, or if the Commissioner has approved a special method, the ruling should be kept as part of the records and should be available upon request. See Chapter 8 of the *VAT 404 – Guide for Vendors* and BGR 16 for more information on input tax and apportionment.

Example 1 – Determining the input tax apportionment percentage

Facts:

Reinsurer V's income of R100 million for the period is made up as follows:

- R60 million in short-term insurance premiums (standard rated). (a)
- R14 million in short-term insurance premiums (zero rated). (a)
- R10 million in long-term insurance premiums (zero-rated). (a)

³⁰ Refer to section 17(1).

- R10 million in long-term insurance premiums (exempt). (b)
- R2 million in interest earned on investments (exempt). (b)
- R4 million in dividends earned on investments (out of scope income not in respect of any supply). (c)

Result:

The extent of taxable supplies is calculated as follows:

$$y = \frac{a}{(a + b + c)} \times \frac{100}{1}$$

$$y = \frac{(R60 \text{ million} + R14 \text{ million} + (R10 \text{ million})^*)}{R84 \text{ million}^* + (R10 \text{ million} + R2 \text{ million}) + R4 \text{ million}} \times \frac{100}{1}$$

Therefore, Reinsurer V will be able to deduct **84%** of its general overhead expenses which cannot be directly attributed to either taxable or non-taxable purposes.

Sections 16(2)(a) to (e) specify the documentation which must be held by a vendor when deducting “input tax” under sections 16(3)(a) and (b) in respect of the acquisition of any goods or services, or on the importation of any goods into South Africa, for example –

- a tax invoice;³¹ or
- the prescribed documents under section 20(8) when second-hand goods are acquired, together with the proof of payment; or
- an import bill of entry together with proof of payment of the VAT on importation.

A vendor may deduct an amount under sections 16(3)(c) – (n) if the vendor is in possession of documentary proof, as prescribed by the Commissioner, at the time a return in respect of the deduction is furnished.

A vendor may, in respect of tax periods from 1 April 2016, under circumstances prescribed by the Commissioner, make a deduction based on alternative documentary proof acceptable to the Commissioner under section 16(2)(g).

³¹ Including a document issued under section 20(7) such as a bordereau as well as other documents referred to in 4.4.

Chapter 6

VAT treatment of specific supplies and imported services

6.1 Introduction

This chapter deals with the VAT treatment of specific supplies made by insurers and intermediaries within the short-term insurance industry as well as imported services. The general income streams are identified and the VAT treatment is discussed from both the supplier and recipient's perspective. It is also important to consider both the time and value of supply rules as this determines the tax period in which the VAT on a transaction must be accounted for. (See 3.6 and 3.7.) A supply may only be zero-rated if the supplier obtains and retains the relevant supporting documents listed in IN 31. In instances where a declaration or confirmation is required to substantiate the supplier's entitlement to charge VAT at the zero rate on a supply, the supplier may accept the declaration in good faith. The declaration or confirmation can form part of the insurance policy or it may be a separate document.

6.2 Insurance premiums

6.2.1 General

Short-term insurers charge insurance premiums as consideration for the supply of insurance cover under an insurance contract. The VAT treatment from the short-term insurer as well as the insured's perspective is discussed below.

(a) Short-term insurer

The short-term insurer is liable to account for output tax on the supply of short-term insurance. It is very important to determine the correct VAT rate (that is 14% or 0%) when accounting for output tax on these supplies. The supply of short-term insurance is usually subject to VAT at the standard rate of 14% unless one of the exceptions applies, in which case, the supply may be zero-rated. Some of these exceptions are dealt with below.

Insuring the international transport of goods

The supply of short-term insurance under inbound and outbound transport policies may be zero-rated under section 11(2)(d). This zero-rating provision also applies to insurance supplied while the insured goods are transported between places in South Africa if the transport service (including ancillary transport services) forms part of an international voyage. Ancillary transport services include the storage of transported goods or goods to be transported and therefore insurance cover provided while the insured goods are stored as part of an international voyage will also qualify for zero-rating. However, insurance cover provided whilst goods are stored in South Africa after being delivered to the final destination does not qualify for zero-rating. An example is when additional cover in the form of an elected static extension to a standard marine cargo policy is provided.

The supply of stock throughput insurance³² is regarded as international transport insurance to the extent that insurance cover is provided in respect of goods transported from an export country to South Africa (and *vice versa*) as part of an international voyage.

³² Refer to 2.4.3.

Stock throughput insurance cover provided whilst the insured goods are not transported as part of an international voyage (for example elected static cover) does not qualify for zero-rating under section 11(2)(d) and is therefore subject to VAT at the standard rate of 14% under section 7(1)(a).

Insurers that levy a single insurance premium which relates to both standard and zero-rated supplies of insurance are required to allocate the premium under section 8(15) to the various risk components used to determine the premium and apply the applicable VAT rate to each component.

Insurers must notify their intermediaries (and insureds, if applicable) of the allocation between the respective standard rated and zero rated portions of the single stock throughput premium. Any subsequent adjustment to the premium must be attributed to the respective standard rated and zero-rated portions using the same allocation based on the initial premium unless the insurer is able to make a more accurate calculation based on specific information relating to that adjustment.

Insuring passengers travelling internationally

The supply of short term insurance under an inbound or outbound travel policy may be zero-rated under section 11(2)(d) to the extent cover is provided whilst the insured is being transported from a place –

- outside South Africa to another place outside South Africa;
- in South Africa to a place in an export country; or
- in an export country to a place in South Africa.

It is acknowledged that there may be instances where the insured is not being transported as part of the international journey (for example while staying in a hotel) or where the insured is required to stop over as part of the international journey. The supply of travel insurance does not qualify for zero-rating under section 11(2)(d) to the extent the insured is not being transported. This creates a difficulty which is addressed by BGR 37.

According to BGR 37, international travel is defined to include stopovers *en route* to the insured's destination. Stopovers include a mandatory stop or delay which is part of a multi-staged international transport service supplied to the insured. Examples include where the insured needs to wait for a connecting flight or where flights are delayed and the insured is forced to stay overnight.

The intention is not to include any periods where the traveller stays in South Africa after entering the country for the first time, unless it forms part of the international travel. For example if the insured flies from –

- Cape Town to Johannesburg before flying to Dubai, the international travel will include the flight from Cape Town to Johannesburg;
- Dubai to Cape Town and visits the Winelands for a weekend before flying to Johannesburg before touring the Kruger National Park, the flight from Dubai to Cape Town qualifies as international travel whereas the time spent in the Winelands and Kruger National Park as well as the flight to Johannesburg would be regarded as domestic travel.

For purposes of BGR 37, a stopover is therefore limited to a period of 24 hours or less from the time of arrival to the commencement of the next stage of the journey (whether local or international). There may, however, be exceptional cases where the delay is longer than 24 hours due to circumstances beyond the control of the insured, for example flights being grounded as a result of weather conditions or airline strikes. In these cases, it is accepted that the zero-rating of the international travel insurance will continue to apply. Refer to **Annexure C**.

Hull insurance

The supply of hull insurance may be zero-rated under section 11(2)(h)(ii) if supplied directly to a person who is not a resident of South Africa and not a vendor to the extent the insurance policy covers the loss to a “foreign-going aircraft” or “foreign-going ship”. The insurer is regarded as supplying the insurance services directly to the insured, irrespective of whether an intermediary assisted the insurer in arranging the insurance or not. The temporary presence of the “foreign-going aircraft” or “foreign-going ship” in South Africa does not prevent the application of the zero rate under section 11(2)(h)(ii).

Insurance cover for moveable property (excluding hull) outside South Africa

Short-term insurance is deemed to be supplied directly in respect of the insured movable property, for example trucks and machines. Insurers may zero-rate the supply of short-term insurance covering movable property outside South Africa under section 11(2)(g)(i).

The temporary presence of the insured property in South Africa does not prevent the application of the zero rate under section 11(2)(g)(i).

Insurance cover for fixed property situated outside South Africa

The supply of insurance in respect of fixed property situated outside South Africa qualifies for zero-rating under section 11(2)(f).

Cancellation of policies

Insurance premiums are generally paid at the beginning of the insurance period, usually monthly or annually. If the insured cancels a policy during the period of insurance cover, the insurer would have received premiums for the full insurance period whilst only rendering the services for a part of that period.

In such cases, the insurer is entitled to a deduction if output tax was already accounted for in respect of the full premium paid by a non-vendor, provided the premium amount in respect of the cancelled period is refunded to the insured.³³ In order to substantiate the deduction, the insurer must obtain and retain, amongst others, proof that the premium relating to the cancelled period was paid to the insured who cancelled the policy. In instances where the insurer does not refund the insured and treat the unearned premium as a fee, no VAT adjustment is required if VAT was already accounted for.

³³ Section 21(2)(b).

(b) Insured

Insured vendors may deduct input tax on taxable short-term insurance premiums paid provided that the normal rules for deducting input tax are met. This includes the following:

- The premium paid must include VAT at the standard rate;
- The insurance service must be acquired by the vendor wholly or partly for consumption, use or supply in the course of making taxable supplies;
- The insurance service must not be acquired for private, exempt or other non-taxable purposes;
- Where the insurance is acquired for mixed taxable and non-taxable purposes, an apportionment of input tax must be made; and
- The insured holds one of the following supporting documents at the time the deduction is made:
 - A valid tax invoice or debit note;
 - An alternative document to a tax invoice or debit note as set out in BGR 14 relating to tax invoices, debit notes and credit notes; or
 - Alternative documents approved by the Commissioner in terms of a ruling issued in accordance with section 16(2)(g).

Based on the application of the time of supply rules which apply to short-term insurance as discussed in **3.6** and paragraph 2.1 of *BGR 14*, input tax on short-term premiums may only be deducted in the tax period in which payment of the premium was actually made, regardless of whether the vendor is registered on the invoice basis or payments basis of accounting. There may also be instances where an insurer agrees to provide insurance cover before the insured pays premiums in which case the time of supply would be the earlier of the date the premium is paid or the date the insured is notified of the obligation to pay the premium.³⁴ See Chapter 8 of the *VAT 404 – Guide for Vendors* for more details with regard to input tax.

6.2.2 Premiums received through intermediaries

Brokers and collection agents that act as independent intermediaries are required under Part 4 of *Regulation 1493 of 27 November 1998: Regulations under the Short-term Insurance Act 53 of 1998* to pay premiums collected on behalf of insurers to the insurers within 15 days of the end of the month in which the intermediary received the premiums. However, the VAT Act requires that the VAT on insurance premiums must be accounted for during the period in which the time of supply occurs. (See **3.6**.)

As any premium received by an agent is regarded in law as a receipt by the principal, the liability to account for VAT arises in the hands of the insurer at the time that the premium is received by the agent. It is therefore very important that intermediaries (agents) who collect premiums on behalf of their principals (insurers) make sure that they supply the necessary information within the 21-day period after the end of each month as required under section 54(3), as insurers will have to account for the VAT on eFiling by the end of the month after the completion of the relevant tax period. This notification can be in the form of a bordereau.

³⁴ Section 9(3)(b)(i).

6.2.3 Premiums on Lloyd's policies (coverholder business)

Lloyd's coverholder business is subject to VAT in RSA on the same principles which apply to other short-term insurance contracts in the Republic, but premiums in respect of "open market business" are not taxable. A Lloyd's correspondent ("coverholder") who acts under binding authority to conclude insurance agreements in the Republic on Lloyd's behalf merely acts as agent in regard to Lloyd's policies and is therefore not required to account for output tax on the insurance service supplied by Lloyd.

The commissions and fees paid to coverholders in regard to such supplies are subject to VAT at the standard rate in the same manner as other commissions and fees discussed in **6.3** below. The VAT on expenses incurred by the coverholder (as agent on behalf of Lloyd's) in conducting coverholder business in the Republic is deductible by Lloyd's in accordance with the normal rules for deducting input tax.

6.3 Commission and fees

Intermediaries may supply intermediary services as well as other services to insurers and insureds. Consideration is charged in the form of commission and fees respectively.

6.3.1 Intermediary

The intermediary must account for output tax on the supply of intermediary and other services according to the general time of supply rule. (See **3.6**.) In the case of upfront commission and fees, the intermediary must declare output tax on the full commission or fee received.

This rule applies irrespective of whether the commission or fee is deducted from premiums or other amounts collected on behalf of the insurer or payment is made directly by the insurer to the broker. The bordereau must meet the requirements set out in **4.4**. (See paragraphs 2.12 and 2.13 of BGR 14.)

STI Act

Commission from insurers for services rendered as intermediary is normally calculated as a percentage of the premium payable, as determined under regulations made under the STI Act concerning the application of section 48 of that Act. Some of the most important provisions contained in these regulations are as follows:

- The maximum commission payable is currently 12.5% of the premium payable under a motor policy and 20% under any other short-term policy.³⁵ In the case where both types of cover are included in a single policy, the maximum commission payable is determined with reference to the proportion of the premium attributable to each type of cover.
- No consideration can be paid to an independent intermediary (whether directly or indirectly) for rendering services as intermediary, except in the form of commission in monetary form.
- Regardless of how many persons render services as intermediary in relation to a policy, the total commission payable for that policy cannot exceed the maximum amount (that is, 12.5% or 20% – as the case may be).

³⁵ Clause 5.3 of Regulation R1493 of 27 November 1998: Regulations under the STI Act.

- Commission shall not be paid or accepted before the date on which the premium in respect of which it is payable, has been paid to the short-term insurer or Lloyd's broker.
- If a premium or any part thereof is refunded by a short-term insurer or Lloyd's broker, the commission payable in respect of that premium (or part thereof) must be refunded to the short-term insurer by the person to whom it was paid.

As the regulations do not see VAT, the view is that, under section 64, the maximum prescribed commission rate includes VAT. Therefore, in the case of the regulated commission rate being applied to –

- a VAT exclusive or zero-rated premium, the commission amount will not include VAT and the applicable VAT rate needs to be applied to the commission to calculate the relevant output tax;
- a standard rated VAT-inclusive premium, the commission will include VAT and output tax is determined by applying the tax fraction (currently 14/114) to the VAT inclusive commission.

The same principle will apply where fees are calculated as a percentage of premiums.

Zero-rating

Generally, intermediaries that are vendors must account for VAT at the standard rate on commissions they earn, unless the intermediary services or other services qualify to be charged with VAT at the zero rate under section 11(2). Note, however, in this regard that if the supply by the insurer is subject to VAT at the zero rate, it does not necessarily follow that the commissions charged will also be subject to VAT at the zero-rate. The arranging of the following types of insurance may be zero-rated:

- Insurance of goods or passengers transported internationally under section 11(2)(d);
- Hull insurance in respect of a “foreign-going aircraft” or “foreign-going ship” under section 11(2)(i)(ii) if the arranging service is supplied to a non-resident who is not a vendor;
- Stock throughput insurance to the extent that the underlying stock throughput insurance qualifies for zero rating under section 11(2)(d); and
- Other insurance, provided the requirements of section 11(2)(f) are met.

6.3.2 Short-term insurer

The insurer is entitled to deduct the VAT paid on the commission or other charge by the intermediary as input tax if the insurer is a vendor. This is based on the assumption that the short-term insurer will use or consume these services wholly for making taxable supplies in the course of supplying short-term insurance.

6.4 No-claim bonuses and cash incentives

There are usually only two instances when the insured will get a payment from the insurer in terms of a short-term insurance policy, namely when –

- there is a claim on the policy and an indemnity payment is made to the insured to settle that claim; and
- a cash bonus is paid to the insured as a result of that person not making any claims on the policy over a specified period of time (sometimes called a “no-claim bonus” or “cash back incentive”).

6.4.1 Short-term insurer

When a no-claim bonus is paid in cash to the insured, the VAT treatment of that payment will depend on the characterisation of the underlying supply or event giving rise to the payment. For example, if the relevant clause in the contract makes it clear that the premiums already paid are recalculated and part thereof is paid back to the insured after a specified claim-free period as a retrospective discount, this will be an adjustment event. In this case, the insurer has to issue a credit note to the insured for the adjustment. The insurer is entitled to deduct input tax in the tax period in which the credit note is issued. This applies whether or not the insured is a VAT vendor. However, if the insured is a vendor, the insured would be obliged to make a corresponding output tax adjustment in the tax period in which the credit note is issued if input tax was previously deducted on the premiums which are now being discounted. In the case of the insured not being a vendor, the insurer is only entitled to the deduction once the amount is paid back to the insured, irrespective of when the credit note is issued.

In instances where the insurer implements the no-claim benefit by reducing the insured's future premiums or by not imposing an increase in premiums which would otherwise apply, the insurer will merely continue to account for output tax on the reduced premium, as and when the output tax liability arises.

6.4.2 Insured

In the case of a repayment of premiums already paid, the insured is, under section 21(6), liable to pay back the VAT already deducted in its VAT return based on the credit note or other notification issued by the insurer. This adjustment can be effected by either decreasing the input tax or increasing the output tax in the return for the tax period in which the adjustment must be declared.

6.5 Recoveries and recoupments

Once the insurer has settled a claim by the insured, any subsequent recoveries are not for the insured's benefit. The insured will therefore not be liable to account for any output tax in respect thereof. The VAT treatment from the insurer's perspective is discussed below.

6.5.1 Recoveries made under subrogation

Subrogation is the right of one person to stand in the place of another in the application of the law. Subrogation therefore refers to the insurer's right to take the necessary steps to recover the amount of any loss incurred by the insured from the responsible third party. These steps may include taking legal action against the responsible third party.

On the basis that the payment by the third party is compensation for a loss caused by that party, the payment is not regarded as consideration for a supply by the insurer exercising its right of subrogation. The insurer is therefore not liable to account for output tax on amounts recovered from the third party (or the third party's insurer) under a subrogation claim, irrespective of whether the whole or only a portion of the claim is recovered.

Similarly, when a short-term insurer pays an amount to another insurer to settle a claim made under a subrogated right of recovery, the insurer making that payment is not entitled to make a deduction under section 16(3)(c).³⁶ The reason is that the receipt is not consideration for a taxable supply. (See Example 6.)

6.5.2 Recoveries from reinsurers

A short-term insurer may reinsure some or all of its claims risk with a reinsurer. "Claims risk" is the risk that one or more of the short-term insurer's policyholders will submit a claim resulting in the short-term insurer having to indemnify the insured. This will, in turn, lead to a claim under the reinsurance policy between the short-term insurer and reinsurer. The claims risk is deemed to be situated at the cedent's address as this is where the cedent's business is situated and where it manages its insurance book.

The amount received as an indemnity payment by the insurer from the reinsurer will be subject to VAT under section 8(8) and the reinsurer will be entitled to deduct input tax on the indemnity payment made under section 16(3)(c). (See **Chapter 8**.)

6.5.3 Contribution from other insurers

In the case where the insured may have cover for the same insurable interest under another short-term insurance policy with a different insurer, each insurer may be required to contribute equally or in proportion to the value of the claim made by the insured. From the insured's perspective, output tax must be declared on each component of the indemnity payment received from the different insurers. Similarly, each insurer will only be able to deduct the tax fraction of that part of the indemnity payment which it is liable to pay to the insured. This will also apply in the case of co-insurance arrangements where two or more insurers enter into a collective policy with the insured to cover the risk in agreed proportions.

6.5.4 Sale of salvage

The remains of damaged goods become the property of the insurer once the insured has been fully indemnified for the loss in terms of the policy when insured goods are damaged beyond economic repair. The insured is obliged to surrender or abandon the damaged goods to the insurer as salvage and there is also a duty on the insured to minimise the loss. The insurer acquires the damaged goods in terms of the doctrine of abandonment under the law of insurance and in accordance with the terms and conditions of the policy. The insurer has a right to dispose of the salvage and to recoup any loss which it may have suffered as a result of the claim by the insured. (See Example 6.)

The sale of salvage will attract VAT in the same way as any other supply of goods. It should, however, be noted that the insurer would have acquired the salvage as second-hand goods for no consideration under the doctrine of abandonment and will therefore not be entitled to deduct any input tax thereon.³⁷ In such cases, the indemnity payment made in terms of the policy to the insured does not constitute consideration for the supply of the salvage.

³⁶ Refer to **7.3.1**.

³⁷ *Holland Insurance Company Limited v Wagenaar, Paul t/a Racedesigns* (36661/2010) [2011] ZAGPJHC 25 (7 April 2011).

The supply will be subject to VAT at the zero rate if the salvaged goods are located outside of the Republic at the time the goods are sold. However, if the salvaged goods are imported before being sold, the insurer will be liable to pay any VAT and customs duties which may be applicable. The VAT paid on importation in such a case may be deducted by the insurer as input tax provided that it holds the appropriate documentation (for example, import bill of entry and proof of payment of VAT).

6.6 Other income from taxable supplies

The term “enterprise” applies not only to the main activity carried on by insurers, brokers and independent intermediaries. Once a person is liable to register for VAT, or if the person registers voluntarily, that person must account for the VAT on all other taxable supplies made. For example, insurers are often involved in making a number of other supplies such as providing financial advice, management of funds, supplying fixed property, rental of fixed property etc. See 3.1 and 5.3.2.

6.7 Imported services

VAT is payable by any person who is a resident of the Republic when that person (the recipient) acquires services from a non-resident business that is not registered for VAT in the Republic, if the services are utilized or consumed in the Republic for non-taxable purposes.³⁸ The recipient of the imported services is responsible for the declaration and payment of the VAT at the standard rate on form VAT 215 if the recipient is not a vendor. In the case of a vendor that imports services for non-taxable purposes, the VAT payable must be declared as output tax in Block 12 of the VAT 201 return together with any other VAT that is payable for the tax period concerned.

The time of supply of imported services is the earlier of the time that an invoice is issued by the supplier or the recipient or any payment is made by the recipient in respect of that supply. The taxable value of the supply is the greater of the consideration payable or the open market value.

An insured will be liable for VAT on imported services if insurance is provided by a non-vendor foreign insurer to the extent the insured does not use or consume the insured goods in the course or furtherance of making taxable supplies. An example is where a person insures an aircraft used for recreational purposes with a foreign insurer.

The application of the imported services provisions in the case of an insurer is as follows:

- When services are imported exclusively by a vendor for the purposes of conducting short-term insurance business, the services will not comply with the definition of “imported services” as the services are imported wholly for taxable purposes. In this case, there will be no liability to declare any VAT.
- When the services are imported exclusively for the purposes of conducting exempt long-term insurance business, or exclusively for other non-taxable purposes (for example, exclusively in regard to a share transaction or other investment activities), VAT must be declared and paid on the greater of the consideration payable or the open market value in the tax period that an invoice is issued by the supplier or the insurer (recipient), or any payment is made in respect of that supply.

³⁸ Refer to section 7(1)(c).

- When the services are imported partly for taxable and non-taxable purposes, the consideration payable or open market value (as the case may be), must be attributed according to the extent that the services are used for taxable and non-taxable purposes. VAT is only declared and paid on imported services to the extent that the imported services are acquired for non-taxable purposes.

The VAT Act also provides for the following supplies not to be subject to VAT³⁹ even if these fall within the definition of “imported services”:

- Supplies that would be exempt from VAT or zero-rated if supplied in the Republic; or
- Supplies that are subject to VAT at the standard rate (presently 14%); or
- The supply of educational services by an educational institution established in an export country which is regulated by an educational authority in that export country;
- Supplies where the value of that supply does not exceed R100 per invoice; or
- The supply of services of a non-resident employee under an employment contract.

Note that imported services can never be subject to VAT at the zero rate. This principle and others relating to the application of the imported services provisions in the VAT Act and the exemptions which are provided in that regard were confirmed in the judgment in *Metropolitan Life Ltd v Commissioner for SARS* 2009 (3) SA 484 (C), 70 SATC 162.

³⁹ Refer to section 14(5).

Chapter 7

Trade payments, indemnity payments and excess

7.1 Introduction

An insurer will make a payment to the insured or repair or replace the damaged article to settle the claim if the policy holder makes a valid claim against an insurance policy after suffering a loss. This process is called a “settlement”. The word “settlement” is also used to describe an agreement, or determination regarding payment to be made as a result of legal action or threatened legal action. This could relate to insurance or any other legal proceedings. The word “settlement” indicates that it is a final agreement made between the two parties or a final determination made by a court or arbitrator regarding the amount to be paid. For example if the insurer and the insured settle on a certain amount, the insured cannot claim a further amount after having accepted the settlement amount. Settlement options are available in the case of life insurance as the insured can usually choose from various options available. In short-term insurance, the insurer decides on whether a damaged item such as a car will be repaired or replaced or if a payment will be made as compensation for the loss or damage.

The terms “indemnity” and “indemnify” are used in the context of sections 8(8) and 16(3)(c), with reference to payments made by insurers to indemnify the insured party in terms of a taxable contract of insurance. These terms are not defined in the Act, and therefore take their ordinary meaning. Further, although these terms are not used in the VAT Act with specific reference to short-term insurance contracts, it is only possible for a deemed taxable supply to arise under section 8(8) if the indemnity payment was made in terms of a taxable short-term insurance contract. These rules also apply if the payment relates to a non-indemnity clause contained in the short-term insurance contract, for example, for personal accident cover or third party liability claims.

For the purposes of this guide it is necessary to distinguish between a so-called “trade payment” to reinstate or restore goods lost or damaged under a short-term insurance policy and a settlement paid as compensation to the insured to cover the loss. A settlement of the latter type is referred to as an “indemnity payment” or “claims payment”.

7.2 Trade payments

A trade payment is a payment made by an insurer to a supplier of goods or services to repair or replace insured goods which have been lost, damaged or destroyed. Trade payments made to suppliers under short-term insurance policy claims will generally be incurred by the insurer in the course or furtherance of its enterprise. A trade payment may also be effected by way of a reinstatement voucher which will allow the insured to acquire specified goods or services as a replacement for the lost or damaged articles from specific suppliers. The VAT incurred in such circumstances may usually be deducted under section 16(3)(a) or (b), which means that the insurer must obtain and retain the required tax invoices. In instances where the insurer acquires goods or services from non-vendors, no input tax may be deducted. Similarly, the insurer may not deduct input tax if any exempt or zero-rated goods or services are acquired to settle the claim.

When a trade payment is made by a non-resident insurer, it is possible that the services rendered could be subject to VAT at the zero rate. The supply of goods will generally not be subject to the zero rate in these circumstances unless they are exported. For example, if a vehicle is repaired in the Republic for a non-resident insurer, the supply will be made directly in connection with movable goods situated in the Republic and VAT must be charged at the standard rate. However, if the vehicle is temporarily imported specifically for the purpose of making those repairs, the panelbeater's services (as well as any goods incorporated into the repaired vehicle) may be subject to VAT at the zero rate as the vehicle must be exported by the owner after the repairs are done.⁴⁰

The VAT incurred on the costs associated with handling claims and making indemnity payments may also be deducted as input tax in the same way as trade payments as discussed above. This will include, for example, claims handling fees charged by brokers, loss adjuster and assessor fees to determine the validity and extent of claims, and other administrative charges by intermediaries and agents which are incurred in the claims handling process.

7.3 Indemnity payments

7.3.1 Legal provisions

Section 16(3)(c) contains a special provision relating to insurers. In terms of this provision, insurers are entitled to deduct an amount equal to the tax fraction (currently 14/114) of any amount paid to indemnify another person in terms of a contract of insurance.

The provision reads as follows:

- (a) an amount equal to the tax fraction of any payment made during the tax period by the vendor to indemnify another person in terms of any contract of insurance: Provided that this paragraph —
 - (i) shall only apply where the supply of that contract of insurance is a taxable supply or where the supply of that contract of insurance would have been a taxable supply if the time of performance of that supply had been on or after the commencement date;
 - (ii) shall not apply where that payment is in respect of the supply of goods or services to the vendor or the importation of any goods by the vendor;
 - (iii) shall not apply where the supply of that contract of insurance is a supply charged with tax at the rate of zero per cent under section 11 and that other person is, at the time that that payment is made, not a vendor and not a resident of the Republic;
 - (iv) shall not apply where that payment results from a supply of goods or services to that other person where those goods are situated outside the Republic or those services are physically performed elsewhere than in the Republic at the time of that supply;

The contra (output tax) provision to the above is contained in section 8(8) which applies to the insured receiving the indemnity payment. The application of the above provisions for the insurer and the insured is explained in 7.3.2 and 7.3.3 below.

⁴⁰ An example of this is section 11(2)(g).

7.3.2 The insurer

An insurer may only deduct an amount equal to the tax fraction of an indemnity payment made to an insured if the insurance provided was a taxable supply. The indemnity payment referred to here is the net amount after deducting the excess payable by the insured, whether deducted as part of the calculation, or recovered separately from the insured.

The insurer will be able to make the deduction regardless of whether the insured is a vendor or if the insured goods or services were used by the vendor for exempt, private, or other non-taxable purposes.

The wording of section 16(3)(c) is wide enough to include indemnity payments made to cover claims arising from the losses of third parties which may have been caused by the insured. In such cases, the insurer will also be able to deduct the tax fraction of the indemnity payment made to the third party (or the third party's insurer) as input tax. (See Example 2 below.)

Provisos (ii) to (iv) to section 16(3)(c) make it clear that the insurer will not be entitled to make a deduction for any indemnity payment made in the following circumstances:

- *Proviso (ii)* – if the payment is made in respect of the supply of goods or services to the vendor or the importation of any goods by the vendor. This refers to a situation where the insurer purchases or imports goods or services to reinstate or replace the insured goods instead of making an indemnity payment. In other words, this is when a “trade payment” is made as discussed in 7.2. Input tax on any trade payment made by the insurer to a third-party supplier is deductible under section 16(3)(a)⁴¹ and not under section 16(3)(c).
- *Proviso (iii)* – where the indemnity payment is made under an insurance contract if –
 - the supply of insurance was zero-rated; and
 - the person indemnified is not a vendor and not a resident of the Republic at the time that the indemnity payment is made.

This will apply, for example, in certain marine insurance policies where the insured is a non-resident and not a vendor in the Republic.

- *Proviso (iv)* – where the indemnity payment made to the insured was in respect of either –
 - a supply of goods situated outside the Republic; or
 - a supply of services which were physically performed outside of the Republic. For example, if the indemnity payment is a reimbursement of the cost of repairing a vehicle damaged in an accident in Namibia, the repairs would have been physically performed by a service provider in Namibia and the insurer will not be entitled to make a deduction in that case.

⁴¹ The deduction is subject to the requirements of sections 16, 17 and 20 being met.

A few other cases where the insurer will not be entitled to deduct input tax in regard to payments made:

- *Ex gratia payments* – The term *ex gratia* refers to something that is being done voluntarily, out of kindness or as an “act of grace”. In a purely legal context, it refers to a payment that is being made “without the giver recognizing any liability or legal obligation”⁴² and in the context of insurance; it refers to “an insurance payment not required to be made under an insurance policy”.⁴³ *Ex gratia* payments are therefore made without the admission of liability or waiver of any rights on the part of the insurer.

As *ex gratia* payments are not regarded as being made in terms of a contract of insurance, the insurer will not be entitled to deduct any input tax in respect thereof. However, it is important to establish the true nature of such payments and not to make a decision based merely on the fact that the payment has been called “*ex gratia*”. Ultimately, the context and circumstances in terms of which any payment is made will determine whether or not it is received “*under*” or made “*in terms of*” a contract of insurance, and consequently, whether it has the characteristics of an *ex gratia* payment or not.

- *Interest* – Interest represents a financial charge related to the time value of money and is consideration for an exempt supply of financial services for VAT purposes. It follows that no deduction can be made by the insurer where the interest is calculated, for example, as an amount related to making the indemnity payment later than expected. However, if interest is a factor which has to be considered as an integral part of the formula or method of determining the quantum of the loss (and hence the amount of the actual indemnity payment), it may be included in the amount used to determine the deduction allowed to the insured under section 16(3)(c).

The insurer will also not be entitled to deduct input tax in regard to indemnity payments if the following required documentary proof is not obtained and retained:

- The original copy of the insurance contract and any other evidence of endorsements (electronic or otherwise) relating to the claim or the contract terms and conditions.
- Proof that the supply is a taxable supply. For example, a copy of the tax invoice or a statement contained in the contract documentation.
- Proof that the indemnity payment (in money) was made. For example, payment advice, bank statement or internet payment confirmation.
- In instances where the above cannot be obtained, the insurer may, in respect of tax periods from 1 April 2016, under circumstances prescribed by the Commissioner, make a deduction based on alternative documentary proof acceptable to the Commissioner under section 16(2)(g).

In instances where the insurer makes an indemnity payment to a third party to indemnify the insured, the insurer must notify the insured of the potential output tax liability arising from the claim settled on behalf of the insured. The policy contract should be clear as to how this liability will feature in the determination of the amount which is payable to the third party and whether or not the VAT component of the claim will be paid to the insured. This is important because the amount is deemed to include VAT and must be declared as output tax by the

⁴² http://en.wikipedia.org/wiki/Ex_gratia.

⁴³ Black's Law Dictionary, 9th edition, p. 654.

insured regardless of whether the payment (or any part thereof) was actually made to the insured to cover the VAT liability.

7.3.3 The insured

As mentioned in 7.3.1, section 8(8) is the contra (output tax) provision in relation to section 16(3)(c), although there will not be an exact matching of inputs and outputs between these two provisions in every case. This is because the insurer may be entitled to deduct input tax regardless of whether or not the insured must declare output tax on the receipt of the indemnity payment. Although there are a few exceptions, the general position is that when an insurer makes an indemnity payment in terms of a contract of short-term insurance, the insurer will claim a deduction equal to the tax fraction of the indemnity amount paid on the VAT return concerned. The insured (being a vendor) will declare output tax on the same amount if the payment related to a loss incurred in the course or furtherance of the insured's enterprise. This is because the indemnity payment is deemed to be consideration for a taxable supply of services made by the insured to the insurer. In instances where the insured is not a vendor, section 8(8) is not applicable and the insured will not be liable to account for output tax in respect of the indemnity payment.

This rule applies to all indemnity payments received on or after 30 September 1991 by a vendor, regardless of when the short-term insurance contract is concluded. Furthermore, even if the payment was not physically received by the insured, but rather, paid directly to a third party on behalf of the insured, the insured is still required to account for output tax on the full indemnity payment.

Output tax at the standard rate must also be declared when the indemnity payment relates to a monetary loss in the enterprise. For example –

- when there is a loss in the enterprise resulting from money stolen in a robbery;
- when funds have been stolen by employees and cannot be recovered, or as a result of fraud;
- credit guarantee indemnity payments received as a result of debtors failing to pay for goods or services supplied on credit.

The deemed supply which arises under section 8(8) in respect of the receipt of the indemnity payment is not the same as the actual supply of the insurance service which was supplied in terms of the policy by the insurer. The VAT treatment of the deemed supply should also not be confused with the VAT treatment of the supplies of goods or services made by the insured to which the insurable interest may relate. An example is where the insured carries on a business of transporting passengers or goods to or from an export country in an aircraft. In this instance, the insurance premium is consideration for the taxable supply of insurance which is zero-rated under section 11(2)(d). The indemnity payment is consideration for another service which is deemed to be supplied by the insured to the insurer. The deemed service is supplied on the day the payment is received by the insured or paid to the relevant third party (as the case may be).

Section 8(8) does, however, provide that the insured will not be liable to declare output tax on an indemnity payment received in terms of a contract of short-term insurance in the following situations:

- When the indemnity payment relates to insurance services which are exempt or out of scope (that is, the insurance service is not a taxable supply);

- To the extent that the indemnity payment is to compensate the insured to reinstate goods which were subject to a denial of input tax upon acquisition under section 17(2), there is no liability to declare output tax. The term “to the extent” refers to instances where an enterprise has not separately insured assets on which input tax is specifically denied, such as motor cars and entertainment goods, but includes these in the insurance cover for all the enterprise assets. This means, for example, that if the indemnity payment relates to a number of different business assets, the value of the claim which is attributable to enterprise assets on which input tax was specifically denied under section 17(2) must be identified separately and no output tax will be declared on that portion. Despite the fact that the input tax on the acquisition of certain goods and services is specifically denied in under section 17(2), the input tax on the insurance of those goods and services is not specifically denied under this provision.
- To the extent that the insured goods and services (which are the subject of the claim) were used for non-enterprise purposes, the loss in this case would not have been incurred in the course of carrying on an “enterprise”. This applies, for example, if the vendor makes both taxable and exempt supplies and does not, for insurance purposes, take out separate policies for the assets used for taxable and exempt activities respectively. Similarly, where private assets and enterprise assets are all insured in terms of one policy, the vendor will not declare any output tax to the extent that the indemnity payment relates to a loss of the private and other non-enterprise assets, as the VAT on the premiums payable in respect thereof would have been denied as input tax to that extent, as would be the case for other non-enterprise assets insured. In this instance, the insured (being a vendor) is only required to account for output tax in respect of the indemnity payment to the extent it relates to its taxable business.

Remember also the point made in **Chapter 2** that the word “insurance” as defined in section 1(1) means “a guarantee against loss, damage, injury or risk of any kind whatever, whether pursuant to any contract or law”. Further, that the term “contract of insurance” is not restricted to short-term policies as envisaged in the STI Act. This means, for example, that there will also be a liability to account for output tax when an indemnity payment is received in terms of certain self-insurance contracts which fall within the meaning of “insurance” as defined in section 1(1). For example, this could apply to certain contractual arrangements between holding companies or head offices and their subsidiary companies.

Example 2 – Output tax on indemnity payments received

Facts:

Vendor G receives an indemnity payment from Insurer H in respect of a fire at his home from where G also conducts an enterprise as an estate agent. The damaged goods, all of which were insured, were as follows:

- Motor car used exclusively in the enterprise.
- 50% of the house burned down, including the room which was used as an office. SARS allowed a partial input tax credit of 10% based on the square meterage, being the extent that the room formed part of the fixed property acquired and used for enterprise purposes.
- Computer equipment and office furniture used exclusively for enterprise purposes.
- Furniture, fixtures and fittings in the lounge used for private purposes.

Result:

The VAT implications for Insurer H and Vendor G with regard to the claim for damages to the assets destroyed or damaged in the fire are as follows:

G will have to split the indemnity payment between the different assets insured as some of them were used for enterprise purposes and some were not. The VAT on the acquisition of the motor car (although used exclusively for taxable supplies) would have been specifically denied under section 17(2)(c). G will therefore have to declare output tax under section 8(8) only on the amount of the indemnity payment which is attributable to the loss of the home office, the computer equipment and office furniture. Output tax on the home office will be $1/5$ ($10 / 100 \times 50\%$) of the value of the indemnity payment which relates to the damage to the house.

No output tax must be declared on –

- that part of the indemnity payment which relates to the private assets which were not used for enterprise purposes; and
- the motor car (as input tax was specifically denied on the acquisition thereof).

Insurer H will deduct input tax on the full indemnity payment made under section 16(3)(c). Insurer H should, however, supply the necessary details of how the indemnity payment is split between the different assets so that Vendor G will be able to calculate the output tax which must be declared on the VAT 201 return.

Example 3 – Output tax on indemnity payments received*Facts:*

Vendor J damages X's delivery vehicle and both parties submit claims to their respective insurers. The insurers pay the claims and after negotiations, J's insurer (K) agrees to pay X's insurer (Y) R20 000 to cover the costs of the claim paid out by Insurer K to Vendor J under the contract of insurance.

Result:

Under section 8(8), J is required to account for output tax on the indemnity payment received from Insurer K if the loss was incurred in the course of carrying on an enterprise. Insurer K is entitled to a deduction under section 16(3)(c), calculated by multiplying the tax fraction by the amount of the indemnity payment made to Vendor J.

Insurer Y is not liable to account for output tax in respect of the R20 000 received from Insurer K as this amount is not consideration for any taxable supply made by Insurer Y. (Section 8(8) is not applicable in this case as the payment is not made under a contract of insurance between the insurers, therefore no deemed supply exists in this instance). Insurer K may not make a deduction under section 16(3)(c) as the R20 000 is not paid in terms of an insurance contract but as part of a settlement with Insurer Y.

7.4 Excess

7.4.1 General

An excess is the first amount payable by the insured in the event of a loss, and is regarded as the uninsured (or self-insured) portion of the loss. The excess amount can be a single amount payable in the event of any claim under the insurance policy (inner excess) or an aggregate excess. Aggregate excess or deductible is the sum of all the different excess amounts applicable to the different goods and services insured in terms of the policy (or in terms of different policies) which will be deductible from a claim. For the purposes of this guide, the term “excess” includes all references to inner and aggregate excess. In most cases when a claim is made by the insured, an excess payment will be required.

The amount of the excess is either expressed as a fixed monetary amount or as a percentage of the value of the goods or services insured. Payment of the excess can be effected in a number of different ways. For example, when the insured's vehicle is damaged in an accident and the claim is to be settled by way of a trade payment by the insurer to the panel beater, the insured may pay the excess amount to the insurer or the panel beater repairing the vehicle. Alternatively, if the insurer decides that the vehicle is too badly damaged to repair, it may choose to make an indemnity payment to the insured instead. The insurer will then assume ownership of the damaged goods which it will sell as salvage. See 6.5.4.

The VAT Act does not deal with matters relating to the determination of insured values, excess amounts or how the final amount of an indemnity payment is calculated, as these are contractual matters between the insured and the insurer. The VAT Act only provides that where VAT is applicable to the transaction, the supplier must declare output tax thereon, or if the expense is incurred in the course or furtherance of the enterprise, the insured (or the insurer – as the case may be) will be entitled to deduct input tax if registered for VAT. Further, where it concerns contract prices, the agreed price will include VAT if it relates to a taxable supply, whether or not the parties have included VAT in the amount of the consideration which is payable.

The wording of the policy document relating to the business operations of the insurer should therefore be clear as to how VAT features in the calculation of insured amounts and the net amount of any indemnity payment which is made in terms of the policy. In this process, both the insurer and the insured should be mindful of the fact that VAT may have to be paid to a supplier to repair or replace the insured articles, and that the insured may be liable to declare output tax under section 8(8) if registered for VAT.

Depending on the wording of the policy document, the insured may be required to pay the excess amount directly to the third party supplier or to the insurer. The VAT treatment of these transactions is discussed below.

7.4.2 Excess paid to a third party supplier

In the case where the insured pays the third party supplier directly, the third party supplier must split the consideration and issue two tax invoices, one to the insured for the excess amount and one to the insurer for the balance of the account. The insurer and insured will then be entitled to deduct input tax on their relevant portion of the goods or services acquired from the third party supplier based on the tax invoices received. Also see paragraph 2.7.1 of BGR 14 for further information.

7.4.3 Excess paid to an insurer

In instances where the insurer pays the full amount to the third party supplier and subsequently recovers the excess from the insured, the insurer is not making a supply to the insured in respect of the excess and the insurer is therefore not liable to account for output tax based on the excess received. The third party service provider, if registered for VAT, is required to account for output tax on the full amount charged for the goods or services supplied. The insurer is required to issue a document to the insured which contains at least the following information regarding the excess:

- The insurer, insured and third party's VAT registration number and address;
- A description of the goods or services supplied by the third-party supplier;
- The date on which the supply was made by the third part service provider; and
- The amount of the excess paid or payable by the insured reflecting either the VAT amount separately or a statement that the amount payable includes VAT and the rate at which VAT was charged.

In this instance, the insurer is only entitled to deduct input tax to the extent the amount paid to the third party supplier exceeds the excess paid by the insured.

According to paragraph 2.7.2 of BGR 14, an arrangement is made under section 72 to regard the aforementioned document to be a “tax invoice” for the purposes of section 16(2)(a). Based on this document, the insured is entitled to deduct the tax fraction of the excess payable to the insurer as input tax if the loss was incurred in the course or furtherance of carrying on an enterprise. The insurer will, however, not be liable to account for output tax based on this document.

Example 4 – VAT treatment of trade payments and excess – Excess paid to third party supplier

Facts:

Insurer A (a short-term insurance company which is a vendor), supplies Vendor B (the insured) with insurance cover under a policy of insurance, to cover any damage or loss to a delivery truck. The delivery truck is used wholly for taxable supplies by Vendor B and the premium payable is R228 per month (including VAT). The truck is subsequently damaged in an accident and the cost of repairs is R12 540 (including VAT). Vendor B submits a claim to Insurer A, who undertakes to cover the full cost of the repairs. However, as Vendor B is liable for the excess payment of R1 140 in terms of the policy, the insurer will only actually cover the net amount of R11 400 (R12 540 – R1 140). Insurer A appoints Vendor C, as the approved service provider to effect the repairs and pays Vendor C directly. Vendor B pays the excess amount of R1 140 to Vendor C as required by Insurer A.

Result:

Insurer A

Insurer A is making a taxable supply of short-term insurance to the insured (Vendor B). Insurer A must therefore declare output tax of R28 each month in respect of the premiums received. Insurer A has engaged Vendor C to effect repairs to Vendor B's truck to the extent of R11 400. Insurer A will therefore be entitled to deduct input tax of R1 400 (that is, $R11\,400 \times 14 / 114$) under section 16(3)(a) in regard to the trade payment made to Vendor C. The deduction as contemplated in section 16(3)(c) will not be available to Insurer A. The deduction of input tax by the insurer is subject to obtaining the tax invoice from Vendor C as required under section 16(2).

Vendor B

Vendor B may deduct input tax of R28 each month in respect of the insurance premiums paid, as it is using the truck wholly for enterprise purposes. The input tax deduction is subject to Vendor B being in possession of the required tax invoice for each supply or alternative documents are held (see **5.3.3**). Vendor B is not required to account for output tax on the repair of the truck, as the payment for the repairs by Insurer A is a trade payment and not an indemnity payment as contemplated in section 8(8). Vendor B will be entitled to input tax of R140 (that is, $R1\ 140 \times 14 / 114$) on the excess payment made to Vendor C under section 16(3)(a). Vendor B must obtain a tax invoice from Vendor C as required under section 16(2) before making an input tax deduction. Vendor C will declare output tax on the payments received from Insurer A and Vendor B. Vendor C must issue one tax invoice to Insurer A for a consideration of R11 400 and another tax invoice to Vendor B for a consideration of R1 140.

Example 5 – VAT treatment of trade payments and excess – Excess paid to insurer*Facts:*

Assume the same facts as in **Example 4**, except that Insurer A pays Vendor C and recovers the excess from Vendor B.

*Result:***Insurer A**

Insurer A must declare output tax of R28 each month in respect of the premiums received. Even though the tax invoice from Vendor C reflects consideration of R12 540, Insurer A only incurs the portion for which it is liable. Consequently Insurer A may deduct input tax of R1 400 (that is: $[(R12\ 540 - R1\ 140) \times 14 / 114]$) under section 16(3)(a) on the trade payment made to Vendor C. Insurer A is required to issue a document to Vendor B reflecting the required information to enable Vendor B to deduct input tax in respect of the excess payment.

Vendor B

Vendor B may deduct input tax of R28 each month in respect of the insurance premiums paid. Vendor B will be entitled to input tax of R140 (that is, $R1\ 140 \times 14 / 114$) on the excess payment made to Insurer A under the section 72 arrangement in BGR 14. Vendor B must however obtain the required document from Insurer A to substantiate the input tax deduction.

Vendor C

Vendor C will declare output tax on the payments received from Insurer A.

Example 6 – VAT treatment of indemnity payments and excess*Facts:*

Assume the same facts as in **Example 4**, except that:

- Insurer A decides to make an indemnity payment to Vendor B to settle the claim instead of having the truck repaired.
- The “excess” amount of R1 140 will be deducted from the R12 540 indemnity payment before paying the balance of R11 400 to Vendor B.
- The truck is sold by Insurer A as salvage to D for R2 000. D is not a vendor.

*Result:***Insurer A**

Input tax of R1 400 (that is: $[(R12\ 540 - R1\ 140) \times 14 / 114]$) may be deducted under section 16(3)(c) on the indemnity payment made and output tax of R245.61 ($R2\ 000 \times 14 / 114$) must be declared on the sale of the salvaged truck. However, no input tax may be deducted on the acquisition of the second-hand truck, as it was acquired as salvage under the contract of insurance and no consideration was paid.

Vendor B

Output tax of R1 400 (that is: $R11\ 400 \times 14 / 114$) must be declared under section 8(8) on the indemnity payment of R11 400 as the payment was received in respect of an enterprise asset. No input tax may be deducted on the excess amount of R1 140 which was deducted from the total claim amount, as it does not constitute consideration paid for any taxable supply.

Non-vendor D

As Non-vendor D is not registered for VAT, no input tax deduction will be allowed. When Non-vendor D sells the salvage to its customer, no VAT will be charged on the sale. The VAT charged by Insurer A therefore becomes a cost to Non-vendor D.

Chapter 8

Short-term reinsurance

8.1 Introduction

This chapter deals exclusively with short-term reinsurance. It briefly explains the nature of reinsurance and focuses in general on the time of supply and documentation rules relating to specific reinsurance transactions. As there are some important differences between insurance and reinsurance, this paragraph provides a general introduction to the topic of reinsurance.

Reinsurance is insurance that is acquired by an insurance company (cedent) from one or more other insurance companies (reinsurers) directly or through a reinsurance broker. An insurer generally enters into a reinsurance agreement for one or more of the following main reasons:

- To protect the insurer against very large claims;
- To reduce exposure to “peaks and troughs”;
- To obtain an international spread of risk; or
- To increase the capacity of the insurer.⁴⁴

The reinsurer provides insurance cover against the risk that the cedent will incur a “loss” as a result of a successful claim submitted by the insured. This “claims risk” is different from the underlying insurance cover provided by the cedent to its clients. The location of the underlying insured goods will therefore not influence whether the supply of reinsurance services is subject to VAT at the standard or zero-rate. The reinsurer has to consider where the cedent’s reinsured risk (the “book”) is located (that is, the cedent’s business address) to determine the appropriate VAT rate.

The two main categories of reinsurance are treaty and facultative reinsurance. Under a treaty reinsurance contract, the reinsurer covers a specified share of all the insurance policies issued by the cedent within the scope of the contract. The reinsurance contract may oblige the reinsurer to accept reinsurance of all contracts within the scope (known as “obligatory” reinsurance), or it may provide the reinsurer with the option to reinsure the risk under each contract (known as “facultative-obligatory” or “fac oblig” reinsurance). Facultative reinsurance is negotiated separately for each insurance contract that is reinsured. This includes risk cover for unusual risks or cases where the individual risks are not covered (or insufficiently covered) by reinsurance treaties.

Loss coverage can be allotted between the parties: either proportionally or non-proportionally. In the case of proportional reinsurance, the cedent obtains coverage for the pre-arranged portion or percentage of the loss or risk from the reinsurer. The pre-agreed proportion or percentage of coverage is typically used as a base to calculate the percentage of premiums received by the cedent from the insured to be paid to the reinsurer. For example, if the reinsured pays 40% of the premiums to the reinsurer, then the reinsured recovers 40% of its losses when it pays the original policyholder according to the original policy terms.

⁴⁴ Importance of reinsurance – www.lloyds.com/lloyds/about-us/what-we-do/what-is-insurance [Accessed 12 December 2016].

In contrast, non-proportional reinsurance covers an agreed upon amount of loss which is stated in the reinsurance contract. A base or deductible amount is set in the reinsurance policy and any loss exceeding that amount is paid by the reinsurer. The indemnity amount payable by the reinsurer in the case of a claim has no relationship to the premiums received. Either type of coverage can be used in facultative or treaty insurance contracts.

Reinsurance can be provided across borders between reinsurers and cedents in different countries. In the context of this guide, “foreign reinsurance inwards” refers to instances where a South African reinsurer reinsures the risk of a foreign insurer whereas “foreign reinsurance outwards” refers to instances where a South African insurer reinsures its book (or part thereof) with a foreign reinsurer.

8.2 Time of supply

A reinsurer must consider the type and nature of reinsurance that is supplied to determine the applicable date on which the supply is deemed to be made. In the case where a confirmation process is required before the premium is determined, the bordereau will only be regarded as an invoice once the bordereau is confirmed. (See **8.2.3.**)

8.2.1 Facultative reinsurance

In the case of facultative reinsurance, the premium is determined before the reinsurance contract becomes effective. The facultative reinsurance contract specifies whether premiums are payable upfront as a single annual premium or periodically.

In instances where a single upfront premium is payable, the general time of supply rule in **3.6** will apply. The reinsurer is, however, deemed to make successive supplies of reinsurance services if premiums are payable periodically. In this instance each periodic payment will trigger the time of supply when (and to the extent) that the premium becomes due, or is received by the insurer (whichever occurs first).

8.2.2 Non-proportional treaty reinsurance

Under a non-proportional treaty reinsurance contract, the reinsurer uses historical information to estimate the premium payable. The full annual premium is split into periodic payments of which the first is generally payable within 30 days from the date cover commences. At the end of the year, the reinsurer calculates the actual premium (based on the risks actually covered during the year) and makes an adjustment for the variation. Unless the adjustment is reflected on the bordereau, the reinsurer must issue a separate debit or credit note if the consideration for the supply of reinsurance services is altered. In instances where a single upfront premium is payable, the general time of supply rule discussed in **3.6** will apply. The reinsurer is, however, deemed to make successive supplies of reinsurance services if premiums are payable periodically. In this instance each periodic payment will trigger the time of supply when (and to the extent) that the premium becomes due, or is received by the insurer (whichever occurs first).

8.2.3 Proportional treaty reinsurance

In the case of proportional treaty reinsurance, the premium is not known at the time the reinsurance contract becomes effective. The premium generally depends on the value of policies reinsured and the estimated claims risk in respect thereof. The cedent will therefore submit the required information to the reinsurer (or its reinsurance broker) to determine the premium on a periodic basis.

The reinsurer (or the reinsurance broker) needs to verify whether the amounts are correct in respect of zero-rated and standard rated premiums, cedent commission, brokerage fees, claims and recoveries. Once the verification process is completed, the cedent is informed of the net amount due and the information or bordereau is regarded as “confirmed”. This notification of confirmation, whether in the form of an email, a bordereau or any other written form, is regarded as an “invoice” as defined in section 1(1).

On the basis that the premium is not known at the time the reinsurer provides reinsurance cover to the cedent, section 9 (4)(b) deems the supply of reinsurance to take place when (and to the extent) that any premium in terms of that reinsurance contract is due or received or an invoice relating to that supply is issued, whichever is the earliest.

8.2.4 Intermediary and cedent services

Under section 9(1), intermediaries and cedents are required to account for output tax in the tax period during which payment is received or an invoice (including a bordereau) is issued in respect of the taxable supply of intermediary and cedent services, whichever is earlier.

8.3 Tax invoices, credit and debit notes

Short-term reinsurers and cedents generally use bordereaux to summarise all the supplies of reinsurance and cedent services during the reporting period specified by the reinsurance contract. The format of the bordereaux used may differ from reinsurer to reinsurer and may not contain all the information required by section 20 (4). For example, the document might not contain the words “tax invoice”, “VAT invoice”, “invoice”, “credit note” or “debit note” (as the case may be). In such cases, BGR 32 confirms that the document issued by the reinsurer, cedent or intermediary in respect of the supply of reinsurance, intermediary and cedent services will be accepted for VAT purposes, provided that it contains all the other information as required by sections 20(4) or 21(3).

In the case of local reinsurance, the bordereau must contain the following statement (or substantially similar wording):

“In terms of Binding General Ruling No. 32 this document constitutes a tax invoice, debit note or credit note as contemplated in sections 20(7)(a) or 21(5)(a) of the VAT Act respectively.”

This approval is subject to the supplier and recipient of the service retaining proof of each amount paid in respect of reinsurance, intermediary or cedent services reflected on the relevant bordereau.

Under section 20 (1), an intermediary is required to issue tax invoices in respect of any other taxable supplies made to their clients, unless these supplies are reflected in the relevant bordereau.

8.4 Recipient-created tax invoices, credit and debit notes

In many cases, recipients of services such as reinsurers, intermediaries, reinsurance brokers and cedents are required to determine the consideration payable in respect of services received. BGR 15 provides, under sections 20(2) and 21(4), that in such cases the recipient may issue the relevant recipient-created tax invoices, credit or debit notes. This is on condition that the recipient of the services complies with the requirements of Interpretation Note 56: Recipient-Created Tax Invoices, Credit and Debit Notes. The requirement to obtain a written agreement between the supplier and recipient allowing the recipient to create tax invoices, credit and debit notes may be contained in the bordereau or other agreement.

8.5 Documentary proof

8.5.1 Zero-rating

A reinsurer, cedent and broker may only zero-rate a supply if the documentary proof (as provided for under section 11(3) read with IN 31) is obtained within 90 days from the earlier of the time –

- A bordereau or other invoice is issued; or
- any payment of consideration is received in respect of that supply.

The policy document is only regarded as a tax invoice after the reinsurer obtains proof that the premium was paid and therefore the supply of reinsurance is deemed to take place on the date (and to the extent) the premium is paid unless an invoice (such as a bordereau) is issued in respect of that supply at an earlier date.

The vendor would be liable to effect the relevant adjustments if the vendor fails to obtain and retain the required documents as stipulated in IN 31.

8.5.2 Input tax and other deductions

The statements contained in this chapter regarding input tax and other deductions are conditional upon the reinsurer, cedent or broker obtaining and retaining the relevant documentary proof as provided in section 16(2). Failure to obtain and retain the required documentary proof will result in the vendor not being entitled to the deduction.

8.6 Reinsurance premiums

A short-term reinsurer charges a reinsurance premium to the short-term insurer (cedent) for taking over the cedent's claims risk (or part thereof). The VAT treatment of the supply of this reinsurance service is discussed below from the reinsurer and cedent's perspective.

8.6.1 Reinsurer

As a vendor, a reinsurer is required to levy VAT under section 7(1)(a) on the supply of short-term reinsurance services to a cedent. This supply is subject to the standard VAT rate of 14% unless the supply is specifically zero-rated under section 11(2). One such provision is section 11(2)(f) which allows a reinsurer to zero-rate the taxable supply of reinsurance to a non-resident cedent if the insured risk (that is, the "book" of the cedent) is located outside the Republic and the reinsurer meets the documentary requirements in **8.5.1**. This means that the South African reinsurer may zero-rate the supply of foreign reinsurance inward services to a non-resident short-term insurance company.

It is important to note that the claims risk insured by the reinsurer is one step removed from the underlying risk insured by the cedent. It follows that the location of the cedent's business (insurance book / portfolio) will determine whether section 11(2)(f) may be applied and not the location of each individual underlying risk insured by the cedent. Reinsurance services supplied by a South African reinsurer to a South African cedent would therefore be subject to the standard rate of VAT regardless of where the underlying insured goods are located.

8.6.2 Cedent

A cedent may reinsure its claims risk with a South African or non-resident reinsurer. VAT registered cedents may, under section 16(3)(a), deduct VAT charged by a VAT registered reinsurer in respect of reinsurance services to the extent these premiums relate to short-term insurance risks which are reinsured and the documents referred to in **8.5.2** are retained.

Cedents may not deduct input tax in respect of reinsurance premiums paid to non-resident reinsurers if South African VAT was not levied by the non-resident reinsurer. Outward reinsurance does not give rise to VAT on imported services, as defined in section 1(1), as the cedent acquires the services in the course of making taxable supplies, being the taxable supply of short-term insurance.

Example 7 – Reinsurance premiums*Facts:*

Mr B is a South African resident who owns game farms in South Africa and Namibia. Mr B insures his game viewing vehicles with Insurer A (a South African short-term insurance company which is a vendor). Half of the game viewing vehicles are permanently used in Namibia. Insurer A reinsures 50% of its game viewing vehicle insurance portfolio with Reinsurer C. Reinsurer C is registered for VAT in South Africa.

Result:

Reinsurer C must levy 14% VAT on the full reinsurance premium as the claims risk linked to Insurer A's insurance book is located in South Africa.

Insurer A may deduct the input tax incurred in respect of the reinsurance service supplied by Reinsurer C.

8.7 Cedent commission

Even though the reinsurer takes over the claims risk (or part thereof) from the cedent, the cedent performs the majority of the services to manage and administer the underlying policies. The cedent incurs marketing and sales costs to attract potential policy holders and also assesses the validity of a claim before submitting it to the reinsurer. Reinsurers generally accept claims submitted by the cedent without investigating the underlying claim from the insured as the reinsurer relies on the cedent's processes and controls. In order to compensate the cedent for these services rendered, the reinsurer will pay cedent commission. In practice, the cedent withholds the cedent commission before paying the net proceeds over to the reinsurer.

8.7.1 Cedent

The supply of cedent services (including administrative and other services) to a reinsurer is a taxable supply which is generally subject to VAT at the standard rate. The supply may, however, be zero-rated under section 11(2)(l) if the services are supplied to a non-resident reinsurer located outside South Africa.

8.7.2 Reinsurer

VAT registered reinsurers may, under section 16(3)(a), deduct input tax in respect of any cedent services acquired, provided that –

- the cedent is a registered VAT vendor who levied VAT at 14% on the supply of cedent services;
- the reinsurer acquired the cedent services wholly in the course of supplying short-term reinsurance; and
- the reinsurer retains the relevant supporting documents such as the tax invoice (including a bordereau).

A reinsurer may therefore not deduct input tax in respect of cedent services provided under an inwards reinsurance contract as these services would have been acquired from a non-resident who is not a VAT vendor which would not have charged South African VAT on its supplies. These services would not constitute imported services to the extent that the reinsurer acquired those services wholly for the purpose of providing short-term reinsurance services.

8.8 Indemnity payments

Once a cedent submits a valid claim under a reinsurance contract, the reinsurer will indemnify the cedent for the loss incurred as a result of the claim submitted by the cedent's client. The cedent may submit an insurance claim to cover an indemnity payment made to its client or a trade payment made to a third party supplier to repair the underlying insured goods. The indemnification is however limited to the ultimate loss incurred by the cedent. The ultimate loss is determined by reducing the cedent's claim against the reinsurer by any subsequent recoveries received by the cedent from third parties in respect of the claim. (See 8.9.)

8.8.1 Reinsurer

A reinsurer that is a vendor may, under section 16(3)(c), deduct an amount equal to the tax fraction ($14 / 114$) of any amount paid to indemnify the cedent under a reinsurance contract. This deduction is determined by applying the tax fraction to the total value of indemnity payments made during the tax period less any recoveries received from the cedent during that tax period.⁴⁵ The deduction will however not be permissible if the payment was made in respect of –

- a supply of reinsurance that was not a taxable supply; or
- the supply of reinsurance which was zero rated under section 11(2) where the cedent, at the time of the payment, is not a vendor and not a resident of South Africa.

8.8.2 Cedent

The cedent, being a vendor, is required to account for output tax in respect of the indemnity payment received [that is, a deemed supply of services under section 8(8)], to the extent that the payment relates to a loss incurred in the course of carrying on the cedent's enterprise. This service is deemed to be supplied on the day the cedent (or the cedent's broker) receives the indemnity payment. The cedent's output tax liability in respect of indemnity payments received during a tax period is determined by applying the tax fraction to the total value of indemnity payments received during the tax period less any recoveries paid to a reinsurer during that tax period. (Recoveries are dealt with in 8.9.)

The provisions of section 8(8) will not apply if the cedent services supplied under the reinsurance contract were not taxable supplies under section 7(1)(a). The cedent will therefore not be liable to account for output tax when an indemnity payment is received from a reinsurer that is not a vendor. This is on the basis that, in this instance, the reinsurer's supply of reinsurance services would have been out-of scope and no South African VAT would have been charged in respect thereof.

⁴⁵ Paragraph 2.3 of BGR 32.

8.9 Recoveries

Recoveries under a reinsurance contract differ from recoveries in the normal short-term insurance relationship between short-term insurers and their clients. In the case where a short-term insurer exercises its right to subrogation and recovers the loss (or part thereof) related to a claim submitted by an insured, the short-term insurer is under no obligation to pay any further amounts to the insured who has already been indemnified. However, under a contract of reinsurance, the cedent is obliged to pay the recovery (or relevant part thereof) to the reinsurer as the reinsurer is only liable to indemnify the ultimate loss incurred by the cedent. The recovery reduces the claim previously submitted and is therefore treated as an adjustment to the indemnity payment previously made to the cedent.

8.9.1 Reinsurer

On the basis that the recovery reduces the value of the indemnity payment made by the reinsurer to the cedent, the reinsurer is required to decrease the VAT amount previously deducted in respect of the indemnity payment made to the cedent.⁴⁶ This adjustment should be made by the reinsurer in the tax period during which the recovery is –

- received from the cedent; or
- the recovery is set-off against indemnity payments made to the cedent, whichever is earlier.

The reinsurer is therefore not liable to account for output tax on recoveries to the extent the recovery is set off against indemnity payments. See paragraph 2.4 of BGR 32 for more information.

8.9.2 Cedent

Under section 21(2)(b) the cedent must adjust the output tax previously declared⁴⁷ in respect of the indemnity payment received from the reinsurer by applying the tax fraction to the amount recovered and paid to the reinsurer. The cedent may, however, not deduct the tax fraction of recovered amounts paid to a reinsurer to the extent this amount is set off against indemnity payments received from that reinsurer. The cedent is required to retain the relevant bordereau reflecting the recovery as well as proof that the recovery was paid to the reinsurer to substantiate the adjustment.

The VAT treatment of recoveries is illustrated in the next example.

Example 8 – VAT treatment of recoveries

Facts:

Insurer A (a short-term insurance company which is a vendor), supplies Vendor B (the insured) with insurance cover under a policy of insurance, to cover any damage or loss to a delivery truck. Insurer A (the cedent) reinsured 50% of its motor insurance portfolio to Reinsurer C. The reinsurance contract stipulates that all recoveries in respect of reinsured policies have to be remitted to Reinsurer C in proportion to the risk reinsured.

⁴⁶ Section 16(3)(c).

⁴⁷ Section 8(8) read with section 7(1)(a).

The truck is subsequently damaged in an accident and Insurer A makes an indemnity payment on 20 May 2015 to Vendor B of R 22 800. Insurer A submits a claim to Reinsurer C who indemnifies Insurer A on 31 May 2015. Insurer A subsequently exercises its right to subrogation and recovers R10 000 on 15 July 2015 from Mr D who caused the accident in which the truck was damaged. Insurer A sells the damaged truck as scrap metal on 31 July 2015 for R5 700 (including VAT). Insurer A pays the relevant portion of the amounts recovered to Reinsurer C on 15 August 2015.

Vendor B, Insurer A and Reinsurer C account for VAT on a monthly basis. For purposes of this example, cedent commission may be ignored.

Result:

Vendor B

Vendor B is required to account for output tax under section 8(8) in respect of the indemnity payment received from Insurer A. B therefore has to include $R22\,800 \times 14/114 = R2\,800$ in its May 2015 VAT return.

Insurer A

May 2015 tax period

Insurer A may deduct the tax fraction of the indemnity payment made to Vendor B in its May 2015 VAT return, that is $R22\,800 \times 14/114 = R2\,800$. Insurer A will however also submit a claim to Reinsurer C in respect of a portion of the amount paid to indemnify Vendor B.

Insurer A is required to account for output tax under section 8(8) in respect of the indemnity payment received from Reinsurer B, as follows:

$$R22\,800 \times 50\% \times 14/114 = R1\,400.$$

July 2015 tax period

The recovery of R10 000 during July 2015 by Insurer A does not constitute consideration for a taxable supply. Insurer A is not liable to account for output tax in respect of this amount.

As a vendor, Insurer A is liable to account for output tax on the sale of scrap during the July 2015 tax period as follows:

$$5\,700 \times 14 / 114 = R700.$$

August 2015 tax period

In terms of the reinsurance contract, Insurer A is liable to pay 50% of the recoveries to Reinsurer C. The total amount recovered consists of the amount recovered from Mr D as well as the consideration received when the scrap metal was sold. Insurer A therefore has to pay the following amount to Reinsurer C $(R10\,000 + R5\,000) \times 50\% = R8\,200$. Insurer A may set off the VAT portion of the recovered amount paid over to the reinsurer against output tax accounted for on indemnity payments received during August 2015. The amount that may set off is calculated as follows:

$$(R10\,000 + R5\,000) \times 50\% \times 14 / 114 = R921.$$

Reinsurer C

Reinsurer C may deduct the tax fraction of the indemnity payment made to Insurer A in its May 2015 VAT return. The deduction is calculated as follows: $R11\,400 \times 14 / 114 = R1\,400$.

On receipt of the amounts recovered from Insurer A, Reinsurer C may set off the VAT portions of the recovered amount against the output tax accounted for on indemnity payments made in that tax period before determining the amount to be deducted under section 16(3)(c).

8.10 Reinsurance broker commission and fees

Reinsurance brokers may supply intermediary services as well as other services to reinsurers and cedents. Consideration is usually charged in the form of commission and fees.

8.10.1 Reinsurance broker

The reinsurance broker must account for output tax on the supply of intermediary and other services according to the general time of supply rule. (See **3.6**.) In the case of upfront commission and fees, the reinsurance must declare output tax on the full commission or fee received.

This rule applies irrespective of whether the commission or fee is deducted from premiums or other amounts collected on behalf of the reinsurer / cedent or payment is made directly by the reinsurer / cedent to the reinsurance broker. The bordereau must meet the requirements set out in **4.4**. (See paragraphs 2.12 and 2.13 of BGR 14.)

Zero-rating

Generally, reinsurance brokers that are vendors must account for VAT at the standard rate on commission and fees charged unless the supply qualifies to be charged with VAT at the zero rate under section 11(2). A VAT registered reinsurance broker may, for example, zero-rate the supply of services to a non-resident cedent under section 11(2)(f), provided all the requirement of that section are met.

8.10.2 Short-term reinsurer or cedent

The reinsurer / cedent is entitled to deduct the VAT paid on the commission or other fees charged by the reinsurance broker as input tax if the reinsurer / cedent is a vendor. This is based on the assumption that the short-term insurer will use or consume these services wholly for making taxable supplies in the course of supplying short-term insurance.

Annexure A – Binding General Ruling (VAT) 14 (Issue 2)

BINDING GENERAL RULING (VAT) 14 (Issue 2)

DATE: 18 March 2016

ACT : VALUE-ADDED TAX ACT NO. 89 OF 1991

SECTION : SECTIONS 1(1), 7, 8, 9, 11, 16, 20, 21, 54 AND 72

SUBJECT : VAT TREATMENT OF SPECIFIC SUPPLIES IN THE SHORT-TERM INSURANCE INDUSTRY

Preamble

For the purposes of this ruling, unless the context indicates otherwise –

- **“BGR”** means a binding general ruling issued under section 89 of the Tax Administration Act No. 28 of 2011 (TA Act);
- **“bordereau”** means a document issued by an insurer or intermediary in the form of a memorandum, statement or invoice which contains detailed information such as –
 - insurance premiums collected;
 - commission and fees payable in respect of intermediary services supplied; and
 - claims paid.
- **“inbound policy”** means a transport policy which provides insurance cover in respect of goods transported from an export country to South Africa as part of an international voyage;
- **“indemnity payment”** means a cash payment made by the insurer under an insurance policy to indemnify the insured on the occurrence of the insured event;
- **“insurer”** means any vendor supplying “insurance” as defined in section 1(1);
- **“intermediary”** means any broker or agent supplying intermediary services to an insurer or insured;
- **“intermediary services”** has the meaning assigned thereto in section 1 of the Financial Advisory and Intermediary Service Act No. 37 of 2002 and includes the management and administration of a policy as well as the collection of premiums and processing of claims;
- **“international voyage”** means the transportation of goods from the insured’s premises (or other named location) in South Africa to a destination in another country (and *vice versa*) or between two places outside the Republic. The international voyage includes transit to packers, forwarders, consolidators, hauliers, warehouses and other places of storage until the goods are safely delivered at the final destination as specified in the insurance contract;
- **“outbound policy”** means a transport policy which provides insurance cover in respect of goods transported from South Africa to a destination in an export country or from a place outside South Africa to another destination outside South Africa as part of an international voyage;

- “**policy document**” means a document which is evidence of a contract of insurance, including any renewal notice, premium notification or endorsement in respect thereof;
- “**section**” means a section of the VAT Act;
- “**temporary presence**” means a period of six months or less;
- “**third party supplier**” means a supplier of goods or services receiving trade payments from insurers;
- “**trade payment**” means a payment made under a contract of insurance by an insurer to a third party supplier to replace or repair the insured’s goods which were lost, damaged or destroyed;
- “**VAT**” means value-added tax;
- “**VAT Act**” means the Value-Added Tax Act No. 89 of 1991; and
- any other word or expression bears the meaning ascribed to it in the VAT Act.

1. Purpose

This BGR sets out the VAT treatment of the issues listed below:

- The time of supply in relation to the supply of insurance and related intermediary services
- International transport insurance including stock throughput, goods in transit and marine insurance policies
- Hull and associated liability insurance
- Insurance cover provided in respect of fixed property and movable property located in an export country
- Excess payments
- Indemnity payments
- Third party payments
- Recoveries
- Group accident claims
- Intermediary services
- Documents accepted as alternatives to tax invoices in respect of the supply of insurance and related intermediary services
- Approval to issue recipient-created tax invoices, debit and credit notes

This BGR replaces and withdraws BGR 14 dated 22 March 2013 “VAT treatment of specific supplies in the short-term insurance industry” with effect from the dates specified in **3**.

It is recommended that this BGR is read in conjunction with the *VAT 421 – Guide for Short-Term Insurance*.

2. Ruling

This ruling constitutes a BGR issued under section 89 of the Tax Administration Act No. 28 of 2011.

2.1 Time of supply – Insurance

An insurance policy, renewal notice or endorsement that does not notify the insured of an obligation to make payment is not regarded as an invoice and will therefore not trigger the time of supply. In instances where the insurer (or its intermediary) does not issue an “invoice”, the supply of insurance is deemed to be on the date the insurer (or the insurer’s intermediary) receives the insurance premium in respect of that supply.

2.2 International transport insurance

The supply of insurance under inbound and outbound policies, including insurance cover during periods in which “ancillary transport services”⁴⁸ are supplied, may be zero-rated under section 11(2)(d).

2.3 Stock throughput insurance

The supply of stock throughput insurance is regarded as international transport insurance (see **2.2**) to the extent that insurance cover is provided in respect of goods transported from an export country to South Africa (and *vice versa*) as part of an international voyage.

2.3.1 Insured goods transported or stored in South Africa

The supply of insurance under a stock throughput policy which provides cover for insured goods whilst the goods are transported between places in South Africa (including periods during which “ancillary transport services” are supplied in respect of those goods) is subject to VAT at the zero rate under section 11(2)(d). The zero rating is only applicable if the transport service (including any “ancillary transport services”) is supplied by the same supplier providing the international transport services as envisaged by section 11(2)(c).

2.3.2 Insured goods in South Africa but not transported or stored

Insurance cover provided while insured goods are in South Africa and not being transported (or stored) as part of an international voyage does not qualify for zero rating under section 11(2)(d). Such supplies are therefore subject to VAT at the standard rate under section 7(1)(a).

2.3.3 Single insurance premium

Insurers that levy a single premium in respect of the single supply of stock throughput insurance relating to both standard and zero-rated supplies are, under section 8(15), required to allocate the premium to the various risk components which were used to determine the premium and to apply the applicable VAT rate to each component. The same ratio must be used in respect of subsequent adjustments to the premium, unless the insurer can determine the allocation more accurately. The insurer is required to notify the insured and, where applicable, the intermediary of the original allocation of the premium between the standard and zero-rated portions as well as

⁴⁸ “Ancillary transport services” include storage of the insured goods while being (or to be) transported.

any subsequent adjustments in respect thereof. The insurer is required to retain proof of such notification.

2.4 Hull insurance

The supply of hull insurance is regarded as a service provided in connection with the operation or management of a “foreign-going aircraft” or “foreign-going ship”, and may therefore be zero-rated under section 11(2)(h)(ii) if supplied directly (that is, not through an agent or other person) to a non-resident that is not a vendor.

The temporary presence of the underlying insured foreign-going ship or aircraft in South Africa will not disqualify the supply from being zero-rated.

2.5 Insurance cover for fixed property situated in an export country

Insurance is regarded as being supplied directly in connection with the insured land, or any improvement to it, situated in an export country and is therefore subject to VAT at the zero rate under section 11(2)(f).

2.6 Insurance cover for movable property situated in an export country

Insurance is regarded as being supplied directly in respect of the insured movable property and is subject to VAT at the zero rate under section 11(2)(g)(i), provided that the insurer obtains and retains proof that the movable property is situated outside South Africa during the period for which the insurance cover is provided. Such proof may be reflected in the insurance contract or a declaration provided by the insured.

The temporary presence of the movable property in South Africa will not disqualify the supply of insurance relating to the property from being zero-rated.

2.7 Excess payments

2.7.1 Insured pays excess directly to third party supplier

The third party supplier must issue two tax invoices, that is, one to the insured to the extent of the excess payment and one to the insurer to the extent of the trade payment.

2.7.2 Insurer pays full amount to third party service provider and recovers excess from insured

An excess payment received by an insurer from the insured does not constitute “consideration” as the payment is not received in respect of any taxable supply made by the insurer. The insurer is, however, required to issue documentation to the insured in respect of the receipt of the excess payment which must include the following minimum information:

- (a) The insurer’s name, VAT registration number and address.
- (b) The insured’s name, VAT registration number (where applicable) and address.
- (c) The third party supplier’s name and VAT registration number (where applicable).
- (d) A full description of the goods or services supplied by the third party service provider.
- (e) The date on which the supply was made by the third party service provider.

- (f) The amount of the excess paid or payable by the insured reflecting either the VAT amount separately or a statement that the amount payable includes VAT and the rate at which VAT was charged.

The insurer is, under section 16(3)(a), entitled to deduct input tax on the goods or services acquired from the third party supplier. The deduction must be calculated as follows:

(Total VAT inclusive amount paid to the third party supplier less excess received from insured) × tax fraction.

The insured may deduct the VAT incurred in relation to the excess payment made to the insurer. The deduction is calculated as follows:

Excess payment × tax fraction.

An arrangement is made under section 72 to regard the document issued by the insurer to the insured in respect of excess received or due to be a “tax invoice” for the purposes of section 16(2)(a). This arrangement is only applicable if –

- (i) the insured is a registered vendor;
- (ii) the third party supplier is a registered vendor; and
- (iii) the insured and insurer obtains and retains the document issued by the insurer in respect of the excess payment.

2.8 Indemnity payments

The input tax deduction allowed under section 16(3)(c) applies not only to indemnity payments made in respect of “indemnity insurance” cover, but also in respect of “non-indemnity insurance” such as personal accident and third party liability cover that may be included in an insurance policy.

An insurer making an indemnity payment which gives rise to a deduction under section 16(3)(c) must issue a document to the insured informing the insured of a potential output tax liability that may arise under section 7(1)(a) read with section 8(8). This requirement applies irrespective of whether the insured is a vendor or not.

2.9 Recoveries

An insurer is not liable to account for output tax on amounts recovered from a third party or the third party’s insurer under a subrogation claim, irrespective of whether the whole or only a portion of the claim is recovered.

2.10 Group personal accident insurance

2.10.1 Insurer

An insurer may deduct VAT under section 16(3)(c) in respect of indemnity payments made to the insured under group personal accident insurance.

2.10.2 Employer acting as principal

An employer, being a vendor, may deduct input tax in respect of the taxable supply of group personal insurance acquired to the extent it is acquired for the purpose of making taxable supplies.

Any indemnity payments received by the employer (as principal) under a contract of insurance will result in the employer being liable to account for output tax under section 8(8). The employer will not be entitled to deduct any VAT in respect of amounts subsequently paid to the employee.

2.10.3 Employer acting as agent on behalf of employees

The employer, when acting as the agent of its employees in entering into a group personal accident insurance contract with an insurer, will not be entitled to deduct input tax in respect of that contract. The employer will not be required to account for output tax under section 8(8) if the employee receives an indemnity payment from the insurer, irrespective of whether the payment is made through the employer or directly to the employee.

2.11 Intermediary services

The zero rate may be applied to services consisting of the arranging of –

- the insurance of goods or passengers transported internationally⁴⁹ under section 11(2)(d); or
- hull⁵⁰ insurance in respect of a foreign-going aircraft or ship under section 11(2)(i)(ii) if the arranging service is supplied to a non-resident who is not a vendor (refer to 2.4).

An intermediary arranging stock throughput insurance may however only zero rate the supply of intermediary services to the extent that the underlying stock throughput insurance qualifies for zero rating under section 11(2)(d). (Refer to 2.3.3.)

2.12 Tax invoices, credit and debit notes

2.12.1 Supply of insurance

The Commissioner directs, under section 20(7)(a) and 21(5)(a), that the policy document, although not an invoice, is regarded as a tax invoice, debit note and credit note which need not contain the words “tax invoice”, “VAT invoice”, “invoice”, “debit note” and “credit note” provided –

- the insurer retains proof that the insured paid premiums in accordance with the policy document; and
- the policy document reflects all the other information as required by section 20(4); and
- the policy document contains the following statement (or substantially similar wording):

“In terms of Binding General Ruling No. 14 this document constitutes a tax invoice, debit note and credit note as contemplated in sections 20(7)(a) and 21(5)(a) of the VAT Act.”

⁴⁹ Refer to 2.2, , 2.3 and 2.5.

⁵⁰ Refer to 2.4.

2.12.2 Supply of intermediary services

The Commissioner directs, under sections 20(7)(a) and 21(5)(a), that the document (generally known as a bordereau) issued by the intermediary to the insurer in respect of the supply of intermediary services does not have to contain the words “tax invoice”, “VAT invoice”, “invoice”, “credit note” or “debit note”, as the case may be, provided the bordereau reflects the other information required by sections 20(4) and 21(3) respectively.

2.13 Recipient-created tax invoices, credit and debit notes

An insurer that is required to determine the consideration payable in respect of intermediary services may, under sections 20(2) and 21(4), issue recipient-created tax invoices, credit or debit notes in respect of the supply of intermediary services.

This approval is subject to –

- the recipient-created tax invoice, credit or debit note complying with sections 20(4), (5), 21(3) or the special approval set out in **2.12**, as applicable; and
- the insurer complying with all other requirements listed in Interpretation Note No. 56 “Recipient-created tax invoices, credit and debit notes”.

In addition, permission is granted under sections 20(7)(a) and 21(5)(a) that the bordereau issued by the insurer to the intermediary in respect of the supply of intermediary services does not have to contain the words “tax invoice”, “VAT invoice”, “invoice”, “credit note” or “debit note” (as the case may be).

2.14 Conditions

2.14.1 Zero rating

The zero rating of supplies contained in this BGR is conditional upon the insurer and intermediary (as applicable) obtaining and retaining the documentary proof as provided for under section 11(3) read with Interpretation Note No. 31 “Documentary Proof Required for the Zero Rating of Goods and Services” (Interpretation Note No. 31). Failure to obtain and retain the required documentary proof within the required time period will result in the vendor being required to make the relevant adjustments as stipulated in Interpretation Note No. 31.

2.14.2 Input tax and other deductions

The statements contained in this BGR regarding input tax and other deductions are conditional upon the vendor obtaining and retaining the documentary proof contemplated in section 16(2) (including the bordereau referred to in **2.12**) by the time the relevant VAT return is submitted. The deductions are subject to section 16 and 17. Failure to obtain and retain the required documentary proof will result in the vendor not being entitled to make the deduction.

3. Period for which this BGR is valid

This BGR is effective in respect of policy documents entered into on or after 1 June 2016. The following paragraphs will however only apply from 1 September 2016:

- **2.3.**
- **2.6** to the extent that the required proof must be obtained from an insured.
- **2.7.2** to the extent of information to be reflected on the notification.
- **2.8.1** to the extent of the requirement that the insurer must notify the insured of the potential output tax liability in relation to indemnity payments.

This BGR will apply from the date of issue until it is withdrawn, amended or the relevant legislation is amended.

To the extent that this BGR does not provide for a specific scenario in respect of the supply of short-term insurance, vendors may apply for a VAT ruling or VAT class ruling in writing by sending an e-mail to **VATRulings@sars.gov.za** or by facsimile to 086 540 9390. In this regard a clearly motivated application complying with the provisions of section 79 of the Tax Administration Act, excluding section 79(4)(f) and (k) and (6), must be submitted.

Senior Manager: Indirect Taxes
Legal and Policy Division
SOUTH AFRICAN REVENUE SERVICE
Date of 1st issue : 23 March 2016

Annexure B – Binding General Ruling (VAT) 32

BINDING GENERAL RULING (VAT) 32

DATE: 18 March 2016

ACT : VALUE-ADDED TAX ACT NO. 89 OF 1991

SECTION : SECTIONS 1(1), 7, 8, 9, 11, 16, 20 AND 21

SUBJECT : VAT TREATMENT OF SPECIFIC SUPPLIES IN THE SHORT-TERM REINSURANCE INDUSTRY

Preamble

For the purposes of this ruling, unless the context indicates otherwise –

- **“BGR”** means a binding general ruling issued under section 89 of the Tax Administration Act No. 28 of 2011;
- **“bordereau”** means a document issued by a cedent, intermediary or reinsurer in the form of a memorandum, statement or invoice which contains detailed information such as –
 - reinsurance premiums collected;
 - claims paid; and
 - fees and commission payable in respect of intermediary services supplied;
- **“cedent”** means the short-term insurer that reinsures part, or all, of its claims risk associated with insurance policies held;
- **“cedent commission”** means the amount paid or payable by a reinsurer to the cedent in terms of a reinsurance contract;
- **“claims risk”** means the risk of the cedent incurring a loss as a result of paying a claim submitted by its client under a policy of insurance;
- **“facultative reinsurance”** means the reinsurance of a single risk or a defined package of risks which are individually underwritten by the reinsurer;
- **“indemnity payment”** means a cash payment made under a contract of reinsurance by the reinsurer to the cedent to indemnify the cedent in respect of a reinsured claims risk;
- **“intermediary”** means the reinsurance broker who serves as agent of the reinsurer to facilitate reinsurance contracts;
- **“intermediary services”** has the meaning assigned thereto in section 1 of the Financial Advisory and Intermediary Service Act No. 37 of 2002 and includes the management and administration of a policy as well as the collection of premiums and processing of claims on behalf of the cedent or reinsurer;
- **“inward reinsurance”** means the acceptance of any reinsurance risk by a South African reinsurer under a contract with a non-resident cedent;
- **“local reinsurance”** means reinsurance services supplied by a South African reinsurer to a South African cedent;

- **“non-proportional treaty reinsurance”** is also known as excess reinsurance and involves the reinsurer bearing risk once the cedent's loss exceeds an agreed threshold;⁵¹
- **“proportional treaty reinsurance”** is treaty reinsurance which involves the proportional sharing of risk;
- **“recoveries”** means any amount paid or payable by a cedent to a reinsurer, in accordance with a reinsurance contract, through the exercising of the cedent's right of subrogation or the sale of salvaged insured goods;
- **“reinsurance”** means short-term insurance in terms of which the cedent reinsures part, or all, of its claims risk associated with insurance policy documents with a reinsurer. For purposes of this BGR, reinsurance includes retrocession, facultative and treaty reinsurance;
- **“reinsurance contract”** means a document which is evidence of a contract of reinsurance, including any renewal notice, premium notification, slip, certificate or endorsement in respect thereof;
- **“reinsurance premium”** means the consideration paid or payable by the cedent to the reinsurer in respect of a supply of reinsurance service;
- **“reinsurer”** means the person that supplies short-term reinsurance to a cedent under a reinsurance contract;
- **“retrocession”** means an agreement in terms of which a reinsurer transfers reinsured risks to another reinsurer;
- **“section”** means a section of the VAT Act;
- **“treaty reinsurance”** means reinsurance provided under a pre-negotiated agreement between the cedent and the reinsurer in terms of which the cedent agrees to cede all risks within a defined class or classes to the reinsurer and, in return, the reinsurer agrees to provide reinsurance on all risks ceded without individual underwriting.
- **“VAT”** means value-added tax;
- **“VAT Act”** means the Value-Added Tax Act No. 89 of 1991; and
- any other word or expression bears the meaning ascribed to it in the VAT Act.

1. Purpose

This BGR deals with the following:

- Taxable supplies made by reinsurers, cedents and intermediaries.
- Reinsurance claims and recoveries.
- The time of supply in relation to the supply of short-term reinsurance, intermediary services and cedent services.
- Information to be reflected on a tax invoice, debit and credit note as contemplated in sections 20(7) and 21(5) respectively, in respect of the supply of short-term reinsurance, cedent services and the related intermediary services.
- Approval to issue recipient-created tax invoices, debit and credit notes.

⁵¹ Reinecke MFB et al *General Principles of Insurance Law* (2002) LexisNexis in paragraph 526.

It is recommended that this BGR is read in conjunction with the *VAT 421 – Guide for Short-Term Insurance*.

2. Ruling

This ruling constitutes a BGR issued under section 89 of the Tax Administration Act No. 28 of 2011.

2.1 Reinsurance premiums

The taxable supply of reinsurance by a local reinsurer to a non-resident cedent is subject to VAT at the zero rate under section 11(2)(f).

2.2 Cedent commission

The supply of cedent services to a non-resident reinsurer may be zero-rated under section 11(2)(f), provided the requirements of that section are met.

2.3 Indemnity payments

A reinsurer's deduction in respect of indemnity payments under section 16(3)(c), must be reduced by the tax fraction of any recoveries received from the South African cedent during that tax period.

A cedent's output tax liability in respect of indemnity payments received during a tax period is determined by applying the tax fraction to the total value of indemnity payments received during the tax period less any recoveries paid to a VAT-registered reinsurer during that tax period.

2.4 Recoveries

A reinsurer is not liable to account for output tax on recoveries received to the extent the amount is offset against indemnity payments made by the reinsurer as contemplated in **2.3**.

The cedent may not deduct the tax fraction of recovered amounts paid to a reinsurer to the extent this amount is offset against indemnity payments received.

2.5 Time of supply

2.5.1 Supply of short-term reinsurance

The reinsurance contract or any other document disclosing the premium amount without imposing an obligation to make payment is not regarded as an invoice.

Facultative and non-proportional treaty reinsurance

Facultative and non-proportional treaty reinsurance are deemed, under section 9(1), to be supplied at the earlier of the time a bordereau is issued or consideration is received in respect of that supply, unless the reinsurance contract requires the premiums to be paid periodically. In this instance, the reinsurance services are, under section 9(3)(a), deemed to be successively supplied when (and to the extent) that the premiums become due or are received, whichever is earlier.

Proportional treaty reinsurance

The time of supply in respect of the supply of proportional treaty reinsurance is, under section 9(4)(b), when and to the extent that any payment in terms of the reinsurance contract is due or is received, or the bordereau relating to that supply is issued by the supplier or the recipient, whichever is earliest.

2.5.2 Supply of intermediary or cedent services

The supply of intermediary and cedent services is deemed to take place, under section 9(1), at the earlier of the time payment is received or an invoice (including a bordereau referred to in **2.6**) is issued in respect of that service.

2.6 Tax invoices, credit and debit notes

The Commissioner directs under sections 20(7)(a) and 21(5)(a), that the document (generally known as a bordereau) issued by the reinsurer, cedent or intermediary in respect of the supply of reinsurance, intermediary and cedent services does not have to contain the words “tax invoice”, “VAT invoice”, “invoice”, “credit note” or “debit note”, as the case may be, provided the document reflects all the other information as required by section 20(4) or 21(3).

In the case of local reinsurance, the bordereau must contain the following statement (or substantially similar wording) confirming the Commissioner’s direction under section 20(7) and 21(5), as the case may be:

“In terms of Binding General Ruling No. 32 this document constitutes a tax invoice, debit note or credit note as contemplated in sections 20(7)(a) and 21(5)(a) of the VAT Act respectively.”

Intermediaries are, under section 20(1), required to issue tax invoices in respect of any other taxable supplies made to their clients, unless these supplies are reflected in the relevant bordereau.

2.7 Recipient-created tax invoices, credit and debit notes

Reinsurers, intermediaries, reinsurance brokers and cedents that are required to determine the consideration payable in respect of reinsurance, intermediary or cedent services may, under sections 20(2) and, where applicable, 21(4), issue recipient-created tax invoices, credit and debit notes. This decision is on condition that the recipient of the services complies with the requirements of Interpretation Note No. 56 “Recipient-Created Tax Invoices, Credit and Debit Notes” and that the bordereau contains the information stipulated in **2.6**.

2.8 Conditions**2.8.1 Zero rating**

The zero rating of supplies contained in this BGR is conditional upon the reinsurer, cedent or intermediary (as applicable) obtaining and retaining the documentary proof as provided for under section 11(3) read with Interpretation Note No. 31 “Documentary Proof Required for the Zero-Rating of Goods and Services” (Interpretation Note No.31). Failure to obtain and retain the required documentary proof within the required time period will result in the vendor being required to make the relevant adjustments as stipulated in Interpretation Note No.31.

2.8.2 Input tax and other deductions

The statements contained in this BGR regarding input tax and other deductions are conditional upon the vendor obtaining and retaining the documentary proof contemplated in section 16(2) (including the bordereau referred to in **2.6**) by the time the relevant VAT return is submitted. Failure to obtain and retain the required documentary proof will result in the vendor not being entitled to the deduction.

3. Period for which this ruling and decision are valid

This BGR is effective in respect of policy documents entered into on or after 1 June 2016. The following paragraphs will however only apply from 1 September 2016:

- 2.6 to the extent of the statement to be reflected on the bordereau.
- 2.7 to the extent of the written agreement regarding recipient-created tax invoices, debit and credit notes to be reflected on the bordereau as are required by Interpretation Note No.56.

This BGR applies from date of issue until it is withdrawn, amended or the relevant legislation is amended.

To the extent that this BGR does not provide for a specific scenario in respect of the supply of short-term reinsurance, vendors may apply for a VAT ruling or VAT class ruling in writing by sending an e-mail to **VATRulings@sars.gov.za** or by facsimile to 086 540 9390. In this regard a clearly motivated application complying with the provisions of section 79 of the Tax Administration Act No. 28 of 2011 excluding section 79(4)(f) and (k) and (6), must be submitted.

Senior Manager: Indirect Taxes
Legal and Policy Division
SOUTH AFRICAN REVENUE SERVICE

Annexure C – Binding General Ruling (VAT) 37

BINDING GENERAL RULING (VAT) 37

DATE: 12 December 2016

ACT : VALUE-ADDED TAX ACT 89 OF 1991

SECTION : SECTIONS 11 AND 72

SUBJECT : ZERO-RATING OF INTERNATIONAL TRAVEL INSURANCE

Preamble

For the purposes of this ruling –

- **“BGR”** means a binding general ruling issued under section 89 of the Tax Administration Act 28 of 2011;
- **“inbound policy”** means a travel policy which provides insurance cover in respect of a passenger transported from an export country to South Africa or between two places in South Africa as part of an international journey;
- **“international journey”** means a journey commencing from the “point of departure” in South Africa to a destination outside South Africa (and *vice versa*), including (where applicable) stopovers *en route* to the destination, time spent in the destination country and the return journey;
- **“outbound policy”** means a travel policy which provides insurance cover in respect of a passenger transported from South Africa to a destination in an export country or from a place outside South Africa to another destination outside South Africa as part of an international journey;
- **“point of departure”** means the insured person’s normal place of business, residence or other location from where the insured person departs to commence an “international journey” in a direct and uninterrupted manner;
- **“policy document”** means a document which is evidence of a contract of insurance, including any renewal notice, premium notification or endorsement in respect thereof;
- **“stopover”** means a stop, delay or brief stay as a result of a multi-staged international transport service supplied to the insured, which is less than 24 hours from the time of arrival to the commencement of the next stage of the international journey or longer period resulting from circumstances beyond the insured’s control such as flight delays;
- **“VAT”** means value-added tax;
- **“VAT Act”** means the Value-Added Tax Act 89 of 1991; and
- any other word or expression bears the meaning ascribed to it in the VAT Act.

1. Purpose

The purpose of this BGR is to make an arrangement under section 72 relating to the zero-rating of international travel insurance.

2. Background

A person travelling to an export country may obtain travel insurance to cover risks, such as medical care and lost baggage. The insurance is generally provided under an outbound or inbound insurance policy document which covers the entire journey or cover may be limited to a certain number of days that the insured is travelling. Insurers generally determine a single premium with reference to the insured's destination and the duration of cover required.

The supply of travel insurance while the insured is transported as part of an international journey qualifies for zero-rating under section 11(2)(d). This section does however not extend to zero-rating insurance cover provided during the period that the insured is –

- transported to and from the insured's original point of departure; and
- not being transported while on the international journey (for example, while the insured stays in a hotel).

Consequently, these insurance services would be subject to VAT at the standard rate, unless an arrangement is made under section 72. On the basis that, for all practical purposes, insurers regard the supply of international travel insurance as a single supply in respect of which a single premium is charged (irrespective of whether the insured is being transported or not) there is a difficulty in the application of the VAT Act.

3. Ruling

An arrangement is made under section 72 to allow insurers to zero rate travel insurance supplied in respect of an international journey which includes periods during which the insured is –

- outside South Africa but not being transported while on an international journey; and
- inside South Africa while *en route* to the place of departure from another place in South Africa as part of the international journey (and *vice versa*).

This arrangement will only apply if the cover is provided under a single outbound or inbound policy levying a single premium.

In instances where the local and international travel are covered by separate policies, only the supply of international travel insurance qualifies for zero-rating whereas the local travel insurance is subject to VAT at the standard rate.

This ruling constitutes a BGR issued under section 89 of the Tax Administration Act 28 of 2011.

4. Period for which this ruling is valid

This BGR applies from date of issue until it is withdrawn, amended or the relevant legislation is amended.

To the extent that this BGR does not provide for a specific scenario in respect of the supply of international travel insurance, vendors may apply for a VAT ruling or VAT class ruling in writing by sending an e-mail to VATRulings@sars.gov.za or by facsimile to 086 540 9390. The application should consist of a completed VAT301 form, a clearly motivated application and must comply with the provisions of section 79 of the Tax Administration Act 28 of 2011 excluding section 79(4)(f), (k) and (6).

Executive

Legal Counsel: Indirect Taxes

SOUTH AFRICAN REVENUE SERVICE

Annexure D – Legal principles of insurance

This annexure is purely for informational purposes and does not constitute legal advice.

1 Indemnity

Indemnity is one of the most fundamental principles of insurance law and is directly linked to the principle of insurable interest. Indemnification is described as the act of providing compensation for a loss where the clear intention is for restoration of the insured party to the financial position before the loss. The object of indemnity is, therefore, to restore the insured party after the loss, to the same position that the person occupied immediately before the loss occurred. The person should not be placed in a better or worse position. Indemnity is a process of taking over the responsibility for loss by the insurer in exchange for the payment of insurance premiums. Benefits are not set at a predetermined level or amount, but rather, are based on restoring the policyholder's financial position.

The following are some other important aspects of indemnity:

- Not all insurance contracts are contracts of indemnity. For example, life insurance is not an indemnity contract.
- The insured will not always be indemnified to the full extent of the loss, unless appropriate cover has been taken specifically to deal with those losses. These factors include under-insurance, the amount of the excess, inadequate sums insured as well as non-adherence to the terms of the policy. Account is also taken of depreciation in some policies. The principles of “average”, “contribution” and “subrogation” which impact on the concept of indemnity are dealt with below.
- Indemnity claims can be settled in a number of ways, including:
 - Monetary payment to the insured, or to a third party.
 - Reinstatement, replacement or repair of assets destroyed or damaged.
 - Unless the policy specifically makes provision for settling claims on a “new for old” basis, claims are settled on the actual value of the property at the time of the loss. In most cases, this value is determined by deducting an amount in respect of age and wear-and-tear.
 - Most insurance policies give insurers the right to decide whether to repair, replace or reinstate the damaged property or to pay its value in cash.

2 Insurable interest

Insurable interest is required for all types of insurance and is a characteristic which underlies the legitimacy of insurance business as distinguishable from gambling. The principle is that if the insured can show that there is a risk of losing something of appreciable commercial value by the loss or destruction of the thing insured, then the interest will be an insurable one. Also, as a general rule, insurable interest should exist at the time of taking out the policy as well as at the time the loss is incurred. This means, for example, that if a person has an insurable interest in an asset at the time of taking out the policy but subsequently disposes of that asset, the policy will immediately cease to be valid and enforceable in regard to that asset as there is no longer any insurable interest.⁵²

⁵² This applies in short-term insurance contracts. There are some exceptions with regard to insurable interests in long-term insurance contracts.

3 Duty of disclosure

Insurance contracts are based on the information provided by the insured, and generally, the insured will know more about the risk and circumstances concerning the asset to be insured than the insurer. Insurance law therefore requires that disclosure of information between the parties must take place with good faith (*bona fides*). This means that the parties must deal with each other openly and honestly and without suppressing material facts that may influence the judgment of the other party. As in the case of insurable interest, the duty to act in good faith applies to all types of insurance contracts.

The South African courts accept the need for disclosure but have rejected the definition of “materiality” as used in English law, which requires that every circumstance must be disclosed that would influence the judgment of a prudent insurer in fixing the premium or to determine whether cover for the risk will be provided under the policy.

The proper test of materiality in South Africa is the standard test of a reasonable person and not that of a prudent insurer. Failure to disclose material facts renders the contract voidable at the discretion of the insurer. However, the insured is only expected to disclose facts that are known, or that should reasonably be expected to be known.

4 Average

Average is a concept that applies when the insurer is of the view that the insured has insured the asset for less than its market value. The difference between the insured value and the market value is referred to as the amount “under-insured” or the “self-insured” amount. The principle of average means that if there is under-insurance, the insured party is regarded as its own insurer to the extent of the under-insurance. Consequently, the insured will be required to bear part of the loss as a penalty. The application of the principle of average is not automatic in law, but it will be found in most cases that insurers will include a clause in the policy for average to apply in the event of an indemnity claim. The principle of average only applies to contracts of indemnity and not to life insurance contracts.

Formula for average: $\frac{\text{Sum insured}}{\text{Market value}} \times \text{Loss sustained}$

Example – Application of the principle of average

Facts:

B has a homeowner’s insurance policy which covers loss or damage to B’s home in the event of a variety of perils occurring. B’s house has a market value of R500 000 but the house is only insured for R300 000.

Half of B’s house burns down in a fire and B makes a claim to the insurers for R250 000, being the estimated cost of repairing the damage to restore the house to its original condition.

Result:

Due to under-insurance, B will only be covered for 60 per cent (300 000/500 000) of losses if the policy has a clause relating to average. B would therefore only be entitled to claim R150 000 (60% × R250 000) whilst having to fund the rest of the loss (R100 000) in another manner.

5 Contribution

This principle applies when a person has insurance cover of the same type on the same asset under more than one policy. As the principle of indemnity forbids the insured from recovering more than the actual loss suffered, the insured cannot in such a case recover the full value of the loss from each of the policies. Under the principle of contribution, if the insured has cover under more than one policy from different insurers, the insured can claim indemnity from any of the insurers. The insurer that pays the indemnity can then claim a contribution from the other insurer(s) involved. Normally the insurers contribute on a *pro-rata* basis towards the loss, but in some cases they may be required to contribute equally.

6 Subrogation

The literal meaning of subrogation is “to stand in place of”. Subrogation is therefore the right of one person to stand in the place of another in the application of the law. In terms of this principle, the person who has subrogation rights is availed of all the rights and remedies to which the insured is entitled. The principle of subrogation applies as a way of preserving the principle of indemnity and to prevent the insured party from profiting from any loss arising in terms of a contract of insurance.

Example – Application of the principle of subrogation

Facts:

S drives negligently and causes an accident which results in T's car having to be written off. Under the insurance contract, the replacement value of T's car is R114 000 (including VAT).

Result:

T has two options to recover the loss, that is:

- Sue S in delict for damages of R114 000, or
- Claim the amount from T's insurer.

If T pursues both options, T will receive double compensation and would profit from the misfortune. Therefore, when the insurer replaces T's car, or pays the insured amount of R114 000, T will be prevented from pursuing damages against S in court. Instead, the insurer will acquire T's rights of action against S under the principle of subrogation. The insurer can then decide if it wishes to take the necessary legal action to recover the R114 000 from S.

There are a number of principles which apply to subrogation, such as:

- The insurer cannot acquire the rights of action of the insured under subrogation unless and until the insurer makes good the loss to the insured.
- The insurer cannot acquire any additional rights of action under subrogation over and above those which would have been available to the insured.
- The insured cannot prejudice the insurer's right of subrogation by, for example, renouncing any right of action against the third party if by that action the loss would be diminished. For example, the insured cannot accept a payment from the third party as compensation for not pursuing his or her right to damages in court.
- The insurer may also not make a profit from the subrogation rights, but is entitled to recover only the exact amount paid as indemnity. If a larger amount is recovered, the balance should be paid to the insured.

- Subrogation gives the insurer the right of salvage over the insured goods. This means that if the goods are damaged and cannot be repaired (or are lost, but later recovered), the insurer will be legally entitled to take control over those goods and to sell them to recover any loss it has suffered as a result of the indemnity payment made to the insured.

7 Proximate cause

Proximate cause is described as the direct, dominant or specific cause of a loss or the uninterrupted chain of events that brought about the loss. For a loss to be paid under a policy of insurance it must have been caused by an insured peril and the onus of proving proximate cause by an insured peril rests with the insured. If the insured submits reasonable evidence to conclude that the loss was proximately caused by an insured peril, the insurer is obliged to pay the indemnity unless the policy provides for an exception to apply. For example, if furniture is thrown out of a burning house to diminish the effect of a spreading fire, and the furniture is damaged in the process, the proximate cause of the damage to the furniture would be the fire.

Glossary

PART 1 – VAT TERMINOLOGY

Consideration This is generally the total amount of money (incl. VAT) received for a supply. For barter transactions where the consideration is not in money, the consideration will be the open market value of goods or services (incl. VAT) received for making the taxable supply. Section 10 determines the value of supply or consideration for VAT purposes for different types of supplies.

Any act of forbearance whether voluntary or not for the inducement of a supply of goods or services will constitute consideration, but it excludes any donation made to an association not for gain. Also excluded is a “deposit” which is lodged to secure a future supply of goods and held in trust until the time of the supply.

A supply for no consideration has a value of “nil”, except when a special value of supply rule is applicable, for example, in certain cases when a supply is between connected persons.

Exempt supplies An exempt supply is a supply on which no VAT may be charged (even if the supplier is registered for VAT). Persons making only exempt supplies may not register for VAT and may not recover input tax on purchases to make exempt supplies.

Section 12 contains a list of exempt supplies.

Examples:

- Certain supplies of financial services.
- Supplies by any "association not for gain" of certain donated goods or services.
- Rental of accommodation in any "dwelling" including employee housing.
- Certain supplies of educational services.
- Services of employee organisations for example, trade unions.
- Certain services to members of a sectional title, share block or retirement housing scheme funded out of levies. (Not applicable to timeshare schemes.)
- Public road and railway transport for fare-paying passengers and their luggage.
- Childcare services in a crèche or after school care centre.

Goods	The term “goods” includes – • corporeal (tangible) movable things, goods in the ordinary sense (including any real right in those things); • fixed property, land and buildings (including any real right in the property for example servitudes, mineral rights, notarial leases etc.); • sectional title units (including timeshare); • shares in a share block company; • electricity; • postage stamps; and • second-hand goods. The term “goods” excludes – • money, that is. notes, coins, cheques, bills of exchange, etc. (except when sold as a collector's item); • value cards, revenue stamps, etc. which are used to pay taxes (except when sold as a collector's item); and • any right under a mortgage bond.
Insurance	Insurance or guarantee against loss, damage, injury or risk of any kind whatever, whether pursuant to any contract or law (including reinsurance). The term “contract of insurance” includes a policy of insurance, an insurance cover, and a renewal of a contract of insurance. The definition of “insurance” does not apply to any insurance specified in section 2 (financial services).
Invoice	A document notifying a person that there is an obligation to make payment in respect of a supply.
Person	The entity which is liable for VAT registration and includes – • sole proprietor that is, a natural person; • company / close corporation; • partnership / joint venture; • deceased / insolvent estate; • trusts; • incorporated body of persons for example, an entity established under its own enabling Act of Parliament; • unincorporated body of persons, for example, club, society or association with its own constitution; • foreign donor funded project; and • municipalities / public authorities.

Recipient	The recipient is the person to whom a supply of goods or services is made. The recipient is not always the same as the person who pays for the supply. In the case of imported services, the recipient is liable to pay the VAT.
Resident of the Republic	This is a person who is regarded as a “resident” as defined in section 1(1) of the Income Tax Act. However, any other person (including a company) is deemed to be a resident of the Republic for VAT purposes to the extent that a person carries on an enterprise or other activity in the Republic through a fixed place of business or permanent establishment in the Republic.
SARS	The acronym for the South African Revenue Service.
Services	The term “services” is very broad and includes – • the granting, assignment, cession, surrender of any right; • the making available of any facility or advantage; and • certain acts which are deemed to be services under section 8. The term excludes – • a supply of goods; • money; and • any stamp, form or card which falls into the definition of “goods”. <u>Examples:</u> • Commercial services – electricians, plumbers, builders; • Professional services – doctors, accountants, lawyers; • Advertising agencies; • Intellectual property rights - patents, trade marks, copy rights, know-how; • Restraint of trade; and • Cover under a short-term insurance contract.
Supply	Includes performance in terms of a sale, rental agreement, instalment credit agreement and all other forms of supply, whether voluntary, compulsory or by operation of law, irrespective of where the supply is effected.
Taxable supply	A supply (including a zero-rated supply) which is chargeable with tax under the Act. There are two types of taxable supplies, namely – • those which attract the zero rate (listed in section 11); and • those on which the standard rate of 14% must be charged. A taxable supply does not include any exempt supply listed in section 12, even if supplied by a registered vendor.
VAT	The acronym for value-added tax.

Vendor	Includes any person who is registered, or is required to be registered for VAT. Therefore any person making taxable supplies in excess of the threshold amount (presently R1 million) prescribed in section 23 is a vendor, whether the person have actually registered with SARS or not.
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PART 2 – SELECTED INSURANCE TERMS

The terms and phrases in the **Glossary** are not agreed definitions which have a universal meaning, but are intended merely to provide the reader with a general understanding of insurance terminology which is used in the industry and in this guide. These terms have been compiled from a number of sources, but are mainly derived from the information available on the Insurance Gateway website www.insurancegateway.co.za.

Accident Insurance	A contract of insurance to provide for loss sustained through an accident, or as compensation for personal injuries. Various types of policies are included within the category of accident insurance. These include personal accident and health insurance
Assurance	Insurance cover against an eventuality that (sooner or later) must occur. For example, the death of the person covered under a life insurance policy. It is therefore a term commonly used to distinguish life (long-term) "assurance" from short-term (that is, non-life and property) "insurance".
Adjuster	See loss adjuster.
Agent	A person who acts on behalf of another and in the case of insurance is the intermediary between the proposer and the insurer. (Also referred to as "broker" and "intermediary").
Average	A clause in a contract to ensure that in the event of a claim, insurers are not prejudiced by under-insurance. For example, if an item or property is valued at R10 000, but insured for only R6 000 the insurer will not cover the balance or shortfall of R4 000. The insured must in these cases carry a rateable proportion of any loss in regard to the claim for any under-insured items forming part of the claim.
Assessor	Similar to a loss adjuster but may just do motor claims and is not necessarily independent and is not a member of the Institute of Loss Adjusters.
Bordereau	A bordereau can be described as a detailed memorandum, especially one that lists information, documents or accounts, or financial transactions in respect of insurance and reinsurance policies, premiums and claims. It can also include a memorandum or invoice prepared for a company by an underwriter, containing a list of reinsured risks.
Cancellation	A complete termination of an existing policy before its expiration. Usually the insured may only cancel a policy if all premiums due have been paid.
Cedent	An insurer that reinsures part or all of its claims risk associated with insurance policies held.
Claims	A demand on the insurer for indemnification for a loss incurred from an insured event.

Claims risk	The risk of the cedent incurring a loss as a result of paying a claim submitted by its client under a policy of insurance.
Co-insurance	An arrangement whereby two or more insurers enter into a single contract with the insured to cover risk in agreed proportions at an overall premium.
Collective policy	Policy issued by the leading insurer on behalf of all the insurers who share a risk by way of co-insurance.
Commission	The fee paid to a broker for the provision of intermediary services (per the FAIS Act) and is calculated as a percentage of the premium generated on the insurance policy. Also referred to as brokerage. Commission levels are presently capped by law.
Composite insurance company	An insurer conducting both life and non-life business.
Contribution	This clause is similar to the average clause but applies in circumstances where there is more than one policy covering the same loss. Under these circumstances each policy (insurer) will pay a rateable proportion of the loss in the ratio that their policy's sum insured bears to the loss.
Cover	The scope of the protection provided by an insurance policy.
Cover note	Confirmation of insurance cover or temporary evidence of the granting of insurance.
Credit life insurance	A single or recurring premium term life insurance policy taken out by borrowers. Its purpose is to cover payment of outstanding loan balances in the event of their dying, or on the happening of other specified events. This class of business is sold in both the life and short-term insurance industries.
Damages	An amount of money claimed by or awarded to a third party as compensation for injury or loss.
Deposit premium	An advance payment made by the insured before the final premium has been calculated.
Duty of disclosure	The duty of the parties to a contract of insurance to reveal all material facts to each other before a policy is issued and before each renewal. See <i>Uberrimae fidei</i> .
Endorsement	Documentary evidence of a change to an existing policy, for example, change of address, increase in sum insured etc. An endorsement may result in an additional premium, a return premium or no premium adjustment.

Excess	A policy condition whereby the insured is required to pay a portion of the loss, as stipulated in the policy (for example the first R2 000 of a motor vehicle damage claim). Excess is also referred to as a “deductible” or “first amount payable” and can be in the form of inner excess or aggregate excess. The insurer would pay the balance over that amount. In general there are three types of excess, namely: • Standard excess; • Additional excess; and • Voluntary excess.
Exclusions	Provisions in a policy or treaty that exclude certain types of risk from coverage under the policy or treaty. Two of the more common exclusions are in connection with aviation and war.
Ex-gratia payment	Payment of a claim which is not covered in terms of the policy wording. <i>Ex-gratia</i> means, literally, “an act of grace”. If a claim is paid in full or in part by an insurer without admission of liability and without waiver of right it is paid <i>ex gratia</i> .
FSB	Acronym for the Financial Services Board which is a public authority established in terms of the Financial Services Board Act 97 of 1990 to oversee the South African Non-Banking Financial Services Industry in the public interest. Amongst other functions, the FSB acts as the regulatory authority and the registrar for long-term and short-term insurance in South Africa.
Foreign insurer	An insurer situated outside the Republic of South Africa.
Good faith (Bona fide)	The principle where the parties to a contract undertake to deal with one another honestly and openly in good faith regarding disclosure of material facts. (See <i>uberrimae fidei</i> .)
Health insurance	Insurance providing for the payment of benefits as a result of sickness or injury. Includes various types of insurance such as accident insurance, disability income replacement insurance, accidental death, dismemberment insurance and hospital cash plans.
Householders insurance	This covers loss or damage in respect of household contents.
Homeowner’s insurance	This covers loss or damage to the home of the insured from a variety of perils, essentially fire and allied perils.
Hull insurance	Insurance against loss of or damage to an aircraft, ship and other air and water borne craft.
Insurable interest	You are only able to insure property in circumstances where you stand in some legally recognised relation thereto whereby you will benefit by the safety of the property or object or be prejudiced by its loss. Examples include: owners of property or goods, mortgages, finance houses, bailees, trustees.

Indemnity	This is the basis upon which a claim is settled if the property of the insured is destroyed or lost for any event which is covered by the policy. The insurer undertakes to place the insured party back in the same financial position immediately before the loss occurred. It is against public policy for a person to benefit from a misfortune as there would be no inducement for the protection of property and deliberate losses would, as a result, proliferate. Unless the policy specifically makes provision for settling claims on a “new for old” basis, claims are settled on the actual value of the property at the time of the loss. In most cases, this value is determined by deducting an amount in respect of age and wear-and-tear. Most insurance policies give the insurers the right to decide whether to repair, replace or reinstate the damaged property or to pay its value in cash. Indemnity is also affected by the application of average, excesses, limitations and the adequacy of the sums insured.
Insurance	A risk transfer arrangement whereby the responsibility for meeting losses passes from one party (the insured) to another (the insurer) on payment of a premium. Under an insurance contract, the insurer indemnifies the insured against a specified amount of loss, occurring from specified eventualities within a specified period, provided a fee called a “premium” is paid. In general insurance, compensation is normally proportionate to the loss incurred, whereas in life insurance usually a fixed sum is paid. Insurance provides protection only against tangible losses. It cannot ensure continuity of business, market share, or customer confidence, and cannot provide knowledge, skills, or resources to resume the operations after a disaster.
Insurance policy (or policy)	A document which is evidence of a contract of insurance. A contract whereby one party (the insurer), in return for consideration known as a premium, agrees to indemnify another party (the insured) against specified damage, loss or liability arising from the occurrence of specified risks or to compensate the insured or beneficiary upon the occurrence of a specified event.
Insured	The person whose interest is insured, usually the policy owner.
Insured peril	Source of loss which is covered under an insurance policy. A peril is a contingency or fortuitous happening which could cause losses. Possible loss occurrences against which insurance cover is obtained. For example, fire, windstorm, collision, hail, bodily injury, property damage, loss of profits etc.
Insurer	The person offering risk protection via insurance policies.

Lloyd's of London	An association of persons grouped together in syndicates providing insurance. Also refer to the following in this regard: • Lloyd's broker: A broker that has been given the responsibility by Lloyd's of placing insurance at Lloyd's. • Lloyd's syndicate: A group of underwriters with Lloyd's of London who specialises in underwriting particular risks. • Lloyd's underwriter: An individual member of a Lloyd's syndicate.
Loss adjuster	An independent, qualified person who acts on behalf of the insurer, or the insured, to investigate the circumstances of a loss and assesses the size or value of a loss to recommend the amount to be paid. Also known as an adjuster, assessor, or loss assessor.
Market value	The price at which an item can be bought or sold at a specific time.
Marine insurance	Marine insurance covers the risk of loss to ships and vessels and also provides cargo cover. Marine cargo insurance may be divided into two divisions: inland marine, which covers property and goods in transit between locations without requiring sea transport, and ocean marine, which covers property and goods subject to a sea voyage. Marine cargo policies are issued in various forms depending on the requirements of the shipper, the ship-owner, the charterer, the consignee etc.
Material fact	Anything which would affect the judgment of a reasonable person in accepting or rejecting or deciding the terms for a risk. A false description of a material fact is called a misdescription and a false statement of a material fact is called a misrepresentation.
New business	Policies written in response to applications for insurance, as distinguished from renewal.
No-claims bonus	The amount by which a renewal premium is reduced if the insured has not made a claim under the insurance policy for one or more consecutive preceding years. Applied particularly to motor comprehensive cover.
Personal accident	A class of insurance which provides a fixed payment in the event of an insured being injured in an accident or killed in an accident. The amount paid varies according to the nature of the injury, for example, loss of a finger, loss of an arm.
Policy	See "insurance policy".
Premium	The monetary consideration which the policyholder pays to the insurance company for a contract of insurance.

Proposal	A request for insurance submitted to the insurer by or on behalf of the insured. The proposal usually includes sufficient facts for the insurer to determine whether or not it wishes to accept the risk. It will be illegal for a broker to allow an insured to sign a partially completed or blank proposal form upon the introduction of the policy holder protection rules.
Proximate cause	The direct cause of a loss without the intervention of any other event, which may contribute to the loss. The direct, dominant or specific cause of a loss or the uninterrupted chain of events that brought about the loss.
Public liability insurance	A prescribed class of insurance business covering liability exposures of individuals and businesses for damage to property and injury to individuals.
Reinsurance	An agreement whereby an insurance company transfers part or all of its risk of loss under insurance policies it writes by means of a separate contract or treaty with another insurance company. The insurance company providing the reinsurance protection is the reinsuring company or reinsurer. The insurance company receiving the reinsurance protection is the ceding company. Reinsurance protection provided is known as reinsurance accepted; from the standpoint of the ceding company, reinsurance protection received is known as reinsurance ceded. Reinsurance agreements are generally in the form of facultative or treaty reinsurance.
Renewal	The process for continuing a policy for a further period after the first or current period of cover has expired.
Risk	The hazard exposure or chance of loss. The term “risk” is used also in a general way to designate the subject matter of an insurance policy. It may also be used as a generic term for the insured.
Salvage	Whatever is recovered after an insured item or part of it has been lost or damaged beyond repair. Also refers to the amount received by an insurer from the sale of property (usually damaged) on which a total loss has been paid to the insured.
Self-insurance	An insured protects his or her own risk out of own resources. This can be done in different ways, including inter-company transactions, special accounts or <i>via</i> a risk financing arrangement.
Short-term insurance	The business of providing or undertaking to provide policy benefits under a short-term policy including an engineering policy, guarantee policy, liability policy, miscellaneous policy, motor policy, accident and health policy, property policy or transportation policy or a contract comprising of a combination of any of those policies and any contract whereby any such contract is renewed or varied.

Sub-agent	A person appointed by an agent to perform some duty, or the whole of the business relating to the agency. Sub-agents may be considered in two points of view, firstly, with regard to their rights and duties or obligations, towards their immediate employers, and secondly, as to their rights and obligations towards their superior or real principals. A sub-agent is generally invested with the same rights and incurs the same liabilities in regard to the immediate employers as if that person was the sole and real principal.
Subrogation	The insurer's right to take whatever steps it deems necessary to recover the amount of the loss from the responsible third party, after the insured party has been compensated for that loss. This includes instituting legal action in the name of the insured as it is usually a policy condition that the insurer be provided with the necessary assistance in exercising these rights.
Sum insured	The stated monetary amount or amounts of indemnity or cover under an insurance policy.
Third party	Any person, not a party to the insurance contract, who has an alleged or actual right of action for injury or damage against the person insured under the policy.
Under-insurance	The difference between the possible loss and limit in insurance.
Underwriter	Another name for an insurer. Underwriting is the process of assessing a proposal for insurance to decide on its acceptability and if so, on what terms and conditions.
Void	Where the insurance policy has no legal effect.
Waiver	The surrender of a right or privilege which is known to exist, or might exist.
Warranty	A condition, which must be complied with literally. A clause in an insurance contract presenting a condition relating to the degree of risk, non-compliance with which invalidates the contract.

Contact details

The **SARS website** contains contact details of all SARS branch offices and border posts.

Contact details appearing on the website under “Contact Us” (other than branch offices and border posts) are reproduced below for your convenience.

SARS Head Office

Physical Address

South African Revenue Service
Lehae La SARS
299 Bronkhorst Street
Nieuw Muckleneuk
0181
Pretoria

Postal Address

Private Bag X923
Pretoria
0001
South Africa

SARS website

www.sars.gov.za

Telephone

(012) 422 4000

SARS Fraud and Anti-Corruption hotline

0800 00 28 70

Complaints Management Office

Telephone

0860 12 12 16

Website (via eFiling)

www.sars.gov.za

Office

Any SARS branch

e-Filing

Call Centre

0800 00 7277

Website

www.efiling.gov.za

National Call Centres / SARS Contact Centres

- You may contact SARS by phone, e-mail, fax or visiting a SARS Branch
- Call our SARS Contact Centre on 0800 00 7277
- International Callers may contact our Contact Centre on +27 11 602 2093
- E-mail or fax one of our dedicated four contact centres:

Area	Telephone	Fax	E-mail
Northern South Africa Vendors residing in Gauteng north (including Centurion and Pretoria), North West, Mpumalanga and Limpopo.	0800 00 7277	012 6706880	Contact.north@sars.gov.za
Central South Africa Vendors residing in Gauteng south (including Midrand, the Greater Johannesburg area, Kempton Park, Boksburg, Vereeniging and Springs), the Free State and Northern Cape.	0800 00 7277	010 2085005	Contact.central@sars.gov.za
Eastern South Africa Vendors residing in KZN and northern parts of the Eastern Cape (up to and including East London).	0800 00 7277	031 3286018	Contact.east@sars.gov.za
Southern South Africa Vendors residing in the Eastern Cape, south of East London and the Western Cape.	0800 00 7277	021 4138905	Contact.south@sars.gov.za

Practitioners Unit

Telephone / Call Centre
0800 00 72 77

E-mail
pcc.pavilion@sars.gov.za

Business hours
Weekdays 8:00 – 16:00 (except Wednesdays)
Wednesdays 9:00 – 16:00

Physical Address
Pavilion
217 Bronkhorst Street
Nieuw Muckleneuk
Pretoria

This facility is for Tax Practitioners already registered with SARS (Pretoria area only). Appointments can be made online by visiting: **www.sars.gov.za**, then go to the Tax Practitioners' web page.

VAT Rulings

Should there be any aspects relating to VAT on which a specific VAT ruling is required, you may submit a ruling application on a VAT301 to SARS by facsimile or e-mail. All applications must comply with section 79 of the TA Act [excluding section 79(4)(f), (k) and (6)].

Facsimile

+27 86 540 9390

E-mail

VATRulings@sars.gov.za