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IRELAND'S INTERNATIONAL FINANCIAL SERVICES SECTOR: NEWS COMMENT AND ANALYSIS

## Ireland cited as domicile for distressed assets

The credit crisis is providing a developing opportunity for IFSC-based banks with access to liquidity to purchase high quality distressed assets, with some bankers identifying it as a major opportunity for such banks in 2009.

Indeed, in the opinion of one observer, Ireland could become a leading location for the domiciliation of distressed assets as the world emerges from the credit crisis.

The opportunity is considered likely to last for some time, given the continued bearish outlook for assets.

The continued price depression of quality assets in ABS bond markets has increased the interest amongst bank investors in the possibility of recovery, but focussing the mind of IFSC based

banks in particular is the prospect of a fiscal enhancement of returns arising from the IFSC's lower corporation tax rate.

With distressed assets falling to a fraction of their par values, the need for banks to write off values on a mark-to-market basis is resulting in realisation of losses in banking entities incorporated in jurisdictions with high corporation tax rates, at those higher prevailing corporation tax rates.

The sale of such assets to Irish banks, for domiciliation in Irish SPVs, will result in a lower tax charge on the gains arising in the event of their recovery to par values, when an improvement or normalisation of market conditions occurs, and the realisation of historic mark-to-market values for the assets.

## Red tape cut: 15 new treaties

Ireland's tax treaty network is due for a major boost, following a relaxation of rules in the 2009 Finance Bill.

The relaxation is expected to achieve effective tax treaty status for up to 15 additional countries during the course of 2009, Government sources estimate. According to the Finance Dublin Yearbook 2008, Ireland had tax treaties with 44 countries on January 1st 2008.

This will mean the biggest effective widening of Ireland's tax treaty network in any year. In recent years, following steady progress in widening the tax treaty network in the 1990s, expansion slowed to a snail's pace, with only a handful of treaties concluded in the last five years, and with some of those reflecting international rather than Irish initiatives,

for example, in the the case of Ireland's tax treaties with the USA.

The major expansion in the 1990s reflected the international 'tax diplomacy' of the Irish Revenue Commissioners, in the OECD notably.

The Bill refers to 'the application of certain provisions in the Taxes Acts which would grant preferential treatment to payments to and from countries that have signed a Double Taxation Agreement (DTA) but have not yet ratified. The former requirement that a DTA had to be in force with the relevant country is being relaxed to overcome delays in bringing the agreements into force because of ratification procedures in either country.' (See also Deirdre Power on Page 9).

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# Tax authorities keeping a watchful eye

**The passporting of services under various EU Directives is now attracting the attention of tax authorities around Europe who are increasingly alert to Insurance Premium Tax liabilities arising from cross border insurance contracts written from Ireland. KIERAN DESMOND looks at how international IPT works and what Ireland-based insurers should be doing to ensure they are keeping clients, the European tax authorities and regulators happy.**

**I**nsurance Premium Tax (IPT) is a worldwide tax, in many forms, on insurance contracts. It is generally calculated as a percentage of the gross premium. In most countries, initially, it is the insurer or captive who is responsible for the calculation, collection and payment of any taxes.

**'In the past 18 months, IPT due from insurance contracts written from Ireland has caught the attention of foreign tax authorities. The obvious reason is the growth of FOS programmes from Ireland – and who better to tax than a foreign insurance company?'**

In most countries, the policyholder is next in line for the tax liability. Should the contract issuer fail to take care of the IPT, then the tax authorities are able to pursue the insured party. It is this last requirement that has been propelling IPT compliance up the 'to-do' lists of insurers. Policy holders are becoming increasingly concerned that they will be left holding the liability if the insurer ignores IPT. With this worry in mind, they are often looking for an indemnity from the insurer or broker against any unsettled EU IPT liabilities.

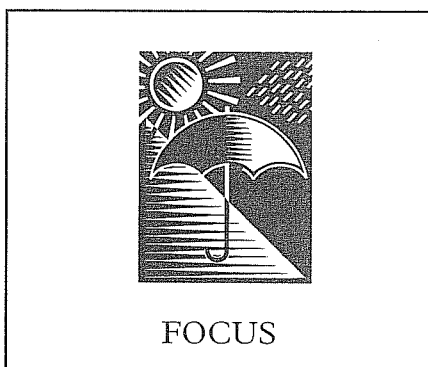
In addition to IPT, there are also a number of other levies on insurance, payable to various local bodies. These 'parafiscal charges' range from the standard fire brigade levy on property in most territories through to funding national priorities, such as contributions for earthquake losses in Iceland.

Many countries exclude life and marine cover from IPT, and reinsurance is largely exempt.

## Where is European IPT due?

For many years, it was assumed that the IPT liability was determined by the place where the contract was written. In Europe, it was eventually clarified in the 2nd Non-Life Directive as lying where the risk was located.

This last point was underlined in the key European Court of Justice Kvaerner Case (2001). This centred on the



Norwegian engineering giant, Kvaerner, which had taken out insurance cover in London for its European subsidiaries. At the time of the policy being written, IPT was calculated on the basis of UK tax rules. The Dutch tax authorities brought this case, claiming that elements of the insurance risk covering Kvaerner's Dutch operations were instead liable to Dutch IPT. This view was upheld and the policyholder, Kvaerner, was held liable for IPT in the Netherlands.

**'Several European regulators have been actively cooperating with the foreign tax offices on exchanging information on the activities of multi-programme insurers. It is therefore vital that Irish underwriters are clear on their international IPT liabilities and see that these are dealt with promptly, or they could be putting the insurer at risk with the regulators.'**

Following this case, there has been a scramble by international insurers and captives to be fully compliant with local tax regulations, especially in Europe. There have been a number of follow on European IPT cases since Kvaerner, including the DSG Case in 2007, where an operating structure was set up which appeared to avoid UK IPT.

## Freedom of Services IPT

Unlike VAT - a sales tax based on European Union rules - there is no overriding tax-setting authority for

European IPT. This means there are many variations in terms of rates, treatment of classes, payment methods etc.

**'The good news is that most of the tax authorities remain open to discussion on settling previous liabilities without harsh fines or punishment. In these cases, the key seems to be to contact the relevant tax authorities (through a local fiscal representative if this a local requirement) to detail the background to the situation.'**

What has simplified the process for pan-European insurers is the Freedom of Services (FOS) regime. This enables insurers and captives to write business across European borders without establishing local branches. European insurers are required to seek 'passporting rights' from their local regulator, which then notifies each relevant country regulator and then permission is automatically granted. This system has enabled Ireland to build itself up as a low-tax centre for insurers writing business across Europe. The FOS regime applies to EU countries, plus Norway, Iceland, Lichtenstein and Switzerland.

## European IPT variations

The implementation of IPT regimes across Europe is varied. In simple terms, most of 'old Europe' has an IPT system of some sort. There are variations: Portugal applies stamp duty instead, and Greece has both IPT and stamp duties. In 'new Europe' there is only Slovenia which applies IPT to FOS-basis insurers. Some other countries, such as Romania, have an IPT regime, but it does not yet apply to FOS insurance. The complexities in Central and Eastern Europe come down to parafiscal charges and whether Irish insurers will be liable. Many countries levy charges on fire & property, and there are a number of catastrophe levies coming into place. In addition, some countries may expect a contribution to the local insurance association.

**European IPT compliance**

Once the Irish insurer has determined the location of any IPT liability, the next phase is to tackle compliance. The insurer or captive must calculate the taxes due on any premiums written within the reporting period. This is based on the risk category and appropriate rate in the target country. Details of the main European IPT rates are provided on TMF's website [www.tmf-vat.com](http://www.tmf-vat.com); this also includes the principal parafiscal charges.

The taxes should be charged to the policy holder, as part of the premium, and then remitted to the relevant tax office. This requires the insurer to have registered as a taxpayer in each territory, and submit periodic filings with accompanying tax settlement payments.

In many countries, the insurer is required to appoint a local fiscal representative. Their role is to assist with the IPT calculations and payments, as well as maintain in-country records of premiums.

However, due to the opaque nature of IPT, and the difficulty in finding up-to-date guidance on regulations and rates, this can be a fraught experience. Often, many Irish insurers can believe that they are correctly calculating and submitting IPT payments to the relevant authorities, but actually may be missing several sub-rules on rates or parafiscal charges. Several tax offices are lax in checking filings on a regular basis, so potential liabilities can go missing for years. Unfortunately, when the tax authorities do then come to audit back returns, this can leave large balances outstanding which attract hefty penalties and interest payments. Mediterranean countries seem to be a major source of concern in this area for Irish insurers, where applications to bring IPT filings up-to-date are sometimes ignored.

**The tax man's interest in Ireland-originated IPT**

In the past 18 months, IPT due from insurance contracts written from Ireland has caught the attention of foreign tax authorities. The obvious reason is the growth of FOS programmes from Ireland – and who better to tax than a foreign insurance company? But local insurers, through their national insurance associations, have also been lobbying their tax office for a fairer implementation of local taxes on overseas insurers.

Evidence of the tax authorities' interest grows by the day. For example, authorities in Germany are writing to

Irish international insurers asking them to declare any risks covered in their territories. This includes signing statements of policy for dealing with the German IPT. The Austrian tax authorities have also followed this procedure for Austrian IPT.

Often, the foreign tax authorities will know about Irish insurers' intentions to write business in their territory even before the first premium is written. In Spain, the tax office will automatically set up an IPT file on an Irish insurer as soon as they apply for Spanish Passporting Rights.

Likewise, in Belgium, the tax authorities check the local equivalent of Ireland's *Stubbs Gazette*, which publishes details of foreign insurers seeking Belgian Freedom of Services rights. If the Irish insurer has not already notified the Belgian tax office of these intentions, action will be forthcoming.

It now seems that insurance regulators are also getting involved. Several European regulators have been actively cooperating with the foreign tax offices on exchanging information on the activities of multi-programme insurers. It is therefore vital that Irish underwriters are clear on their international IPT liabilities and see that these are dealt with promptly, or they could be putting the insurer at risk with the regulators. A good example is Italy, where the regulator is taking an active role with the Italian IPT authorities on resolving outstanding IPT liabilities, and assessing the reasons for any default.

Many policyholders have also been asked to confirm the tax treatment on their cover. This is leading many corporates and their captive managers to seek indemnities from their insurers.

**Steps to take if non-compliant**

As outlined above, most insurers who have been writing risk-cover across borders are probably liable to European IPT. However, the complexities and lack of clear guidance on EU IPT mean that there are still many insurers who are non-compliant.

The good news is that most of the tax authorities remain open to discussion on settling previous liabilities without harsh fines or punishment. In these cases, the key seems to be to contact the relevant tax authorities (through a local fiscal representative if this a local requirement) to detail the background to the situation.

Many countries have been very flexible with this approach. It is recommended not to try to pre-calculate any potential penalties or fines as the tax

authorities may consider waiving some of them if approached first.

**Summary**

IPT on international insurance has always been a complex and confusing area, historically overlooked by insurers, policyholders and the tax authorities. However, with Ireland's success as a preferred location for pan-European risk cover, there is now a pick-up in interest from the overseas tax authorities that are eager to catch up on any outstanding liabilities.

This has to be tackled now if Irish insurers are to be certain of maintaining their clients' trust and their own valuable reputations.

*Kieran Desmond is managing director of TMF Ireland.*

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## Reinsurance growth in 2007

The Irish global reinsurance market grew by 5.1 per cent between 2006 and 2007 according to the Standard and Poor's Global Reinsurance Highlights 2007 Edition. The rate of growth is down however from the 2007 report which showed that the Irish reinsurance industry grew by 23.7 per cent between 2005 and 2006. Indications for 2008 are that the market is strong and that premiums are rising as insurers are turning to reinsurers rather than raising more capital in current environment.

In 2005, the total net reinsurance premiums written by Irish-based firms stood at \$2,745.1 million. This figure stood at \$3,400.8 million by the end of 2006 up further to \$3575.8 million.

Among the Irish firms, Hannover Life Re (Ireland) is the company that writes the most net reinsurance premiums, growing its premiums by 6.3 per cent from 2006 to \$737.3 million. XL Re Europe Limited are second at \$695.2 million and Hannover Reinsurance Ireland Ltd at \$653 million increasing its business by 14.8 per cent.

AXIS Re LTD increased its business by 26.1 per cent to \$517.6 million. Mitsui Sumitomo Reinsurance Ltd also showed big growth of 29 per cent to \$166.6 million

SCOR Global Life Reinsurance Ireland Ltd. premiums fell from \$173.2 million down to \$111.9 million a fall of 35.4 per cent.