STATUTORY INSTRUMENTS

1995 No. 1730

INCOME TAX

The Insurance Companies (Taxation of Reinsurance Business) Regulations 1995

Made - - - -	*7th July 1995*
Laid before the House of Commons - - - -	*7th July 1995*
Coming into force - -	*28th July 1995*

The Commissioners of Inland Revenue, in exercise of the powers conferred on them by sections 431C(1), 439A and 442A(2) to (6) of the Income and Corporation Taxes Act 1988(**1**), and paragraph 58 of Schedule 8 to the Finance Act 1995, hereby make the following Regulations:

Citation, commencement and effect

1. These Regulations may be cited as the Insurance Companies (Taxation of Reinsurance Business) Regulations 1995, shall come into force on 28th July 1995, and shall have effect with respect to accounting periods beginning on or after 1st January 1995.

Interpretation

2. In these Regulations unless the context otherwise requires—

"accounting period" means an accounting period of a cedant company during which a reinsurance arrangement is in force;

"basic life assurance and general annuity business" has the meaning given by section 431F of the Taxes Act(**2**);

"the Board" means the Commissioners of Inland Revenue;

"deposit-back arrangement" means an arrangement whereby an amount is deposited with the cedant company by the reinsurer;

"EEA Agreement" means the Agreement on the European Economic Area signed at Oporto on 2nd May 1992(**3**) as adjusted by the Protocol signed at Brussels on 17th March 1993(**4**);

(**1**) 1988 c. 1; section 431C was inserted by paragraph 2, section 439A by paragraph 26, and section 442A by paragraph 34, of Schedule 8 to the Finance Act 1995 (c. 4).
(**2**) Section 431F was inserted by paragraph 2 of Schedule 8 to the Finance Act 1995.
(**3**) O.J. No. L1, 3.1.94, p.3.
(**4**) O.J. No. L1, 3.1.94, p.572.

"EEA State" means a State, other than the United Kingdom, which is a Contracting Party to the EEA Agreement;

"inspector" includes any officer of the Board;

"internal linked fund" means an account to which an insurance company appropriates certain linked assets and which may be subdivided into units the value of which is determined by the company by reference to the value of those assets;

"investment return" means the investment return to be treated as accruing to a cedant company in respect of a policy pursuant to subsection (1) of section 442A in an accounting period;

"linked assets" has the meaning given by section 432ZA(1) of the Taxes Act(**5**), and "non-linked assets" means assets other than linked assets;

"linked business" means business which comprises the effecting and carrying out by an insurance company of policies where benefits provided for under each policy are to be determined by reference to the value of linked assets;

"morbidity risk" in relation to a policy means the risk that the person whose life is insured by the policy will suffer any sickness, accident or infirmity;

"mortality risk" in relation to a policy means the risk that the person whose life is insured by the policy will die;

"periodical return" has the meaning given by section 431(2) of the Taxes Act;

"policy" includes an annuity contract;

"reinsurance arrangement" means a reinsurance arrangement to which section 442A applies;

"relevant profits" has the meaning given by section 88(3) of the Finance Act 1989(**6**);

"section 431C", "section 439A" and "section 442A" mean respectively section 431C, section 439A and section 442A of the Taxes Act;

"90% subsidiary" means a body corporate 90 per cent. or more of whose ordinary share capital is owned directly or indirectly by another body corporate;

"the Taxes Act" means the Income and Corporation Taxes Act 1988.

Calculation of investment return in sole accounting period

3.—(1) Where the period during which a reinsurance arrangement is in force falls wholly within a single accounting period, the amount of the investment return in that accounting period ("I") shall be calculated in accordance with the formula—

$$I = (C - P) \times R$$

where—

C is the aggregate of the sums paid by the reinsurer to the cedant company during that accounting period by way of commission or as a result of the surrender in whole or in part of the rights under the policy or otherwise, but excluding any sum which—

(a) forms part of the relevant profits of the cedant company, or

(b) is paid by way of commission that has been deducted from expenses of management pursuant to section 76(1)(ca) of the Taxes Act(**7**);

P is the aggregate of the sums paid by the cedant company to the reinsurer during that accounting period by way of premium; and

(**5**) Section 432ZA was inserted by paragraph 11(2) of Schedule 8 to the Finance Act 1995.
(**6**) 1989 c. 26; section 88(3) was substituted by paragraph 21(2) of Schedule 8 to the Finance Act 1995.
(**7**) Paragraph (ca) of section 76(1) was inserted by section 44(3) of the Finance Act 1990 (c. 29).

R is the percentage rate of return prescribed by paragraph (2) below.

(2) The percentage rate of return prescribed is 100 per cent.

Calculation of investment return in first accounting period

4. Where the period during which a reinsurance arrangement is in force falls within more than one accounting period, the amount of the investment return in the first accounting period (“I_1”) shall be calculated in accordance with the formula—

$$I_1 = (P - C) \times R$$

where—

P is the aggregate of the sums paid by the cedant company to the reinsurer during that accounting period by way of premium or otherwise;

C is the aggregate of the sums paid by the reinsurer to the cedant company during that accounting period by way of commission or as a result of the surrender in part of the rights under the policy or otherwise; and

R is the percentage rate of return prescribed by regulation 7(2);

but where the result is less than zero, taking the amount to be zero.

Calculation of investment return in second and subsequent accounting periods other than final accounting period

5.—(1) Where the period during which a reinsurance arrangement is in force falls within more than one accounting period, the amount of the investment return in the second or any subsequent accounting period other than the final accounting period (“I_n”) shall be calculated in accordance with the formula—

$$I_n = ((P_n - C_n) + I_{n-1}) \times R$$

where—

PÅnÉ is the aggregate of the sums paid by the cedant company to the reinsurer during that accounting period and earlier accounting periods by way of premium or otherwise;

CÅnÉ is the aggregate of the sums paid by the reinsurer to the cedant company during that accounting period and earlier accounting periods by way of commission or as a result of the surrender in part of the rights under the policy or otherwise;

IÅn − 1É is the aggregate amount of the net investment return in previous accounting periods, that is to say, net of tax at the rate prescribed by paragraph (2) below; and

R is the percentage rate of return prescribed by regulation 7(4) or (6), as the case may be;

but where the result is less than zero, taking the amount to be zero.

(2) The rate prescribed by this paragraph is the rate applicable in accordance with section 88(1) of the Finance Act 1989(**8**).

Calculation of investment return in final accounting period

6.—(1) Where the period during which a reinsurance arrangement is in force falls within more than one accounting period, the amount of the investment return in the final accounting period is the amount by which the profit over the whole period during which the policy and the reinsurance arrangement was in force (“the whole period”) exceeds the aggregate of the amounts of the investment returns in earlier accounting periods.

(**8**) Section 88(1) was amended by section 45(1) of the Finance Act 1990.

(2) For the purposes of paragraph (1) above, the profit over the whole period is the amount by which the aggregate of the amounts specified in paragraph (3) below exceeds the aggregate of all amounts paid to the reinsurer by way of premiums in respect of the policy.

(3) The amounts specified in this paragraph are—

(a) any amount payable by the reinsurer to the cedant company as a result of the maturity of the policy concerned;

(b) so much of any amount payable by the reinsurer as a result of the death, illness, or infirmity of, or accident to, any person as does not exceed the amount which would have been paid by the reinsurer if the policy had been surrendered immediately before the death, illness, infirmity or accident;

(c) any amount payable by the reinsurer as a result of the surrender in whole of the rights conferred by the policy;

(d) any amount payable by the reinsurer as a result of the surrender in part of the rights conferred by the policy;

(e) any amount not falling within any of sub-paragraphs (a) to (d) above which is payable by the reinsurer to the cedant company in respect of the policy, other than an amount which—

(i) forms part of the relevant profits of the cedant company, or

(ii) is paid by way of commission that has been deducted from expenses of management pursuant to section 76(1)(ca) of the Taxes Act.

Prescribed percentage rates of return for the purposes of regulations 4 and 5

7.—(1) Where the period during which a reinsurance arrangement is in force falls within more than one accounting period, the percentage rate of return—

(a) in relation to the first accounting period, is the rate prescribed by paragraph (2) below;

(b) in relation to any subsequent accounting period other than the final accounting period or an accounting period falling within paragraph (6) below, is the rate prescribed by paragraph (4) below.

(2) The rate prescribed by this paragraph is the rate ("R") found by the formula—

$$R = \frac{(D - E)}{G} \times F$$

where—

D is such percentage rate as is specified in any of paragraphs (7) to (10) below and is applicable to the reinsurance arrangement concerned and, if more than such rate is so applicable, is the first applicable rate specified in the order of those paragraphs;

E is the percentage rate which results from applying the formula specified in paragraph (3) below;

F is the number of days in the first accounting period falling after the date prescribed by regulation 8(2); and

G is the number of days in that accounting period;

but where the result is less than zero, taking the rate to be zero.

(3) The formula specified in this paragraph is—

$$\frac{A}{P - C}$$

where—

A is the amount of any payment made by the reinsurer to the cedant company which forms part of the relevant profits of that company for the first accounting period, other than a payment which falls to be taken into account under these Regulations in calculating the investment return to be treated as accruing to that company in that accounting period; and

P and C have the meanings given by regulation 4.

(4) The rate prescribed by this paragraph is the rate ("R") found by the formula—

$$R = (D - H)$$

where—

D has the meaning given by paragraph (2) above; and

H is the percentage rate which results from applying the formula specified in paragraph (5) below;

but where the result is less than zero, taking the rate to be zero.

(5) The formula specified in this paragraph is—

$$\frac{B}{((P_n - C_n) - I_{n-1})}$$

where—

B is the amount of any payment made by the reinsurer to the cedant company which forms part of the relevant profits of that company for the subsequent accounting period concerned, other than a payment which falls to be taken into account under these Regulations in calculating the investment return to be treated as accruing to that company in that accounting period; and

PÅnÉ, CÅnÉ and IÅn − 1É have the meanings given by regulation 5(1).

(6) In any case where a subsequent accounting period other than the final accounting period is less than 12 months in duration, the percentage rate of return prescribed in relation to that accounting period is the rate ("R") found by the formula—

$$R = \frac{J \times K}{365}$$

where—

J is the rate prescribed by paragraph (4) above, and

K is the number of days in that accounting period.

(7) In any case where—

(a) assets by reference to the value of which benefits payable under the reinsurance arrangement concerned are to be determined are held by the reinsurer in an internal linked fund, or by another company in an internal linked fund, or

(b) such assets are held directly by the reinsurer, that is to say, without being appropriated to an internal linked fund,

the percentage rate of return specified is the rate, expressed as a rate per annum, which is found by the formula—

$$\frac{X \times 100}{Y}$$

where—

X is the amount of investment income arising from those assets for the accounting period concerned, increased by the amount of any increase in the value of those assets which is identified in the records of the reinsurer or (as the case may be) the other company, or reduced by the amount of any reduction in the value of those assets which is so identified; and

Y is the mean of the value of those assets at the beginning and end of the accounting period concerned, as identified in those records;

but where the result is less than zero, taking the rate to be zero.

(8) In any case where—

(a) there is in force a deposit-back arrangement as part of the reinsurance arrangement, and

(b) the calculation of the rate of return on the deposit is capable of being expressed as a percentage rate per annum,

the percentage rate of return specified is such of the calculated rates of return on the deposit as is applicable to a period which includes any part of the accounting period concerned and is capable of being expressed not later than six months after the end of that accounting period and, if there is more than one such rate of return, is the average of those rates for periods beginning with the period which includes the date of commencement of the accounting period and ending with the period which includes the date of the end of the accounting period.

(9) In any case where the policy being reinsured provides for a percentage rate of return which is fixed or is capable of being determined for the accounting period concerned not later than six months after the end of that period, the percentage rate of return specified is that percentage rate plus 1 per cent.

(10) In any case not falling within paragraph (7), (8) or (9) above, the percentage rate of return specified is either—

(a) the rate found by—

(i) expressing the amount of the expected income from non-linked assets for the accounting period concerned as a percentage of the value of the total non-linked assets (other than assets not providing income) as identified in the relevant part of the periodical return of the cedant company specified in paragraph (11) below, and

(ii) adding 2 per cent to the result; or

(b) where—

(i) that periodical return contains no relevant part, or

(ii) the cedant company is not required to make a periodical return, or

(iii) the cedant company shows that in the circumstances the calculation specified in sub-paragraph (a) above would not produce a reasonable result,

such rate as the inspector determines to be just and reasonable in the circumstances after taking into account the factors specified in paragraph (12) below.

(11) The periodical return specified in this paragraph is the periodical return for the period of account immediately preceding the period of account in which the accounting period concerned falls, and "the relevant part" of that return means—

(a) in the case of a cedant company whose head office is in the United Kingdom, the part which shows the expected income from non-linked assets in respect of the whole of the company's long term business;

(b) in the case of a cedant company which is an overseas life insurance company—

(i) the part which shows the expected income from non-linked assets of the company's long term business fund relating exclusively to business carried on through a branch or agency in the United Kingdom or, if there is no such part,

(ii) the part which shows the expected income from non-linked assets of the company's long term business fund relating exclusively to business carried on through branches and agencies in the United Kingdom and EEA States taken together.

(12) The factors specified in this paragraph are—

(a) the nature of the policy concerned;

(b) the rate of interest assumed by the cedant company in determining the valuation of its liabilities in respect of the policy for the purposes of its periodical return;

(c) any undertaking by the cedant company with respect to—

(i) the nature of the assets in which the premiums it receives will be invested, or

(ii) the rate of return which it is offering or has offered on that or any similar policy.

(13) An appeal may be brought against a determination of the inspector under paragraph (10)(b) above by giving written notice to the inspector within 30 days of receipt of written notice of the decision.

(14) An appeal under paragraph (13) above shall lie to the Special Commissioners who may confirm or vary the determination appealed against (whether or not the variation is to the advantage of the appellant).

Ascertainment of investment return — prescribed dates of payments made under reinsurance arrangements

8.—(1) For the purposes of ascertaining the investment return in each accounting period, the payments specified in paragraphs (2) to (6) below shall be treated as paid on the dates prescribed by those paragraphs in relation to the payment concerned.

(2) In any case where under the reinsurance arrangement a premium or any other amount is payable to the reinsurer within 30 days of the date on which the first premium is paid to the reinsurer, the date prescribed as the date on which that premium or other amount is to be treated as paid is the date on which the first premium is paid.

(3) In any case where under the reinsurance arrangement commission or any other amount is payable by the reinsurer in respect of the policy concerned at the same time as the first premium is paid to the reinsurer or within 30 days of the date on which the first premium is paid to the reinsurer, the date prescribed as the date on which that commission or other amount is to be treated as paid is the date on which the first premium is paid.

(4) In any case where under the reinsurance arrangement—

(a) a premium other than the first premium or a premium falling within paragraph (2) above, or any other amount not being an amount falling within paragraph (2) above, is paid to the reinsurer before the end of the accounting period in which the first premium is paid, or

(b) commission or any other amount, not being commission or an amount falling within paragraph (3) above, is paid by the reinsurer to the cedant company before the end of that accounting period,

the date prescribed as the date on which that premium or other amount is to be treated as paid to the reinsurer, or that commission or other amount is to be treated as paid by the reinsurer, is the first day of the next accounting period.

(5) The dates prescribed as the dates on which any premium or any other amount paid to the reinsurer under the reinsurance arrangement, other than a premium or amount falling within paragraph (2) or (4)(a) above, is to be treated as paid are the following—

(a) as to one half of the amount of the premium or other amount, the date on which the premium or other amount is paid;

(b) as to the other half, the first day of the accounting period next following that in which the premium or other amount is paid.

(6) The dates prescribed as the dates on which any commission or any other amount paid by the reinsurer under the reinsurance arrangement, not being commission or an amount falling within paragraph (3) or (4)(b) above, is to be treated as paid are the following—

(a) as to one half of the commission or other amount, the date on which the commission or other amount is paid;

(b) as to the other half, the first day of the accounting period next following that in which the commission or other amount is paid.

Exclusion of certain reinsurance arrangements from section 442A

9.—(1) There shall be excluded from the operation of section 442A any reinsurance arrangement in respect of a policy which falls within any of the descriptions prescribed by paragraphs (2) to (4) below.

(2) The description prescribed by this paragraph is of any reinsurance arrangement where—

(a) both the cedant company and the reinsurer are insurance companies which are either resident in the United Kingdom or, as respects the reinsurance arrangement or, as the case may be, the business to which the reinsurance is attributable, are within the charge to corporation tax by virtue of section 11 of the Taxes Act(**9**);

(b) the cedant company is a 90% subsidiary of the reinsurer, or the reinsurer is a 90% subsidiary of the cedant company, or each is a 90% subsidiary of another body corporate; and

(c) the reinsurer is not a company which is charged to tax under Case I of Schedule D.

(3) The description prescribed by this paragraph is of any reinsurance arrangement where—

(a) the reinsurer is a company which in the relevant period is chargeable to tax under the laws of the territory in which it is domiciled or resident in respect of amounts to which the reinsurance arrangement gives rise;

(b) the head office of the reinsurer is in an EEA State;

(c) the charge to tax in the relevant period is such a charge made otherwise than by reference to profits as (by disallowing their deduction in computing the amount chargeable) to require sums payable and other liabilities arising under reinsurance arrangements to be treated as sums or liabilities falling to be met out of amounts subject to tax in the hands of the reinsurer;

(d) the rate of tax fixed for the purposes of that charge in relation to the amounts subject to tax in the hands of the reinsurer (not being amounts arising or accruing in respect of investments that are of a particular description for which a special relief or exemption is generally available) has in the relevant period been at least 20 per cent.;

(e) none of the obligations of the reinsurer under the reinsurance arrangement to pay any sum or meet any other liability, other than obligations in respect of mortality risk or morbidity risk, has itself been the subject of a reinsurance arrangement;

(f) no deposit-back arrangements are in force in respect of the reinsurance arrangement; and

(g) the reinsurer is not subject in the relevant period to a restriction in the amount of the expenses which may be deducted in computing its liability to tax, where the restriction is calculated by reference to the amount of its profits.

(4) The description prescribed by this paragraph is of any reinsurance arrangement under which—

(a) (i) only the mortality risk or the morbidity risk is being reinsured, or both the mortality risk and the morbidity risk (but no other risk) are being reinsured, and

(**9**) Section 11 was amended by section 98(4) of, and Part V of Schedule 19 to, the Finance Act 1990, paragraph 14(2) of Schedule 10 to the Taxation of Chargeable Gains Act 1992 (c. 12), and Part III (9) of Schedule 23 to the Finance Act 1993 (c. 34).

(ii) no payment by way of surrender value is capable of being made by the reinsurer to the cedant company; or

(b) either—

(i) no profit such as is referred to in regulation 6(2) is capable of arising; or

(ii) such profit is capable of arising only as a result of the death, illness or infirmity of, or accident to, a person or the lapsing of the policy.

(5) In paragraph (3) above, "the relevant period" means a period for which the reinsurer draws up accounts and which ends in or at the end of an accounting period of the cedant company or, if there is more than one such period ending in or at the end of the same accounting period, the period which is the first to end.

(6) For the purposes of paragraph (4) above, the fact that a premium payable by the cedant company under the reinsurance arrangement is calculated so as to reflect a guarantee by that company under the terms of the policy that it will issue a different policy at a future date shall not be taken to mean that risks other than mortality risk or morbidity risk are being reinsured under the reinsurance arrangement.

Exclusion of policy and contract from section 442A

10. There shall be excluded from the operation of section 442A—

(a) any policy to which paragraph 10 of Schedule 1 to the Financial Services Act 1986(**10**) does not apply by reason of Note (1) to that paragraph; and

(b) any annuity contract under which—

(i) payment of the annuity is to commence not later than 12 months after the date of the contract, and

(ii) no surrender value is capable of being produced.

Exclusion of certain business from section 431C

11. There shall be excluded from section 431C any reinsurance business where—

(a) in relation to the reinsurance arrangement—

(i) the cedant company is a 90% subsidiary of the reinsurer, or the reinsurer is a 90% subsidiary of the cedant company, or each is a 90% subsidiary of another body corporate,

(ii) the cedant company is either resident in the United Kingdom or is an overseas life insurance company which, as respects the reinsurance arrangement or, as the case may be, the business being reinsured, is within the charge to corporation tax by virtue of section 11 of the Taxes Act, and

(iii) the business being reinsured is basic life assurance and general annuity business in the hands of the cedant company; or

(b) the business is of any of the descriptions specified in section 431D(1)(b) of the Taxes Act(**11**); or

(c) the business—

(i) is the reinsurance of the business of a company which is not resident in the United Kingdom,

(**10**) 1986 c. 60.
(**11**) Section 431D of the Taxes Act was inserted by paragraph 2 of Schedule 8 to the Finance Act 1995.

(ii) is not business of any of the descriptions specified in section 431D(1)(b) of the Taxes Act, and

(iii) is linked business where the linked assets concerned consist wholly or substantially of land in the United Kingdom.

Exclusion of certain reinsurance business from section 439A

12. There shall be excluded from section 439A any reinsurance business carried on by a company ("the reinsurer") whose reinsurance business is limited to arrangements where—

(a) the cedant company is a 90% subsidiary of the reinsurer, or the reinsurer is a 90% subsidiary of the cedant company, or each is a 90% subsidiary of another body corporate, and

(b) the cedant company either—

(i) is resident in the United Kingdom, or

(ii) is not so resident but, as respects all the business reinsured with the reinsurer, is within the charge to corporation tax by virtue of section 11 of the Taxes Act.

S. C. T. Matheson
G. H. Bush
7th July 1995 — Two of the Commissioners of Inland Revenue

EXPLANATORY NOTE

(This note is not part of the Regulations)

Section 442A of the Income and Corporation Taxes Act 1988 ("section 442A") (inserted by paragraph 34 of Schedule 8 to the Finance Act 1995) provides for the taxation of the investment return on an insurance policy or annuity contract which is the subject of a reinsurance arrangement by the insurance company concerned. These Regulations make provision in relation to the calculation of the investment return, and also exclude certain reinsurance arrangements and policies from the operation of section 442A. Finally the Regulations exclude certain reinsurance business from specified provisions of the Income and Corporation Taxes Act 1988 concerned with reinsurance business.

Regulation 1 provides for citation, commencement and effect and regulation 2 contains definitions.

Regulations 3 to 6 provide for the methods of calculation of the amount of the investment return for each accounting period during which the reinsurance arrangement is in force, and regulation 7 prescribes the percentage rate of return for the purposes of calculating that amount for consecutive accounting periods other than the final accounting period.

Regulation 8 prescribes, for the purpose of ascertaining the investment return in each accounting period, the dates on which payments of premium, commission or other amounts under the reinsurance arrangement are to be treated as made.

Regulation 9 excludes specified reinsurance arrangements, and regulation 10 excludes specified policies and contracts, from the operation of section 442A.

Regulation 11 excludes certain reinsurance business from section 431C of the 1988 Act (meaning of "life reinsurance business") and regulation 12 excludes certain reinsurance business from section 439A of that Act (taxation of pure reinsurance business). (Sections 431C and 439A were inserted by paragraphs 2 and 26 respectively of Schedule 8 to the Finance Act 1995).

By virtue of paragraph 58 of Schedule 8 to the Finance Act 1995, these Regulations have effect in relation to accounting periods beginning on or after 1st January 1995.