هيئة الزكاة والضريبة والجمارك
Zakat, Tax and Customs Authority

VAT Guideline:

INSURANCE & REINSURANCE ACTIVITIES

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This guideline is addressed to all natural and legal persons who carry on an economic activity and who are subject to VAT. The purpose of this guideline is to provide more clarifications regarding to insurance and reinsurance activities.

This guideline represents ZATCA's view on the application of the unified VAT agreement, the VAT law and the VAT implementing regulation regarding to insurance and reinsurance activities as of the date of this guideline. This guide amounts to a guideline and does not include or purport to include all the relevant provisions for insurance and reinsurance in the unified VAT agreement, the VAT law or the VAT implementing regulation. It is not binding on ZATCA or any taxpayer in respect of any transaction carried out and it can not be relied upon in any way.

For further advices on a specific transaction, you may apply for a ruling or visit the official website of the authority gazt.gov.sa which contains a wide range of tools and information that has been established as a reference to support persons subject to VAT, as well as visual guidance materials, and all relevant information and FAQ's.

Subject matter of this guideline

This guideline addresses the application of VAT on the insurance and reinsurance activities made by businesses, and provides interpretation on the KSA Value Added Tax Law and its Implementing Regulation.

1.Insurance activities

- The core of the insurance business model is for the insurer (insurance company) to agree to take on risks on behalf of a customer ("policyholder") in case of an uncertain event materializes in the future. When the uncertain event materializes, the policyholder/the beneficiary of the policy can make a claim against the insurance company. The policyholder also, is required to pay a premium to the insurer in exchange for protection for this uncertain future events according to the insurance policy›s scope.
- In most of the cases within KSA, policyholders are KSA residents companies and/or individuals insuring themselves or their assets in the KSA. Some insurers also appoint insurance agents/brokers for selling life insurance and general insurance products in the market on the insurer's behalf.
- From a VAT perspective, broadly two services will be recognised when entering into an insurance transaction where a broker is also involved:
  - Premium that is paid/owed by the policyholder to the insurer as a consideration for supplying insurance services from the insurer;
  - Brokerage commission that is paid/owed by the insurer to the insurance broker as a consideration for brokerage services which provided by the insurance broker.
- The default VAT position for all non-life insurance provided in the KSA is that contracts of insurance and all insurance products are standard rated. This includes all products defined by Saudi Central Bank to be general insurance or health insurance – and any other insurance related services[1].

2.Reinsurance activities

- Insurers commonly share a portion of risks which they have underwritten. They do this as a way to reduce their possible losses when they are liable to indemnify policyholders for large sums of money, upon the occurrence of an insured event. Insurers commonly manage risk of losses by taking out reinsurance policies from one, or a panel of, reinsurance providers ("reinsurers"). Reinsurance providers may be located in the same country as the insurer or may operate in a different country.

- From a VAT perspective, broadly three services› fees could be recognised when entering into reinsurance transactions:
  - Reinsurance broker commission paid/owed by the reinsurer to the reinsurance broker/agent;
  - Reinsurance premium paid/owed by the insurer to the reinsurer in return for insuring the risk portfolio of the insurer;
  - Reinsurance commission received by the insurer from the reinsurer for giving the reinsurer the possibility to profit from the insurer's risk portfolio, and to compensate the insurer for its costs in this respect.

3.Treatment of VAT on insurance contracts and premiums premiums (for both insurance company & policyholder)

3.1 Life insurance

- Life insurance contracts[(2)] in KSA are exempted from VAT, under which life insurance services would be supplied from an authorized service provider (insurance company) in KSA, or any other similar contract provided by a non-resident supplier. Therefore, no VAT is charged.

(2) Article 29(8), financial services, VAT implementing regulation," life insurance contract means, any contract of conventional insurance or takaful or another form of Islamic insurance provided by a regulated provider in the KSA which results in the payment of a sum contingent on death or another significant event of human life, or a similar contract provided by a non-resident supplier".

Example: Insurance company XYZ, a Saudi registered company, sells employee term life insurance to company ABC at a premium of SAR 50,000. As life insurance is exempt from VAT, no VAT is charged on the term life insurance premium of SAR 50,000 and Company ABC only pays SAR 50,000 as premium to Insurer XYZ.

3.2 General insurance

- Conversely, general or health insurance contracts are subject to VAT at the standard rate, under which insurance services would be provided by service provider (insurance company).

Example: Insurer XYZ, also sells general insurance to Company ABC at a premium of SAR 100,000. Insurer XYZ charges VAT at 15% on the premium as follows:

Premium	SAR 100,000
VAT @ 15%	SAR 15,000
Total	SAR 115,000

Company ABC pays SAR 115,000 to insurer XYZ but will be able to deduct the VAT of SAR 15,000 from ZATCA, providing the general insurance purchased is related to its taxable business activities – subject to normal input tax deduction rules and requirements.

4.Treatment of VAT on reinsurance contracts (for both principal insurance company & the reinsurance company)

4.1. Resident insurer & Resident reinsurer

4.1.1. Life Insurance

- Reinsurance of life insurance contracts in ksa are exempted from vat, under which reinsurance of life[3] services would be supplied from an authorized service provider (insurance company) in ksa, or any other similar contract provided by non- resident supplier in ksa. Therefore, no vat is charged.
- However, reinsurance commission on reinsurance of life insurance shall be subject to VAT, although, the resident reinsurer will not be able to deduct the VAT paid because it is related to an exempt supply.

Example: Insurer XYZ reinsures its term life insurance portfolio to resident reinsurer AAA, with a reinsurance premium of SAR 50,000 and charges reinsurance commission at 20%. Insurer XYZ pays SAR 50,000 to resident reinsurer AAA for the reinsurance premium, no VAT is charged on the reinsurance premium of SAR 50,000 as the underlying insurance is life insurance.

Insurer XYZ charges VAT at 15% on the reinsurance commission as follows:

Reinsurance Commission	SAR 10,000
VAT @15%	SAR 1,500
Total	SAR 11,500

Resident reinsurer AAA pays SAR 11,500 to Insurer XYZ. However, no VAT deduction is possible on this transaction by AAA as the expense is related to an exempt supply.

4.1.2. General Insurance

- Reinsurance premium for general, or health insurance in KSA is subject to VAT, which is paid by a taxable resident insurer for a resident reinsurer. And as such the input VAT should be deductible because it is related to a taxable supply.

- Reinsurance commission on reinsurance of general, or health insurance shall be subject to VAT, and the insurance company shall impose and collect the tax under tax invoices from the reinsurer (customer), and the resident reinsurer should be able to deduct the VAT paid because it is related to a taxable supply.

Example: Insurer XYZ reinsurers its general insurance portfolio to resident reinsurer AAA with a reinsurance premium of SAR 100,000 and charges reinsurance commission at 20%. Insurer XYZ pays SAR 115,000 to resident reinsurer AAA and deducts VAT of SAR 15,000 from ZATCA as the expenses are related to a taxable supply. The taxable reinsurer shall declare about the tax and supply it to ZATCA within the tax return.

Resident reinsurer AAA charges VAT at 15% on the reinsurance premium as follows:

Reinsurance Premium	SAR 100,000
VAT @15%	SAR 15,000
Total	SAR 115,000

Also, insurer XYZ charges VAT at 15% on the reinsurance commission as follows:

Reinsurance commission	SAR 20,000
VAT @15%	SAR 3,000
Total	SAR 23,000

Resident reinsurer AAA pays SAR 23,000 to Insurer XYZ and deducts VAT of SAR 3,000 from ZATCA as the expenses are related to a taxable supply. The taxable insurer shall declare and pay the due tax to ZATCA within the tax return.

4.2. Resident insurer & Non-Resident reinsurer

4.2.1. Life Insurance

- Reinsurance premium for life insurance paid by a resident insurer for a non-resident reinsurer will be exempted from VAT (i.e. VAT is not accounted for in principal).
- Reinsurance commission on the reinsurance of life insurance shall be subject to VAT at the zero rate. Taking into consideration that the fulfillment of all conditions mentioned in the provisions of article (33) of VAT Implementing Regulation is a must.

Example: Insurer XYZ reinsures its term life insurance portfolio to non-resident reinsurer BBB, with a reinsurance premium of SAR 50,000 and charges reinsurance commission at 20%. Non-resident reinsurer BBB does not charge VAT on the reinsurance premium.

Insurer XYZ pays non-resident reinsurer BBB SAR 50,000 as the reinsurance premium and is not required to account for VAT via the reverse charge mechanism.

Insurer XYZ charges VAT at 0% on the reinsurance commission as follows:

Reinsurance Commission	SAR 10,000
VAT @0%	SAR 0
Total	SAR 10,000
Non-resident reinsurer BBB pays	SAR 10,000 to Insurer XYZ.

4.2.2. General Insurance

- Reinsurance premium for general, or health insurance paid by a taxable resident insurer for a non-resident reinsurer will be subject to VAT at the standard rate, and as such VAT will be accounted for through the reverse charge mechanism.

- Reinsurance commission on reinsurance of general, or health insurance shall be subject to VAT at the zero rate. Taking into consideration that the fulfillment of all conditions mentioned in the provisions of article (33) from VAT Implementing Regulation is a must.

Example: Insurer XYZ reinsurers its general insurance portfolio to non-resident reinsurer BBB with a reinsurance premium of SAR 100,000 and charges reinsurance commission at 20%. Non-resident reinsurer BBB does not charge VAT on the reinsurance premium.

Insurer XYZ pays non-resident reinsurer BBB SAR 100,000 as the reinsurance premium and accounts for the VAT via the reverse charge mechanism.

Insurer XYZ charges VAT at 0% on the reinsurance commission as follows:

Reinsurance Commission	SAR 20,000
VAT @ 0%	SAR 0
Total	SAR 20,000
Non-resident reinsurer BBB pays	SAR 20,000 to Insurer XYZ.

5.Insurance Claims

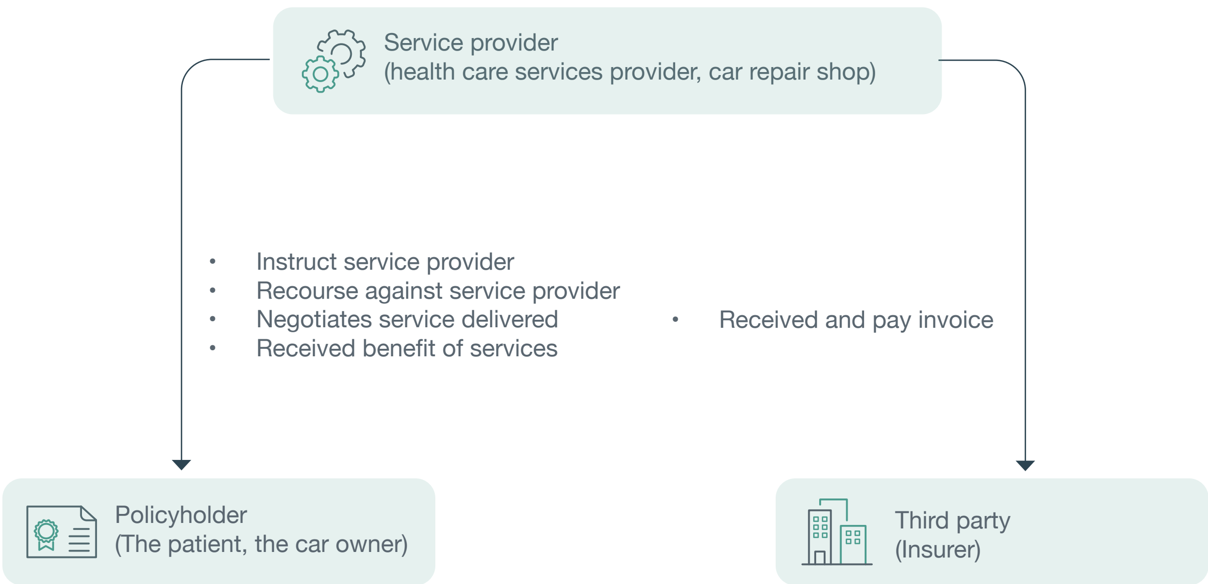
- The customer for VAT purposes is the person who is the recipient of a supply of goods or services[4] under general VAT principles, the customer is normally determined by the contractual arrangements, such as:
  - The person instructs the supplier in connection with the supply of goods or services;
  - The person enters into a contract with the supplier; or
  - The person has the power to compel the supplier to perform and comply with their contractual obligation in connection to the supply of goods or services.

(4) Article 1, Definitions, Unified VAT Agreement

- Generally, the value of the concluded insurance contracts with non-taxable individuals or persons is calculated so that the amounts paid by the insurance companies under the insurance policy included VAT, whereas the value of the concluded contracts with taxable persons who are registered for VAT purposes is calculated so that the payments under the insurance policies from the insurance company do not include the tax, and that's because of the ability of the policyholders to deduct tax incurred.

- In the insurance claim context, the policyholder (e.g., the patient in the health insurance, the car owner in the car insurance) receives a direct benefit from the service provider's services (e.g., health care services provider, car repair shop). When the uncertain event materializes, the policyholder can make a claim against the insurance company. Therefore, it will be presumed that the policyholder is the recipient of the service provider's services, unless this is expressly evidenced otherwise. This is the case even where the service provider issues the invoice to the insurer, or it is the insurer who is responsible for paying the service provider, as illustrated in the following diagrams:

Diagram (1): The policyholder is the customer for VAT purposes



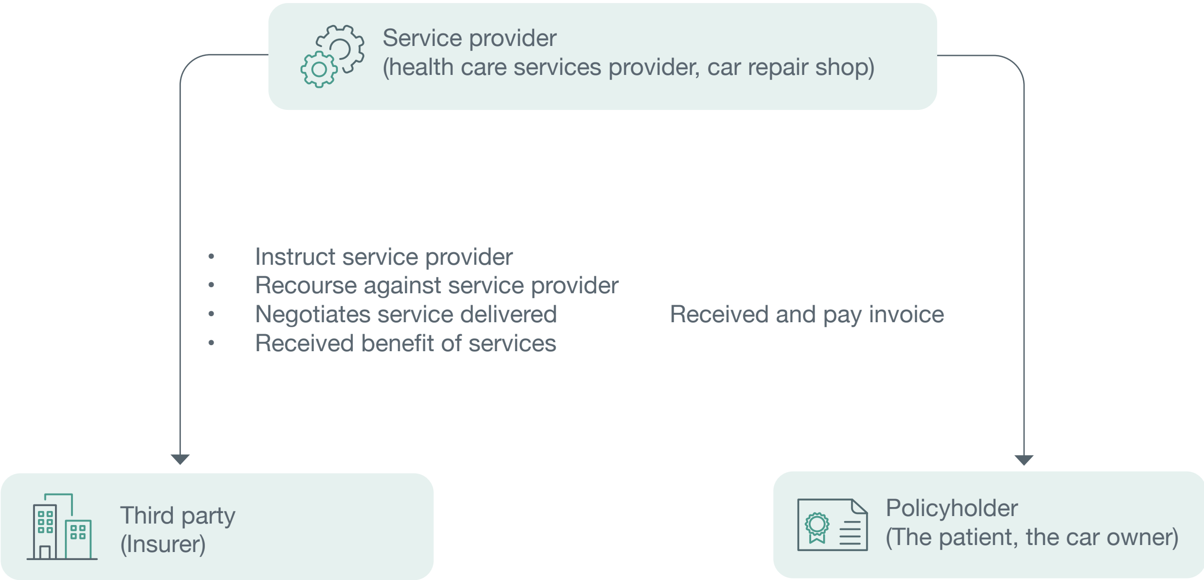
- A variation to the above scenario can occur where the policyholder pays the service providers and then submits a reimbursement claim to the insurer.

Diagram (2): The policyholder pays the services provider and then submits a reimbursement claim to the insurer

- Insurance companies cannot claim to deduct input tax which related to payments of owed monetary claims to the insured. Where it is not allowed to deduct input tax except the one that incurred by the insurance company on supplies provided for it. And so, there will be additional cost on insurance companies regarding disbursement of funds which included VAT under insurance policies provided to non-taxable persons.

- In some cases, the insurer may be able to instruct the service provider to carry out the services to the policyholder to satisfy their own obligation under an insurance contract or policy to provide services. In these cases, it may be possible for that insurer to be the primary recipient of the services, even though it is the policyholder who receives the benefit from the services.

Diagram(3): The policyholder is the customer for VAT purposes



- It is clear from this that it is possible for a person to has the right to benefit or use from goods or services provided under a contract where he might not be one of its parties directly. in spite of that he is not the «customer» as defined for VAT purposes.

- For VAT purposes, the claim payments are considered outside the scope of tax, where the insurance company pay it according to its obligation under the insurance policy, and it is not a consideration for a supply to the insurance company, and this in situations where the reimbursement claim is payed to the policyholder, or the policyholder is the costumer/ services recipient.

5.1. Reinsurer's share of claim

- Under a reinsurance agreement between an insurer and a reinsurer, the reinsurer is obligated to reimburse the insurer for payments made by the insurer on their insurance business.

- The extent of the reinsurer's obligation is based on the actual payments made by the insurer in settlement of the insurer's obligation under an insurance contract with a policyholder, where a claim event had occurred (e.g. hospitalization).

- Generally, unless the insurer has paid or is required to pay, the reinsurer has no obligation to the insurer under the reinsurance agreement.
- The reinsurance agreement could be seen as an indemnity the reinsurer provides to the insurer (subject to the terms of the reinsurance agreement) for the claims that the insurer pays out on its insurance business.
- The indemnity payments are out of scope for VAT purposes, as the reinsurer is paying the amount out of an obligation pursuant to a reinsurance agreement, and not as consideration for a supply from the insurer.

6.Treatment of insurance claims (maintenance – medical treatments) – for both principal insurance company & the policyholder

- An insurance claim may be settled by payment of a monetary claim, or by the insurer agreeing to arrange or pay for treatment or repairs the assets to return them to their original standard. If an insurer makes a pay-out to a policyholder, this is not regarded as a supply made by the insurer for VAT purposes. No VAT obligations arise in respect of the pay-out received.
- Services provided to a policyholder pursuant to a contract between the insurer and service provider will be subject to VAT. The resident insurer should be entitled to deduct VAT paid and the policyholder is not obligated for any VAT liability.
- In the case of services provided to a policyholder without a contract between the insurer and service provider, VAT is also charged. However, the resident insurer cannot deduct VAT paid and the policyholder is not obligated for any VAT liability.
- If the policyholder pays the service provider and submits a reimbursement claim to the insurer, then VAT must be charged. The resident insurer cannot deduct VAT paid, however, the resident policyholder will be able to deduct VAT if it is related to the policyholder's taxable economic activities.

Example: Policyholder DDD seeks services from service provider SSS under an insurance contract with insurer XYZ. The cost of the service is SAR 1,000. Service provider SSS raises an invoice to insurer XYZ. There is a contract between the service provider SSS and insurer XYZ.

Service provider SSS charges VAT at 15% on the services provided to policyholder DDD as follows:

Services	SAR 1,000
VAT @15%	SAR 150
Total	SAR 1,150

Policyholder DDD enjoys the benefit of the services and the insurer pays the service provider SSS SAR 1,150 and deducts VAT of SAR150 from ZATCA as it is related to a taxable supply.

In cases where there is no contract between the service provider and the insurer, then the service provider SSS charges VAT at 15% on the services provided to policyholder DDD as follows:

Services	SAR 1,000
VAT @15%	SAR 150
Total	SAR 1,150

Policyholder DDD enjoys the benefit of the services. Insurer XYZ pays service provider SSS SAR 1,150.

No VAT deduction is possible as there is no contract between service provider SSS and insurer XYZ.

Another scenario is where a policyholder seeks services from service provider SSS. The service provider raises an invoice to the policyholder, who subsequently submits a reimbursement claim under an insurance contract to insurer XYZ.

Service provider charges VAT at 15% on the services provided to the policyholder:

Services	SAR 1,000
VAT @15%	SAR 150
Total	SAR 1,150

Policyholder pays SAR 1,150 to the service provider and deducts the VAT of SAR 150 since it is related to its business activities. The insurer pays policyholder SAR 1,000 as a settlement for the reimbursement claim.

7.VAT Deduction

- The right of an insurer (or reinsurer) to deduct VAT incurred on its purchases is based on the goods and services being used for the purpose of carrying on its business activities, in the course of making taxable supplies[5].
- The terms "for the purpose of carrying on business activities" and "in the course of making taxable supplies" means that VAT deduction requires the supplies purchased to have a sufficient link between these supplies and the onward supplies of the insurer.
- VAT incurred on purchases made outside of the insurer's business activities or purchases related to the insurer's VAT exempt activities (e.g. selling life insurance) are not deductible. Conversely VAT incurred on expenses directly attributable to taxable supplies (e.g. general insurance) are fully deductible.
- VAT incurred on expenses which are related partly to taxable and exempt supplies must be apportioned for deduction purposes. Expenses that cannot be directly attributed to taxable or exempt supplies are often referred to as general expenses or non-attributable expenses[6].

No	Details	Deduction
1	VAT incurred on expenses exclusively and directly related to taxable supply	Fully deductible
2	VAT incurred on expenses exclusively and directly related to exempt supply	Non-deductible
3	VAT incurred on expenses that cannot be directly attributable to taxable or exempt supply	Partially deductible based on apportionment

(5) Article 49 (1), Input Tax deduction, VAT Implementing Regulation
(6) Article 51, Proportional deduction of Input Tax, VAT Implementing Regulation

7.1. Partial VAT Deduction

- The expenses incurred by the insurer for making both taxable and exempt supplies must be apportioned to most accurately reflect the use of those costs in the taxable portion of the insurer's business activities.

  A prescribed default method of apportionment is calculated on the value of supplies made in the year, using the following formula:[7]

$$\frac{\text{The value of taxable supplies made by the person in the last calendar year}}{\text{The total value of taxable supplies and exempt supplies made by the person during the last calendar year}}$$

- Following the end of the completed calendar year, the insurer, using the default method must carry out an exercise to compare the values used in the fraction during that year (based on the previous year or an estimate for the current year) with the actual values of supplies made in that calendar year.

- The person must then make an adjustment to the VAT deducted in the final tax return of the calendar year to reflect the correct proportional deduction based on the actual supplies for the entire year.

Example: Insurer XYZ utilizes the services of Broker ZZZ to sell general insurance to Company ABC and pays commission at 10%.

Broker ZZZ charges insurer XYZ VAT at 15% on the commission:

Commission	SAR 10,000
VAT @15%	SAR 1,500
Total	SAR 11,500

Insurer XYZ pays SAR 11,500 to broker ZZZ and deducts VAT of SAR 1,500 from ZATCA as the expenses are related to a taxable supply.

Alternatively, if insurer XYZ utilizes the services of Broker XXX to sell employee term life insurance to Company ABC and pays commission at 10%, then VAT at 15% will also be applicable on the commission by the broker. However, no VAT deduction is possible as the expense is related to an exempt supply (life insurance).

Example: Insurer XYZ's total taxable supply for the calendar year is SAR 1,000,000 and total exempt supply for the year is SAR 500,000. The Insurer also purchases furniture for its office for SAR 100,000 and incurred VAT of SAR 15,000. The office furniture is used both for making taxable and exempt supplies.

Insurer XYZ pays VAT at15% on the purchase of the office furniture:

Furniture	SAR 100,000
VAT @15%	SAR 15,000
Total	SAR 115,000

Insurer XYZ's partial VAT deduction ratio is (1,000,000 (1,000,000+500,000)) 67%. Accordingly, the VAT deductibility is SAR 10,000 (67% * SAR 15,000), and the VAT not deductible is SAR 5,000.

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