# EXPLANATORY MEMORANDUM

## THE INSURANCE COMPANIES (TAXATION OF REINSURANCE BUSINESS) (AMENDMENT) REGULATIONS 2004 No. 2189

1. This explanatory memorandum has been prepared by the Commissioners of Inland Revenue and is laid before the House of Commons.

### Description

2. These regulations amend the Insurance Companies (Taxation of Reinsurance Business) Regulations SI 1995/1730 ("the Principal regulations") to remove an exemption from their operation for certain financial reinsurance contracts and to provide for cases where payment of premiums for reinsurance is made indirectly as well as directly.

### Matters of Special interest to the Select Committee on Statutory Instruments

3. None.

### Legislative Background

4. These regulations are being made under powers conferred by section 442A of the Income and Corporation Taxes Act 1988 ("ICTA"). The regulations are being made under the negative resolution procedure.

### EU legislation

6. The Regulations do not implement EU legislation.

### Extent

7. The instrument applies to all of the United Kingdom.

### Policy Background

8. Section 442A ICTA was enacted in 1995 to prevent avoidance of corporation tax by the use of reinsurance. Where a company carrying on life assurance business enters into a contract of reinsurance under which it reinsures the investment risk in policies which constitute basic life assurance and general annuity business, section 442A ICTA provides that an amount of income is imputed to the contract which comes within the charge to corporation tax. Without this charge, any investment return arising from the business and which is paid to the cedant company by way of a reinsurance claim would escape tax.

9. The details of the calculation of the taxable amount are left to regulations. They proceed by identifying certain types of reinsurance arrangement which are not affected by section 442A ICTA , and by setting out the rules for calculation of the investment return in other cases.

10. Some types of reinsurance contract are in substance financing transactions. It was thought that such contracts could not be used to create the mischief against which section 442A was directed, and in 2003 such contracts were excluded from the scope of section

442A by Taxation of Reinsurance Business (Amendment No. 2) Regulations SI 2003/2573.

11. Subsequently it has been discovered that entering into such reinsurance contracts can be used, in conjunction with other arrangements, to avoid corporation where there is a simultaneous transfer of business. A new section 82C Finance Act 1989 is inserted by Schedule 7 Finance Act 2004 to counter such avoidance. Some such arrangements also seek to avoid a charge to tax under section 442A.

12. These regulations remove the exemption in the Principal regulations for such contracts. It has also been discovered that the same arrangements attempt to circumvent section 442A and the Principal regulations by not paying the premiums for the reinsurance contract directly to the reinsurer. The regulations ensure that indirect payments are caught by the Principal regulations.

**Impact**

13. A Regulatory Impact Assessment has not been published for this instrument. These regulations close a loophole in the Taxation of Reinsurance Business Regulations (SI 1995/1730) (as subsequently amended) under which companies carrying on life assurance business could avoid section 442A ICTA be entering into complex financial reinsurance contracts, including in circumstances where the premium for the contract is paid indirectly. There are no impacts on the industry.

14. The regulations will have an Exchequer impact. They will prevent the avoidance of tax by the use of financial reinsurance contracts.

**Contact**

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