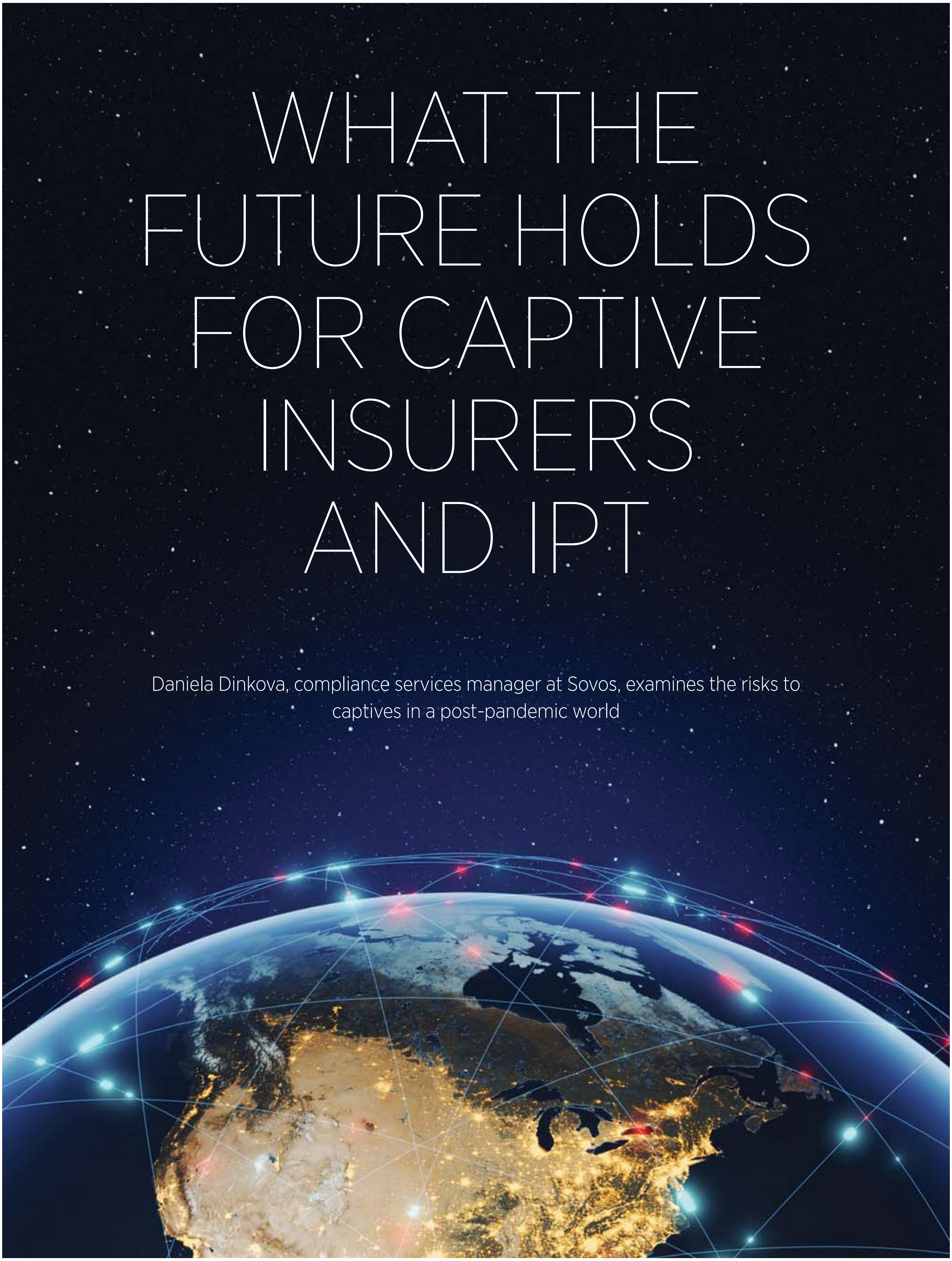
WHAT THE FUTURE HOLDS FOR CAPTIVE INSURERS AND IPT

Daniela Dinkova, compliance services manager at Sovos, examines the risks to captives in a post-pandemic world



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Wherever you are in the world, tax reporting is incredibly complex. Governments globally have and continue to show a keen interest in digitising tax to propel their economies forwards following the Covid-19 pandemic. In order to ensure they recoup taxes owed, some governments have already mandated real-time reporting and many more are looking to do the same.

Digitisation is meant to simplify and streamline compliance operations for businesses. However, regular new rates that differ across each jurisdiction means, in reality, that captives which operate across different territories have their work cut out to stay on top of the myriad of compliance requirements imposed by different tax authorities.

It's impossible to disregard the impact that the pandemic has had on the captive insurance market. It caused fundamental changes to organisations in almost every industry and, since the beginning of the pandemic, the number of captives has plateaued. Despite all this, global markets have resumed business as usual and Europe remains the third largest home to captive insurers, with around 15% of companies registered on the continent.

The question now is, how can captives prepare for what's next and cover any other potential risks? Let's look at what the future holds for captive insurers.

An evolving landscape facing captives

One question for captives in the coming months and years ahead will be their ability to cover pandemic risks. While some argue that insurance captives are a good tool to cover business interruption risks and, in practice, already cover pandemic risks and business interruption not related to material damage, others are quick to point out the scale of the current pandemic as well as the fact that it affects virtually every single countries in the world.

There is a difference in insuring a pandemic locally and globally, as if all countries covered by a captive programme are affected, it becomes more complicated for a captive (or any other insurance company) to compensate all its local insureds.

The pandemic will have offered captives valuable lessons, being the first time since digital technology emerged that a health crisis on this scale has caused such disruption. While the pandemic is referred to as a 'once in a lifetime' event, captives will need to take considerations from the last few years to plan for any potential future risks.

What we can say for certain is that the digital transformation of tax authorities and growing complexity for filing and reporting tax across different authorities will continue. This will further increase the complexity and fragmentation demands for captives operating across different jurisdictions, so the need for technology to ease the burden on administrative tasks will only grow.

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In terms of insurance premium tax (IPT), there's a lot to cause headaches for captives. With varying currencies, rates, deadlines and penalties for non-compliance, knowing exactly what is required by each tax authority is now essential. That's another reason why captives are increasingly looking at technology or to outsource in order to manage compliance and risk.

Staying ahead of IPT changes

Due to the increasing complexity of IPT compliance, the consequence for non-compliance has become a major concern for captive insurers. Risks now go beyond simple statutory or legal penalties. The inconvenience and cost of fixing reporting errors is higher than ever, not to mention the added reputational damage non-compliance can cause.

IPT has traditionally been difficult for governments to regulate, as the responsibility falls on the insurer to register and pay. With this in mind, last year the UK government published a report of its 'administration and unfair outcomes' IPT consultation. The consultation covered three main issues:

1. Unregistered insurers that fail to fulfil their IPT obligations
2. The use of avoidance structures by some members of the insurance industry
3. Whether the administration of IPT could be improved to reduce the administrative burden on industry stakeholders and HMRC.

One suggested solution was the introduction of joint and several liability for IPT. Many of the parties involved in the consultations were firmly against this. Abolishing IPT altogether is another option that the UK government is also considering.

VAT would take its place and help streamline processes for HMRC to monitor compliance, as well as for taxpayers to report and pay their dues. One consideration for this is whether the standard VAT rate (currently at 20%) would be applied to all non-life insurance policies, instead of the current standard IPT rate (12%), and whether varying tax rates would be applied for different insurance policies.

Several other countries across Europe, such as Spain, Portugal, Luxembourg and recently Ireland, have already introduced online filing for IPT. This gives their tax authorities the capability to comprehensively audit IPT compliance, however, it also increases the burden on administrative teams in terms of collecting all the data required to comply with IPT. Automating these processes at the tax authorities' level will make reporting, remittance and payment for IPT easier for each jurisdiction.

With all this in mind, captives are sure to see changes ahead. With the continued digitisation of tax, lessons learnt from the pandemic and evolving IPT compliance, captives will need to leverage technology to stay ahead of major changes as the market evolves.