

Regulation suggestions of the Federal Ministry of Finance on the taxation of "Insurance mantles" dated September 2008

We have been aware that some suggestions were made by the Federal Ministry of Finance (BMF) for amending the taxation of life insurance contracts. The BMF has targeted contracts that are commonly referred to as "Life insurance wrappers".

BMF Plans

Alongside a distinction between policy loans and the tax treatment of payments on maturity as well as a specification of the requirements of retirement policies, the BMF suggestions include the following two aspects:

New rules on the extent of the risk coverage (minimum death coverage (*Mindesttodesfallschutz*)): 10% of the current fund value or 60% of the sum of the premiums

According to the information available, the BMF will accept "sufficient / considerable risk coverage" if one of the two following requirements is met:

- the death coverage is, throughout the duration of the contract at least 60% of the sum of the premiums due during the savings period of the policy
- at the occurrence of the insured event (death of the insured person) the coverage payment exceeds the fair value of the insurance by at least 10%.

Recurrent allocation of taxable income

The BMF intends to attribute, taxwise, income from the capital investments to the policyholders as the beneficial owners of the policy provided the following criteria are met:

- the investment consists of "individual investment funds" or of other capital investments as investment fund units;
- the policyholder or an administrator appointed by him determines the acquisition and disposal of underlying investments;
- the policyholder can demand a transfer of the investments and exclude the insurance company from any influence on the investments.

Act or Decree / question of the retroactive effect

The BMF suggests an administrative directive as an "alternative solution" to a parliamentary amendment of the relevant laws. Thus, it is still unclear in what form the changes may come. Currently the BMF is planning a real retroactive effect and would like to apply the new rules to all open assessment periods. In the past, these types of intensifications like the minimum requirements for death coverage were generally introduced with future effect only (e.g. introduction of the minimum-death coverage as of 01.01.1996). A retroactive effect would also be subject to constitutional limits.

Evaluation

- The suggestion by the BMF for the new rules on minimum death cover can in principle be supported, as it provides for legal and planning certainty based on concrete numbers. For providers whose products do not currently include minimum death coverage of the type described above, there may be a need to react. For the conclusion of insurance contracts the new rules on minimum-death coverage should be taken into account accordingly. There are also possible options for the adjustment of documents already in existence on the market that do not contain the planned rules for minimum death coverage. Additionally, for new insurance contracts a new documentation could also prove useful in meeting the standards of the German Insurance Contract Law Act (cost transparency, product information page).
- The BMF has focused on life-insurance products which are offered by providers "from neighbouring countries". The freedom-of-services rules within the EU market might prevent the BMF from discriminating against products which are only offered by Non-German EU insurers. The approach of the BMF or German legislature could therefore potentially be challenged under EU law. Furthermore, it remains to be seen to what extent the plans of the BMF might violate the constitutional restriction on retroactive laws.
- The BMF introduces a new term ("asset-management insurance policies") and compares it with fund-connected insurance. It appears that some misleading conclusions are reached because certain fundamental statements of the harmonised Insurance Regulatory Law are not sufficiently considered.
- At the core of the plan, capital income e.g. in the form of interest, dividends etc. shall be attributed to the *beneficial owner* on a continuing basis. The beneficial owner would - under the current opinion of the BMF - be the holder of the future claim under the insurance policy (i.e. the policy holder). Consequently, the capital income that flows to the portfolio held by the insurance company would need to be taxed annually at the level of the beneficial owner.

We will continue to follow the BMF plans and will keep you informed.

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