Tanzania’s new VAT Act impacts financial services

Executive summary
Tanzania’s new Value-Added Tax (VAT) Act (Act), effective 1 July 2015, brings far reaching changes for resident and nonresident financial services companies. The new Act categorizes a “financial service” as an intermediary service which is exempt from VAT, with certain limited exceptions.

Detailed discussion

Insurance services
Not all insurance services will constitute a financial service as from 1 July 2015. The new definition defines “financial services” to mean (but is not limited to):

Transactions involving the granting or transferring of ownership of a health or life insurance contract or the provision of reinsurance in respect of such contract.

This means that the supply of any other insurance will no longer be exempt in terms of the new Act, as it no longer constitutes an exempt financial service. Supplies of e.g., auto or home insurance therefore constitute taxable supplies of ordinary “services.” In light of the fact that the transitional rules for progressive supplies are cumbersome, suppliers of such insurance should obtain advice with respect to the receipt of pre-paid premiums, received prior to 1 July 2015, but which relate to the supply of short-term insurance after 1 July 2015.

Adjustments
The new Act contains special rules for adjustments relating to the payment and receipt of indemnity payments under a contract of insurance.

In addition, the rules relating to the issuing of credit notes, as well as to rebates and other adjustments, has also changed. The effect thereof is that suppliers of financial services may need to change their processes and amend their ERP systems.
Facilitation fees
The new definition of “financial services” does not include any arranging services supplied to facilitate the financial service. This means that the fees to facilitate a financial service will be taxable, while the financial service which is the subject of the facilitation service will be exempt. This will create apportionment issues regarding a supplier’s entitlement to input tax credits.

Change in apportionment rules for input tax
Banks, insurers, equity traders and other financial service companies will be required to apportion their input tax going forward, and will only be able to claim input tax credits to the extent that an expense is incurred to make VAT taxable supplies, i.e., to earn facilitation fees. In addition, entitlement to an input tax credit will vary in accordance with the ceiling and floor de minimis rules.

At the outset, a supplier will no longer have the option to choose an appropriate method of apportionment. Instead, companies making mixed supplies (taxable and exempt supplies) whose taxable supplies are equal to between 10% and 90% of total turnover, will be required to apportion their input tax credit in accordance with the “average method” set out in the new Act. The de minimis rules provide that entities with taxable supplies exceeding 90% of their total supplies qualify for a full input tax credit,4 while entities with taxable supplies of less than 10% of total supplies are not entitled to an input tax credit at all.5 Direct allocation is not impacted by the apportionment rules.

The new Act, however, does allow for a regulation prescribing further methods of apportionment for use by financial service companies,6 and furthermore provides that the current regulations, issued in relation to the repealed VAT Act, remain in force until such regulations are themselves revoked, amended or cancelled.7

Branch rules
Where the business in Mainland Tanzania is carried on from a fixed place of business, the branch of a nonresident company situated inside Mainland Tanzania is deemed to be a separate person to the main company situated outside Mainland Tanzania, despite the two branches both being a part of a single legal entity. From a VAT perspective, services provided by the Mainland Tanzanian branch to the person outside Mainland Tanzania will constitute a taxable supply of services. Services from the main branch outside Mainland Tanzania to the Mainland Tanzanian branch are discussed below under “imported services.”

Imported services
In most instances VAT on imported services is no longer applicable i.e., “services” supplied by the head office outside Mainland Tanzania to the Mainland Tanzanian branch will not generally constitute “imported services.” Note however, that to the extent the head office outside Mainland Tanzania allocates costs to its branch in Mainland Tanzania, a taxable supply of services is deemed to take place, upon which VAT must be accounted8 for by the branch inside Mainland Tanzania.

VAT registration is also determined in terms of an “economic activity” definition,9 the ambit of which is very wide. The “economic activity” definition may serve as a catch-all provision and services which previously would have constituted “imported services” may in the future constitute “economic activity” in Tanzania. Any person conducting an “economic activity,” who exceeds the threshold, is required to register for VAT in Tanzania. Whether or not the VAT only registration may expose the business for income tax remains to be seen in practice.

Implications
The Financial Service and Insurance industries in Tanzania will be directly impacted by these changes, effective 1 July 2015. The Tanzania Revenue Authority strictly applies these deadlines, and it is recommended that nonresident multinationals supplying financial services in Tanzania, or to recipients in Tanzania, seek advice to ensure compliance.
Endnotes
3. Section 2 financial service definition par(f).
4. Section 70(4)(b).
5. Section 70(4)(c).
7. Section 95.
8. Section 65(2).
9. Section 1.

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