FUNDAÇÃO GETULIO VARGAS
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FILIPE REIS ARAÚJO

THE NATURE OF PIS / COFINS AND THE BRAZILIAN GENERAL INSURANCE SECTOR

A review of the nature of PIS / COFINS and their accounting treatment in the Brazilian general insurance sector

SÃO PAULO
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Trabalho Aplicado apresentado a Escola de Administração de Empresas de São Paulo da Fundação Getúlio Vargas, como requisito para a obtenção do título de Mestre em Gestão para a Competitividade.

Linha de Pesquisa: Finanças e Controladoria

Orientador: Prof. Dr. Ricardo Cardoso Lopes

Co-Orientadora: Prof. Dr. Vanessa Rahal Canado

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RESUMO

As inconsistências encontradas entre o desenho da legislação fiscal e estrutura tributária brasileira, aliadas às especificidades da indústria de serviços financeiros, levaram a abordagens muito diferentes no tratamento contábil do PIS / COFINS. Por exemplo, enquanto alguns bancos e seguradoras multinacionais com operações no Brasil categorizaram e reportaram o PIS / COFINS como imposto de renda para fins de IFRS, as normas regulatórias de seguros privados brasileiras exigem que o PIS / COFINS sejam contabilizados como despesas administrativas.

Uma análise da natureza dos impostos sobre o consumo e sobre os impostos sobre valor agregado (IVA) mostrou que o PIS / COFINS são essencialmente impostos sobre o consumo, que compartilham a mesma base econômica do IPI, ICMS e ISS. Ao comparar o modelo brasileiro de PIS / COFINS com o modelo do Imposto sobre Mercadorias e Serviços (GST) australiano para empresas de seguros gerais (GI), fica mais evidente que há similaridades em ambas as abordagens para estimar o valor agregado nesse segmento de serviços financeiros.

Portanto, torna-se necessário reconhecer na legislação tributária brasileira a natureza de consumo do PIS / COFINS e isso não necessariamente exigiria alterações muito significativas na forma como a atual metodologia de PIS / COFINS opera para seguradoras gerais no Brasil. No entanto, as normas e práticas contábeis, bem como o os requereimentos regulatórios, deveriam ser ajustados para garantir que as receitas provindas das atividades do setor de seguros gerais sejam reconhecidas líquidas de PIS / COFINS, resultando em uma abordagem mais consistente do tratamento contábil de PIS / COFINS em ambos BR GAAP e IFRS.

Tratar a receita da empresa sem considerar impostos e outros valores que serão simplesmente repassados ao governo aumenta a qualidade das demonstrações financeiras das empresas. Dessa forma, uma reforma tributária no Brasil se torna necessária nao somente para simplificar o sistema tributário, mas também para permitir tratamentos e práticas contábeis mais coerentes e alinhadas ao IFRS, como a exclusão de impostos sobre o consumo como parte da receita contábil das empresas.

PALAVRAS-CHAVE: seguros gerais, imposto sobre valor agregado, PIS / COFINS, BR GAAP, IFRS.

ABSTRACT

The inconsistencies commonly found in the design of the Brazilian tax legislation and framework, allied to the specificities of the financial services industry, has led to very different approaches to the accounting treatment of PIS / COFINS. For instance, whilst some multinational banks and insurance companies with operations in Brazil have categorised and reported PIS / COFINS as income tax for IFRS purposes, Brazilian private insurance regulatory rules require PIS / COFINS to be accounted for as administrative expenses.

An investigation of the nature of taxes on consumption and value-added taxes (VAT) has shown that PIS / COFINS are essentially taxes on consumption, which share the same economic base as IPI, ICMS and ISS. By comparing the Brazilian PIS / COFINS model with the Australian Goods and Services Tax (GST) model for general insurance (GI) companies, it becomes more evident that there are similarities in both approaches for estimating the value added in this financial services segment.

Therefore, it becomes necessary to recognize in the Brazilian tax legislation the consumption nature of PIS /COFINS and this would not necessarily require very significant alterations to the way the current PIS / COFINS methodology operates for general insurers in Brazil. Nonetheless, accounting standards and practices as well as the regulatory framework should be adjusted to ensure that general insurance revenues would be recognised net of PIS / COFINS, resulting in a more consistent approach to the accounting treatment of PIS / COFINS by general insurance organizations in both Brazilian GAAP and IFRS.

Treating the company's revenue without considering taxes and other values that will simply be passed on to the government increases the quality of the accounting information. A tax reform in Brazil is required to simplify not only the tax system but also to address some inadequate Brazilian accounting practices such as the consideration of some consumption taxes as part of the accounting revenue.

KEY WORDS: General Insurance, Value-added Tax, PIS / COFINS, Brazilian GAAP, IFRS.

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ACRONYMS AND ABBREVIATIONS LIST

AASB	The Australian Accounting Standards Board
BRL	Brazilian Real
CFA	Committee on Fiscal Affairs - OECD
CLT	Consolidação das Leis Trabalhistas (Consolidated Labour Legislation)
COFINS	Contribuição Social para Financiamento da Seguridade Social (Contribution for the Financing of the Social Security)
CTN	Código Tributário Nacional
CSLL	Contribuição Social sobre o Lucro Líquido (Contribution on Net Income or Net Profit)
DTA	Deferred Tax Asset
DTL	Deferred Tax Liability
EU	European Union
FAD	The Fiscal Affairs Department - IMF
GAAP	Generally Accepted Accounting Principles
GDP	Gross Domestic Product
GI	General Insurance
GST	Goods and Services Tax
GWP	Gross Written Premium
IASB	The International Accounting Standard Board
IBGE	Instituto Brasileiro de Geografia e Estatística (Brazilian National Bureau of Statistics)
IBNR	"Incurred But Not Reported" reserves
ICMS	Imposto sobre a Circulação de Mercadorias e a Prestação de Serviços de Transporte Interestadual e de Comunicação (Tax on the Distribution of Goods and the Rendering of Communication and Interstate Transportation Services)
IFRS	International Financial Reporting Standards
IMF	The International Monetary Fund
INSS	Instituto Nacional de Seguridade Social (National Institute of Social Security)
IOF	Imposto sobre Operações de Crédito, Câmbio e Seguro, ou Relativas a Títulos ou Valores Imobiliários (Tax on Financial Transactions)
IPI	Imposto sobre Produtos Industrializados (Tax on Industrialized Products)
IRPF	Imposto de Renda Pessoa Física (individual Income Tax)
IRPJ	Imposto de Renda Pessoa Jurídica (Corporate Income Tax)
ISS	Imposto sobre Serviços de Qualquer Natureza (Tax on the Provision of Services)
OECD	The Organisation for Economic Co-operation and Development

PASEP[1]	Programa de Formação do Patrimônio do Servidor Público (The Civil Servant Saving Program)
PIS	Programa de Integração Social (The Social Integration Program)
RCB	Receita Federal do Brasil (Brazilian Inland Revenue)
SUSEP	Superintendência de Seguros Privados (Brazilian Insurance Regulator)
TAC	Tax Calculation Account
UCR	Unpaid Claims Reserves
UPR	Unearned Premium Reserves
VAT	Value Added Tax

[1] As the focus of this work is on private insurance companies and once PASEP is aimed at the public sector, “PIS / PASEP” will be referred simply as “PIS”.

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1. Introduction

As explored by Canado (2011), the 1988 Brazilian constitution uses, implicitly or explicitly, terminology common to private law in order to elect the tax jurisdiction of each federative entity such as property ownership; donation and transmission of goods after death; transfer of property and real estate; services; and billing or revenue. However, Viol (2000) argues that the 1966 tax reform, which led to the creation of the Brazilian Tax Code, adopted the concept of economic factors by focusing on economic bases rather than the usual legal framework.

Although this might have resulted in efficiency and effectiveness gains when compared to the previous taxation model from 1946, the tax system needed be dynamic and sufficiently flexible to ensure that it would be able adjust itself in line with economic developments. Otherwise, as stated by Viol (2000), the tax system would gradually become obsolete and inefficient with the emergence of, for example, new and more evolved economic sectors (e.g. high-tech industry, e-commerce). Under these circumstances, regulation changes or adaptation to the tax legislation would become imperative to ensure that the actual economic bases used for taxation would effectively and equitably reflect the domestic economy.

The Brazilian tax system is based on four main type of tax bases (i.e. payroll, income, property and consumption) but the apparent contradiction between private law determining tax competence versus the economic base approach to taxation has resulted in a tax legal framework consisting of several different taxes for each economic base of taxation rather than a single tax being applied to each economic base.

According to the Brazilian Federal Revenue Service, the top 10 taxes and contributions[2] made up circa 85% of the total tax revenues generated by all levels of government in 2015. Five of them are taxes whereas the remainder are contributions. The five taxes in this top ten list account for circa 46% of the total tax revenues whilst the other five contributions make up approximately 39% of all taxes collected in Brazil in 2015. These figures show clearly the importance of contributions for the Federal Government.

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[2] In Brazil, one of the key differences between tax and contribution is their destination. On the one hand, taxes, including income tax itself, have no defined destination determined by the Brazilian Constitution hence they can be freely allocated per the Federal Union´s budget and policies. However, the proceeds of taxes can be distributed also with states and municipalities. On the other hand, social contributions (e.g. CSLL, PIS, COFINS), which are aimed at funding the social security systems, are not redistributed between states and cities. Two of these social contributions were created by the Federal Government after the 1988 Constitution. CSLL and COFINS were created in 1988 and 1991, respectively.

PIS and COFINS contributions, which are the focus of this work, represent together approximately 13% of all tax revenue collected in 2015 as shown in Table 1. Additionally, they made up circa 4,3% of the Brazilian GPD in that same year. Table 1 also shows the top ten taxes and contributions by total revenue as well as the proportion of the Brazilian GDP during 2015.

Table 1 – The Top Ten Taxes & Contributions by Total Revenue – Year 2015

	Tax / Contribution	**2015**		
		R$ billion	**Total**	**% GDP**
	Tax & Contribution Revenue	**1.928,2**	**100,0%**	**32,7%**
1	ICMS	396,5	20,6%	6,7%
2	Imposto de Renda	341,9	17,7%	5,8%
3	Contribuição para a Previdência Social	320,4	16,6%	5,4%
4	COFINS	199,9	10,4%	3,4%
5	Contribuição para o FGTS	118,3	6,1%	2,0%
6	Contribuição Social sobre o Lucro Líquido	59,1	3,1%	1,0%
8	ISS	58,1	3,0%	1,0%
7	Contribuição para o PIS/Pasep	52,6	2,7%	0,9%
9	Imposto sobre Produtos Industrializados	48,0	2,5%	0,8%
10	Impostos sobre o Comércio Exterior	39,0	2,0%	0,7%
(4 + 7)	PIS / COFINS	252,5	13,1%	4,3%

Source: Receita Federal do Brasil - RFB

As a way to illustrate how the Federal Government[3] uses these contributions as tax revenue adjusting mechanism, PIS and COFINS rates on financial revenues were reduced to 0% in 2004, except for revenues relating to transactions and interests on hedge net assets. In 2005, the percentage of 0% was extended to transactions and companies partially subjected to the non-cumulative assessment regime. However, because of the economic recession, the Federal Government increased (Decree no. 8.426, of 1st April 2015) the rates back to 0,65% for PIS and 4% for COFINS on financial revenues earned by legal persons under the non-cumulative assessment regime from 1st July 2015. Legal persons partially subject to the non-cumulative assessment regime were also subjected to PIS/COFINS payment on financial revenues from 1st July 2015.

[3] Please see explanatory note on the RFB´s website: http://idg.receita.fazenda.gov.br/noticias/ascom/2015/abril/nota-explicativa-sobre-o-decreto-no-8-426-2015

PIS and COFINS are a very important source of tax revenue in Brazil but the incoherence of the Brazilian legal framework for establishing the tax competences and setting up the tax calculations has resulted in numerous taxes being applied on the same tax base. This complexity, added to the specificities associated with the financial services industry, has led to certain distortions in the accounting treatment of PIS / COFINS. For instance, some multinational companies have categorised and reported PIS / COFINS as income tax for IFRS purposes. This is a very different treatment required by the Brazilian insurance regulator hence it becomes necessary to explore the essence of PIS / COFINS and some examples around the world with the aim of identifying the most adequate accounting treatment.

The purpose of this paper is to examine the nature of the PIS / COFINS focusing on the general insurance sector with the objective of analysing the accounting treatments used by Brazilian GI companies in both local GAAP and in IFRS.

As contained in the Collins English Dictionary “general insurance is insurance coverage for property and liability risks”. General insurance seeks to cover protection against different areas of hazards including property, enterprise, vehicle, money lending and various other forms of professional casualties, except the casualty of death, which is life insurance. In other words, while life insurance caters to risk of death and its consequent eventualities; general insurance seeks to protect risks posed by several aspects of life and its varied assets. General insurance usually involves a short-term agreement between the insurer and the insured with the term extending not more than a year. This agreement is formalized in an insurance policy, which is a contract whereby an insurer promises to pay the insured a sum of money or some other benefit upon the happening of one or more uncertain events in exchange for the payment of a premium.

This paper is divided in 6 chapters, including this short introduction. Chapter 2 consists of very brief explanation of the hypothesis to be tested in this paper as well as the methodology adopted. In Chapter 3, a brief overview of value added tax is provided, including discussions on some of its fundamental concepts and principles as well as the “hard to tax” view associated with VAT in financial services. In Chapter 3 there is also a section on the Australian GST model for the general insurance sector. In Chapter 4, the attention turns to the analysis of consumption taxation in the Brazilian tax system, with focus on PIS / COFINS on GI companies. Chapter 5 is dedicated to the Brazilian accounting requirements for PIS / COFINS in light of the Brazilian Corporation Law and Income Tax Regulations tax as well as the different accounting treatments applied by Brazilian GI companies in local GAAP and IFRS.

Chapter 5 also looks at the accounting treatment of the Australian GST. Lastly, in Chapter 6, the key findings and conclusions are discussed and explained.

2. Hypothesis and Methodology

Brazil appears to have a preference for consumptions taxes rather than income taxes and the decentralized nature of the Brazilian tax system has led to numerous taxes being applied on each of the four tax bases (i.e. payroll, income, property and consumption). As a result, PIS / COFINS, together with the state tax ICMS, municipal services tax (ISS) and the federal tax on industrialized products (IPI) fall under the same structure of taxation of goods and services in Brazil.

The specificities of the financial industry make it difficult to measure its value added, but in order not to exempt it from VAT, its value added must be worked out using different methods to the more commonly applied invoice-credit method. Some countries have made progress in this field such as Norway, Denmark and Canada. New Zealand was the first country to adopt a VAT regime in which general insurance (GI) was taxed using a modified cash flow basis method and Australia has taken this model and created a modified version, which reflects the "pooled" nature of GI businesses. This approach has resulted in very consistent accounting treatments of consumption taxes that are simply transferred to the taxation authorities such as the revenue recognition being net of such taxes, which is consistent with IFRS rules.

Within this context, the hypothesis to be testes is:

> The Brazilian PIS / COFINS applied to the general insurance industry has a consumption taxation nature and, therefore, should be treated as value added tax rather than administrative expenses or income taxes in the financial statements of general insurance companies.

The methodology consists firstly in the investigation of the nature of value added tax, its fundamental concepts and principles but focusing on the challenges associated with VAT in financial services. By looking at more advanced tax systems where methodology advancements have allowed GI services to be taxed, the Australian GST model is then chosen to be analysed. Subsequently, the analysis of PIS / COFINS on GI companies is carried out, including the Brazilian accounting requirements for these contributions, with the aim of contrasting it to the Australian GST model for GI firms. As part of this process, financial statements of Brazilian and Australian companies are analysed in order to compare the PIS / COFINS and GST regimes and draw some findings and conclusions as to whether the hypothesis is proven true or not.

3. VAT in General Insurance

The OECD´s International VAT / GST Guidelines (2017) lists five principles[4] that are generally accepted as good practice for tax policy making and for the development of tax systems: neutrality, efficiency, certainty and simplicity, effectiveness and fairness, and flexibility. Within the context of VAT, these five principles bring two interlinked implications. The first one relates to the "destination principle", which requires that VAT is levied in the jurisdiction where the final consumption takes place. This means that to respect the principle of neutrality when international trade is concerned, exports of goods and services should be exempt from VAT. Thus, VAT systems should have mechanisms for identifying the final jurisdiction of consumption.

Secondly, in order to keep the whole VAT system and framework efficient, simple, effective and fair, a policy on VAT should allow for very few exceptions and deviations. Warren (1993) cited the inefficiencies created in VAT systems where certain products and services were exempted or zero-rated from VAT. According to him, such concessions increased administration and compliance costs, whilst also leading to distortions in allocation of consumer resources between different types of goods and services.

Additionally, although there is a general understanding that few specific exemptions such as education and health are justifiable as part of a broader political, social and economic agenda, Warren (1993) also refutes this belief noting that this sort of compensation should be carried out via the social welfare and income tax systems. In his view, any VAT exemption or differentiation is an inefficient way to compensate those with more disadvantaged social-economic backgrounds.

[4] Firstly, the principle of "neutrality" dictates that business decisions should be motivated by economic reasons rather than tax considerations. Likewise, taxpayers under the same conditions and situations carrying out similar transactions should be subject to similar levels of taxation. Secondly, the principle of "efficiency" means that the design of the taxes and the tax systems should minimize as much as possible the compliance costs for businesses as well as the administrative costs for the tax authorities. Thirdly, the principles of "certainty and simplicity" require that tax rules should be clear and simple to understand so that taxpayers could anticipate their impact. Fourthly, the principles of "effectiveness and fairness" indicate that taxation should produce the right amount of tax at the right time. Additionally, effectiveness and fairness help ensure that the potential for tax evasion and avoidance is mitigated while keeping counteracting measures proportionate to the risks involved. As the fifth and final principle it comes "flexibility", which requires the design and maintenance of taxation systems to be sufficiently flexible and dynamic to ensure that they keep pace with technological and commercial developments.

This Chapter is focused to VAT and the first two sections are dedicated to it definition and key features as well as the discussion around best practice and empirical evidence on the adoption of VAT. The last two sections treat the challenges associated with measuring the value added in financial services and some successful experiences in imposing VAT on general insurance. The emphasis is on the Australian VAT model designed for the general insurance industry.

3.1. The Definition of VAT and its Key Features

The OECD´s Commmittee on Fiscal Affairs (CFA) has developed the International VAT / GST Guidelines since 2006 with the aim of reducing uncertainty related to cross-border activities. In other words, the CFA objetive was to reduce the risks of double taxation of VAT or no taxation of VAT at all in the context of internationl trade. Although these guidelines have focused on cross-border activities and have not attempted to being a prescriptive recipe for VAT legislation, it brings very pragmatic concepts and principles associated with VAT.

According to the OECD International VAT/GST Guidelines (2017, p.10), the terms "value added tax" and "VAT" are used to refer to any national tax by whatever known acronym (e.g. Good and Services Tax or simply GST), which is "*a broad-based tax on final consumption collected from, but in principle not borne by, businesses through a staged collection process (by whatever aproach, e.g. invoice-credit method or subtraction method)*".

This definition clearly points out two very important features of VAT. Firstly, it means that the overaching purpose of VAT is to tax the purchases of individual househoulders hence VAT is a tax on final consumption. Secondly, VAT systems consist of multi-stage collection processes designed to ensure that the burden of these value added taxes do not rest with businesses. This second feature requires that there must be no breaks in the VAT multi-stage process, otherwise there might be double taxation of VAT at certain links in the chain.

To explain this multi-stage process in more simple words, the seller passes on an invoice[5] showing the amount of VAT charged, which in turn will be used as credit by the purchaser to

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[5] This explanation is based on the invoice-credit method used to determine VAT liability, which is the most used method. There are two other methods to determine VAT liability: the "subtraction" method and the "addition" method. In the "subtraction" method, tax is levied directly on an accounts-based measure of value added calculated for each firm by subtracting allowable purchases from revenues. On the other hand, in the "addition" method, tax is levied on an estimated value added calculated by adding some income factors and making some allowed adjustments when deemed necessary.

The invoice-credit method is transaction-based whereas the subtraction and addition methods are entity-based. The invoice-credit method has advantages such as being easier to account for different VAT rates and allow the

reclaim that same amount of VAT. This way, at each subsequent stage of the production process, net tax is payable only on the difference between sales price and purchase amounts. In effect, the tax on inputs are eliminated with outputs being taxed at each stage of the production process. The tax on all goods and services subsequently used as input to productions must be refunded to the purchasers of those inputs until the goods and / or services are sold to the final individual consumer, who is not entitled to VAT refund.

3.2. Best Practice and Empirical Evidence from VAT

The Fiscal Affairs Department (FAD) of the IMF provides some advice on the adoption of VAT, including its most effective features. The most consistently adopted pieces of advice include the creation of a detailed preparation plan for the implementation of VAT, which requires time and effort. This includes the establishment of large taxpayer units to provide support to the general public through the changes and their implementation. Additionally, to be more effective VAT must be a national tax which is administered centrally and adopts the invoice-credit method. Moreover, the design of the VAT system must extend to all the retail stages, with only few and well-specified exemptions (i.e. education, health) being allowed. It is also advisable that thresholds are defined for incorporated businesses, individual entrepreneurs and unincorporated businesses, with the smallest businesses being excluded from the VAT net.

There are other few advices which are not consistently observed by policy makers and tax authorities when implementing VAT. This includes the lack of adequate training and staffing of the tax authorities, the non-adoption of zero-rating on exports in line with the destination principle, and allowance for input credits for capital goods. Some countries also insist in adopting cash basis for the tax liability calculations rather than the accrual basis as advised by the FAD. More worryingly though is the proliferation of VAT rates rather than the adoption of a single positive rate, leading to unnecessary complexity.

As noted by James (2015), VAT helps increase tax revenues and there is empirical evidence also showing that countries with VAT raise more tax revenues relative to Gross Domestic Product (GDP) than countries without it. Additionally, the revenue gain with the adoption of VAT seems to increase with GDP per capita but decrease with the rise in relative importance

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exemption on exports. Additionally, it also facilitates a more transparent tax charging display that encourages firms to check and oversee each other. On the other hand, the subtraction and addition methods might incur lower compliance costs depending on how efficiently the overall tax system operates. In any case, there is a consensus that that the best method to determine VAT liability is the invoice-credit method.

of agriculture and exporting activities in the economy. Likewise, those countries which have adopted VAT have increased their VAT rates over time and, consequently, their tax revenues. Additionally, another significant trend among VAT adopters is that the number of different rates applied has also increased dramatically, which adds complexity to the system over time[6]. Nonetheless, VAT is perceived as being an effective tax which has increasingly gained importance as a source of tax revenues.

3.3. VAT in Financial Services

The amount of the VAT liability is measured by subtracting a company´s income originated from the sales of its good and services from the costs and expenses coming from its supplies of inputs. In the financial industry´s case, there are some specificities that make it difficult to measure its value added, which is implicitly diluted, for example, in the interest rate spread or financial margins of its products.

Another complicating factor to consider is that "financial services" is a broad concept as it is associated with many different types of products, services and transactions. For instance, financial services may imply deposits, borrowing and lending, which are products associated with banking and credit card operations. Alternatively, financial services might be associated

[6] The experience of the UK, which introduced VAT in 1973, illustrates this well. The UK introduced VAT as part of set of conditions to joining the European Economic Community (EEC) in the 1970´s. All countries joining the EEC had to replace their indirect taxes with the VAT and in the UK´s case, VAT replaced the Purchase Tax, which was a complex system that had many different rates.

The UK VAT commenced as a simple 10% tax on nearly all goods bought from a business with a few exceptions and exemptions but it has since then swollen in size and complexity. During the 1980´s under Baroness Thatcher, the luxury rate was scrapped and merged into a higher standard rate of 15%, then raised again to 17.5% in 1991. Then, in the 1990´s VAT on utility bills rose from zero-rated to a new 8% reduced rate, which was subsequently lowered to 5 per cent by Chancellor Gordon Brown under Tony Blair´s premiership.

The zero-rating VAT has also led to confusion and legal uncertainty. Snacks, for instance, carry full VAT because they are deemed to be non-essential. However, as food manufacturers and retailers get more innovative, the system struggles to cope with it. Two of the most famous legal battels have involved chocolate covered treats: Jaffa Cakes and marshmallow teacakes. The UK Tax Authority (HMRC) believed that they were both chocolate-covered snacks, but lawyers successfully argued that were both cakes, which were zero-rated for VAT.

The UK VAT rate currently is 20% and it makes up approximately 20% of the countries tax revenues. The current tax legislation handbook has more than three thousand pages only on VAT. Most European countries' VAT rate is about 20 per cent.

with the purchase, sale and issuance of financial securities such as bonds, shares, options, guarantees and foreign currencies. Moreover, financial services may be connected to brokerage and other agent services such as the buying and selling of financial securities.

Similarly, financial services associated with insurance might differ significantly as well. For instance, the value added in life insurance products with a fifteen-year term and investment performance guarantees is significantly different from a 12-month house insurance policy. As a result, it is vital that any VAT method to be designed for financial services take into account the nature, size and complexity of each of the financial services sectors as well as their products and services.

Merrill (2011) mentions that most countries with VAT have chosen to exempt a broad range of financial services precisely because of this difficulty in measuring implicit financial fees. However, he also notes that this approach has led to VAT rules that are neither simple nor economically neutral. Another reason for exempting VAT on financial services relates to the “hard to tax” argument due to the wide-ranging nature of financial services and their outputs, as pointed out above. As this would bring many conceptual, administrative and compliance challenges, it is considered more convenient to simply exempt them from VAT.

Within this context, the value added in financial services must be worked out using different methods to the more commonly applied invoice-credit method. Bird & Gendron (2007) mention a variety of methods already in use in some countries as well as some proposals that have been made to include financial services within the base of the VAT. For instance, certain countries (e.g. Norway, Denmark, the Province of Quebec in Canada) impose certain taxes on payroll[7], capital and premium on financial institutions to compensate for the tax revenue losses associated with VAT. Some other countries such as Israel use the addition method (i.e. the value added is calculated by adding wages and profits) to impose tax on financial services (e.g. non-life insurance).

Merrill (2011) mentions that the Meade Commission report released by the Institute for Fiscal Studies in London in 1978 proposed a cash flow tax on business that consisted of an economic

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[7] Mirrless (2011) notes that as the starting point for calculating profits and value added have a lot in common, the relationship between a VAT and a tax on profits plus wages becomes clearer. In both cases, there is a net base consideration with the basic calculation consisting of recording income from sales and deducting expenditure on inputs. The biggest difference is that wages are treated as a deductible expense for corporation tax, but not as a creditable input for VAT. Thus, a tax on profits must be added to tax on wages to be comparable to VAT.

or real component (R) coupled with financial flows (F). The R base would be an origin-based, subtraction method VAT with a deduction for employee compensation whilst the F base equalled financial inflows less financial outflows.

From an insurance company perspective, for example, the financial inflows component would include receipt of insurance premiums and insurance claims whilst the financial outflows consisted of payments of insurance claims and insurance and reinsurance premiums. In other words, the net cash flow from financial transactions would be the VAT tax base as all cash inflows would be treated as taxable sales on which VAT should be levied on. On the other hand, all cash outflows would be considered as taxed purchases with entitlement for input VAT credit.

Bird & Gendron (2007) point out that the above suggested approach has two variants for financial institutions. Firstly, there is the Tax Calculation Account (TCA) system, which is a tax suspension account for margin transactions where tax or credit amounts are accrued until the TCA is closed and the net VAT remitted to the tax authority. The second variant is quite similar in its approach except for applying zero-rated VAT to business transactions. Although this seems conceptually more accurate, it is very complex to be adopted.

A few countries have worked on these proposed methods for specific types of financial services to depart from the common practice of exempting such services. For instance, New Zealand was the first country to adopt a VAT regime in which general insurance (GI) was taxed using a modified cash flow basis method. Under the New Zealand system, GI premiums are subject to VAT whilst VAT incurred by an insurance company for repair or replacement of insured property is deductible. In case a policyholder is reimbursed for the cost of repairs, for instance, the claims payment is viewed as VAT inclusive with the respective amount being also refunded to the insurance company.

The New Zealand approach to taxing GI has caught the attention of other jurisdictions, with South Africa adopting the New Zealander model. Likewise, Australia has taken this model and created a modified version, which is discussed in more detail in the next sub-section.

3.4. The Australian General Insurance GST Model

In simple terms, general insurance businesses collect moneys (i.e. premiums) from its various customers (i.e. insured) in exchange for providing them with guarantees that the insured will be compensated in case they incur any financial or economic loss because of an adverse event (e.g. an accident or illness). This simple explanation helps show the “pooled” nature of GI businesses, where insurers manage a pool of premiums which are used to fund a group of

claims. If the insurers do it effectively and efficiently, they are able to profit from this business model. This shows that from a holistic perspective rather than an individual GI policy viewpoint, the value added by the GI business activities may in fact be measured by the difference between the premiums collected versus claims pay-outs.

As discussed in the previous sub-section, New Zealand was the first country to design VAT on GI products taking a pooled basis rather than individual view of the policies. Then the Australian tax policymakers further developed this model with the assistance of the insurance industry. Under the Australian GST legislation[8], the insurer collects from the final consumer GST at 10% of the premium and pays the tax authority the total GST collected at the end of each month less the adjustments which the insurer is allowed on the settlements or claims paid out. If the insured is a fully registered tax entity, it must advise the insurer that it is entitled to an Input Tax Credit so that any settlements or claims are also GST adjusted. Similarly to New Zealand, the Australia´s GST works out the value added by general insurance activities by separating them into two streams: inflow of premiums and outflow of settlements and claims. Appendix 1 contains an illustration of a portfolio of four GI policies and the way GST payable on premium, Input Tax Credit for registered tax entities and GST recoverable on claims work. The Australian GST rules also contain specific accounting requirements and practices. Under these rules, the larger businesses must use the non-cash accounting method, which means that the GST base is calculated on the business activity statement that covers a specific tax period, including the cashflow behaviour over this period. Hence companies must account for the GST payable on the sales made in the reporting period in which a tax invoice was issued or a

[8] The Goods and Services Tax (GST) is the Australian version of the more commonly known VAT. The GST system is designed to collect tax on the value that is added by registered entities at each stage of the production chain. This is achieved through a two-step process followed by each of the registered entities which make taxable supplies. First, a registered entity includes the GST in the price of all its taxable supplies. Then, subsequently, this registered entity reclaims the GST component of those inputs which it has acquired in making its own taxable supplies. As this process goes through the production chain, with each registered entity being able to reclaim the amount of input tax credits to which it is entitled, the net result for each of the registered entities is the value that they have added to their taxable supplies. Only when a taxable good or service is consumed by a final consumer, who is not entitled to claim input tax credits, the full amount of GST included in the price is remitted to the Australian Taxation Office.

The GST treatment of general insurance is set out in Division 78 of the Goods and Services Tax Act from 1999 (i.e. the 'GSTAct'). The GST recognises three types of insurance each of which is taxed in a different way: life insurance is input-taxed due to its saving component; similarly, to many other countries, private health insurance is GST-free, and; general insurance is fully taxable at the GST rate of 10 per cent.

payment was received, whichever happened first. Likewise, for purchases, large companies are entitled to GST credits in the reporting period in which the company either received the tax invoice from its supplier or made some payments to them, whichever came first.

4. VAT in the Brazilian General Insurance Market

The insurance companies established in Brazil operate in a very regulated environment. The Decree-Law 73 from 1966 created the National Private Insurance System, which sits under the Ministry of Finance. The regulatory framework consists of two governmental agencies: the National Private Insurance Council (CNSP) and the Superintendence of Private Insurance (SUSEP). CNSP is responsible for formulating the overall policy framework whilst the SUSEP is in charge of regulating the insurance market by issuing and enforcing the rules, supervising authorized insurers, applying fines and penalties in case of noncompliance, resolving disputes, etc.

All insurance market players (i.e. insurers, reinsurers) must be organised as corporations (i.e. "sociedades anônimas") and authorized by SUSEP to operate in Brazil. Other usual business legal requirements also apply such as having company tax codes, state and municipality registrations, etc. Foreign companies may hold direct equity stakes in Brazilian insurers and after the termination of the reinsurance monopoly by the Brazilian Government in 2007 – Complementary Law 126 – the market has attracted considerable foreign investments.

All insurance contracts are regulated by the Brazilian Civil Code and there are customer protection rules for the insured under the Brazilian Consumer Defence Code as well as specific SUSEP rules. According to SUSEP[9], the Brazilian private insurance system is an important sector within the Brazilian economy accounting for circa 2.5% of the Brazilian GDP in 2006.

This Chapter discusses VAT in the Brazilian insurance industry. The first section lists the key Brazilian consumption taxes related to the general insurance industry whilst the second section gives a brief overview of the PIS / COFINS legal framework, including its main calculation methods. The third and last section is dedicated to the calculation methodology for PIS / COFINS in the general insurance industry.

4.1. Consumption Taxes Applicable to the Brazilian Insurance Industry

According to the Brazilian Federal Revenue Services, the total tax revenue in Brazil as a proportion of the GDP is slightly below the average registered in the OECD countries. However, taxes on goods and services are the most important source of tax revenue for Brazil

[9] For further information, visit http://www.susep.gov.br/english-susep/insurancemarket

at 16% of the GDP whilst for the OECD members, income taxes play that role. These differences between Brazil and the average in OECD countries became slightly more relevant during the 2006-2014 period with taxes on goods and service increasing their relative importance to the Brazilian tax revenues and income taxes going in the opposite direction.

Table 2 shows the relative importance of tax revenues in Brazil and in the OECD[10] countries by type as a percentage of GDP in 2006 versus 2014. This analysis clearly demonstrates that in Brazil, in contrast to developed countries, there is a preference for consumptions taxes rather than income taxes[11].

Table 2 – The Relative Importance of Taxes by Nature as % of GDP – 2006 VS. 2014

Nature	2006		2014	
	Brazil	**OECD**	**Brazil**	**OECD**
Goods & Services	16,2%	11,1%	16,3%	11,4%
Payroll	8,1%	9,0%	8,4%	9,7%
Income	6,2%	12,6%	5,9%	12,0%
Property	1,2%	1,9%	1,4%	1,9%
Other	1,6%	0,2%	0,5%	0,3%
% GDP	**33,3%**	**34,9%**	**32,4%**	**35,3%**

Source: Receita Federal do Brasil – RFB and OECD Revenue Statistics

https://stats.oecd.org/Index.aspx?DataSetCode=VER

The decentralized nature of the Brazilian tax system, allied to the fact that private law determines the tax competence whereas taxation is based on an economic methodology approach, led to numerous taxes from different government levels being applied on each of the four tax bases (i.e. payroll, income, property and consumption). For instance, while in most countries consumption tax is only a broad-based value-added tax (VAT), the structure of taxation of goods and services in Brazil has four restricted tax bases: the state tax (ICMS), municipal services tax (ISS), federal tax on industrialized products (IPI) and PIS / COFINS.

In other words, there are five consumptions taxes in Brazil which are the most important in terms of raising revenues for all the government levels in Brazil. Three of them are closer in nature to a pure value added tax and they are IPI, ICMS and ISS. These taxes come from the

[10] The Organisation for Economic Cooperation and Development – OECD was created originally in 1960 with 20 founding members and since then another 15 countries have joined the Organization.

[11] Although it is not the objective to this study, it is important to point out that taxing people indirectly via consumption taxes rather than directly on income leads to lower income taxpayers assuming a higher proportion of the tax burden relatively to the rich. This becomes even more inadequate in countries where there is severe economic and social inequality, which is the case in Brazil. Additionally, indirect taxation in complex tax systems tends to jeopardize transparency as to how much tax is paid on specific goods and services, clouding, therefore, people´s ability to make informed purchases and decisions.

Federal Government, State and the Federal District government and municipalities, respectively. "*Imposto sobre produtos industrializados*", which is better known for its acronym IPI, is a Federal Government sales tax on industrialized goods. ICMS, on the other hand, is a tax applied by State and the Federal District governments on the circulation of goods and transportation and communication services. Municipalities have their own version of VAT called ISS, which is a taxation on services other than those included in the scope of the ICMS. Within this context, the Brazilian consumptions taxes that are directly or indirectly applicable to the GI activities are three: ISS, PIS and COFINS. Firstly, GI firms are required to retain, collect and pay to the municipal tax authorities ISS from brokerage services industry. Additionally, GI companies must pay PIS / COFINS on their gross revenue at 4,65%.

It is important to note that Decree 6.306 from 2007 defined the Tax on Financial Transactions (i.e. "IOF"), which also applies to insurance. Specifically for the GI industry, IOF is an insurance premium tax and is calculated as an amount of the premium at a rate ranging from 0% to 7.38% depending on the type of insurance. For instance, agri-business insurance´s rate is 0% whilst car insurance is 7,38%. IOF is paid by the insured rather than the insurer. Nevertheless, insurance companies are required to retain and pay IOF on behalf of their customers. Alternatively, insurance companies may set arrangements with their partnering banks to retain and pay IOF on the premiums collected directly to the Brazilian tax authorities hence the insurers receive the premium net of IOF.

Table 3 below shows the key feature of these four taxes and contributions which are applicable to the GI activities in Brazil.

Table 3 – Consumption Tax on General Insurance

Tax	Year	Government	Type	Tax Base	Rates
ISS	1968	Municipal	Cumulative	Services	2% to 5%
PIS	1970	Federal	Cumulative or Non-cumulative	Gross Revenue	0,65% or 1,65%
COFINS	1991	Federal	Cumulative or Non-cumulative	Gross Revenue	3% or 7,6%
IOF	2007	Federal	Cumulative	Financial Transactions (i.e. premium)	0% to 7,38%

Source: Receita Federal do Brasil – RFB

4.2. The PIS and COFINS Contributions

The Social Integration Program (PIS) and the Civil Servant Saving Program (PASEP), better known by their acronyms PIS / PASEP, are social contributions of a tax nature, owed by legal

entities, in order to finance the payment of unemployment benefits and other related payments for workers of both private and public sectors, respectively. They were created in 1970 via the Complementary Law 7/70 from the 7th September 1970. PIS is aimed at funding benefits for employees of private sector under the Consolidation of Labour Laws (CLT) regime. PASEP, on the other hand, is intended for civil servants governed by the Federal Statutory Regime. These contributions are currently administered by the Federal Revenue Services and they have undergone a few legal changes since their inception. As the focus of this work is on private insurance companies and PASEP is aimed at the public sector., PIS / PASEP is referred simply as PIS throughout this paper.

Contribution for the Financing of the Social Security (COFINS) is a Brazilian federal contribution, of a tax nature, levied on the gross revenue of companies in general, to finance social security, which covers social security, health and social assistance. The constitutional authorization for the creation of COFINS, a tax levied on gross revenue and destined to Social Security, is centred on item "b" of item I of article 195 of the Federal Constitution. Complementary Law No. 70 from the 30th December 1991 established COFINS. Later, the legislation of the Contribution for PIS / PASEP and COFINS levied on gross revenue was merged with the publication of Law No. 9.718 from the 27th November 1998.

Up to 2002, the calculation basis for the PIS / COFINS remained relatively simple and well understood. Then on the 29th December 2003, the COFINS non-cumulative calculation method was established by Law 10.833, which created a credit method whereby deductions were allowed for the purchase of goods and commodities as well as some deductible expenses. After successive tax changes, which included the introduction of PIS / COFINS on imported products and services, a high level of complexity was introduced.

There are two main types of tax methods for PIS / COFINS: noncumulative and cumulative. Appendix 2 explains briefly the main features of these two methods. It is also important to note that the type of PIS / COFINS calculation method adopted is intrinsically linked to the

type of income tax regime[12] used by the company. Additionally, PIS / COFINS levies on imported products and services have been introduced[13].

The Brazilian legislation has created some special or differentiated regimes for PIS / COFINS, which usually result in a differentiated calculation base and / or different tax rates. As described previously, differentiated schemes are usually a variation of the PIS / COFINS under the non-cumulative or cumulative regimes according to the nature of the businesses and their revenue.

Some companies, notably the financial institutions which are under the cumulative regime, have differentiated calculation basis as well as rates. Some other sectors of the economy such as factoring and foreign exchange services firms have differentiated basis for calculation. There are special arrangements for products such as cigarettes, fuels, pharmaceuticals, beverages and biodiesel, which get special rates each. On the other hand, some other segments of businesses get reduced or even zero-rated PIS / COFINS. Commercialization of technical books for instance, have a rate of zero whereas other products (e.g. petrochemical naphtha, paper used for the printing of periodicals and newspapers, certain vegetables and fruits, chemical and pharmaceutical products) have different and specific rates.

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[12] There are three main income tax regimes applicable to companies in Brazil: the real profit regime, the presumed or deemed profit regime and the simplified regime. The requirements as to which regime to be adopted by companies depend usually on their nature a size. For instance, small enterprises with annual turnover smaller than two hundred and forty thousand Brazilian reais are entitled to adopt the simplified regimes (i.e. "Simples Nacional"). Articles 13 and 14 of Law No. 9.718 from the 27th November 1998 clearly determine that companies with annual turnover smaller or equal to seventy-eight million Brazilian reais per year may adopt the presumed profit regimes whilst larger companies must adopt the real profit regime.

The key difference in terms of methodology between the presumed profit regime and the real one is that in the first a specific tax rate is applied on gross revenue based on profitability margins assumed by the tax authorities for each business segment. On the other hand, the real profit regime is based on the actual profit and loss accounting calculations carried out monthly, where company's gains and revenues get adjusted by operating costs and expenses as well as other allowed deductions.

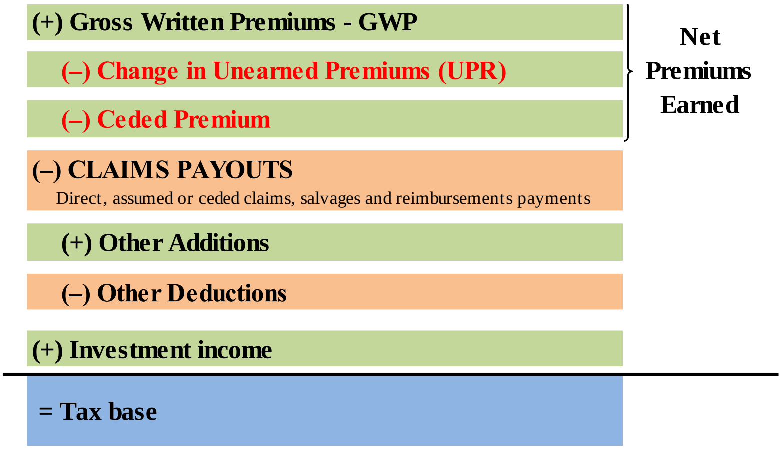
There are exceptions in terms of the size criteria that determine which segments of companies must adopt the real profit regime. Article 14, II, for instance, lists the financial institutions that must adopt the real profit regimes independently of their size.

[13] Law 10.865 / 2004 established that PIS and COFINS should be levied on the importation of goods or services at a rate of 1,65% for PIS and 7,60% for COFINS. This is a specific regime, not linked to revenue, taxing the entry of foreign goods and services into the national territory. Companies under the noncumulative regime may use credits coming from these charges whereas firms within the cumulative regime are not allowed.

4.3. PIS / COFINS in General Insurance

As noted previously, all insurance companies follow a Special Cumulative method for the calculation of PIS and COFINS. The calculation must be performed monthly considering the non-accumulated result of the period. The tax base for insurance companies registered in Brazil, based on the Brazilian RFB law, is determined by the addictions and deductions demonstrated in the Diagram 4 below.

Figure 4 – PIS COFINS Calculation Based for General Insurers



The permitted deductions on the PIS / COFINS tax base are a mixture of cash and accrual basis. The PIS / COFINS deductions related to the claims reserves are made on a cash basis and, thus a deduction is only accepted as soon there is a cash outflow. This procedure is generating a temporary difference on the calculation basis, once the PIS / COFINS calculation must be performed on an accrual basis.

In case of a negative tax base, it is not possible to compensate it with a positive tax base in the future. The payment is due one month after the calculation is done, without any declaration attached to it. The declaration must be filled two months after the PIS and COFINS calculation. The allowed deductions for the insurance companies represent almost 50% of the taxable revenue each month, characterizing a net rather than a gross tax base.

Another key factor noted by Canado (2017) is the fact that the PIS / COFINS calculation base for the non-cumulative regime created for PIS and COFINS in the years 2002 and 2003, respectively, broadened the definition and scope of revenue to total revenue hence including revenues other than strictly coming from commercial operations (i.e. sales of goods and services). This tax led to development resulted in PIS and COFINS becoming hybrid taxes combining characteristics of taxation on consumption as well as income.

GI companies are under the differentiated cumulative regime but as illustrated in Diagram 10, the investment income coming from the assets kept by insurers to cover the technical reserves

is also included in the PIS / COFINS base. Investment returns are an important source of income for GI companies in Brazil and as they do not necessarily come from the sales of insurance policies, some companies have argued in court the unconstitutionality of their taxation. Thus, companies have argued that the PIS / COFINS base has a broad approach to revenue, which might carry hybrid income-consumption features discussed earlier. In other words, PIS / COFINS is levied on the equity increase coming from this particular source of income (i.e. investment of assets), which may have some implications for the accounting treatment of PIS / COFINS in IFRS.

However, when compared to the Australian GST model for GI companies, the Brazilian PIS and COFINS model is conceptually very close as both models calculate the value added by considering the amount of premiums collected, less the amount of insurance claims pay-outs it has made. In terms of recognition of revenues (i.e. net premium earned), the Brazilian model states that the PIS / COFINS base is strictly calculated on the business activity statement for the premium and other income elements, which differs slightly from the Australian model (i.e. premium issued or full or partial payment received, whichever came first). On the expenses side, the Brazilian model takes a more stricter approach once again as only the cash outflow elements are considered. On the Australian model, for claims pay-outs, insurers are entitled to GST credits in the reporting period in which the company either received the tax invoice from its supplier or made some payments to them, whichever came first.

5. Accounting Treatment of PIS / COFINS in the Brazilian General Insurance Market

CPC 30, which is the Brazilian accounting standards on revenues, defines in item 7 revenue as being "the gross inflow of economic benefits during the period from the entity's ordinary activities that result in the increase of its shareholders 'equity, except for the owners' contributions." Item 8 of CPC 30 also mentions that "revenue includes only the gross inflows of economic benefits received and receivable from the entity when originating from its own activities. Amounts collected on behalf of third parties - such as sales taxes, taxes on goods and services and value added taxes - are not economic benefits that flow to the entity and do not result in an increase in shareholders' equity. By interpreting these CPC 30 guidance, it is clearly stated that those taxes and contributions collected on behalf of tax authorities to which entities do not benefit should not be recognized as revenues.

CPC 30 was replaced by CPC 47 ("*Receita de Contrato com Cliente*") from January 2018. CPC 47 is the Brazilian interpretation of IFRS 15 - Revenue from Contracts with Customers,

which became effective for annual reporting periods beginning on or after 1st January 2018. These new standards establish the principles that an entity applies when reporting information about the nature, amount, timing and uncertainty of revenues and cash flows from a contract with a customer. For the purpose of this paper, the most relevant section of both IFRS 15 and CPC 47 is article 47 which requires that entities when determining the transaction price must consider the amount which they are entitled in exchange for transferring promised goods or services to a customer. This means that the price must exclude the amounts collected on behalf of third parties and article 47 specifically notes sales taxes as example of such exclusions. Thus, in line with the replaced CPC 30, IFRS 15 and CPC 47 clearly state that those taxes and contributions collected on behalf of tax authorities to which entities do not benefit or are entitled to should not be recognized as revenues.

However, Martins, Gelbcke, Santos & Iudícibus (2013) notes that the Brazilian Law no. 6.404 of 15th December 1976 more commonly known as “Lei das S.A.”, which provides de legal framework for corporations or joint stock companies in Brazil. This Law stipulates that a corporation shall be deemed to be a commercial entity and shall be governed by commercial laws and practices. More specifically in article 187, item I stipulates that companies should present in their annual statement of financial position the gross revenue, sales deductions, discounts, and taxes. Additionally, in item II, companies are required to disclose net revenue, cost of goods and services sold, and gross profit. Thus, these specific items of this article require companies to consider their sales revenues at their gross values including taxes. Additionally, taxes and other listed items should be registered as deductions of gross sales so that “net revenues” (i.e. sales net of sales deductions, discounts as well as taxes) are also disclosed.

As pointed out by Martins, Gelbcke, Santos & Iudícibus (2013), the Brazilian Income Tax Regulation (Article 280 of the RIR / 99) defines net revenue as the gross revenue minus sales cancelations, discounts granted unconditionally and taxes levied on sales. As it turns out, the tax legislation followed the same guidelines of the Brazilian Corporation Law with one exception. Article 31 of Law 8.981 of 20th January 1995, added that "gross revenue does not include non-cumulative taxes, levied on purchases of goods or services from which the seller of the goods or services is a mere depositary of such taxes. However, the Brazilian Income Tax Regulation elected only taxes on Industrialized Products (i.e. IPI) as being the Brazilian non-cumulative tax in which the seller is a mere depositary.

This legal framework means that in practice, from CPC 47 and IFRS 15´s perspective, only IPI is considered as sales tax collected on behalf of tax authorities to which entities do not benefit or are entitled to should not be recognized as revenues. In other words, contrary to the tax on consumption nature common to IPI, ICMS, ISS and PIS / COFINS, only IPI is allowed to be excluded from the gross revenue in Brazil while ICMS, ISS and PIS / COFINS must be included.

Given this inconsistency, for the purposes of the publication of their financial results, some companies have standardized the treatment of IPI with other consumption taxes (i.e. ICMS, ISS, PIS / COFINS) through the adoption of a debtor account that reduces gross revenue, as it is done, for example, with ICMS. For the tax declaration, however, IPI is excluded from gross revenues. Other companies follow the law literally and simply exclude IPI from gross revenue in their financial statements. These accounting practices do not appear to be in accordance with the spirit of the Brazilian Corporation Law, whose purpose was to standardize the presentation of the financial statements of corporations to ensure the principle of comparability.

Brazil adopted IFRS as of 2010 which means that IPI is undoubtedly one of the taxes that should not be included in the recognition of gross revenues. Since IPI, which is a tax on consumption, has this legal and accounting framework that puts it in compliance with the international financial reporting standards, it is fair to assume that the other taxes levied on consumption - ICMS, ISS, PIS / COFINS – should have a similar interpretation. Although there are some differences from a legislation point of view (e.g. tax competence), the essence and nature of these taxes are the same hence they should be accounted for in a similar manner. Nonetheless, nowadays accounting practices in Brazil require that the amounts related to PIS / COFINS are accounted for in two main forms: PIS / COFINS as deduction accounts of gross revenues or as administrative expenses related to other operational revenues (e.g. investment income). Within this context, what really matters from a Brazilian accounting perspective is the concept that accounting revenue represents the differences between the taxable revenue (i.e. gross revenue) and all the taxes included in it.

This Chapter consists of three sections. In the first one, the treatment of PIS / COFINS under the Brazilian GAAP by the general insurance industry is discussed, including accounting practices which have been adopted by some of them. The second part looks at the implications of the Brazilian PIS / COFINS legal framework, which has led to different accounting

treatments in IFRS. In the final section, the accounting treatments of the Australian GST is explained in more detail.

5.1. The Accounting Treatment of PIS / COFINS in General Insurance – BR GAAP

As explained previously, insurance companies are subject to a special regime for PIS / COFINS, which consists of a specfic calculation methodology and contribution rates. Additionally, insurance companies operate a in very regulated environment with very detailed accounting rules. This includes very strict regulatory requirements associated with the treatment of PIS / COFINS.

For instance, SUSEP has a very prescriptive chart of accounts for each type of regulated and authorized firms. In Appendix 3 there is a summarized version of a chart of accounts for an insurer containing the main PIS / COFINS accounts. There are specific accounts in the balance sheet on both assets and liabilities side as well as specific PIS / COFINS expenses accounts for the income statements. This clearly shows that SUSEP considers PIS / COFINS as administrative expenses hence insurance revenues must be recognized gross of PIS / COFINS. Appendix 4 contains an example of a monthly calculation of PIS / COFINS for an insurer. The resulting PIS / COFINS expense is recognized and provisioned with impact on the administrative expenses. In the following month, the respective provision is released once the payment to the Brazilian tax authority is made.

Interestingly, it has become common accounting practice within the Brazilian insurance market to recognize a deferred tax asset equivalent to the PIS / COFINS proportion of certain insurance reserves[14] due to its temporal effect. The permitted deductions on PIS and COFINS

[14] Due to the nature of its business where a premium is received with a promise to settle a claim in the future if it were to happen, insurance companies must be able to adequately quantify its liabilities, especially its reserves for claims, in order to assess its financial position correctly, both for statutory and for internal purposes. There are reserves for future claims arising from risks covered by the insurer over the remaining period of the policy (i.e. Unearned Premium Reserve – UPR).

However, for the purpose of PIS/COFINS, consideration must be given to the claims reserves in respect of events which have already occurred: Unpaid Claims Reserves and IBNR. Unpaid Claims Reserves (UCR) relate to claims for which the event has occurred, and which are already known and reported to the insurer. "Incurred But Not Reported" (IBNR) reserves, on the other hand, relate to claims for which the event has occurred, but which have not yet been reported to the insurer.

Unpaid claims reported must be recorded and evaluated individually, separated in administrative and judicial classes and adjusted periodically. The amount recorded must be the best estimate of loss and limited to the amount insured and the coverage of the policy. Taxation follows accounting treatment hence the expenses incurred are fully tax-deductible.

tax base are a mixture between cash and accrual basis related to the Unpaid Claims Reserve (UCR) and Incurred But Not Reported (IBNR) reserve. This means that the PIS and COFINS deductions related to the UCR and IBNR provisions are made on a cash basis and, for consequence, its deductions are only accepted when it becomes a cash outflow. This procedure ends up generating a temporary difference on the calculation basis, once the PIS / COFINS calculation must be performed on an accrual basis.

According to IAS 12, when assessing the probability that taxable profit will be available against unused tax credits, an entity must consider if the it has sufficient taxable temporary differences and it is probable that it will have taxable profits before the tax credits expire.

Considering the going-concern-principle, which means that the GI company will continue to write business and report premiums in the future, it is expected that sufficient taxable profits will be incurred to support the PIS / COFINS calculation. Therefore, any deferred tax assets based on UCR and IBNR provision will be realizable in the future. Furthermore, as PIS / COFINS taxes are paid on a current basis depending on net revenue (i.e. net premiums volumes), considering the “going-concern principle”, insurance companies will still have an obligation to pay PIS / COFINS even if insurance companies report accounting losses. Thus, the PIS/COFINS tax base is only dependent on the continuation of the business, as once it reports net premiums greater than claims volumes paid, it consequently incurs a positive PIS / CONFINS tax base. As a result, the insurance company is required to pay PIS / COFINS on net revenue at 4,65%.

Within this context, as stated previously, it has become common practice for Brazilian insurance companies to register deferred tax assets (DTA) in the local statutory accounts equivalent to 4,65% of the UCR and IBNR provisions. This means that there might be a significant economic benefit when the DTA is initially recognized.

Subsequently, following local accounting practices, which are aligned with IFRS (IAS 12), as soon as there is a change in the UCR and IBNR provisions, an increase or decrease of the deferred tax asset has to be recognized, depending on the movement of the reserves. This change in the deferred asset position needs to be reversed as soon as the respective claim is settled and thus leads to a deduction in the PIS/COFINS tax base, whereas in the same period a new change in the UCR / IBNR provision results again in an increase or decrease of the

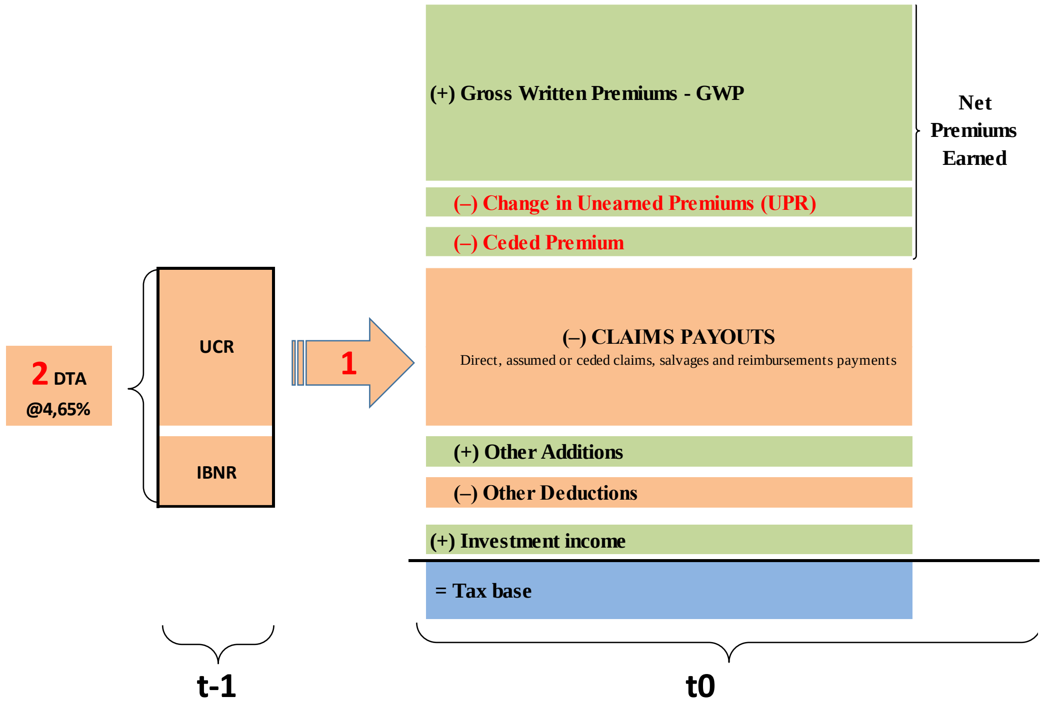
IBNR, based on a documented actuarial technical methodology, must be constituted on an actuarial basis upon the losses occurred in previous periods. Similarly to UCR, IBNR follows the accounting treatment and the related expenses incurred are fully tax-deductible.

deferred asset position. In this sense, in order equalize this temporary effect in the P&L, the recognition of the deferred asset on the amounts provisioned for claims and IBNR is required in order to ensure the correct presentation of PIS/COFINS expenses.

It is important to note that due to the size of these reserves, the impact of the first recognition of these DTAs can be significant. These DTAs shall be treated as a deductible expense and taxable income, which means that the initial recognition effect and going forward adjustments will be offered to IRPJ and CSLL taxation at currently 45%.

This whole concept and approach is illustrated in the Figure 5.

Figure 5 – Deferred Tax Asset related to PIS / COFINS on the UCR and IBNR



1 - The deductions on PIS and COFINS tax base are only permitted once the UCR and IBNR go from reserves to actual claims pay-outs (i.e. cash outflows).

2 - A deferred tax asset (DTA) equivalent to the PIS / COFINS proportion of UCR and IBNR is recognized due to this temporal effect.

There is a key element of this approach that leaves it very open to question though. There is also a provision for unearned premium (i.e. unearned premium reserve - UPR), which incurs the same temporal effect as the UCR and IBNR. However, as premiums are earned, they are added to the PIS / COFINS tax base rather than deducted from it as it happens with UCR and IBNR. Based on the same rationale used to set up the DTA, deferred tax liabilities (DTL) should also be set up on the PIS / COFINS proportion of the UPR, offsetting therefore partially or fully the amount of the corresponding UCR and IBNR DTAs.

An analysis of the financial statements for December 2017 of the top ten insurers available in SUSEP´s website revealed that five of those companies constitute deferred tax assets related to the PIS / COFINS proportion of their reserves. However, it was not clear in the financial statements of three companies which reserves those DTAs related to. In other words, it was not clear if the DTAs related to the UCR, IBNR or both reserves. In one of them, it was clearly identified that the DTAs related only to UCR whilst the another one registered DTAs over both reserves. Nonetheless, there was no detailed notes mentioning or explaining those DTAs in any of those five companies´ financial statements. This is summarized in Table 6 below.

Table 6 – Analysis DTAs - PIS / COFINS from the top 10 Brazilian Insurers

#	GENERAL INSURER	DTA PIS COFINS	BRL MILLIONS	COMMENTS
1	BRADESCO	NO	-	
2	SULAMÉRICA	**YES**	**27,2**	Not clear is only on UCR and / or IBNR
3	BB MAPFRE	**YES**	**19,8**	Not clear is only on UCR and / or IBNR
4	PORTO SEGURO	**YES**	**34,0**	Clearly stated for both UCR and IBNR
5	ZURICH	NO	-	
6	CAIXA SEGUROS	NO	-	
7	ITAÚ	NO	-	
8	TOKIO MARINE	NO	-	
9	HDI	**YES**	**21,8**	Only UCR
10	ALLIANZ	**YES**	**38,3**	Not clear is only on UCR and / or IBNR

The total DTA PIS / COFINS from the five Brazilian GI companies adopting this practice at 31st December 2017 was BRL 141,1 million. Appendix 5 contains the extracts from the financial statements of these insurance companies for year ending in 2017.

5.2. The Accounting Treatment of PIS / COFINS in General Insurance – IFRS

SUSEP has determined that from 2010 insurance companies would be required to prepare individual and consolidated financial statement according to IFRS rules, it is perfectly reasonable to state that IFRS financial accounts could follow the BR GAAP practices when accounting for PIS / COFINS. However, the specificity of SUSEP´s accounting rules for PIS / COFINS explained in the previous section, combined with the very strict local legal requirements, has led to different approaches in the treatment of PIS / COFINS for local

statutory purposes and for IFRS reporting. This development seems to contradict the regulator's intention of Brazilian insurance industry to adopt IFRS rules. This is particularly relevant for multinational financial services companies headquartered in the EU with presence in Brazil.

Contrary to the local regulatory requirement to book PIS / COFINS as expenses reported in the premium taxes lines under administrative expenses, some subsidiaries of multinational financial services organizations headquartered in the European Union (EU) countries based in Brazil are adopting the approach to treat PIS / COFINS as income taxes. This appears to be in line with IFRS rules and within the spirit of the "substance over form[15] accounting principle.

Considering that PIS / COFINS are compulsory contributions only practiced in Brazil, the specificity and corresponding accounting rules are not directly mentioned in the IFRS Standards. IAS 8 determines that in the absence of an IFRS Standard that specifically applies to a transaction, event or condition, management shall use its judgement in developing and applying an accounting policy. In making the judgement, management shall refer to, and consider the applicability of, the following sources in descending order:

- the requirements in IFRS dealing with similar and related issues; and
- the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the framework.

In addition, management may also consider the most recent pronouncements of other standard-setting bodies that use a similar conceptual framework to develop accounting standards, other accounting literature and accepted industry practices, to the extent that these do not conflict with the previously mentioned sources.

Going back to the PIS / COFINS calculation methodology, these contributions´ base is calculated as a percentage of gross revenue plus certain addictions and less certain specific expenses as demonstrated in Appendix 4. Considering these significant deductions and additions, PIS / COFINS are levied on a net rather than on a gross basis.

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[15] The "substance over form" accounting principle implies that business transactions should be accounted in accordance with their economic substance instead of their legal form. In other words, it is important to recognize and consider the economic implications of the transactions in the financial statements rather than its strict legal form as a way to more adequately reflect the financial position of the entity.

The International Financial Reporting Standards (IFRS) makes widespread use of substance over form concept such as in the IFRS 16 – Lease. For instance, if lease payments in form contain variability but, in substance, are fixed, the standard states that the lease payments are in-substance fixed if there is no genuine variability therefore should be disclosed as such.

As PIS / COFINS are recognized as part of an insurer´s revenue going through its balance sheet as well as statement of financial position, allied to the fact that PIS and COFINS are levied on a net basis as describe previously, the analysis of the IFRS framework showed that PIS / COFINS could fall under the rules of Income Taxes following, consequently, the IAS 12 accounting procedures[16].

Using this interpretation for the insurance and banking sectors, the PIS / COFINS calculation methodology seems to follow the requirements of IAS 12. In fact, certain foreign financial institutions such as Santander Bank already classify and report PIS / COFINS as income tax in their IFRS financial statements. And once again, the fact that the Social Contributions on Net Income (i.e. CSLL) is classified as income tax shows that social contributions can be classified as income tax based on the nature and essence of its net basis calculation.

As demonstrated previously, the nature of PIS / COFINS is consumptions tax and this argument is supported by the fact the Australian GST approach to the general insurance industry is close in nature to the PIS / COFINS model. However, the accounting treatment required by SUSEP recognises revenue gross of PIS / COFINS rather than net as practiced by the GI industry in Australia. Thus, although the nature of PIS / COFINS indicates that the treatment of these contributions as income tax in IFRS seems inappropriate, the Brazilian insurance regulatory authority´s view of PIS / COFINS as administrative expenses going through the profit and loss (P&L) accounts, allied to the fact that PIS / COFINS are levied on a net basis, gives margin to a different interpretation as practiced by some financial services organizations.

5.3. The Accounting Treatment of GST by Australian General Insurers

In practice, the accounting treatment of the Australian GST is very simple. There are a series of GST clearing accounts in the balance sheet and all GST balances that are either payable or recoverable are posted directly to these clearing accounts and they do not go through the P&L and there are no deferred taxes. In a nutshell, GST on premiums is credited, whilst input tax credits (i.e. GST recoverable) on claims, management expenses and commission are debited, with the net amount being either paid to or recovered from the tax office in the following month, thereby clearing the balance of the clearing accounts.

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[16] This assumption is in addition supported by KPMG’s “Insights into IFRS” 3.12.760.30, which refers to taxes related to net revenues and further deductions and that it has to be assessed in each particular case if it is in scope of IAS 12. Paragraph 3.13.40.10 explains/defines in more detail the taxable profit concept of IAS 12 (is levied on a net amount).

An analysis of the 2017 financial statements of two of the largest Australian GI insurers[17] - IAG and Suncorp - found that premium revenues include applicable levies and charges but excludes stamp duty and taxes collected on behalf of the Australian tax authority such as GST. The financial statements of three other insurance companies (Australian Unity, Elders and AAI[18]) were analysed and this same treatment of premium as being net of GST was observed. IAG had also disclosed the amount of GST payable to the tax authority in its balance sheet as part of its financial statements for December 2017.

IAG, Australian Unity, Elders and AAI´s accounting policy for the treatment of GST related to other receivables and payables, which are stated with the amount of GST, considers values inclusive of GST. Finally, Australian Unity and Elders also disclosed that their cash flows statements are presented on a GST gross basis, which are presented as operating cash flows. Financial statements for the Australian GI units of Allianz and QBE could not be found.

The treatment described above by the Australian insurance companies is consistent with the International Financial Reporting Standards (IFRS Standards) set by the International Accounting Standards Board (IASB). Australia adopted IFRS from 1st January 2005 and under IFRS 15:47[19], when determining the transaction price, firms must consider the amount which they are entitled in exchange for transferring promised goods or services to a customer and the

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[17] Per the Northern Australia Insurance Inquiry ISSUES PAPER (24 October 2017), there are 82 insurers authorised to conduct GI business in Australia but four large groups made up 68% market share of total gross written premium in the year ended June 2017. These groups are Allianz, IAG, QBE and Suncorp. https://www.accc.gov.au/about-us/inquiries/northern-australia-insurance-inquiry/issues-paper

[18] AAI is a subsidiary of Suncorp Group.

[19] IFRS 15 - Revenue from Contracts with Customers, which in Brazil has been transformed into CPC 47 (“*Receita de Contrato com Cliente*”), became effective for annual reporting periods beginning on or after 1 January 2018. IFRS 15 establishes the principles that an entity applies when reporting information about the nature, amount, timing and uncertainty of revenue and cash flows from a contract with a customer. The recognition of revenues from contracts with customers takes a five-step process: i) identify the contract(s) with a customer; ii) identify the performance obligations; iii) determine the transaction price; iv) allocate the transaction price to performance obligations, and; v) recognise revenue when performance obligations are satisfied.

It is important to note that the Financial Accounting Standards Board (FASB), which is establishes financial accounting and reporting standards for public and private companies and not-for-profit organizations in the USA, has decided to amend Topic 606 to provide an accounting policy election that permits an entity to exclude all sales and other similar taxes from the measurement of the transaction price. In other words, FASB´s decision promotes an alignment with IFRS 15.

price must exclude the amounts collected on behalf of third parties. The IFRS standards specifically cites sales taxes as example of such exclusions hence VAT must be excluded from transaction prices and revenue recognition. However, although it is natural to think about taking revenues net of VAT for insurance companies as well, insurance contracts are currently within the scope of IFRS 4, which will be replaced by the recently issued IFRS 17 from the year 2021[20].

Looking at IFRS 17, once again the Australians have moved ahead of the pack in terms of detailing the accounting rules. The Australian Accounting Standards Board (AASB), which is an Australian Government agency, has issued its interpretation of IFRS 17 named by the acronym of AASB 17. In line with the Australian approach to GST, AASB 17 shows that IFRS 17 takes a portfolio or group view of insurance policies. This means that an insurer needs to present its revenue arising from groups of similar insurance contracts net of transaction-based taxes, including GST. Additionally, as insurance revenue includes the total of the changes in the liability for remaining period of coverage that relates to services for which the entity expects to receive consideration, it somehow reflects the value-added of the business. Thus, insurance revenues clearly continue to be net of GST and the value-added from business activities carry on being considered on an overall portfolio view rather than individual policy by policy basis.

6. Conclusions

The analysis of the key features of VAT has demonstrated that the overaching purpose of VAT is to tax the purchases of individual householders hence VAT is a tax on final consumption. When discussing VAT and the challenges associated with financial services, it was made clear that VAT could not be applied to them in the standard way because of the practical difficulties in measuring the implicit value of those services. Consequently, most financial services have historically been exempt from VAT in many parts of the world, including in the EU and other developed countries.

[20] IASB has issued the IFRS 17 for insurance contracts replacing IFRS 4, with a mandatory effective date of 1 January 2021. The new standards are aimed at better reflecting the nature of insurance contracts and the impact of the accounting changes is significant, including the implications to taxation. However, the proposed changes will have greater impact on long-term contracts rather than the usual 12-month general insurance contracts. Insurers may use the simplified the Premium Allocation Approach (PPA) in case the coverage period of their contracts is one year or less, which usually applies to GI.

However, methodology and technological developments in recent years, allied to the need to include financial services within the scope of VAT, have made the VAT exemption given to financial services simply unnecessary. As proven by New Zealand and Australia, particularly for GI companies, it is possible to tax financial services by measuring and taxing value added on transactions with unregistered customers on an aggregated basis rather than each individual insurance policy.

Apart from increasing revenue by taxing VAT on financial services, there are some other clear advantages in this approach to taxing VAT on GI products and services. For instance, following the principle of “efficiency “, the design of this tax and its methodology minimizes the compliance costs for smaller traders and service providers (e.g. car parts traders; car repair shops, car garages; small firms of risk inspectors and loss adjusters) as the burden of retaining and paying VAT rests with insurance companies. Additionally, the administrative costs for the tax authorities decreases significantly due to the greatly reduced number of taxpayers (i.e. a few hundred insurers rather than millions of service providers and other third parties as well as customers).

Overall, PIS and COFINS are a very important source of tax revenues in Brazil and the financial services industry contributes significantly to these revenues. However, the three-layered government tax system coupled with the economic base approach to taxation resulted in numerous taxes being applied on each of the four tax bases: payroll, income, property and consumption. The analysis carried out has showed that PIS / COFINS are essentially taxes on consumption. Moreover, the Brazilian PIS and COFINS model for GI companies is conceptually very close to the Australian GST model, which is clearly defined as value added tax on final consumption. Under these circumstances, it would seem to be more appropriate to consider the tax on consumption nature of PIS / COFINS when deciding on their accounting treatment.

However, the Brazilian Law no. 6.404 from 1976 and the complementary Brazilian Income Tax Regulation created the concepts of gross and net revenues where only IPI is not part of an entity´s revenue recognition. This means that in practice, from CPC 47 and IFRS 15´s perspective, only IPI is considered as sales tax collected on behalf of tax authorities, which goes against the tax on consumption nature common to IPI, ICMS, ISS and PIS / COFINS. From an accounting point of view, only IPI is allowed to be excluded from the gross revenue in Brazil while ICMS, ISS and PIS / COFINS must be included. Although there are some

differences from a legislation point of view (e.g. tax competence), the essence and nature of these taxes are the same hence they should be accounted for in a similar manner.

Unsurprisingly, the Brazilian insurance regulator´s approach to the accounting treatment of PIS / COFINS is aligned with the Brazilian legal and tax framework. SUSEP states that insurance revenues are recognised gross of PIS / COFINS rather than net as practiced by the GI industry in Australia. Thus, the Brazilian insurance regulatory authority´s view is that PIS / COFINS are administrative expenses which must go through the profit and loss (P&L) accounts.

These inconsistencies have left the accounting treatment of PIS / COFINS very open for interpretation and the use of different approaches. Firstly, it has become common practice for Brazilian insurance companies to register deferred tax assets (DTA) in the local statutory accounts equivalent to 4,65% of the UCR and IBNR provisions. However, there is a provision for unearned premium (i.e. unearned premium reserve - UPR), which incurs the same temporal effect as the UCR and IBNR but with opposite effect. This means that as premiums are earned, they are added to the PIS / COFINS tax base rather than deducted from it as it happens with UCR and IBNR. Based on the same rationale used to set up the DTA, deferred tax liabilities (DTL) should also be set up on the PIS / COFINS proportional to the UPR, offsetting therefore partially or fully the amount of the corresponding UCR and IBNR´s DTAs. Given this reason, allied to the tax on consumption nature of PIS / COFINS as well as the noticeable similarities with the Australian GST model, the constitution of DTA´s over the PIS / COFINS relative to their proportion of the UCR and IBNR (i.e. 4,65%) seems inadequate.

Secondly, some multinational organisations with operations in Brazil have taken the same approach given to CSLL and categorised PIS / COFINS as income tax for IFRS purposes. As PIS / COFINS are recognized as part of an insurer´s revenue going through its balance sheet as well as statement of financial position, allied to the fact that PIS and COFINS are levied on a net basis, the analysis of the IFRS framework showed that PIS / COFINS could fall under the rules of Income Taxes following, consequently, the IAS 12 accounting procedures.

However, the nature of PIS / COFINS is consumptions tax and this argument is supported by the fact the Australian GST approach to the general insurance industry is close in nature to the PIS / COFINS model. Even though the accounting treatment required by SUSEP recognises revenue gross of PIS / COFINS rather than net as practiced by the GI industry in Australia. the substance over form nature of PIS / COFINS indicates that the treatment of these contributions as income tax in IFRS seems inappropriate

As already anticipated, the adoption of IFRS 17, which comes into effect in 2021, will not change the approach to revenue recognition from insurance contracts as already demonstrated by Australia. The Australian AASB 17 shows that IFRS 17 takes a portfolio or group view of insurance policies, which means that an insurer needs to present its revenue arising from groups of similar insurance contracts net of transaction-based taxes, including GST. IFRS 17 also brings a very significant development which is the recognition that accounting practices for insurance organizations best reflect their business model when a holistic portfolio view rather than individual policy by policy basis is taken, including the measurement of its value added.

IFRS 17, CPC 47 and the corresponding IFRS 15 and all the previous standards that have been replaced (e.g. CPC 30 / IAS 18; the soon to be replaced IFRS 4 – Insurance Contracts) clearly guide that revenues should be recognized net of transactional taxes, including VAT. Although Brazil adopted IFRS as of 2010, Brazilian accounting practices still consider some taxes as part of accounting revenue, which goes against the guidance given by IASB. Treating the company's revenue without considering values that will simply be passed on to governments and other third parties increases the quality of the accounting information whilst truly reflecting an entity´s revenue as well as its nature, size and complexity.

Based on all these arguments, it can be positively affirmed that the Brazilian PIS / COFINS applied to the general insurance industry has a consumption taxation nature similar to the Australian GST model and, therefore, should be treated as value added tax rather than administrative expenses or income taxes in the financial statements of general insurance companies. Furthermore, in line with IFRS guidance, general insurers´ revenues should be recognized net of transactional taxes, including PIS / COFINS.

As final comments, the recent experience of Australia, which introduced “The New Tax System” (TNTS) in July 2000, is proof that it is possible to simplify a national tax systems by abolishing several consumption taxes and contributions and replacing them with a single rate and more harmonised VAT. The complexity of the Brazilian tax system requires a major simplification exercise. Specifically for the insurance industry, any solution would also require both SUSEP and RFB to come together and tackle the known legal and regulatory issues. For instance, RFB should review the mixed accrual-cash features of the PIS / COFINS base for insurance companies. On SUSEP´s side, there should be changes to its accounting rules, including the chart of accounts, to reflect the need to recognize insurance revenues net of PIS / COFINS as practiced in Australia and contained in IFRS instructions.

Nonetheless, taking the Australian GST approach to the GI sector, it is quite clear that the way the current PIS / COFINS methodology for the Brazilian GI industry operates is quite close to a true value-added tax on general insurance products and services. In fact, the GI industry could well benefit from changes to the Brazilian tax system that would result in PIS / COFINS being replaced by a similar Australian GST as value-added tax. This could bring more certainty as to the legal nature and the VAT essence of PIS / COFINS, which in turn would result in a more consistent approach to the accounting treatment of PIS / COFINS by financial services organizations.

Appendix 1: Illustration of Australian GST with portfolio of four GI Policies

	Insured	Premium	Settlement	Net GST
Policy 1	Fully Registered	$10.000,00	$1.000,00	$0,00
Policy 2	Final Consumer	$800,00	$790,00	$0,91
Policy 3	Final Consumer	$2.000,00	$3.000,00	-$90,91
Policy 4	Final Consumer	$4.000,00	$0,00	$363,64

		Insurer	GST Registered Insured (1)	Insurer	GST Unregistered Insured (2)
	Premium	$10.000,00	$10.000,00	$800,00	$10.000,00
(a)	GST @ 1/11th	$1.000,00	$0,00	$72,73	$0,00
(b)	Input Tax Credit - ITC	$0,00	-$1.000,00	$0,00	$0,00
	Claims pay-out	$1.000,00	$1.000,00	$790,00	$790,00
(c)	GST Credit*	$0,00	$0,00	-$71,82	$0,00
	Australian Tax Office		$0,00		$0,91

		Insurer	GST Unregistered Insured (3)	Insurer	GST Unregistered Insured (4)
	Premium	$2.000,00	$2.000,00	$4.000,00	$2.000,00
(a)	GST @ 1/11th	$181,82	$0,00	$363,64	$0,00
(b)	Input Tax Credit - ITC	$0,00	$0,00	$0,00	$0,00
	Claims pay-out	$3.000,00	$3.000,00	$0,00	$0,00
(c)	GST Credit*	-$272,73	$0,00	$0,00	$0,00
	Australian Tax Office		-$90,91		$363,64

*Decrease of Insurer´s GST liability

Insurer Balance Sheet			
(c) GST Recoverable	$344,55	(a) GST Payable	$1.618,18
Australian Tax Office Balance			$1.273,64

GST Registered Insured´s Tax Statement			
(b) ITC	$1.000,00	(a) GST Payable	$0,00
Australian Tax Office Balance			-$1.000,00
Australian Tax Office Net GST = (a - b - c)			**$273,64**

Appendix 2:PIS / COFINS Noncumulative and Cumulative Methods

a. The Noncumulative Method

The noncumulative methods for PIS / COFINS, which have higher rates (i.e. 1,65% for PIS and 7,60% for COFINS), were established by Law 10.637 / 2002 for PIS / PASEP and Law 10.833 / 2003 for COFINS. Although no tax base deductions are permitted, companies are allowed to use credits in order to reduce the payable amounts. The legislation details which types of credits are allowed and they are usually related to those items used within the production process such as machinery and raw materials. Examples include:

- Electricity used to support the production process;
- Lease of real estate properties, machines and equipment paid to other legal entities and used by the company to achieve its fundamental purposes (e.g. manufacturing);
- Machines, equipment and other assets (i.e. fixed assets) acquired to render services.

Legal entities which calculate income tax (i.e. IRPJ) based on the real profit regime are usually subject to the non-cumulative method but there are exceptions such as financial institutions. Due to nature of these credits, the non-cumulative method is applicable to more traditional industries such as manufacturing and services.

b. The Cumulative Method

In the cumulative system, the rates are lower than in the non-cumulative system: 0,65% for PIS and 3,00% for COFINS. However, companies cannot use credits to reduce the payable amounts and similarly to the non-cumulative method, no tax base deductions are allowed.

Legal entities, which calculate the income tax (i.e. IRPJ) based on the presumed profit regime, must adopt the PIS / COFINS cumulative method hence the basis of calculation is the gross operating revenue of the legal entity without deductions in relation to costs, expenses and charges. In other words, those companies with annual turnover smaller or equal to seventy-eight million Brazilian reais per year allowed to adopt the presumed profit regimes gross revenue fall within the cumulative regime for PIS / COFINS.

However, there are legal entities (e.g. construction and civil engineering firms[21]) presumably falling in the non-cumulative method basket that are allowed by law to adopt the cumulative one, adding complexity to the system.

[21] The Brazilian government, through Law nº 10.833 / 2003 and Law nº 13.043 / 2014, permitted the construction and civil engineering companies, even if opting for the real profit income tax regime, collect PIS and COFINS according to the cumulative Regime despite the creation of the non-cumulative regime.

Appendix 3: SUSEP´s PIS / COFINS specific Balance Sheet and Expense Accounts

Chart of Accounts for Insurers

SUSEP Circular 517

CONTA	DESCRIÇÃO	
1	**ATIVO**	
11	CIRCULANTE	
114	TÍTULOS E CRÉDITOS A RECEBER	
1144	CRÉDITOS TRIBUTÁRIOS E PREVIDENCIÁRIOS	
11442	CRÉDITOS DE CONTRIBUIÇÃO SOCIAL	
11445	CRÉDITOS DE COFINS E PIS	Asset Accounts
114451	COFINS A COMPENSAR	
114453	PIS A COMPENSAR	
1213423	CONTRIBUIÇÃO SOCIAL COMPENSADA COM COFINS	
121345	CRÉDITOS DE COFINS E PIS	
1213451	COFINS A COMPENSAR	
1213452	PIS A COMPENSAR	
2	**PASSIVO**	
21	CIRCULANTE	
211	CONTAS A PAGAR	
2116	IMPOSTOS E CONTRIBUIÇÕES	Liability Accounts
21163	COFINS	
21164	PIS/PASEP	

355	**DESPESAS COM TRIBUTOS**	
3551	DESPESAS COM TRIBUTOS	
35512	CONTRIBUIÇÕES	Expense Accounts
355121	SOBRE OPERAÇÕES DE SEGUROS	
3551211	COFINS	
3551212	PIS/PASEP	

Appendix 4: PIS / COFINS Base – Calculation Methodology

General Insurance PIS / COFINS Base Example

APURACAO DO PIS/PASEP E DA COFINS

CONTA	CONTA OPERATIVA	DESCRICAO	31/01/20XX
311	**-**	**PREMIOS GANHOS**	**100.000.000**
312		**RENDAS COM TAXAS E EMISSÃO DE APÓLICES**	**0**
3131		**SINISTRO AVISADO DIRETO.ACEITO**	**-57.350.000**
31311110000006	6111101264	SIN-AVIS-IND-DIRETO-ADM-CY-PAGO	-57.350.000
3132		**SINISTRO AVISADO - CEDIDO**	**800.000**
31321100000013	6111201041	SIN-AVIS-IND-CEDIDO-ADM-PY-PAGO	800.000
3133		**SALVADOS - DIRETO.ACEITO.CEDIDO**	**7.500.000**
31331100000017	6111204002	SIN-AVIS-IND-SALV-DIRETO-ADM-PY-PAGO	7.500.000
3134		**RESSARCIMENTOS - DIREITO.ACEITO.CEDIDO**	**150.000**
31341100000013	6111104075	SIN-AVIS-IND-RESSARC-DIRETO-ADM-CY-PAGO	150.000
3151		**OUTRAS RECEITAS OPERACIONAIS**	**80.000**
3191		**SINISTRO AVISADO RESSEGURO - DIRETO.ACEITO**	**3.500.000**
31911110000013	6121201002	SIN-AVIS-IND-RESSEG-DIRETO-ADM-LOCAL-PY-PAGO	3.500.000
31911110000017	6121101111	SIN-AVIS-IND-RESSEG-DIRETO-ADM-LOCAL-CY-PAGO	0
3192		**RECEITA COM PARTICIPAÇÃO EM LUCROS - RESSEGURO**	**0**
3193	-	**PREMIOS CEDIDOS EM RESSEGURO**	**-6.350.000**
31941		**SALVADOS - RESSEGURO - DIRETO.ACEITO**	**-1.000.000**
31941110000009	6121204008	SIN-AVIS-SALV-RESSEG-DIRETO-ADM-LOCAL-PY-PAGO	-1.000.000
31942		**RESSARCIMENTOS - RESSEGURO - DIRETO.ACEITO**	**-1.300.000**
31942110000017	6121204002	SIN-AVIS-RESSAR-RESSEG-DIRETO-ADM-LOCAL-PY-PAGO	-1.300.000
361	-	**RECEITA FINANCEIRA ATIVOS GARANTIDORES**	**8.000.000**
36121200000001	5222001002	ATUAL.MONET.-TIT.RF-PRIVADOS-FINANC.	8.000.000
		TOTAL DO FATURAMENTO (01)	**54.030.000**

		BASE DE CÁLCULO - OPERACIONAL	**45.950.000**
		PIS/PASEP APURADO - 0,65%	298.675
		COFINS APURADA - 4,00%	1.838.000

		BASE DE CÁLCULO - OUTRAS RECEITAS	**80.000**
		PIS/PASEP APURADO - 0,65%	520
		COFINS APURADA - 4,00%	3.200

		BASE DE CÁLCULO - FINANCEIRO	**8.000.000**
-		PIS/PASEP APURADO - 0,65%	52.000
-		COFINS APURADA - 4,00%	320.000

		BASE DE CÁLCULO - TOTAL	**54.030.000**
7510001006	4422004058	**PIS/PASEP APURADO - 0,65%**	**351.195**
7510001005	4422004057	**COFINS APURADA - 4,00%**	**2.161.200**

Appendix 5: Brazilian General Insurers Financial Statements

i. Sul América Companhia Nacional de Seguros December 2017

Explanatory Note nº 9.1.2 – Tax Assets and Liabilities

9.1.2. Movimentação dos créditos e débitos tributários: As tabelas abaixo demonstram os créditos e débitos tributários do imposto de renda e da contribuição social e as respectivas movimentações nos períodos.

Descrição	Saldo em 01/01/2016	Constituição	Realização	Saldo em 31/12/2016
Provisão para perda em investimentos	782	–	–	782
Provisão para ações judiciais e obrigações fiscais	203.744	21.106	(24.776)	200.074
Redução ao valor recuperável de créditos	45.902	18.569	(381)	64.090
Provisões	5.220	5.617	(5.903)	4.934
Participações nos lucros	8.902	1.517	(8.869)	1.550
Perda atuarial com plano de benefício definido	3.873	1.347	(78)	5.142
Ajuste a valor de mercado	13.638	1.204	(9.709)	5.133
Outros	(94)	–	(20)	(114)
Total dos créditos tributários sobre diferenças temporárias	**281.967**	**49.360**	**(49.736)**	**281.591**
Prejuízos fiscais e bases negativas de contribuição social	**–**	**7.805**	**–**	**7.805**
PIS e COFINS sobre reservas técnicas	**31.031**	**1.021**	**(2.910)**	**29.142**
Total dos créditos tributários	**312.998**	**58.186**	**(52.646)**	**318.538**
Atualizações de depósitos judiciais	(93.928)	(20.357)	1.146	(113.139)
Resultado no exterior	(252)	–	–	(252)
Outros	(1.156)	–	–	(1.156)
Total dos débitos tributários	**(95.336)**	**(20.357)**	**1.146**	**(114.547)**

Descrição	Saldo em 31/12/2016	Constituição	Realização	Saldo em 31/12/2017
Provisão para perda em investimentos	782	–	–	782
Provisão para ações judiciais e obrigações fiscais	200.074	34.362	(735)	233.701
Redução ao valor recuperável de créditos	64.090	474	(648)	63.916
Provisões	4.934	8.414	(4.443)	8.905
Participações nos lucros	1.550	1.941	(1.733)	1.758
Perda atuarial com plano de benefício definido	5.142	2.565	–	7.707
Ajuste a valor de mercado	5.133	–	(5.133)	–
Outros	(114)	61	(4)	(57)
Total dos créditos tributários sobre diferenças temporárias	**281.591**	**47.817**	**(12.696)**	**316.712**
Prejuízos fiscais e bases negativas de contribuição social	**7.805**	**–**	**(7.199)**	**606**
PIS e COFINS sobre reservas técnicas	**29.142**	**568**	**(2.476)**	**27.234**
Total dos créditos tributários	**318.538**	**48.385**	**(22.371)**	**344.552**
Atualizações de depósitos judiciais	(113.139)	(24.129)	2	(137.266)
Resultado no exterior	(252)	–	–	(252)
Ajuste a valor de mercado	–	(1.004)	–	(1.004)
Outros	(1.156)	–	–	(1.156)
Total dos débitos tributários	**(114.547)**	**(25.133)**	**2**	**(139.678)**

ii. MAPHRE Seguros Gerais S.A. December 2017

Explanatory Note nº 28. *DETALHAMENTO DE CONTAS DAS DEMONSTRAÇÕES DE RESULTADOS* – Item "h"

	2017	2016
h) Despesas com tributos	**(101.913)**	**(36.393)**
COFINS	(94.321)	(76.973)
COFINS - Crédito tributário	16.416	54.786
PIS	(15.589)	(12.902)
PIS - Crédito tributário	2.668	8.903
Taxa de fiscalização	(3.836)	(3.904)
Outras despesas com tributos	(7.251)	(6.303)

iii. PORTO SEGURO COMPANHIA DE SEGUROS GERAIS December 2017

Explanatory Note nº 9.1 – Tax Assets

9. TRIBUTOS: 9.1 Créditos Tributários e Previdenciários

	Dezembro de 2017	Dezembro de 2016
Circulante		
Imposto de renda	1.627	34.560
Contribuição social	–	26.310
Outros	3.479	1.190
	5.106	**62.060**
Não circulante		
Imposto de renda e contribuição social diferidos (*)	[illegible]	[illegible]
PIS e COFINS diferidos sobre PSL e IBNR	33.965	23.915
Outros	3.226	4.813
	276.123	**288.354**

(*) Vide nota explicativa nº 9.2.1.

iv. HDI Seguros S.A. December 2017

Explanatory Note nº

7. Créditos tributários e previdenciários: a. Composição:	2017	2016
Créditos tributários sobre diferenças temporárias (nota 7b e 14)	17.652	17.572
Crédito tributário de PIS e COFINS sobre a provisão de sinistros a liquidar (1)	21.786	20.757
Imposto de renda a compensar	7	2.783
Contribuição social a compensar	–	2.727
Outros créditos	2.516	2
Total	**41.961**	**43.841**
Ativo circulante	**9.527**	**14.627**
Ativo não circulante	**32.434**	**29.214**

(1) Créditos tributários sobre os sinistros provisionados e ainda não pagos.

v. ALLIANZ SEGUROS Seguros S.A. December 2017

Explanatory Note nº 19.1 Tax Assets

19.1 Créditos Tributários e Previdenciários

A rubrica do Ativo circulante referente a créditos tributários e previdenciários está assim constituída:

Curto Prazo	**2017**	**2016**
Antecipação de IRPJ e CSLL	8.294	-
IOF a recuperar	8.474	-
Tributos federais compensação órgãos publicos	466	1.444
Outros impostos retidos a compensar	211	780
Totais	**17.445**	**2.224**

A composição dos créditos tributários sobre diferenças temporárias, prejuízo fiscal de imposto de renda e base negativa de contribuição social, registrados no longo prazo, é demonstrada a seguir:

	Saldos em 31.12.2016	**Movimentação Constituição**	**Utilização**	**Saldos em 31.12.2017**
Imposto de Renda				
Provisões para contingências fiscais e cíveis	26.888	27.047	(26.890)	27.045
Provisões para perdas	13.100	9.817	(13.100)	9.817
Provisões com funcionários	8.122	8.752	(8.768)	8.106
Outras provisões	15.109	10.049	(15.106)	10.052
Prejuízo fiscal	-	70	(70)	-
Contribuição social				
Provisões para contingências fiscais e cíveis	15.986	16.040	(15.984)	16.042
Provisões para perdas	10.479	7.853	(10.480)	7.852
Provisões com funcionários	7.014	6.486	(7.014)	6.486
Outras provisões	12.086	8.039	(12.085)	8.040
Base negativa	-	480	(480)	-
Créditos tributários	**108.784**	**94.633**	**(109.977)**	**93.440**
Créditos tributários de ajustes de avaliação patrimonial	(1.148)	6.550	(15.439)	(10.037)
(-) Tributos diferidos passivos	(18)	-	18	-
PIS e COFINS - Diferido	-	38.326	-	38.326
Totais	**107.618**	**139.509**	**(125.398)**	**121.729**

	Saldos em 31.12.2015	**Movimentação Constituição**	**Utilização**	**Saldos em 31.12.2016**
Imposto de Renda				
Provisões para contingências fiscais e cíveis	29.275	27.579	(29.966)	26.888
Provisões para perdas	21.678	13.100	(21.678)	13.100
Provisões com funcionários	5.860	8.264	(6.002)	8.122
Outras provisões	203	15.106	(200)	15.109
Prejuízo fiscal	102.654	29.332	(131.986)	-
Contribuição social				
Provisões para contingências fiscais e cíveis	13.039	21.391	(18.444)	15.986
Provisões para perdas	13.006	14.815	(17.342)	10.479
Provisões com funcionários	3.681	8.637	(5.304)	7.014
Outras provisões	119	12.125	(158)	12.086
Base negativa	62.466	17.413	(79.879)	-
Créditos tributários	**251.981**	**167.762**	**(310.959)**	**108.784**
Créditos tributários de ajustes de avaliação patrimonial	17.306	108	(18.562)	(1.148)
(-) Tributos diferidos passivos	(20)	-	2	(18)
Totais	**269.267**	**167.870**	**(329.519)**	**107.618**

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