

Insurancewide: A Flawed Decision

Although we understand HMRC believes that the outcome simply reinforces its current position, the *Insurancewide.Com Services Ltd* case (V20394) casts doubt on the well-established guidance in *Public Notice 701/36/02*, which was written when the March 1997 changes to Group 2 were implemented. Although this was a collaborative effort between the industry and HMRC, it is now evidently at best misleading and at worst wrong.

In our opinion HMRC has occasionally displayed a certain amount of neo-Luddite scepticism when dealing with intermediaries that you have to switch on rather than go and speak to. In this HMRC is not alone. In many parts of the European Union the perception of the insurance broker or agent is very much of a professional sitting in an office, who negotiates appropriate deals for the policyholder, whilst receiving commission from the insurer. In the UK you can, and many do, achieve the same result via on-line processes.

BACKGROUND

The Tribunal had to consider the service offered by Insurancewide in its five phases, each one more sophisticated than the last, as the insurance comparator service developed. The prospect would complete online details of his circumstances and requirements. The software behind the website analysed the information to select a number of insurers (from a list of those for whom Insurancewide was authorised to act), and selection was based on price and suitability. The website then generated a results page and e-mail with a prioritised shortlist of recommended insurers for the prospect. It was up to the prospect to click through to the website of one of the recommended insurers and complete the application.

In its last phase the applicant's information from the Insurancewide website would be assembled to display a range of on-screen quotes, with features, together with a star rating. The applicant's form was automatically transferred to the chosen insurer's website so that the

Nick Warner and Barbara Mosedale of PKF (UK) LLP consider the implications of the Insurancewide.Com Services Ltd case, which decided that a comparator insurance website provided standard-rated services

prospect did not have to complete a second application form.

The Tribunal decided that, in all its phases, the service offered by Insurancewide did not qualify for exemption.

Internet comparator websites are commonplace in the UK and it has usually been accepted by HMRC that provided the service is one of more than merely advertising, commission received will qualify for VAT exemption under VATA 1994, Sch 9, Group 2, Item 4, Note (1)(a) and (b), which exempts services related to an insurance transaction when provided by an insurance broker or insurance agent acting in an intermediary capacity.

ECJ and it was accepted by HMRC in its consultation document of July 2005 that the finding of prospects was *the* essential activity in determining whether or not such a person qualified as an insurance agent. An appropriate question would seem to be: would the insurance transaction have taken place without the involvement of Insurancewide?

SO WHY DID INSURANCEWIDE LOSE?

The taxpayer lost for one reason only: the company did not qualify as an insurance agent. The reasons that the Tribunal gave for this were as follows.

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Services provided by an insurance intermediary include the bringing together of persons seeking insurance with those providing it, and also work preparatory to the conclusion of insurance contracts.

Indeed, in this case the Tribunal confirmed that Insurancewide qualified as an insurance intermediary, a conclusion surely envisaged in HMRC's guidance in *Public Notice 701/36/02*, which gives the factors indicating exemption as:

- acting between insurers and insured (or prospective insured) parties;
- requirement for some specific insurance input rather than pure facilitation; and
- direct connection to contracts of insurance ... by bringing them about initially, or administering them, or handling claims made under them.

This was supported in the case of *Arthur Andersen & Co* (C-472/03) at the

It had no authority or contract to act on the insurer's behalf, which was missing throughout the arrangements

The Tribunal rejected the taxpayer's contention that the nature of the arrangements demonstrated that it had authority to present the insurer's offering via its website in a manner agreed with the insurer. The Tribunal chose to interpret this 'authority' in a more restrictive way, in that it had to have the power to commit or bind the insurer, referring to the case *Taksatorringen* (C-8/01) [2006] for its authority.

It was not acting on behalf of the insurer, but in its own name

The fact that Insurancewide sent out renewal reminders in its own name, rather than on behalf of an insurer, gave a strong indication that no agency existed.



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Insurancewide itself stated that it was not an agent

In paragraph 73 of the judgment this was considered ‘relevant’. (However, at paragraph 77, it was a ‘matter of law’ that Insurancewide was acting as an insurance intermediary, ‘despite its disclaimer’.)

There was also considerable debate on the meaning of ‘negotiation’, although this is more relevant to the earlier phases in development.

WHAT THIS MIGHT MEAN (IF LEFT ALONE)

This is a troublesome decision for the industry, as it will mean that many Internet-based businesses will add VAT to their charges, thus increasing the acquisition costs for insurers and increasing premiums for customers. It may also lead to HMRC questioning previous exempt rulings given to other comparator websites.

Another potential risk is that it might trigger a change in the application of the *Morganash* Tribunal decision (V19777). *Morganash* organised health questionnaires on behalf of life insurers as part of the assessment of underwriting risk but could not bind or even recommend what was a suitable risk. The Tribunal decided that *Morganash* did not qualify as an insurance broker or an insurance agent under the Sixth Directive but decided that its activities were within the scope of activities in Article 2(1)(b) of the Insurance Intermediaries Directive 77/92/EC (upon which the 1997 legislation had been based) and was therefore, as far as UK law was concerned, acting as an insurance agent. Moreover, its work was preparatory to



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the conclusion of contracts and therefore both insurance-related and performed in an intermediary capacity.

If the power to commit the insurer and an active role in mediation are now key factors, even in UK law, it is doubtful whether the services supplied by *Morganash* are still exempt from VAT. This is especially critical for the medical sector, which has relied on the insurance exemption – *Morganash* in particular – for the continued exemption of services of a medical nature performed as part of the underwriting and claims processes.

If *Insurancewide* is a correct application of the UK exemption for insurance services, *C&V (Advice Line) Services Ltd* (V17310) may also be wrongly decided. Indeed the Tribunal in *Insurancewide* implicitly did consider it to have been overruled by the ECJ in *Taksatorringen*, a significant case although, until recently, largely ignored by the UK. In *C&V* the taxpayer operated a helpline for the insured of a particular insurance company if they wished to make a claim. It did not have power to bind the insurer to accept a claim.

IS THE DECISION RIGHT?

Power to bind

Did *Insurancewide* decide that to be an agent under the EU or UK insurance exemption the taxpayer must have power to bind? It looks that way, although the Tribunal did give other reasons (see above) why the taxpayer in the case was not an insurance agent.

Is it right that an insurance agent must have power to bind? The leading authorities are the ECJ decisions in *Taksatorringen* and *Arthur Andersen*. They examined the Insurance Intermediaries Directive (77/92

– superseded by Directive 2002/92), which was concerned with freedom to establish and not taxation. Recital 8 of the former seems to regard an agent as one who has power to bind its principal but the Directive itself is much wider. Article 2.1(b) defines an agent as someone ‘instructed under one or more contracts or empowered to act in the name and on behalf of, or solely on behalf of, one or more insurance undertakings in introducing, proposing and carrying out work preparatory to the conclusion of, or in concluding contracts of insurance, or assisting in the administration and performance of such contracts...’.

Our reading of Article 2.1(b) is that it envisages that an agent may merely introduce and carry out preparatory work without binding the insurer to the contract. In this we are in company with the Court of Appeal in *Century Life* [2000] EWCA Civ 336 whose interpretation (at paragraphs 12 and 13) was that the Intermediaries Directive did not limit ‘insurance agent’ solely to those with power to bind.

Nevertheless, this does not seem to be the reading given by the ECJ. The Opinion of the Advocate-General in *Taksatorringen* (at paragraph 91), endorsed by the Court (at paragraph 45), was that an agent under this Directive must have authority to bind. This seems to us to be a misreading of the Directive which, although it does require the agent to have a contract with each insurer it represents, does not necessarily require the agent to conclude contracts, as there is a disjunctive ‘or’ in the sentence (see above). Nonetheless, this part of the *Taksatorringen* decision was cited by the Court in *Arthur Andersen* but both courts left open whether the definition in the Intermediaries Directive was to be applied in the context of the VAT Directive.

The chairman in *Insurancewide* decided that the Tribunal was entitled to derive assistance from the Insurance Intermediaries Directive and the definition of agent (as interpreted in *Taksatorringen*) should be read across to the VAT Directive and UK legislation. The Tribunal chairman in *Morganash* also considered the Insurance Intermediaries Directive definition applicable but not the interpretation put on it in *Taksatorringen*, thus reaching the opposite conclusion (at paragraphs 10 to 12) that power to bind was not essential.

The irony of the position is that the UK’s long and convoluted enactment in Sch 9, Group 2 of the very concise insurance exemption in Article 13B(a) of the Sixth Directive was based on the Intermediaries Directive. Therefore the

definition of an insurance intermediary does not require a power to bind. Indeed, the Tribunal in *Insurancewide* went on to say that *if* it was wrong in requiring an agent to have power to bind, the taxpayer would be exempt under the definition of an insurance intermediary in UK law.

The UK, including the FSA, accepts the principle that it is not your professional status that determines whether or not you are an insurance broker or insurance agent. In paragraph 9.1 of *Public Notice 701/36/02* it is stated that:

‘for the purposes of the VAT exemption, however, brokers and agents are defined in terms of what they do rather than what they are and, as well as insurance brokers and agents by profession, it can apply to other intermediaries making supplies of “related services”’.

The Tribunal acknowledges the fact that the Public Notice equates the concept of ‘agent’ with ‘intermediary’ but believes that the VAT Act distinguishes these. In the run-up to the introduction of the new Group 2 in March 1997 there was much consultation between the industry and HMRC and there was a clear belief from both sides that an agent or a broker could equate to an insurance intermediary. In the example of a specialist claims-handling company or even another insurer providing related services, exemption was to apply because they were both ‘insurance intermediaries’. It is clear that there will need to be revisions to the Public Notice if this case is to stand.

Negotiation

Referring to the Advocate-General’s opinion in *CSC Financial Services Ltd (C-235/00)* [2002] the Tribunal stated that Insurancewide had not been meaningfully involved in the negotiation of the terms and price between the prospective customer and the insurer, such mediation being expected from an intermediary.

As regards the role of mediation (or negotiation) the Tribunal has interpreted this against the backdrop of the roles of a traditional insurance broker or agent and this is partly outmoded in the UK insurance market. Insurance, especially household and motor, has long been a commodity in the UK and there is little or no room for any negotiation in the old-fashioned sense. All insurers have a set of underwriting rules that will provide a functional response, in terms of cover and price, that can be applied to the vast majority of enquiries. This will be used in the same format whether by a traditional broker, an outsourced call centre or an Internet comparator website. Only in unusual cases is there likely to be a referral

to an underwriter. In this case, insofar as there was negotiation with the insurer, it occurred at the outset, when the parameters of product and price were set.

The ‘negotiation’ element is that Insurancewide can compare the products of a range of insurers and recommend an introduction to the best, together with alternative options. The Tribunal, in our opinion, is quite wrong to accept HMRC’s contention at paragraph 68 that there is no recommendation, as this would defeat the whole purpose of the website, which ensured that contacts originating from it were flagged as such to the insurer (otherwise you may as well start with ‘A’ in the telephone directory). It also implicitly criticised the taxpayer for citing non-insurance ‘negotiation’ cases. It is highly probable that the EU Commission’s amended legislation will adopt a uniform definition of negotiation that will apply to both insurance and finance transactions.

AN ALTERNATIVE INTERPRETATION?

We think that there is an interesting point made by the taxpayer at paragraph 18, where a director of the company describes the activities of Insurancewide in its later phases as ‘being in a position comparable to an insurance broker’. We think the

The Intermediaries Directive would tend to suggest Insurancewide was an agent, as it was acting under a number of contracts with various insurance companies (see Article 2.1(b)) so it is ironic that one of the reasons given by the Tribunal for deciding that it was not an agent was that it could choose between insurers and was thus seen as acting in its own name.

WHAT WOULD BE THE RESULT UNDER THE PROPOSED AMENDMENTS TO THE SIXTH DIRECTIVE?

Insurancewide is clearly prospecting and introducing in the *Andersen* sense. HMRC’s current interpretation of introductory services means that the intermediary has to target, and recommend, to its own customer base, and be paid according to take-up. Being on Insurancewide’s website is surely the same as being in a specific retail outlet and in both cases there is a clear argument that ‘own customers’ are being targeted.

All these features are present in the Insurancewide case, and it seems to be that it is an online service that has caused HMRC to reach a different conclusion. The *HMRC Brief 69/07* states that the case does not change anything, but merely affirms paragraph 10.5 of the Public Notice, which deals with internet services. Insurancewide

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fact that it could recommend an insurer according to the needs of the prospective customer places it in a similar position to that of a broker and it might have been possible to explore this further. Counsel for the taxpayer chose not to make the case that Insurancewide was a broker (see paragraph 34) and this may have been because a broker is seen as someone without ties to insurance companies acting on behalf of the prospect, when the argument was that there were ties sufficient to establish Insurancewide as an agent in all but the restrictive ‘power to bind’ test. See, for instance, the definition in the Insurance Intermediaries Directive, Article 2.1(a), which describes a broker as ‘acting with complete freedom as to their choice of undertaking’. Insurancewide did choose between the various insurance companies but only those with which it had existing arrangements. In practice this can also be the case with brokers – for example, when insurers and brokers agree panels.

is clearly providing more than ‘just pure facilitation’, and it seems to be the fact that its service is provided by the click of a mouse that somehow diminishes it.

Under the proposed draft amendments following the EU review of financial services, ‘intermediation’ means related services ‘distinct in character and specific to and essential for the conclusion, amendment or prolongation’. It seems these services would be ‘essential’ because without Insurancewide’s involvement there would have been no insurance. The move away from reliance on the Intermediaries Directive and the focus on old-fashioned ‘agents’ and ‘brokers’ is to be very much welcomed.

In the meantime, it is hoped that there will be an appeal, as in our opinion the taxpayer has a very strong case.

The views in this article are the authors’ and do not necessarily reflect the views of PKF (UK) LLP.