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## FAQ **How does GST effect insurance and how does it work?**

### **Application of GST on Insurance Policies**

In accordance with the "Goods and Services Tax Act 1999" (GST Act), insurance is deemed a taxable supply (ie, it is not GST-free). There are, however, particular classes of insurance that DO NOT attract GST. These are:

- Travel Insurance - essentially where it involves the insurance of international travel;
- Certain Marine and Aviation Insurances;
- Private Health, Life & Ambulance Insurance;
- Insurance placed offshore, ie London or USA

For the majority of insurance policies issued, the Insurer has a liability to pay GST. This liability can be passed on to the Insured.

The ability for an Insured to claim any GST back from the Australian Taxation Office (ATO) as an Input Tax Credit (ITC) depends on the purpose for which the insurance is acquired and on the basis that the Insured's business is a registered entity, ie:

- Where the Insured is registered for GST, generally they will be entitled to claim an Input Tax Credit (ITC) for the GST paid.
- Where there is only part business use, the Insured will only be entitled to claim a part of the GST paid as an Input Tax Credit.
- Unregistered entities and individuals not in business will not be entitled to Input Tax Credits.
- Where the insurance relates to making input taxed supplies, the Insured will not be entitled to claim Input Tax Credits.

An Insured's ability to claim Input Tax Credits on an insurance premium is of critical importance when it comes to the treatment of claim settlements.

### **The amount of GST payable**

The consideration paid for an insurance policy consists of premium plus fire service levies (where applicable) and stamp duty.

In their current form, the GST regulations provide that GST is not payable in respect of stamp duty. Therefore, GST is applied to that part of the consideration (ie, total premium due for the policy of insurance) net of stamp duty. GST is payable on the fire services levy.

The GST payable is 1/11th of the GST inclusive price (net of stamp duty) or 10% of the GST exclusive price (net of stamp duty).

Example - application of GST on an insurance premium:

Premium:	\$ 1,000.00	
FSL (36%):	\$ 360.00	
Subtotal:	\$ 1,360.00	
GST (10%):	\$ 136.00	
Sub Total:	\$ 1,496.00	
Stamp Duty (9%):	\$ 134.64	
<b>Total Payable:</b>	<b>\$ 1,630.64</b>	*Includes \$136.00 GST.

### **Declaration of sums insured**

Insureds who are registered for GST purposes should evaluate their sums insured under each policy (and/or advise asset values, turnover etc where applicable) having taken into consideration the following: their entitlement to any ITC; and the fact that after an Insurer has paid a claim under a policy, the Insurer will generally be entitled to claim an ITC for the amount of GST that an Insured is unable to recover.

An Insured who is registered for GST should consider the net amount (after all ITCs have been taken into account) which is to be insured and advise the sums insured or asset values or turnover on a GST



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Exclusive basis.

An unregistered Insured who is wholly input taxed or a registered Insured who is partially input taxed will need to advise the sums insured or asset values or turnover on a GST Inclusive basis in addition to their precise taxable status.

**Insurance Claims and the application of the policy excess or deductible**

Payment of an excess by an Insured is not treated as consideration for a taxable supply and is therefore not subject to GST.

**Insurance Claims and GST**

The treatment of settlements for GST purposes depends on whether or not the Insured is registered for GST and their entitlement to claim a full or partial Input Tax Credit on the premium paid.

**Registered Insured**

A registered Insured is entitled to an Input Tax Credit on a premium to the extent that it is acquired for a taxable purpose. If the Insured is entitled to an ITC in respect of the premium, it must notify the Insurer of the percentage that it is entitled to claim. This must be done on or before making the claim.

So long as the percentage notified by the Insured to the Insurer is correct, the Insured will have no GST liability on a settlement received under the policy.

Where the Insured is partially input taxed, the Insurer will be able to claim a decreasing adjustment on the settlement amount (using the Decreasing Adjustment Mechanism (DAM)) to the extent that the Insured was not entitled to an Input Tax Credit on the premium. For example, if the Insured was entitled to claim 85% of the GST paid on the premium, the Insurer would be entitled to claim as a decreasing adjustment, 1/11th of 15% of the gross amount of a settlement made under the policy.

In effect, the operation of the DAM ensures settlements made to registered businesses that can claim full Input Tax Credits will be for the "net of GST" price of the item insured.

Settlements where a registered business can claim a partial Input Tax Credit will be for an amount somewhere between the GST-exclusive and the GST inclusive price (depending on the entitlement).

**Unregistered Insured**

An unregistered Insured is not entitled to claim an Input Tax Credit on the premium and has no liability to pay GST on the settlement. The Insurer can claim a DAM adjustment equal to 1/11th of the gross payment made.

Settlements to non registered entities will be for the "GST-inclusive price" of the insured item.

It is important to note that an Insured is not liable to pay GST on claim payments, provided they have informed their Insurer as to their entitlement to an ITC on the premium paid on the policy (or their tax status). This must be done at (or before) the time of a claim.

The tax status is the percentage an Insured is entitled to claim as an Input Tax Credit for the GST on the premium paid on any policy. If the Insured is registered for GST, it is a requirement under the GST legislation for the Insured to advise its Insurer(s) of its ABN and tax status. Failure to do so may result in the Insured having a GST liability on any claim settlement made under any policy.

The level of an Insured's tax status is a matter to be determined by a professional tax adviser.

**Below are examples of how the treatment of GST is applied to a claim.**

***Registered ABN Business***



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The Insured incurs \$1,100 (including GST) property damage that is claimable under an insurance policy. The Insured has informed the Insurer of their ABN and a tax status of 100%.

1(a) The Insurer organises the replacement of property (a non-cash settlement).

- Insurer purchases \$1,100 replacement property
- Insurer claims \$100 GST from ATO.

1(b) The Insured organises the replacement of the property and claims reimbursement from the Insurer (a cash settlement).

- Insured buys \$1,100 replacement property
- Insured claims \$100 GST from ATO
- Insurer pays to the Insured \$1,000.

1(c) The Insured is a registered business with a tax status of only 50%

The Insured organises the replacement of the property and claims reimbursement from the Insurer (a cash settlement).

- Insured buys \$1,100 replacement property
- Insured can claim 50% of the GST (being \$50) from the ATO
- Insurer pays to the Insured \$1,050
- Insurer claims 50% of the GST from the ATO (being \$50) with the implementation of DAM.

***Unregistered Business (Private Individual)***

The Insured incurs \$1,100 property damage (including \$100 GST) that is claimable under an insurance policy.

- Insurer purchases \$1,100 replacement property
- Insurer claims \$100 GST from ATO

**Important Note**

The rule is that the registered entity that receives a supply is the one entitled to an Input Tax Credit in relation to the supply. Thus Input Tax Credits could be "lost" if settlements are not handled correctly. For this reason it is reasonable to assume that there are only two basic types of settlement that are possible under GST:

- (a) Cash settlements paid directly to the Insured (or in the case of a non registered Insured, to a third party on behalf of the Insured),
- (b) Settlement by replacement where the Insured contracts directly with someone to replace insured property and is billed directly.

**Our advice to you regarding the application of GST on general insurance policies is offered in our capacity as Insurance Brokers. The level of your Tax Status as a business registered for GST is a matter to be assessed by your professional taxation adviser. We cannot and do not accept liability for the consequences of any information provided to your Insurer regarding your entitlements to Input Tax Credits on the premiums paid on your insurance policies.**