GSTR 2006/10 - Goods and services tax: insurance settlements and entitlement to input tax credits

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This Ruling contains references to provisions of the *A New Tax System (Goods and Services Tax) Regulations 1999,* which have been replaced by the *A New Tax System (Goods and Services Tax) Regulations 2019.* This Ruling continues to have effect in relation to the remade Regulations.

Paragraph 32 of TR 2006/10 provides further guidance on the status and binding effect of public rulings where the law has been repealed and rewritten.

A comparison table which provides the replacement provisions in the *A New Tax System (Goods and Services Tax) Regulations 2019* for regulations which are referenced in this Ruling is available.

This document has changed over time. This is a consolidated version of the ruling which was published on *15 August 2007*

Goods and Services Tax Ruling

Goods and services tax: insurance settlements and entitlement to input tax credits

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Preamble

*This document is a ruling for the purposes of section 105-60 of Schedule 1 to the **Taxation Administration Act 1953**. You can rely on the information presented in this document which provides advice on the operation of the GST system.*

*[**Note:** This is a consolidated version of this document. Refer to the Tax Office Legal Database (http://law.ato.gov.au) to check its currency and to view the details of all changes.]*

What this Ruling is about

1. This Ruling discusses the interaction between Division 11 and Division 78 of *A New Tax System (Goods and Services Tax) Act 1999* (the GST Act) where a payment of money or a supply is made by an insurer in the course of settling a claim under an insurance policy.

2. The Ruling applies to insurers that provide, or are liable to provide, consideration for a supply in settlement of an insurance claim.

3. The Ruling discusses:

- an insurer's entitlement to input tax credits under Division 11;
- the GST consequences of the settlement of an insurance claim where the insurer:
  - organises with another entity to provide goods or services to the insured or a third party;

  - makes a payment to the insured or third party or merely facilitates payment on behalf of the insured; or
  - provides a voucher to the insured or a third party;
- whether an insurer has a decreasing adjustment under Division 78 when the insurer settles a claim; and
- the GST consequences of various payments made under:
  - a workers' compensation scheme; and
  - a compulsory third party scheme.[1]

4. Unless otherwise stated, all legislative references in this Ruling are to the GST Act. Also, it can be assumed that, unless otherwise indicated, the entities referred to in the examples in this Ruling satisfy all of the necessary requirements in:

- section 9-5 for taxable supplies;
- section 11-20 for entitlement to input tax credits; and
- section 78-10 for entitlement to decreasing adjustments.

Date of effect

5. This Ruling explains our view of the law as it applied from 1 July 2000. You can rely upon this Ruling on and from its date of issue for the purposes of section 105-60 in Schedule 1 of the *Taxation Administration Act 1953*. Goods and Services Tax Ruling GSTR 1999/1 explains the GST rulings system and our view of when you can rely on our interpretation of the law in GST public and private rulings.

6. If this Ruling conflicts with a previous private ruling that you have obtained or a previous public ruling, this public ruling prevails. However, if you have relied on a previous ruling, you are protected in respect of what you have done up to the date of issue of this public ruling. This means that if you have underpaid an amount of GST, you are not liable for the shortfall prior to the date of issue of this later ruling. Similarly, you are not liable to repay an amount overpaid by the Commissioner as a refund.

Note: The Addendum to this Ruling that issued on 15 August 2007, explains our view of the law as it applied from 1 July 2007. You can rely upon the Addendum on and from its date of issue for the purposes of section 105-60 of Schedule 1 to the *Taxation Administration Act 1953*.

[1] Note that there are additional provisions in Division 79 that modify the application of Division 78 to compulsory third party schemes.

If this Addendum conflicts with a previous private ruling that you have obtained or a previous public ruling, this Addendum prevails. However, if you have relied on a previous ruling (including the public Ruling that the Addendum amends), you are protected in respect of what you have done up to the date of issue of the Addendum or, if there is a change to the legislation, you are protected in respect of what you have done up to the date the legislative change takes effect. This means that if you have relied on the earlier ruling and have underpaid an amount of GST, you are not liable for the shortfall prior to either the issue date of the Addendum or the date the legislative change takes effect, as appropriate. Similarly, if you have relied on the earlier ruling you are not liable to repay an amount overpaid by the Commissioner as a refund.

Background

Settlement of claims

7. Under a general insurance policy, there are a number of alternatives available to an insurer in settling a claim. For example, if insured goods are damaged, lost or stolen, an insurer may:

- reimburse the insured or a third party with a cash payment for replacing or repairing the goods;
- provide the insured or a third party with a voucher to replace the goods;
- arrange to pay the supplier directly for goods being supplied to the insured or a third party;
- organise for a supplier to repair the goods or to supply replacement goods to the insured or a third party; or
- acquire replacement goods and supply them to the insured or a third party.

8. For the purposes of this Ruling, when we use the term 'third party', we are referring to an entity that the insured has a liability to. For example, the insured has a liability to an entity because of damage caused by the insured to that entity. Consequently, the insurer may make a payment or a supply to that entity in settlement of the insured's claim under the policy.

9. In the case of a motor vehicle accident claim, the insurer may pay an agreed amount to the insured in the event of a total loss or organise with a repairer to repair the vehicle and provide the insured with a replacement vehicle or subsidise car hire for the insured.

10. If a person is injured at work and makes a workers' compensation claim against the employer, then the insurer may make certain arrangements which include payments for:

- medical costs for the treatment of the injury (for example, the injured worker may be referred to a medical specialist for treatment);
- referral to the workers' compensation insurer's nominated medical provider for a report on the injured worker's condition (including any travel costs); and
- other health services (including those listed in section 38-10, such as physiotherapy and acupuncture).

Division 9 – Taxable supply

11. A taxable supply is made by one entity (the supplier) to another entity (the recipient) if all of the requirements listed in section 9-5 are satisfied. A 'recipient' in relation to a supply is defined in section 195-1 as 'the entity to which the supply was made'.

12. In most transactions, the recipient of a supply is also the entity who is provided with that supply. However, the GST Act also contemplates that a single supply can be *made* to one entity, but is *provided* to another entity. That is, a supply made to an entity under an agreement may be provided to another entity.

13. Further, it is possible for two or more supplies to result from a single set of activities by a supplier.[2]

Division 11 – Input tax credits on creditable acquisitions

14. Division 11 deals with entitlements to input tax credits on creditable acquisitions. A supply must be 'made' to an entity for the entity to have a creditable acquisition satisfying the requirements of Division 11.

15. Pursuant to section 11-20, a registered entity is entitled to an input tax credit for any creditable acquisition. Section 11-5 provides for the meaning of a creditable acquisition.

16. An entity makes a creditable acquisition if:

- it acquires anything solely or partly for a creditable purpose;
- the supply of the thing to the entity is a taxable supply;
- the entity provides, or is liable to provide, consideration for the supply; and
- the entity is registered or required to be registered.

17. The amount of the input tax credit for a creditable acquisition is the amount equal to the GST payable on the supply of the thing

[2] This is discussed in paragraphs 217 to 221 of GSTR 2006/9 Goods and services tax: supplies.

acquired. However, the amount of input tax credit is reduced if the acquisition is only partly for a creditable purpose or the entity provides, or is liable to provide, only part of the consideration for the acquisition.[3]

18. In the context of insurance settlements, an insurer may be entitled to input tax credits in respect of payments made for acquisitions, for instance, motor vehicle repairs and replacement goods.

Division 78 – Special rules

Decreasing adjustments

19. The insurance provisions in Division 78 are designed to ensure that an insurer will only pay GST on the value of services provided by the insurer. The legislation measures the value of the insurance services by imposing GST on the full amount of the premiums collected by the insurer and then reducing the insurer's GST by way of a decreasing adjustment under section 78-10.

20. The insurer is entitled to a decreasing adjustment if the insured is not entitled to an input tax credit on the premium it pays under the insurance policy.[4] The amount of the decreasing adjustment is equal to 1/11 ^{h} of the settlement amount.[5]

21. The insurer is also entitled to a decreasing adjustment if the insured is entitled to an input tax credit on the premium it pays under the insurance policy, but that input tax credit is less than the GST payable on the premium.[6] The amount of the insurer's decreasing adjustment is reduced if the insured has a partial entitlement to input tax credits on premiums paid.[7] This would occur where the insurance policy was acquired only for a partly creditable purpose. The amount of the decreasing adjustment is also reduced to the extent (if any) the settlement relates to a non-creditable insurance event.[8]

Insurance settlements

22. If, in settlement of a claim, an insurer makes:

- a payment of money;
- a supply; or
- a payment of money and a supply,

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[3] Sections 11-25 and 11-30.
[4] Subparagraph 78-10(2)(b)(i).
[5] Subsection 78-15(1).
[6] Subparagraph 78-10(2)(b)(ii).
[7] Subsection 78-15(2).
[8] Subsection 78-15(3). What is a non-creditable insurance event is defined in subsection 78-10(3).

the payment or supply is not treated as consideration for an acquisition by the insurer.[9] Therefore, the insurer is not entitled to an input tax credit in relation to the payment or supply made to the insured in settlement of the claim.

23. Furthermore, the payment or supply by the insurer is not consideration for a supply by the insured or any other entity that was entitled to an input tax credit on the premium for the policy.[10] That is, the insured does not have a GST liability on the payment or supply received from the insurer in settlement of a claim. This is provided that, at or before a claim was first made under the policy since the last payment of a premium, the insured notified the insurer of its entitlement to claim input tax credits for the insurance premium it paid.

24. Where the insured does not inform the insurer of its entitlement to an input tax credit on its premiums, or understates its entitlement, the payment or supply by the insurer is treated as consideration for a supply by the insured to the extent of the understatement.[11] The supply made by the insured is treated as a taxable supply whether or not the entity is registered or required to be registered, at the time of the settlement or at the time of the payment or supply by the insurer.[12]

Excess payments

25. In respect of a claim under an insurance policy, the insured may be required to pay an insurance excess to:

- the insurer;
- at the direction of the insurer, to the repairer or another supplier; or
- the repairer or another supplier.

26. If the insured pays an excess directly to the insurer, the insured will not be entitled to claim an input tax credit. Similarly, if the insurer directs the insured to pay an excess to the repairer or another supplier who is acting as an agent of the insurer in respect of this payment, the insured is not entitled to an input tax credit.

27. If, on the other hand, the insured is required under the policy to pay an excess to the repairer or other supplier and that repairer or supplier is not, in respect of the payment, acting as an agent of the insurer, the insured has made an acquisition to the value of the excess and may be entitled to claim an input tax credit in respect of the payment.[13]

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[9] Section 78-20.
[10] Section 78-45.
[11] Section 78-50.
[12] Subsection 78-50(3).
[13] Excess payments are discussed at paragraphs 104 to 115 of this Ruling.

Ruling with Explanation

Claims eligible under either Division 11 or Division 78

28. If an insurer pays a supplier for providing goods, services or anything else to another entity in settling a claim under an insurance policy, then the insurer may be entitled to an input tax credit under Division 11 or, alternatively, a decreasing adjustment under Division 78.

29. When the insurer settles a claim and is entitled to an input tax credit under section 11-20, there is no entitlement to a decreasing adjustment under section 78-10. However, if the insurer has no entitlement to an input tax credit, a decreasing adjustment may be available.

30. It has been argued that an insurer may be eligible to both an input tax credit and a decreasing adjustment when settling a claim. Division 78 reflects the legislative purpose to give insurers decreasing adjustments on settlements to ensure that GST is only levied on the margin between insurance premiums and settlements. Consistent with that intention, the Commissioner considers that there is no entitlement to a decreasing adjustment where an insurance settlement gives rise to an input tax credit for the insurer.

Division 11

31. Division 11 applies if an insurer makes a creditable acquisition from a supplier. In particular, the insurer must have acquired a thing solely or partly for a creditable purpose.[14] This will apply even though the supply may be provided to another entity, the insured or a third party. In this circumstance, the insurer will be entitled to an input tax credit.[15]

32. If the insurer purchases replacement items and acquires title in the goods before supplying the goods to the insured or a third party, then Division 11 applies to the acquisition of the goods and the insurer will be entitled to an input tax credit. The subsequent supply of the goods to the insured or a third party is not a taxable supply.[16]

Division 78

33. If an insurer settles an insurance claim by way of payment of money to the insured or a third party, or reimburses the insured or a third party for costs incurred, or to be incurred, then the insurer may be entitled to a decreasing adjustment.[17]

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[14] Paragraph 11-5(a).
[15] Refer to paragraphs 14 to 18 of this Ruling.
[16] Section 78-25.
[17] Section 78-10.

34. If, in settlement of a claim, the insurer supplies to the insured or a third party a voucher which, for example, entitles the holder to a choice of supplies up to a monetary value stated on the voucher (being a Division 100 voucher[18]), that supply is not a taxable supply. However, the insurer may be entitled to a decreasing adjustment on the supply of the voucher in settlement of a claim.[19]

35. If the insurer merely facilitates the payment as part of the settlement of an insurance claim or provides consideration for a supply by a supplier to the insured or a third party, the insurer is not making a creditable acquisition and, therefore, has no entitlement to an input tax credit. However, the insurer may be entitled to a decreasing adjustment.

Acquisition of a supply in tripartite arrangements

36. Insurance settlements may involve arrangements between the insurer, the supplier of the goods, services or anything else and the insured. Arrangements involving three or more parties are commonly referred to as tripartite arrangements. Under a tripartite arrangement, it is possible that a supply is *made* to one entity under the terms of an agreement, but the supply is *provided* to another entity. For example, an insurer arranges with a supplier (or repairer) to repair the insured's motor vehicle. It is also possible under a tripartite arrangement for two or more supplies to result from a single set of activities by a supplier.

37. Tripartite arrangements can relate to any of the matters referred to in section 9-10, which discusses the meaning of *supply.* The issue to be determined is how to identify the supply or supplies made in these arrangements and by whom and to whom a supply is made.

38. An insurer has a number of alternatives available for settling an insurance claim.[20] Therefore, it is important to analyse the act or transaction that the insurer enters into when settling a claim to determine what supply is being made by whom and to whom.

39. Essentially, the GST consequences for the insurer in tripartite arrangements turn on the identification of:

- a supply and its proper characterisation;
- the recipient (acquirer) of the supply;
- the entity to whom the supply is provided;
- the consideration for that supply;
- who provides, or is liable to provide, the consideration; and

[18] Division 100 has special rules that apply to vouchers that come within the operation of the Division.
[19] Section 78-10.
[20] Paragraph 7 of this Ruling.

- whether there is a sufficient nexus between the consideration and the supply.

40. The identification and characterisation of a supply may not necessarily be determined by the description given to it by the parties to an arrangement.[21] However, where the parties have reduced their understanding of that arrangement to writing and the terms of the agreement are followed by the parties, that agreement is a significant factor in determining the supplies that have been made.

41. An examination of the surrounding circumstances, which together with the agreement form the total fact situation, is relevant for determining whether the agreement correctly records the supplies that are being made between the parties. This is discussed at paragraph 222 and following of GSTR 2006/9.

42. In tripartite arrangements, it may be that the agreement, together with the surrounding circumstances, show that there is a binding obligation between the two parties making the arrangement for goods, services or anything else to be provided to a third party.

43. The identification and characterisation of supplies in tripartite arrangements are discussed in more detail in GSTR 2006/9. The discussion in that Ruling will assist in analysing the arrangements the insurer has entered into when settling claims to determine what supply is being made, by whom, and to whom.

Supply *made* to one entity but *provided* to another entity

44. In most transactions, the recipient of a supply is also the entity who is provided with that supply. However, in analysing tripartite transactions, a supply can be made to one entity and provided to another entity. The term 'provided' here is used to contrast with the term 'made'. It distinguishes between the contractual flow of the supply to the recipient (the entity to whom the supply is made) and the actual flow of the supply to another entity (the entity to whom the supply is provided).

45. This can be contrasted with a payment arrangement where the insurer meets an insured's liability to pay a supplier, such as a repairer. In such cases, there is only one supply, that is, from the supplier to the insured. For a discussion of payment arrangements, refer to paragraphs 65 to 68 of this Ruling.

46. The identification and characterisation of supplies in tripartite transactions have received judicial consideration in the United Kingdom (UK) and New Zealand (NZ). Some of these cases are discussed in this Ruling. We consider that a principle that can be derived from UK cases such as *Customs and Excise Commissioners v. Redrow Group plc*[22] (*Redrow*) is that the entity that contracts for a

[21] *Radaich v. Smith* (1959) 101 CLR 209 at 214.
[22] [1999] 2 All ER 13; [1999] STC 161; [1999] 1 WLR 408.

supply from a supplier is the recipient of that supply, even if the supply is provided to another entity.

Insurer organises goods, services or anything else to be provided to the insured

47. In the context of an insurance settlement, an insurer may arrange with a supplier to provide goods, services or anything else to the insured or a third party. We consider that, if an insurer enters into a binding obligation with a supplier to provide goods, perform services or do something else for the insured or a third party in settlement of an insurance claim, and is liable to pay for that supply, the supplier is *making* a supply to the insurer, even though the supply may be *provided* to another entity, the insured or a third party.

48. In this case, the insurer makes an acquisition as defined in section 11-10 and the acquisition is a creditable acquisition for the purposes of section 11-5.

49. This was one of the issues considered in the Court of Appeal decision in *WHA Limited and Viscount Reinsurance Company Limited v. HM Commissioners of Customs and Excise* (*WHA Ltd*).[23]

WHA Ltd

50. In this case, Viscount, a Gibraltar based company, contracted with WHA Limited (WHA), an English company, to instruct certain garages to carry out repairs under motor vehicle breakdown insurance policies and to pay for that repair work. On each occasion that such work was carried out by a garage on WHA's instructions, the garage rendered an invoice to WHA. VAT was payable on this invoice. The effectiveness of the scheme primarily depended upon WHA being able to treat this VAT as input tax (that is, WHA was entitled to claim a credit for the VAT payable). The ability to claim that deduction depended on whether there was a supply of services to WHA.

51. At the Court of Appeal, Lord Justice Neuberger found (at paragraph 37 of the judgment) that there was a supply of services by the garage to WHA when the garage carried out repair work to a vehicle under a policy:

> In these circumstances, it appears to me that, unless there is some reason for reaching a contrary conclusion, there is indeed a "supply of services" by the garage to WHA when the garage carries out repair work to a vehicle under a policy. ….WHA receives a benefit from the carrying out of the repairs (namely satisfaction of an obligation to Viscount and the ability to earn the £17.60) and it is work which WHA will have authorised to be done. The fact that there is another beneficiary of the work, who may even fairly be said to be the primary beneficiary, namely the owner of the vehicle, should not, at least of itself, prevent the arrangement operating as a supply of "services" to WHA.

[23] [2004] EWCA Civ 559; [2004] BVC 485.

52. For VAT purposes, it was found that a supply had been made to WHA for which it could claim input credits. However, the characterisation of the arrangements in place between WHA and the garages was not made totally clear by the courts. The nature of these arrangements was the subject of some debate. In his High Court decision,[24] Justice Lloyd commented:

> It is more difficult to say, from the material before me, that the garage comes under any positive obligation to WHA to do anything. No doubt it is obliged, if it does the repair work, to do it with reasonable care and skill. But it seems difficult, on the material I have, to say that the garage owes a duty to WHA to do the work, such that if it did not do it WHA could claim that it was in breach of contract.

53. Therefore, in light of Justice Lloyd's comments, *WHA Ltd* should not be taken to be authority for the proposition that mere authorisation of repair work and payment for that work indicates that, for Australian GST purposes, an insurer has acquired something from the repairer or another supplier and is therefore entitled to an input tax credit in these circumstances. The arrangement may be nothing more than payment by a third party for which the payer is not entitled to any input tax credits.

54. We consider that there needs to be a binding obligation between the insurer and the repairer or other supplier of the type discussed below for there to be supplies acquired by the insurer from the repairer or other supplier in respect of which the insurer can claim input tax credits.

Identifying binding obligations

55. When identifying to whom a supply is made, it is necessary to look at the whole arrangement, including the contractual and other agreements made between the parties. In *WHA Ltd*, Lord Justice Neuberger said that 'one must look at the way the parties have actually structured, and indeed, expressed, their transaction or transactions'.[25] He also agreed with the observation by Justice Lloyd that:

> the contractual position is not conclusive as to what taxable supplies are made to whom, but it must be the starting point.[26]

56. An arrangement between the parties will be characterised not merely by the description given to the arrangement by the parties, but by looking at the various transactions entered into and the circumstances in which the transactions are made. This is discussed in GSTR 2006/9.

57. We consider that a repairer or other supplier will be making a supply to an insurer where there is a binding obligation (either written or oral) between the insurer and the repairer or other supplier to

[24] Paragraph 24 of *WHA Ltd & Anor v. Customs and Excise Commissioners* [2003] BVC 537.
[25] Paragraph 29 of *WHA Ltd.*
[26] Paragraph 35 of *WHA Ltd*.

provide goods, services or anything else to the insured or a third party.

58. The existence of a binding obligation between the insurer and a supplier may be evidenced by prior practice or by documentation that passes between the insurer and the supplier. In many situations, insurers will have agreements with approved repairers or other suppliers which specify that repair services or other supplies are to be provided to insured entities or third parties and that the insurer is liable to pay for these supplies. Where an examination of the total fact situation shows that there is a binding obligation between the insurer and the supplier for goods or services to be provided to an insured or a third party, the supply is made by the supplier to the insurer, but the supply is provided to the insured or the third party.

59. In the context of an insurance claim for repairs to goods or for replacement goods, we consider that, if the insurer:

- assesses the loss or damage to goods and instructs the supplier about the repairs to be done, or the goods to be replaced;
- agrees to the price for the agreed work or replacement goods with the supplier;
- is liable for, and pays for, the agreed work or replacement goods (whether or not the claimant may also be liable if the insurer does not pay); and
- satisfies itself that the repairs have been done or the replacement goods have been supplied in accordance with the agreed terms and price,

there is a strong indication that a binding obligation exists between the insurer and the supplier. Such a binding obligation, whether evidenced by written or oral agreement, will establish that the payment made by the insurer is consideration for an acquisition made by the insurer for a supply that is provided to the insured or a third party.

One activity may give rise to two or more supplies

60. A supplier may undertake a single activity that results in more than one supply being made. This is illustrated in *Redrow* where a single set of real estate agent activities within a tripartite arrangement resulted in two supplies of estate agent services being made.

61. In *Redrow*, a builder, Redrow, constructed new houses for sale. To expedite the sale of a 'Redrow' home, Redrow instructed an estate agent to value and market the existing home of each prospective purchaser. Redrow entered into an agreement with both the estate agent and the prospective purchaser that it would pay the estate agent's fee, plus VAT, if the purchaser bought a 'Redrow' home.

62. The prospective purchaser also entered into a similar agreement with the estate agent and was liable to pay the agent's commissions in the event that their existing home was sold, but they did not buy a 'Redrow' home.

63. In *Redrow*, both Redrow and the prospective purchaser contracted for the estate agent's services. The agent's activities resulted in the agent making a supply of services to both Redrow and the prospective purchaser.

64. In the context of an insurance claim, there may be two supplies made by the supplier (such as a repairer), namely one supply to the insurer and a second supply to the insured. This is discussed at paragraph 107 of this Ruling.

Payments by third party entities (payment arrangements)

65. If the insurer meets an insured's liability to the supplier without the supplier taking on any other binding obligation to the insurer, the payment by the insurer is simply a payment by a third party entity, that is, the insurer. This payment arrangement does not change the fact that the supplier makes the supply to the insured, and not to the insurer. The insurer is not making an acquisition under Division 11 and is not entitled to input tax credits for payments made to the supplier. It does not matter that the insurer and the supplier actually have arrangements in place before the event (whether under an agreement or not) to pay for the goods or services supplied to the insured or a third party, whether invoices are sent directly to the insurer or whether costs are directly debited to the insurer.

66. A feature of these arrangements is that the agreement for the supply of the goods or services is between the supplier and the insured and that an obligation to pay remains with the insured. The fact that the insurer meets the insured's liability does not alter this. There is no binding obligation between the supplier and the insurer for the supply of goods or services to the insured. The arrangement between the supplier and the insurer remains that of a payment arrangement.

67. Typical of a payment arrangement is where a person is injured at work and seeks medical treatment under a workers' compensation scheme. In some cases, workers' compensation insurers will have arrangements in place where the invoices for supplies of hospital and ambulance services made to the injured person are sent directly to the workers' compensation insurer. The supply of the medical and ambulance services can nevertheless be made to the injured person and not to the insurer, with consideration for these services being provided by the insurer.

68. In those circumstances, the supply of the medical services to the injured person is a GST-free supply.[27] Regardless of whether the supply to the injured person is a GST-free supply or a taxable supply,

[27] Subject to the requirements of the relevant section in Subdivision 38-B being met.

the workers' compensation insurer is not entitled to claim an input tax credit in respect of the payments for medical and ambulance services because it has not made an acquisition. The insurer may not be entitled to a decreasing adjustment (or may be entitled to only a limited decreasing adjustment) under Division 78, if the insured, for example the injured person's employer, can claim input tax credits on premiums paid under the policy.

Agency

69. For commercial law purposes, an agent is a person who is authorised, either expressly or impliedly, by a principal to act for that principal so as to create or affect legal relations between the principal and third parties. The principal is bound by the acts of an agent as a result of the authority given to the agent.[28]

70. In the context of an insurance claim, an insurance policy may allow the insured to arrange or authorise repairs on behalf of the insurer. It will be a question of fact as to whether the insured is acting as agent for the insurer in arranging or authorising the repairs.

Example 1: Insured is authorised to effect repairs

71. *Trendy Pty Ltd (Trendy) owns a small shopping arcade which is insured with Classic Insurance Company (Classic). After business hours, a truck reverses into an awning which is attached to the building and is above a public thoroughfare. The police contact Trendy about the damage done to the awning which now presents a danger to the public.*

72. *The building insurance policy issued by Classic contains an emergency repairs clause allowing Trendy to arrange emergency repairs to the building where the damage occurs out of normal business hours. The particular clause, while allowing Trendy to arrange emergency repairs, does not establish Trendy as Classic's agent in making those arrangements. Trendy contacts a builder who undertakes emergency repairs to the building so that there is no safety risk to the public. Trendy pays the builder and obtains reimbursement from Classic.*

73. *Although Trendy is allowed to undertake the emergency repairs to the awning, Trendy has not been appointed as agent of Classic in the particular circumstances. Therefore, Trendy, and not Classic, is entitled to an input tax credit in respect of the supply of repairs made by the builder.*

74. *Although Classic is not entitled to an input tax credit in respect of the repairs, it may have an entitlement to a decreasing adjustment under Division 78, but only if Trendy is not entitled to a full input tax credit on its insurance premium.*

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[28] GST and Agency is discussed in GSTR 2000/37 Goods and services tax: agency relationships and the application of the law.

75. In some circumstances, an insurance policy may contain a form of an emergency repairs clause where the insured is acting as agent of the insurer. As noted above, this will be a question of fact in the particular circumstances.

Reinstatement of goods by the insurer

76. The insurer may settle claims for lost, stolen or damaged goods by:

- providing the insured or a third party with a voucher;
- acquiring replacement goods and supplying them to the insured or a third party;
- arranging for a supplier to provide goods to the insured or a third party; or
- reimbursing the insured or a third party with an agreed monetary value for replacing or repairing the goods.

Vouchers

Vouchers subject to section 100-5

77. As part of the settlement of an insurance claim, an insurer may provide an insured or a third party with a voucher that, upon redemption, entitles the holder to supplies up to a monetary value stated on the voucher. If the voucher satisfies the requirements of section 100-5, commonly referred to as a face value voucher,[29] the entity that issues the face value voucher does not account for GST on the supply of that voucher to the insurer. GSTR 2003/5 Goods and services tax: vouchers, contains a detailed discussion on the GST treatment of vouchers.

78. If Division 100 applies, the supply of the face value voucher by the entity to the insurer is not a taxable supply and there is no GST payable by that entity. The insurer is not entitled to an input tax credit on the acquisition of the voucher. When the face value voucher is redeemed, the entity that redeems the voucher for goods is liable for the GST on that supply based on the face value of the voucher.[30] However, the insurer may be entitled to a decreasing adjustment calculated in accordance with section 78-15. For the purposes of calculating the settlement amount in the method statement in that section, the GST inclusive market value of the voucher is its face value.

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[29] A letter of authorisation, which is a document provided by an insurer authorising or instructing a retailer or wholesaler to supply goods to an insured on the presentation of the letter, may be a face value voucher if it has a value stated on it.

[30] Refer to paragraphs 91 to 92 of GSTR 2003/5. Also, if change is given upon redemption of the voucher, refer to the discussion in paragraphs 110 to 115 of that Ruling.

Example 2: Insurer provides a face value voucher to the insured

79. *Mark's house is damaged by fire. Mark is not registered or required to be registered for GST. F & R Insurance Co. (F&R) buys a $5,500 face value voucher from Benny's Store (Benny's) and supplies that voucher to Mark. The face value voucher can be used to buy up to $5,500 worth of goods that are sold by Benny's.*

80. *Benny's is not liable for GST on the supply of the face value voucher to F&R but is liable for GST when it redeems the face value voucher for goods supplied to Mark. F&R is not entitled to an input tax credit on the purchase of the face value voucher from Benny's. However, F&R is entitled to a decreasing adjustment under Division 78 when, in settling the claim, it supplies Mark with the voucher. The decreasing adjustment is equal to 1/11th of the face value of the voucher, that is, 1/11th of $5,500, or $500.*

Vouchers not subject to section 100-5

81. Instead of providing a face value voucher in settlement of an insurance claim, an insurer may provide the insured with a voucher that, upon redemption, will entitle the insured to the supply of replacement items. For example, the insurer may provide the insured with a voucher to replace stolen goods.

82. If an insurer purchases a voucher, not being a face value voucher, from an entity and provides it to an insured as part of the settlement of an insurance claim, the supply of the voucher by that entity to the insurer is a taxable supply if the requirements of section 9-5 are satisfied. GST is payable on the supply of the voucher by the entity and the insurer is entitled to an input tax credit on the acquisition of the voucher from the entity. The supply of the voucher by the insurer to the insured in settlement of the claim is not a taxable supply.[31]

83. When the voucher is redeemed by the insured for the replacement goods, paragraph 9-15(3)(a) limits the consideration for the supply on redemption of the voucher to any additional consideration provided by the insured. If no additional consideration is provided by the insured, there is no consideration for the supply on redemption of the voucher. Therefore, it is not a taxable supply and no GST is payable by the entity that redeems the voucher.

[31] Section 78-25.

Example 3: Insurer provides a voucher that is not a face value voucher

84. *Geoff makes a claim with F & R Insurance Co. (F&R) for a stolen television set. F&R purchases a voucher, which is not a face value voucher, for specified goods, being a new television from Benny's Store (Benny's). F&R pays $990 for the voucher. There is no monetary amount shown on the voucher. F&R is entitled to an input tax credit of $90 (1/11th of $990) on the purchase of the voucher and Benny's accounts for the GST of $90 on the supply of the voucher to F&R.*

85. *F&R provides the voucher to Geoff who redeems the voucher for a new television. Geoff does not provide any additional consideration for the supply of the television. As no additional consideration is provided, there is no consideration for the supply of the television.*[32] *Therefore, no GST is payable on the supply of the television to Geoff.*

Acquisition of goods by the insurer

86. Under a general insurance policy, goods that have been damaged or stolen may be replaced. If the goods are replaced, the insurer may purchase the goods, so that title passes to the insurer, and then supply them to the insured. As the insurer acquires the goods, the insurer will be entitled to an input tax credit under Division 11.

Example 4: Insurer supplies replacement goods

87. *Michael has his television set stolen. Michael is not registered for GST. His insurer buys a new television for $1,100 and supplies it to Michael in settlement of the claim. The insurer is entitled to an input tax credit on the purchase of the television equal to 1/11th of the price, that is, 1/11th of $1,100, or $100.*

88. *When the insurer supplies the television set to Michael, it does not make a taxable supply. Nor is the insurer entitled to a decreasing adjustment.*

Goods or services provided to the insured

89. There are instances where the insurer pays the supplier to provide goods or services, for example, repairs, to the insured or a third party. If there is an arrangement between the insurer and the supplier that establishes binding obligations to provide supplies to the insured or a third party, there is an acquisition made by the insurer for which it may be entitled to an input tax credit.

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[32] Paragraph 9-15(3)(a).

Example 5: Insurer has agreement with supplier to provide goods

90. *If, in Example 4 above, the insurer contracts with a supplier and pays that supplier $1,100 to provide the television to Michael, then the insurer is entitled to an input tax credit for the payment made to the supplier. The amount of the input tax credit is 1/11th of the price (that is, 1/11th of $1,100, or $100). The entitlement only arises if the insurer has an agreement with the supplier establishing binding obligations to have the television provided to Michael.*

Cash settlements

91. If the insurer settles the insurance claim by way of a cash payment to the insured or a third party, the insurer has not made a creditable acquisition and is not entitled to an input tax credit.[33] However, the insurer will be entitled to a decreasing adjustment under Division 78 where the insured does not have an entitlement to a full input tax credit on the premium paid to the insurer.

Example 6: Insurer makes a cash settlement to insured

92. *CaptureIT Pty Ltd is a new professional photography business and is not registered for GST purposes as it expects its GST turnover to be less than $75,000. CaptureIT has contents insurance with BIZinsure Pty Ltd. A $500 excess payable to BIZinsure applies to all claims under the policy.*

93. *CaptureIT's business premises are broken into and a professional photography camera is stolen. The camera is critical to CaptureIT's business needs and, as a result, CaptureIT purchases a replacement camera from a specialist supplier, Photo Opportunity Ltd, for $11,000. CaptureIT contacts BIZinsure and lodges an insurance claim informing the insurer that it has already replaced the camera and that it has no entitlement to input tax credits on its insurance premiums.*

94. *This starts the following sequence of events:*

- *BIZinsure requests a copy of the receipt issued to CaptureIT to assess and approve the replacement cost of the camera.*
- *After assessing the details, BIZinsure approves the claim amount of $10,500 – that is, $11,000 replacement cost less $500 excess.*
- *BIZinsure issues a cheque to CaptureIT for $10,500.*

95. *BIZinsure's payment to CaptureIT is a payment in settlement of a claim under Division 78 and, because CaptureIT has no entitlement to input tax credits on its premiums, BIZinsure has a decreasing adjustment of $954.54 (that is, 1/11th of $10,500).*

[33] Section 78-20.

Example 7: Insurer pays supplier on behalf of the insured (payment arrangement)

96. *Assume the same facts as in Example 6 above, except that, instead of purchasing a replacement camera, CaptureIT places an order with Photo Opportunity for a camera costing $11,000. CaptureIT contacts BIZinsure and lodges an insurance claim informing them that it has ordered a replacement camera from a supplier.*

97. *The following process then occurs:*

- *BIZinsure requests a copy of the purchase order to assess and approve the replacement cost of the camera.*
- *After assessing the details, the insurer approves the claim amount of $10,500 – that is, $11,000 replacement cost less $500 excess.*
- *BIZinsure contacts Photo Opportunity and confirms the following by fax:*

  You have agreed to supply a camera to CaptureIT (our insured) under an agreement between you and CaptureIT. We confirm that we will pay you, on our insured's behalf, an amount of $10,500.
- *BIZinsure pays the supplier $10,500 and CaptureIT pays the supplier the balance of $500 (the excess).*
- *Photo Opportunity supplies the goods to CaptureIT and issues a tax invoice to CaptureIT for the full value of the camera ($11,000).*

98. *BIZinsure's payment to Photo Opportunity, on behalf of CaptureIT, is a settlement payment under Division 78 and, because CaptureIT has no entitlement to input tax credits on its premiums, BIZinsure is entitled to a decreasing adjustment of $954.54 (that is, 1/11th of $10,500).*

99. Note that it is possible for there to be a binding obligation between an insurer and a supplier when the insurer enters the process after the insured has already placed an order with a supplier. This will depend on the facts.

Supply of goods by the insured to the insurer

100. If, in settling a claim under an insurance policy, the insured makes a supply of goods to the insurer, that supply is not a taxable supply.[34] For example, where an insurer takes possession of salvage from an insured, there is no taxable supply made by the insured.

[34] Section 78-60.

Example 8: Insurer makes a cash settlement to an insured whose car is written off in an accident

101. *Noni was involved in a car accident and her car written off. She makes a claim under her insurance policy. Noni's insurance company pays her the agreed value of the car which is $11,000 and, as part of the settlement, takes possession of her written-off vehicle.*

102. *Noni is registered for GST and is entitled to an input tax credit on the payment of her insurance premium. Therefore, her insurer is not entitled to a decreasing adjustment for the $11,000 payment.*

103. *The supply of the damaged vehicle by Noni to the insurer is not a taxable supply*[35] *and the insurer is not entitled to an input tax credit*.[36]

Excess payments

Excess paid directly to insurer

104. If the insured entity is required to pay an excess in respect of an insurance claim directly to the insurer, it is not consideration for a supply by the insurer to the insured.[37] The insurer is entitled to an input tax credit for the GST payable on the full cost of the repairs. The insurer will also have an increasing adjustment in respect of the amount of the excess received.[38]

Excess paid to repairer at the direction of insurer

105. Similarly, if, at the direction of the insurer, the insured pays the excess to the repairer, and the repairer is acting as agent of the insurer in respect of this payment, the payment of the excess is not consideration for a supply made to the insured.[39] In these circumstances, the payment of the excess is treated as part of the consideration paid by the insurer for the supply of repair services made by the repairer to the insurer.

106. As a consequence, the insurer is entitled to an input tax credit for the GST payable on the full cost of the repairs. The corollary is that the insured is not entitled to an input tax credit in respect of the excess paid to the repairer. The insurer will also have an increasing adjustment in respect of the amount of the excess received from the insured.[40]

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[35] Section 78-60.
[36] Section 11-20.
[37] Section 78-55.
[38] Section 78-18.
[39] Section 78-55.
[40] Section 78-18.

Excess paid directly to repairer

107. If, on the other hand, the insured is liable under the policy to pay the excess to the repairer, and the repairer is not acting as agent of the insurer, the excess will be consideration for the supply the repairer is making to the insured. This is consistent with the UK Court of Appeal decision in *Brown & Davis Ltd v. Galbraith*[41] where it was held that, although the primary contract was between the insurance company and the repairer for a supply of repair services, there was a second contract between the insured and the repairer requiring the insured to pay for the repairs only to the extent of the excess under the policy.[42]

108. The payment of the excess by the insured is consideration for the supply of repair services to the value of the excess by the repairer. The insured, if registered for GST, may be entitled to an input tax credit. In this circumstance, the repairer will be required to provide a tax invoice in respect of the services made to the insured if requested.

109. The insurer is entitled to an input tax credit for the GST payable to the extent that the insurer pays, or is liable to pay, for the supply of the repairs made to it.

Example 9: Excess paid to repairer

110. *Billy has a motor vehicle insurance policy with Excello Insurance Co (Excello). The vehicle is a utility which Billy uses 80% for business purposes. Billy has a minor accident. The GST inclusive cost of the repairs, as agreed between Fixitup Smash Repairs (Fixitup) and Excello, is $5,500.*

111. *Under the insurance policy, the insurer's obligation is limited to the extent of the repairs less the excess of $110. Excello's liability to Fixitup for the cost of the repairs is $5,390, while Billy's liability to Fixitup is for the excess ($110).*

112. *Excello is entitled to claim an input tax credit of $490 (1/11th of $5,390) in respect of its payment to Fixitup. Billy is making a creditable acquisition of repair services and is entitled to claim an input tax credit of $8 (80% of 1/11th of $110) in respect of his payment to Fixitup.*

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[41] [1972] 3 All ER 31.

[42] In *Brown & Davis Ltd v. Galbraith*, the issue was whether there was an implied contract between the insured and the repairer to pay for the main cost of the repairs in the event that the insurance company did not pay those costs. When the insurance company went into liquidation, the repairer sought to recover the main costs of the repairs from the insured. It was held that there was no implied contract between the insured and the repairer in respect of these costs. Rather, there were two contracts, one between the insurance company and the repairer whereby the insurance company undertook to pay the main repair costs and the second between the insured and the repairer whereby the insured would pay the excess to the repairer.

Example 10: Excess paid to insurer

113. *Assuming the same facts from Example 9, except that Excello is liable under the agreement with Fixitup for the total cost of the repairs ($5,500), and Billy is required to pay the excess ($110) to Excello. Excello is entitled to an input tax credit of $500 (1/11th of $5,500). Billy has no entitlement to an input tax credit because neither Excello nor Fixitup has made a supply to Billy for which the excess is consideration.*

114. *Excello also has an increasing adjustment in respect of the excess paid by the insured to Excello.*[43] *The increasing adjustment is 1/11th of $110, or $10, meaning that the insurer will have a net input tax credit of $490.*

115. *The same result will apply if the insured is required to pay the excess to the repairer at the direction of, or on behalf of, the insurer.*

Workers' compensation

116. Payments towards or under a workers' compensation scheme (and any settlement under such a scheme) are treated in the same manner as payments for an insurance policy (and a settlement of a claim under an insurance policy). This is only the case if the cover offered by the scheme is within the definition of an 'insurance policy' in section 195-1 or listed in Schedule 10 of the A New Tax System (Goods and Services Tax) Regulations 1999 as a 'statutory compensation scheme'.

117. If an employee makes a compensation claim against the employer and the employer's workers' compensation insurer accepts liability for the workplace injury, then the insurer may pay for certain goods and services to be provided to the employee. The same issues in relation to the payment of similar benefits as for other general insurance settlements arise. Whether the payment is subject to Division 11 or Division 78 depends on whether there is a binding obligation between the insurer and the supplier to provide goods and/or services to the insured's employee.

118. Various examples dealing with workers' compensation claims are discussed below.

Example 11: Medical costs

119. *Sam's employee, Nick, is injured at work. Sam is registered for GST and claims a full input tax credit for his workers' compensation insurance premium. Nick receives treatment at the local doctor's surgery for his injury and pays the bill. After receiving the claim (and accepting liability under the insurance policy), Sam's insurer reimburses Nick for the doctor's bill.*

[43] Subsection 78-18(3).

120. *The insurer has no contractual relationship or binding agreement for the supply of medical services to Nick. The insurer has not made an acquisition for GST purposes and is not entitled to an input tax credit under Division 11. The payment is made as a reimbursement in settlement of an insurance claim.*

121. *The insurer is not entitled to a decreasing adjustment under Division 78 because Sam is entitled to a full input tax credit on the workers' compensation insurance premium.*

Example 12: Travel costs

122. *In attending the local doctor's surgery, Nick incurs taxi fares that are GST inclusive. Nick seeks and receives a reimbursement from Sam's workers' compensation insurer of the taxi fares. The payment is in settlement of an insurance claim.*

123. *Division 11 does not apply to the reimbursement made to Nick as the insurer does not have any binding agreement with the taxi company (the supplier) and has not made a creditable acquisition.*

124. *The reimbursement falls for consideration under Division 78. However, the insurer is not entitled to a decreasing adjustment because Nick's employer is entitled to a full input tax credit for his workers' compensation insurance premium.*

Example 13: Other medical services

125. *Nick needs physiotherapy treatment. Nick is instructed by the workers' compensation insurer to make an appointment with Anne, a nominated physiotherapist of the workers' compensation insurer. Under the agreement that Anne has with the insurer, she is required to provide 'appropriate treatment' to Nick and invoice the insurer in respect of services. Therefore, there is a binding obligation between the insurer and Anne that requires Anne to provide physiotherapy services to Nick.*

126. *Anne is making a taxable supply to the insurer. The supply can not be a GST-free supply of 'other health services' under section 38-10 because the supply is not for the 'appropriate treatment of the recipient of the supply', that is, the insurer. Accordingly, the insurer is entitled to an input tax credit in respect of any fees paid to Anne. A decreasing adjustment is not available to the insurer.*

Example 14: Medical specialist services

127. *Due to the time Nick has had off work, he is referred to the nominated medical specialist of the workers' compensation insurer for a report on his condition. There is a binding obligation between the insurer and the specialist requiring the specialist to examine Nick and provide a report on his condition.*

128. *The supply of the report by the specialist is not a GST-free supply of a medical service under Subdivision 38-B regardless of whether it is supplied to Nick or to the insurer. The supply to the insurer of the specialist's report is a taxable supply by the specialist. It is also a creditable acquisition by the insurer who is entitled to an input tax credit in respect of the creditable acquisition.*

Example 15: Rehabilitation

129. *As part of Nick's therapy, he attends a fitness centre. There is a binding obligation between the workers' compensation insurer and the fitness centre requiring the fitness centre to provide services to the insurer's clients, such as Nick. There is a supply from the fitness centre to the insurer. Therefore, the insurer is entitled to an input tax credit in respect of the payments made to the fitness centre under Division 11.*

130. *However, if there was not a binding obligation between the insurer and the fitness centre for the supply of services, the payment by the insurer to the fitness centre would be a payment in settlement of a claim and Division 11 would not apply. Additionally, the insurer would not be entitled to a decreasing adjustment under Division 78 because Nick's employer is entitled to a full input tax credit for his workers' compensation premium.*

Example 16: Massage services

131. *As part of Nick's therapy, he goes to a masseuse. The workers' compensation insurer informs Nick that he should attend a masseuse mentioned on the insurer's list of approved masseuses because the insurer has an arrangement with each of those masseuses to forward invoices to the insurer for payment. The arrangement is not for a supply to the insurer to have services provided to workers' compensation patients. It is merely a payment arrangement.*

132. *The supply of the massage services by the masseuse to Nick is a taxable supply.*[44] *The arrangement between the insurer and the masseuse is for administration purposes only and there is not a binding obligation for the supply of that service to a third party. Therefore, the insurer is not entitled to an input tax credit in respect of payments to the masseuse. Also, there is no entitlement to decreasing adjustment as the employer is entitled to a full input tax credit for its workers' compensation premium.*

[44] These services do not meet the requirements of section 38-10 and therefore are not GST-free.

Example 17: Legal and related costs

133. *Further to the above example, legal expenses may be incurred by the workers' compensation insurer, for example, its own legal costs. The insurer may also incur other expenses when determining whether Nick's injury was caused by his own negligence, for example, legal representation and advice, private investigation costs and medical reports. These costs give rise to an entitlement to input tax credits under Division 11.*

134. *If, as part of the settlement with Nick, the workers' compensation insurer is ordered or agrees to pay for Nick's legal costs, then the legal costs will form part of the settlement and are considered under Division 78, not Division 11. However, the insurer is not entitled to a decreasing adjustment as Nick's employer is entitled to a full input tax credit for its workers' compensation insurance premiums.*

Example 18: Workers' compensation settlement

135. *Alexis, a building society employee, is injured in a car accident while travelling to work. Her employer's workers' compensation insurer pays Alexis weekly benefits totalling $25,000 and also pays medical expenses of $50,000 on her behalf. The building society has an input tax credit entitlement of 22% on its workers' compensation premiums.*

136. *As a result of her injuries, Alexis is awarded the following lump sum payout:*

- *$150,000 for economic loss; and*
- *$120,000 for permanent impairment.*

137. *The insurer is entitled to a decreasing adjustment in respect of the amount paid to Alexis totalling $345,000 (weekly benefits $25,000, medical expenses $50,000 and lump sum $270,000). The amount of the decreasing adjustment is calculated in accordance with the formula in subsection 78-15(2), namely:*

1/11 × Settlement amount × [1 – extent of employer's input tax credit]

138. *Subsection 78-15(4) provides the method statement for calculating the settlement amount. The settlement amount is:*

the sum of the payments of money × 11/(11- employer's extent of input tax credit)

The settlement amount is therefore:

$345,000 × 11/[11- 0.22] = $352,040

139. *Now using the above formula in subsection 78-15(2), the amount of the decreasing adjustment that the insurer can claim is:*

1/11 × $352,040 × [1-0.22] = $24,963

Compulsory third party motor vehicle insurance

140. Divisions 79 and 80 apply to compulsory third party (CTP) motor vehicle schemes. The principles outlined above apply equally in determining the CTP insurer's entitlement to an input tax credit under Division 11.

Example 19: Supply to CTP insurer

141. *While stopping at a set of traffic lights, Scott's car is hit by David's car. Scott sustains a minor neck strain and makes a claim against David's CTP insurer. The CTP insurer refers Scott to a medical practitioner for a medical assessment. There is a binding obligation between the CTP insurer and the medical practitioner for the examination of Scott and the making of the assessment.*

142. *In this scenario, the medical practitioner is supplying a service to the CTP insurer.*[45] *The CTP insurer is entitled to claim an input tax credit under Division 11 for this service.*

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[45] The supply of the service is a taxable supply under section 9-5.

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Previous Rulings/Determinations:
GSTR 2000/36

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- compulsory third party
- contractual obligation
- creditable acquisition
- decreasing adjustment
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