GSTR 2005/D9 - Goods and services tax: insurance settlements and entitlement to input tax credits

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Draft 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 draft for industry and professional comment. As such, it represents the preliminary, though considered, views of the Australian Taxation Office. This draft may not be relied on by taxpayers and practitioners, as it is not a ruling or advice for the purposes of section 37 of the **Taxation Administration Act 1953**. The final Ruling will be a public ruling for the purposes of section 37 and may be relied upon by any entity to which it applies.*

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
  - makes a payment to the insured or merely facilitates payment on behalf of the insured; or
  - provides a voucher to the insured;
- 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.

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 and section 11-20 for entitlement to input tax credits.

5. Certain terms used in this Ruling are defined or explained in the Definitions section of the Ruling. These terms, when first mentioned elsewhere in the Ruling, appear in **bold type**. Unless otherwise stated, all legislative references in this Ruling are to the GST Act.

Date of effect

6. This draft Ruling represents the preliminary, though considered, view of the Australian Taxation Office. This draft may not be relied on by taxpayers or practitioners. When the final Ruling is officially released, it will explain our view of the law as it applies from 1 July 2000.

7. The final Ruling will be a public ruling for the purposes of section 37 of the *Taxation Administration Act 1953* and may be relied upon, after it is issued, by any entity to which it applies. 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.

8. If the final public ruling conflicts with a previous ruling that you have obtained, the 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 the final 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 effect of the later ruling. Similarly, you are not liable to repay an amount overpaid by the Commissioner as a refund.

Previous ruling

9. This draft Ruling replaces Goods and Services Tax Ruling GSTR 2000/36. GSTR 2000/36 is withdrawn with effect from the date of issue of this draft Ruling.

Background

Settlement of claims

10. 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 with an agreed monetary value for replacing or repairing the goods;
- provide the insured with a voucher to replace the goods;
- arrange to pay the supplier directly for goods being supplied to the insured;
- organise for a supplier to repair the goods or to supply replacement goods to the insured; or
- acquire replacement goods and supply them to the insured.

11. 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, organise with a repairer to repair the vehicle, provide the insured with a replacement vehicle, or subsidise car hire for the insured.

12. 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 his/her 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

13. 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'.

14. In determining to which entity a supply is made, the GST Act contemplates that a single supply can be *made* to one entity, but be *provided* to another entity. That is, a supply made to an entity under a contract may be provided to another entity. A specific example is the special rule in subsection 38-190(3) which denies GST-free status to certain supplies that are 'made' to non-residents outside Australia, but which are 'provided' to another entity in Australia.

Division 11 – Input tax credits on creditable acquisitions

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

16. 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.

17. 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.

18. 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 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.[1]

19. 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 or replacement goods.

Division 78 – Special rules

Decreasing adjustments

20. 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.

21. 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.[2] The amount of the decreasing adjustment is equal to 1/11th of the settlement amount.[3]

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[1] Section 11-25 and 11-30.
[2] Subparagraph 78-10(2)(b)(i).
[3] Subsection 78-15(1).

22. 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.[4] The amount of the insurer's decreasing adjustment is reduced if the insured has a partial entitlement to input tax credits on premiums paid.[5] This would occur where the insurance policy was acquired only for a partly creditable purpose.

Insurance settlements

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

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

the payment or supply is not treated as consideration for an acquisition by the insurer.[6] 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.

24. 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.[7] 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.

25. Note that section 78-50 provides that, if the insured did not inform the insurer of its entitlement to an input tax credit for the premium it paid, or understated 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.

Excess payments

26. 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.

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[4] Subparagraph 78-10(2)(b)(ii).
[5] Subsection 78-15(2).
[6] Section 78-20.
[7] Section 78-45.

27. 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.

28. 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 may be entitled to claim an input tax credit in respect of the payment.[8]

Ruling with Explanation

Claims eligible under either Division 11 or Division 78

29. 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.

30. 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.

31. It has been argued that an insurer may be eligible to both an input tax credit and a decreasing adjustment when settling a claim. We are of the view that the interaction of Division 11 and Division 78 does not give rise to entitlements under both provisions.

Division 11

32. 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.[9] This will apply even though the supply may be provided to another entity, the insured. In this circumstance, the insurer will be entitled to an input tax credit.[10]

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

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[8] Excess payments are discussed at paragraphs 84-94 of this Ruling.
[9] Paragraph 11-5(a).
[10] Refer to paragraphs 15-19 of this Ruling.
[11] Section 78-25.

Division 78

34. If an insurer settles an insurance claim by way of payment of money to the insured, or reimburses the insured for costs incurred, or to be incurred, then the insurer may be entitled to a decreasing adjustment.[12]

35. If, in settlement of a claim, the insurer supplies to the insured 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[13]), 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.[14]

36. 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, 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

37. 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. One form of tripartite arrangement is where a supply is *made* to one entity under the terms of a contract, 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.

38. 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.

39. As noted earlier in this Ruling, an insurer has a number of alternatives available for settling an insurance claim.[15] 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.

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[12] Section 78-10.
[13] Division 100 has special rules that apply to vouchers that come within the operation of the Division.
[14] Section 78-10.
[15] Paragraph 10 of this Ruling.

40. 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
- whether there is a sufficient nexus between the consideration and the supply.

41. The identification and characterisation of a supply may not necessarily be determined by the description given to it by the parties to an arrangement.[16] However, where the parties have reduced their understanding of that arrangement to writing, that contract is a significant factor in determining the supplies that have been made, assuming that the terms of the contract are followed by the parties and that there is no sham or hiding of the true transactions. An examination of the surrounding circumstances, which together with the contract form the total fact situation, is relevant for determining whether the contract correctly records the supplies that are being made between the parties.

42. In tripartite arrangements, it may be that the contract, together with the surrounding circumstances, shows 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 is discussed in more detail in draft GST Ruling GSTR 2005/D8: making supplies and analysing multi-party arrangements. The discussion in that draft 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 a supply is made.

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

44. In most GST transactions, the recipient of a supply is the entity who is also 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).

[16] *Radaich v. Smith* (1959) 101 CLR 209 at 214.

45. This can be contrasted with payment arrangements where the insurer may assume an insured's liability to pay a repairer or another supplier. In such cases, there is only one supply, that is, from the repairer or another supplier to the insured. For a discussion of payment arrangements, refer to paragraphs 61-64 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*[17] is that the entity that contracts for a supply from a supplier is the recipient of that supply, even if the supply is provided to another entity.

47. The NZ courts have also adopted this principle in analysing GST transactions. McKay J highlighted this principle in *Wilson & Horton Limited v. Commissioner of Inland Revenue*[18] where he stated:

> Where two people enter into a contract whereby one is to supply a service, the service can properly be described as supplied 'to' the other, even if it is a service for the benefit of a third party. An example is where a husband contracts with a mechanic to repair his wife's motorcar. The service is provided to the husband for the benefit of his wife.

48. In the terminology we use in the Australian GST context, the supply of the motor vehicle repairs is *made* to the husband, but *provided* to the wife.

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

49. In the context of an insurance settlement, an insurer may arrange with a supplier to provide goods, services or anything else to the insured. We consider that, if an insurer enters into a contractual obligation with a supplier to provide goods, perform services or do something else for the insured 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.

50. 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.

51. 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*).[19]

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[17] [1999] 2 All ER 1
[18] (1995) 17 NZTC 12,325 at 12,333.
[19] [2004] EWCA Civ 559.

WHA Ltd

52. 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.

53. At the Court of Appeal, Lord Justice Neuberger found (at paragraph 37 of the judgement) 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.

54. 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. Justice Lloyd, in his High Court decision,[20] commented (at paragraph 24):

> 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.

55. 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 to be done 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.

[20] Paragraph 24 of *WHA & Anor v. Customs and Excise Commissioners* [2003] BVC 537.

56. We consider that there needs to be a contractual 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 in respect of which the insurer can claim input tax credits.

Identifying contractual obligations

57. When identifying to whom a supply is made, it is necessary to look at the whole arrangement, including the contractual arrangements. 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'.[21] 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.[22]

58. This is discussed in more detail in draft GST Ruling GSTR 2005/D8 Goods and services tax: making supplies and analysing multi-party arrangements.

59. Based on our analysis of the above case, we consider that a repairer (or other supplier) will be making a supply to an insurer where there is a contractual obligation (either written or oral) between the insurer and the repairer or other supplier to provide goods, services or anything else to the insured.

60. The existence of such a contractual 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 which specify that repair services are to be provided to insured entities and that the insurer is liable to pay for such services. Where an examination of the total factual situation shows that there is a binding obligation between the insurer and the supplier for goods or services to be provided to an insured, the supply is made by the supplier to the insurer, but that supply is provided to the insured.

Payments by third party entities (payment arrangements)

61. If the insurer agrees to pay an insured's liability to the supplier without taking on any other contractual obligation, 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 a contract or not) to pay for the goods or services supplied to the insured, whether invoices are sent

[21] Paragraph 29 of *WHA Ltd.*
[22] Paragraph 23 of [2003] STC 658.

directly to the insurer or whether costs are directly debited to the insurer.

62. A feature of these arrangements is that the contractual relationship for the supply of the goods or services is between the supplier and the insured and that the primary obligation to pay remains with the insured. The fact that the insurer agrees to pay the supplier does not alter this. The insurer does not enter into a contract for the supply of goods or services to the insured. The arrangement between the supplier and the insurer remains that of a payment arrangement.

63. 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 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 nevertheless is made to the injured person and not to the insurer. However, consideration for these services is provided by the insurer.

64. In the above case, the supply of the medical services to the injured person is a GST-free supply. Regardless of whether the supply to the injured person is a GST-free supply or a taxable supply, 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. Further, the insurer is unlikely to be entitled to a decreasing adjustment because the insured, for example, the injured person's employer, will usually be entitled to claim input tax credits on premiums paid under the policy.

Reinstatement of goods by the insurer

65. The insurer may settle claims for stolen or damaged goods by:

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

Vouchers

Vouchers subject to section 100-5

66. As part of the settlement of an insurance claim, an insurer may provide an insured 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,[23] 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.

67. 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.[24] However, the insurer may be entitled to a decreasing adjustment calculated in accordance with section 78-15.

Example 1 – Insurer provides a face value voucher to the insured

68. *Mark's house is damaged by fire. F & R Insurance Co. (F&R) buys a $5,000 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 $5,000 worth of goods that are sold by Benny's.*

69. *Benny's is not liable for the GST on the supply of the face value voucher to F&R but is liable for the 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, but is entitled to a decreasing adjustment under Division 78 in settling the claim with Mark.*

Vouchers not subject to section 100-5

70. 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.

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[23] 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.

[24] Unless the supply is GST-free, input taxed or otherwise does not meet the requirements of section 9-5. Also, if change is given upon redemption of the voucher, refer to the discussion in paragraphs 110-115 of GSTR 2003/5.

71. 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.[25]

72. 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 issued the voucher.

Example 2 – Insurer provides a voucher that is not a face value voucher

73. *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 a specified good, 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.*

74. *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.*[26] *Therefore, no GST is payable on the supply of the television to Geoff.*

Acquisition of goods by the insurer

75. 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 may be entitled to an input tax credit under Division 11.

[25] Section 78-25.
[26] Paragraph 9-15(3)(a).

Example 3 – Insurer supplies replacement goods

76. *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 of 1/11th of the price, that is, 1/11th of $1,100 or $100.*

77. *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 to be provided to the insured

78. There may be instances where the insurer pays the supplier for certain goods to be provided to the insured. If there is a contractual arrangement between the insurer and the supplier that establishes binding obligations to provide the goods to the insured, there is an acquisition made by the insurer for which it may be entitled to an input tax credit.

Example 4 – Insurer contracts for supplier to provide goods

79. *If, in Example 3, the insurer contracts with a supplier and pays that supplier $1,100 for it 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 a contractual agreement with the supplier establishing binding obligations to have the television provided to Michael.*

Cash settlements

80. If, instead of the circumstances in Examples 3 and 4, the insurer makes a cash settlement of $1,100 to Michael, then it is not entitled to an input tax credit.[27] However, the insurer may have an entitlement to a decreasing adjustment under Division 78. Because Michael is not registered for GST and therefore has no entitlement to input tax credits on the premiums paid on the policy, the insurer is entitled to a decreasing adjustment of 1/11th of the settlement amount, that is, 1/11th of $1,100 or $100.

Supply of goods by the insured to the insurer

81. 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.[28] For example, the surrender of salvage by an insured to an insurer is not a taxable supply.

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[27] Section 78-20.
[28] Section 78-60.

Example 5 – Insurer makes a cash settlement to an insured whose car is written off in an accident

82. *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. Noni is registered for GST and is entitled to an input tax credit on the payment of her insurance premium.*

83. *Because Noni is entitled to an input tax credit on her insurance premium, the insurer is not entitled to a decreasing adjustment. The supply of the damaged vehicle by Noni to the insurer is not a taxable supply*[29] *and the insurer is not entitled to an input tax credit*.[30]

Excess payments

Excess paid directly to insurer

84. 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.[31] The insurer is entitled to an input tax credit for the GST payable on the full cost of the repairs. The insurer may also have an increasing adjustment in respect of the amount of the excess received.[32]

Excess paid to repairer at the direction of insurer

85. 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.[33] 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.

86. 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 have an increasing adjustment in respect of the amount of the excess.[34]

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[29] Section 78-60.
[30] Section 11-20.
[31] Section 78-55.
[32] Section 78-18.
[33] Section 78-55.
[34] Section 78-18.

Excess paid directly to repairer

87. If, on the other hand, the insured is liable under the policy to pay the excess to the repairer, who is not acting as an agent of the insurer, the insured may be entitled to claim an input tax credit in respect of the excess paid.[35] The payment of the excess is consideration for the supply of repair services made by the repairer to the insured. In this circumstance, the repairer will be required to provide a tax invoice in respect of the services made to the insured if requested.

88. 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 6 – Excess paid to repairer

89. *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.*

90. *Under the insurance policy, the insurer's contractual 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).*

91. *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.*

Example 7 – Excess paid to insurer

92. *Assuming the same facts from Example 6, except that Excello is liable under the contract 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 any input tax credit because neither Excello nor Fixitup has made a supply to Billy.*

93. *Excello also has an increasing adjustment in respect of the excess paid by the insured to the repairer.*[36] *The increasing adjustment is 1/11th of $110, or $10, meaning that the insurer will have a net input tax credit of $490.*

94. *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.*

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[35] Provided the other requirements of section 11-5 are satisfied.
[36] Subsection 78-18(3).

Workers' compensation

95. 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'.

96. 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 contractual relationship between the insurer and the supplier that establishes binding obligations to provide goods and/or services to the insured's employee.

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

Example 8 – Medical costs

98. *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.*

99. *The insurer has no contractual relationship or any other arrangement 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.*

100. *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 9 – Travel costs

101. *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.*

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

103. *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 10 – Other medical services

104. *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 contract 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 contractual arrangement between the insurer and Anne that requires Anne to provide her physiotherapy services to Nick.*

105. *Anne is making a supply to the insurer. This supply is not 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). If Anne is registered and the other requirements of section 9-5 are met, the supply is a taxable supply.*

106. *Accordingly, the insurer is entitled to an input tax credit in respect of any fees paid to Anne. A decreasing adjustment is not available.*

Example 11 – Medical specialist services

107. *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. The insurer has a contractual relationship with the specialist requiring the specialist to examine Nick and provide a report on his condition.*

108. *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 12 – Rehabilitation

109. *As part of Nick's therapy, he attends a fitness centre. The workers' compensation insurer has a contractual arrangement with the fitness centre requiring it 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.*

110. *However, if the insurer did not have a contractual agreement with 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 13 – Massage services

111. *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.*

112. *The supply of the massage services by the masseuse to Nick is a taxable supply.*[37] *The arrangement between the insurer and the masseuse is for administration purposes only and is not a contract 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.*

Example 14 – Legal costs

113. *Further to the above example, any legal expenses incurred by the workers' compensation insurer (for example, its own legal costs), are considered under Division 11 where it has entered into a contractual arrangement with its legal representatives.*

114. *If, as part of the settlement with Nick, the workers' compensation insurer is ordered or agrees to pay for his legal costs, then the legal costs are 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 premium.*

Compulsory third party motor vehicle insurance

115. 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.

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

Example 15 – Supply to CTP insurer

116. *While stopping at a set of traffic lights, Scott's car is hit by David's car. Scott sustains a minor neck strain. David is not registered for GST and is therefore not entitled to claim an input tax credit for his compulsory third party motor vehicle insurance premiums. The CTP insurer refers Scott to a medical practitioner for a medical assessment. The CTP insurer has a contract with the medical practitioner for the examination of Scott and the making of the assessment.*

117. *In this scenario, the medical practitioner is supplying a service to the CTP insurer.*[38] *The CTP insurer is entitled to claim an input tax credit under Division 11 for this service.*

Definitions

Indemnity

118. An undertaking to compensate for loss, damage or expense, as in the protection provided by insurance. The measure for the payment is the measure of loss sustained, and the insured cannot recover more than the actual loss.

Insurance

119. The contractual relationship of **indemnity** that exists between the insurer and the insured.

Insured

120. The party receiving insurance protection (against the risk of loss of an asset or the incurrence of a liability to a third party as a result of negligence or accident).

Insurer

121. The party providing insurance protection (against the risk of loss of an asset by an insured party or the incurrence of a liability by the insured party to a third party as result of negligence or accident).

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

Workers' Compensation

122. Compulsory insurance cover to be taken out by all employers, except for self-insured employers, according to legislative schemes to cover compensation to employees suffering injury or disease in the course of or arising out of employment.

Your comments

123. We invite you to comment on this draft Goods and Services Tax Ruling. Please forward your comments to the contact officer(s) by the due date. (Note: The Tax office prepares a compendium of comments for the consideration of the relevant Rulings Panel. The Tax Office may use a sanitised version (names and identifying information removed) of the compendium in providing its responses to persons providing comments. Please advise if you do not want your comments included in a sanitised compendium.)

Due date:	**17 February 2006**
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Detailed contents list

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Commissioner of Taxation
21 December 2005

Previous drafts:
Not previously issued as a draft

Related Rulings/Determinations:
GSTR 1999/1; GSTR 2003/5; GSTR 2005/D8

Previous Rulings/Determinations:
GSTR 2000/36

Subject references:
- acquisition of goods
- cash settlements
- compulsory third party
- contractual obligation
- creditable acquisition
- decreasing adjustment
- excess payments
- face value voucher
- increasing adjustment
- input tax credit
- insurance
- insurance settlements
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- third party
- tripartite
- vouchers
- workers' compensation

Legislative references:
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