Accounting for government imposts and similar charges under AASB 17[1]

Background

1. This paper aims to identify the main government imposts and related charges in Australia and New Zealand connected with the issue of insurance contracts and identify how they should be accounted for when applying AASB 17 *Insurance Contracts*. It does not address income tax on an insurer's taxable profit (tax loss), which is accounted for under AASB 112 *Income Taxes*.[2]

2. In general, government imposts are expected to fall into one of the following three categories:

   A amounts in substance collected by the insurer on behalf of a 3rd party;

   B costs of the insurer issuing insurance contracts

   C reinsurance premiums ceded.[3]

3. In some cases, the classifications and accounting treatment are clear and, in other cases, there appears to be scope for different views. However, it would be useful to identify a broad consensus that could be consistently applied across the Australian and New Zealand general insurance industry.

4. The paper does not address government imposts paid directly by policyholders.[4]

5. The following accounting pronouncements have been referenced in this paper:

   - AASB 17 *Insurance Contracts* [AASB 17]
   - AASB 15 *Revenue from Contracts with Customers* [AASB 15]
   - AASB 132 *Financial Instruments: Presentation* [AASB 132]
   - AASB Interpretation 1031 *Accounting for the Goods and Services Tax (GST)* [Interpretation 1031]

   The equivalent NZASB pronouncements are NZ IFRS 17, NZ IFRS 15 and NZ IAS 132. There is no NZASB equivalent to Interpretation 1031.

---

1 This paper refers to AASB 17 *Insurance Contracts*, which has the same content as NZ IFRS 17 *Insurance Contracts*.

2 AASB 112 *Income Taxes* has the same content as NZ IFRS 12 *Income Taxes*.

3 While reinsurance is not an 'impost', it is included here because governments are involved in providing reinsurance for particular types of business, sometimes on a compulsory basis.

4 For example, the Queensland levies on CTP: Hospital and Emergency Services, Nominal Defendant, and National Injury Insurance Scheme Qld ($ amounts per contract based on policy type); and South Australian levies on CTP: Emergency Services and Lifetime Support Fund, and Scheme services fee ($ amount based on policy type).

Classification of Government Imposts under AASB 17

	Impost/scheme	Income statement	Balance sheet	Cash flow
A	An amount, in substance, collected by the insurer on behalf of a 3rd party [Note 1] Amounts collected from policyholders equate to a corresponding present obligation to remit such amounts to a levying or taxation authority. For example, GST	Not treated as expenses or revenues of the insurer	Included in cash flows used to measure the insurer's liabilities/assets Any imposts collected and not yet remitted to government would be a payable of the insurer	The relevant cash flows would be included in the appropriate line items in the insurer's statement of cash flows
B	A cost of the insurer issuing insurance contracts The insurer may seek to defray the cost from the premiums it charges policyholders (which is a component of insurance revenue) For example, NSW ESL	Treated as expenses of the insurer	As above	As above
C	An amount relating to reinsurance held [Note 2] For example, ARPC	Treated as reinsurance premiums ceded (fulfilment cash flows) Any recoveries treated as reinsurance revenue	As above	As above
D	Imposts for which the outcome is less clear			

Note 1: The legal obligation to pay amounts collected on behalf of 3rd parties typically falls on the insurer and the insurer explicitly factors the imposts into the premium. See the General Principles section below for more detailed comments on the significance of the legal position.

Note 2: Amounts related to reinsurance are not strictly 'imposts' because the insurer receives reinsurance coverage in return.

General commercial principles applied

6. The classifications in this paper are based on the following principles:

- **Existing outcomes should be preserved** → Unless the text of AASB 17 clearly substantiates a change in expected reporting outcomes, an interpretation which preserves the current accounting practice should be preferred. That is, insurers should distinguish between those taxes which are effectively collected on behalf of Government (and therefore don't contribute to earnings) and those which form part of the cost of issuing insurance contracts or carrying on business more broadly. This approach has been in place for an extended period, makes meaningful distinctions between the relevant types of imposts and has not previously been identified as a source of confusion when interpreting financial statements.

- **Commercial substance approach →** From a legal perspective, the liability to pay most of the imposts falling within Categories A and B will rest with the relevant insurer. However, this feature is merely a mechanism of convenience for Governments in that it simplifies the collection mechanics for transactional level taxes and tends to push the risk of non-collection onto the insurer. For (Category A) taxes that arise at the contract level, it does not detract from the true nature of these imposts as transactional charges designed to tax the consideration provided by the end customer. On that basis, the relevant approach is to treat such amounts as simply passing through the insurer, which is acting on behalf of Government in calculating, collecting and remitting the appropriate amounts based on legislation. That is, the treatment under AASB 17 should align with the substantive nature of the tax and not unduly focus on legal mechanics. This is consistent with AASB 17.2[5] and Interpretation 1031.

- **Unit of taxation, calculation method and timing of payment are relevant →** In distinguishing between Category A and Category B amounts under the substance based method identified above, it is useful to consider various factors including the unit that is subject to taxation, the calculation method and the frequency of payments.

  When imposts are:
  - computed at a transactional level;
  - based on a fixed %; and
  - are remitted on a periodic basis to Government;

  this would tend to indicate the insurer is a mere conduit for the flows to Government.

  In contrast, when imposts are:
  - computed based on entity-level amounts (rather than transactional level amounts);
  - are remitted through estimates or instalments; and/or
  - are paid in relation to longer time periods

  this would tend to indicate classification as a cost of issuing insurance contracts or carrying on insurance business more generally.

Key accounting principles

7. The following extracts from accounting pronouncements are relevant:

- Interpretation 1031.20 states that:

  > 20 The GST component of the consideration promised by a customer does not constitute revenue of the vendor. This is because the transaction gives rise to a present obligation to remit the amounts of the tax collected to the taxation authority.

5 AASB 17.2 says (emphasis added): An entity shall consider its substantive rights and obligations, whether they arise from a contract, law or regulation, when applying AASB 17. A contract is an agreement between two or more parties that creates enforceable rights and obligations. Enforceability of the rights and obligations in a contract is a matter of law. Contracts can be written, oral or implied by an entity's customary business practices. **Contractual terms include all terms in a contract, explicit or implied, but an entity shall disregard terms that have no commercial substance** (ie no discernible effect on the economics of the contract). Implied terms in a contract include those imposed by law or regulation. The practices and processes for establishing contracts with customers vary across legal jurisdictions, industries and entities. In addition, they may vary within an entity (for example, they may depend on the class of customer or the nature of the promised goods or services).

The same logic can be extended to other imposts similar to GST.

- AASB 15.47 states that:

  47 The transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties (for example, some sales taxes).

- Interpretation 1031.8-10 further state that:

  8 Receivables and payables shall be stated with the amount of GST included.

  9 The net amount of GST recoverable from, or payable to, the taxation authority shall be included as part of receivables or payables in the statement of financial position.

  10 Cash flows shall be included in the statement of cash flows on a gross basis …

  The same logic can be extended to other imposts similar to GST.

- The inclusion of GST in balance sheet receivables and payables reflects the total amount of the transaction that will be paid or received by the entity [Interpretation 1031.24].

- A net amount subsequently settled with the ATO/IRD can only be offset against the underlying obligation when the criteria established by AASB 132.42 are satisfied; that is, the entity currently has a legally enforceable right to set off the recognised amounts, and it is intended to settle on a net basis.

- AASB 17.B65 says:

  B65 … The cash flows within the boundary [of an insurance contract] include: …

  (i) transaction-based taxes (such as premium taxes, value added taxes and goods and services taxes) and levies (such as fire service levies and guarantee fund assessments) that arise directly from existing insurance contracts, or that can be attributed to them on a reasonable and consistent basis. …

  (m) any other costs specifically chargeable to the policyholder under the terms of the contract.

9. The following can be gleaned from the above extracts from accounting pronouncements:

- Premium revenue or reinsurance premium expense should not include amounts collected that equate to a corresponding present obligation to remit such amounts to a levying or taxation authority. In substance, such amounts reflect collections on behalf of a 3rd party levying or taxation authority.

- Balance sheet receivables from policyholders (within insurance contract liabilities) or payable to reinsurers (within reinsurance contract assets) should include the total amount receivable or payable as a result of an insurance contract issued or reinsurance contract held.

- Cash flows within the boundary of an insurance contract issued or reinsurance contract held should be included in the statement of cash flows on a gross basis.

Amounts in substance collected on behalf of a 3rd party

A.1 The following government imposts are regarded as collections on behalf of a 3rd party.

- Goods and services tax (GST) and equivalent taxes on overseas jurisdictions
- Stamp duty on insurance contracts

- CTP fund levies
- New Zealand Fire and Emergency Levy
- New Zealand Earthquake Commission (EQC) Levy.

The above list is not intended to be comprehensive.

A.2 Insurers are legally liable for these taxes and levies on insurance contracts that they issue. However, the issuance of the insurance contract creates:

- an obligation on the policyholder for receipt of the total invoice amount due (including these taxes and levies); and
- an equivalent obligation on the insurer to remit taxes and levies to the relevant government authority.

Insurers are generally required to remit amounts due on a periodic basis, often monthly during the subsequent month in Australia and quarterly in New Zealand.

A.3 Consistent with the principles established above:

(a) premiums, expenses, including claims,[6] are recognised in profit or loss exclusive of the above government imposts;

(b) receivables and payables associated with expenses are stated inclusive of the above government imposts; and

(c) cash flows are included in the statement of cash flows inclusive of the above government imposts.

Goods and services tax (GST)

A.4 General insurance contracts are typically subject to GST[7] [8].

A.5 Given that GST is levied at a fixed rate of 10% in Australia and 15% in New Zealand of the consideration provided[9], the amount of GST varies directly with the general insurance premium charged and the amounts collected must be passed onto the ATO/IRD (adjusted for any other relevant GST amounts paid). In that respect, insurance contracts are no different from other contracts for goods and services that are subject to GST.

A.6 The same applies for reinsurance contracts issued domestically.

A.7 Insurers are generally required to remit GST collected/due from policyholders net of GST paid (on expenses) to the ATO on a monthly basis and to the IRD on a quarterly basis.

A.8 AASB Interpretation 1031 addresses Australian GST, but by analogy applies to all similar taxes levied in other jurisdictions, such as New Zealand GST.

Stamp duty

A.9 The following stamp duties are levied on insurance contracts in Australia[10].

---

6 Claims are likely to be a mix of amounts subject to GST and amounts not subject to GST.

7 General insurance contracts issued to an offshore party may be treated as GST free.

8 Life insurance and private health insurance contracts in Australia are GST free.

9 GST is applied to the premium **before** duty is considered. Duty applies to the GST inclusive value.

10 Duty is not applied to reinsurance contracts held. Please note, duty rates may have changed since this table was prepared.

QLD	% of premium on most general insurance contracts 10 cents on each CTP contract $1 plus % of sum insured above $2,000 for life insurance contracts % of net WorkCover premium
NSW	% on general insurance contract premium including any levies and GST % of life insurance contract premium Exemptions available for some risks and policyholders
SA	% of general insurance contract premium % of life insurance contract premium $60 on each CTP contract
TAS	% of general insurance contract premium $1 plus % of sum insured above $2,000 for life insurance contracts
VIC, WA, NT	% of general insurance contract premium including any commissions and GST

A.10 In general, the manner in which stamp duty is levied is highly similar to GST and AASB Interpretation 1031 would apply by analogy.

A.11 However, there may be circumstances in which some stamp duty could be regarded as an expense of the insurer. Typically, a relevant portion of stamp duty (like GST) can be clawed back in the event a policy is cancelled before the coverage period expires. However, in some jurisdictions, there is a time limit (for example, four years) after which stamp duty cannot be clawed back. Accordingly, when some policies are cancelled late in a multi-year coverage period, the insurer may be left to bear the stamp duty cost, which make it a cost of the insurer issuing insurance contracts (see Section B of this paper).

NSW CTP Fund Levies

A.12 The NSW CTP Fund Levy is currently a fixed dollar amount, based on vehicle type and location. It appears as a separate charge on insurer issued greenslips. The Fund Levy is made up of two separate components:

- The largest component of the Fund Levy funds the Lifetime Care and Support Scheme:
    - LCSA General Fund
    - Motor Accident Injuries Treatment and Care Benefits (MAITC) Fund.
- The second component of the Levy is set by the State Insurance Regulatory Authority (SIRA), and is calculated as a percentage of premiums. SIRA uses the SIRA component of the Fund Levy to pay:
    - operating costs of SIRA
    - fees to Transport for NSW (TfNSW) to administer the registration process
    - costs of public hospital, ambulance and other services for people injured in an accident.

A.13 The NSW Fund Levy is collected by insurers and remitted on a regular basis to government.

A.14 CTP levies in QLD or SA are paid by vehicle registrants directly to the authority as part of the overall registration costs. Accordingly, these levies are not included in an insurer's revenues, receivables/payable or cash flows.

Fire and Emergency New Zealand (FENZ) Levy

A.15 All policyholders who insure property in New Zealand against the risk of fire are liable to pay the FENZ levy. The levies are typically calculated as $ amounts per $100 insured (although a fixed $ amount applies to motor vehicles below a certain weight) rather than a percentage of premium.

A.16 However, responsibility for calculating and making payment to FENZ depends on how the insurance cover is arranged:

When:	the levy is payable by:
there is a New Zealand-based insurer underwriting the policy	the insurer (based upon the proportion of insurance).
there is not a New Zealand-based insurer underwriting the policy, but there is a New Zealand-based broker	the broker
in all other circumstances	the insured

A.17 New Zealand based insurers are required to collect the levy and pass it on to Fire and Emergency New Zealand. The levies are accounted for under AASB 17 as an amount collected on behalf of 3rd parties; that is, the levies would be among an insurer's IFRS 17 cash flows, but not its revenues and expenses.

New Zealand Earthquake Commission (EQC) Levy

A.18 Particular types of insurance contracts relating to residential property are subject to a levy (currently 20 cents for every $100 (+GST) of coverage, which is capped at $300 (+GST).

A.19 The insurer passes on the levy collected to the EQC. The EQC provides cover for damage to a residential building up to the cap of $150,000 (+GST) for each specified natural disaster event. The same levy applies regardless of the location or type of property, so there is deliberate cross-subsidisation and no detailed underwriting. The government sets the levy via legislation.

A.20 EQC receives levies up to two months after the cash is collected by the private sector insurers. Since April 2021, the private sector insurers handle all claims. Previously, claims were made directly to EQC. Some private sector insurers currently receive a 2½% commission for collecting premiums. The plan is to phase this out.

A.21 As EQC accepts the first-loss up to NZD150,000, alternative treatments include:

(a) the private sector insurer is issuing one contract as an insurer covering losses above NZD150,000 and an EQC contract on behalf of the EQC covering the first NZD150,000 of losses; or

(b) the private sector insurers act as levy collectors for EQC on the first loss component; or

(c) the private sector insurer selling policies that cover the full risk, and reinsuring the first loss component to the EQC.

A.22 Both (a) and (b) would result in the levies being treated as amounts collected on behalf of 3rd parties.

A.23 Because they manage claims, administratively, insurers might be recording all claims from policyholders and recoveries from EQC. However, this paper considers that (c) is an unlikely outcome because the first NZD150,000 is never the private sector insurer's risk to cede. EQC provides additional coverage for policyholders, not reinsurance for the originating insurer.

Tasmania Asbestos Diseases Levy

A.24 An Asbestos Diseases Levy, which is currently 2.5% of premiums paid is collected from policyholders. [Accordingly, a $100 premium would be $100 + $2.50.] Insurers remit the levies collected to the Asbestos Diseases Commission each month in arrears.

A.25 Insurers are effectively collecting the levy on behalf of the Asbestos Diseases Commission.

Tasmania Fire Services Levy (Tasmania FSL)

A.26 Levies are charged at varying percentages on commercial and motor vehicle insurance contracts.

A.27 Contributions are paid monthly with an approved lodgement return to the Tasmanian government based on the amounts collected.

A.28 The amounts collected are based on entity-wide metrics relating to the issuance of insurance contracts and, therefore, the impost attaches at the entity level. The levy percentage can change based on the Commission's projected costs and based on any over- or under-collections from the previous levy period.

A.29 The levy could be regarded as a cost of the entity operating in the Tasmanian commercial and motor vehicle insurance markets.

A.30 However, the *Fire Service Act 1979* [Tasmania] refers to insurers contributing "the prescribed amount towards the aggregate of the operating costs of brigades" [Section 77C and 77L]. In practice, insurers collect and pay levies at stipulated rates and there are no instalments and/or annual adjustments. The rates have not been varied for approximately 25 years

A.31 On balance, the Tasmania ESL is considered to be an amount collected on behalf of a 3rd party.

Costs of the insurer issuing insurance contracts

B.1 The following government imposts would be regarded as costs of the insurer issuing insurance contracts:

- New South Wales Emergency Services Levy (NSW ESL)
- NSW CTP Transitionary Excess Profit and Loss (TEPL) Adjustment
- APRA Supervisory Levies
- ASIC Funding Levies
- some withholding taxes

The above list is not intended to be comprehensive.

B.2 Insurers are legally liable for these taxes and levies on insurance contracts that they issue, and/or as a consequence of being licenced to issue insurance contracts. However, the issuance of an insurance contract does not create an obligation on the policyholder to pay such amounts to the insurer.

B.3 Consistent with the principles established above:

(a) amounts of these government imposts paid or payable are recognised in profit or loss as 'Insurance Service Expense'

(b) any amounts of these government imposts recovered from policyholders are recognised in profit or loss as 'Insurance Revenue'

(c) amounts payable are stated inclusive of these government imposts

(d) cash flows are presented in the statement of cash flows inclusive of these government imposts.

New South Wales Emergency Services Levy (NSW ESL)[11]

B.4 The NSW ESL is designed to help fund emergency services in NSW. The government sets the annual budget (Contribution Target) for emergency services and, in general, the insurance sector provides a large portion of the funding via levies.

B.5 These levies are charged as a single sum against each insurer and are not calculated based on a % rate applied to individual contracts. Furthermore, the ESL liability an insurer must pay is measured over each year ending 30 June. The annual cost of the ESL for an insurer is only known once the insurer submits an annual return to Revenue NSW and the insurer's weighted premium base is divided by the industry's weighted premium base to determine each insurer's share of the Contribution Target.

B.6 For cash flows purposes, the ESL is collected via quarterly instalments which are based on an insurer's contribution amount from the two prior years. Once the final liability for the 30 June year is determined (usually during the following November), the difference between the amount paid by way of instalments and the final liability is passed to/from each insurer and Revenue NSW as applicable.

B.7 In order to ensure that they collect sufficient amounts from customers to fund their expected ESL liability for a given year, insurance companies will generally estimate their contributions based on their premiums for insurance contracts on relevant property[12] business they are expected to write.[13] In practice, specific ESL rates are determined for in-scope products and applied in determining the total amount due from a customer.

B.8 An insurer might choose to:

(a) explicitly show on its insurance contracts an amount relating to the ESL; or

(b) not show the expected impact of the ESL on its insurance contracts.

In either case, the insurer is responsible for paying the lump sum levy to Revenue NSW.

B.9 The ESL is subject to GST, which means the tax law regards the ESL as revenue of the insurer.

B.10 Given that its ESL liability can only be determined after the end of an ESL year, an insurance company's estimate of its contributions will typically be different from the actual amount that must be paid – and might be more or less that the total of any amounts shown on insurance contracts. In other words, the sum of the amounts collected from customers could be more or less than the final liability for the year in question.

NSW CTP Transitionary Excess Profit and Loss (TEPL) Adjustments

B.11 TEPL adjustments are additional levies that may be imposed on insurers to limit profitability and losses of NSW CTP licenced insurers to designated levels with respect to accidents that occur

---

11 Other jurisdictions collect emergency services levies via local government rates.

12 'Property' has a broad definition under the legislation and includes:
- any insurance of property, including consequential loss
- house owners and householders, however designated (buildings or contents, or both)
- personal jewellery and clothing, personal effects and works of art
- motor vehicle and motorcycle
- marine and baggage.

13 Different legislated percentages apply to different categories of property insurance.

from 1 December 2017. TEPL adjustments are not obligations under individual insurance contracts, but obligations to a government authority that arise as a result of insurance contracts collectively.

B.12 TEPL adjustments are determined with reference to profitability in each Accident Year, as measured using the regulator's (SIRA's) methodology and after allowances provided as a reward for introducing innovations to the market (Innovation Support or "IS").

B.13 TEPL adjustments are used to fund lower CTP levies charged to policyholders in future years. There are no adjustments to amounts paid by policyholders to insurers in respect of the Accident Years subject to TEPL adjustments.

APRA supervisory levies

B.14 Insurers must pay various supervisory levies in respect of APRA supervision. The levies are calculated subject to maximum and minimum amounts and a percentage based on the value of an insurer's assets, which is set out in an annual APRA determination.

B.15 These supervisory levies are a cost of operating an insurance business.

ASIC funding levies

B.16 In 2017, the Australian Government introduced legislation that changed the way the Australian Securities and Investments Commission (ASIC) is funded. ASIC's regulatory costs are allocated across 48 industry subsectors based on the actual costs of ASIC's regulation of each subsector in the previous financial year.

B.17 An insurer's levy for a financial year is equal to its share of flat graduated levies for each subsector of which it is a part in the financial year. A graduated levy applies to insurance product providers and has two components: a minimum amount paid by all entities in a subsector, and a graduated amount based on each entity's level of business activity.

B.18 These levies are a cost of operating an insurance business.

NT Workers' Compensation levies

B.19 Insurers pay an annual licence fee to NT WorkSafe – usually in January/February – based on their market share. Market share is calculated from financial returns for the last year to 30 June that are typically submitted by the end of August. The fee covers the cost of administering WorkSafe.

B.20 The same market share information is used to make a cash call for funding the Nominal Insurer (to meet claims from employees of uninsured employers). Calls are made in some years and not others.

B.21 Insurers also fund the administration cost associated with Mediations and Court matters. This is also an annual fee and is based on 'user pays' rather than market share. This fee is paid in conjunction with the annual licence fee in January/February.

B.22 These levies and fees are all regarded as costs of operating an insurance business.

Tasmania Workers' Compensation levies

B.23 Insurers pay an annual licence fee to WorkSafe Tasmania – usually in September/October – based on their market share. Market share is calculated from financial returns for the last year to 30 June that are typically submitted by the end of August. The fee covers the cost of administering WorkSafe.

B.24 The Nominal Insurer in Tasmania operates in a manner similar to the scheme in the NT.

B.25 These levies and fees are all regarded as costs of operating an insurance business. Please see section A above regarding the Asbestos levy.

ACT Workers' Compensation levies

B.26 In the ACT, a number of levies are paid by insurers based on their market share for the relevant types of insurance business. Market share is calculated from financial returns for the most recent year to 30 June.

B.27 Those levies include the following:

- an annual licence fee to ACT Workcover to fund the cost of administering Workcover;
- a quarterly payment to fund the Default Insurer (to meet claims from employees of uninsured employers).
- An annual levy to fund the ACT Lifetime Care and Support Scheme, which provides benefits for those catastrophically injured in the workplace or a motor vehicle accident.
- An annual Magistrate's Levy to cover the administration support in managing matters that reach dispute or common law pre-trials and trials.

B.28 Insurers may gross up premium to fund one or more of the levies when determining pricing, but the amounts collected are not directly passed through to the relevant government authorities.

B.29 The levies are regarded as a cost of the entity operating in the ACT workers' compensation insurance market.

WA Workers' Compensation levy

B.30 Insurers and self-insurers pay an annual levy of 1.29% of gross written premium (GWP) to fund the operating costs of the regulatory authority, which includes regulation and administration of the scheme, the Conciliation and Arbitration Service for disputed claims, as well as contributing towards claims from employees of uninsured employers.

B.31 The levies paid to WorkCover WA are based on an entity-wide metric (GWP). The levy percentage can change based on the WorkCover WA's projected costs and based on any over- or under-collections from the previous levy period.

B.32 The levy is regarded as a cost of the entity operating in the WA workers' compensation insurance market.

Withholding tax on income replacement payments

B.33 An insurer making claim payments (such as for workers compensation, CTP etc.) that replace a policyholder's income may be required to withhold income tax (PAYG) and amounts for study support (such as HELP debt repayments) and remit the tax to the ATO.

B.34 There is no particular connection with amounts collected as part of premiums, and the amount of tax withheld is a function of the tax status of the particular policyholder. For example, the amount of the benefits paid to the individual versus the ATO would vary based on the individual's tax bracket.

B.35 The tax withheld and paid to the ATO would be among the fulfilment cash flows for the relevant insurance contracts, i.e., the claim expense / liability for incurred claims comprises the net amount payable to the claimant plus the withholding tax payable to the ATO. There is no additional cost to the insurer, merely a direction to allocate claim benefits in a particular manner. This is consistent with AASB 17.B65(m) as a cost specifically chargeable to the policyholder under the terms of the contract. The tax cash flows would be included in the insurer's claims cost in the cash flow statement.

Reinsurance held arrangements

C.1 The following government imposts would be regarded as reinsurance held arrangements:

- Australian Reinsurance Pool Corporation (ARPC) – terrorism
- Australian Reinsurance Pool Corporation (ARPC) – proposed cyclone coverage

The above list is not intended to be comprehensive.

Australian Reinsurance Pool Corporation (ARPC) – terrorism

C.2 The Scheme provides eligible insurance contracts with terrorism cover for any Declared Terrorist Incident (DTI). Eligible insurance contracts are defined in the *Terrorism and Cyclone Insurance Act 2003*. The Minister, in consultation with the Attorney-General, determines whether a DTI has occurred in Australia.

C.3 Eligible contracts include those for commercial property and large residential property insurance contracts. The declaration of the DTI renders terrorism insurance exclusion clauses within eligible contracts of insurance invalid.

C.4 Through ARPC terrorism insurance coverage, insurers have three options – they can:

(1) carry the underwritten risk of terrorism losses following a DTI; or

(2) reinsure the risk through the commercial insurance market, paying terrorism reinsurance premiums; or

(3) reinsure the risk with ARPC by entering into a reinsurance contract and paying terrorism reinsurance premiums.

C.5 Commercial businesses that are insured with ARPC's insurer customers and which hold eligible insurance policies are covered by the Scheme in the event of a DTI.

C.6 Insurers are required to meet claims in accordance with the other terms and conditions of individual policies. Insurer and industry retentions (deductibles or excesses) apply before claiming against the Scheme. Claims against the Scheme will be met once an individual insurer's retention is exhausted. That is, the Scheme requires insurers to retain the first portion of any loss.

Australian Reinsurance Pool Corporation (ARPC) – cyclone coverage

C.7 The current *Terrorism and Cyclone Insurance Act 2003* [which supersedes the *Terrorism Insurance Act 2003*] introduces a regime for coverage of declared cyclone events.

C.8 There are two key differences from the ARPC scheme for terror events.

(a) Insurers (with some exceptions) will be compelled to acquire reinsurance for cyclone-related risks from the ARPC on specified classes of business. 'Large' insurers are required to join the scheme by 31 December 2023 and 'small' insurers by 31 December 2024.

(b) Premiums are set by the ARPC (not the Minister). Given its intent, premiums to be set by the ARPC are likely to be at or below commercial terms (with the benefit of the proposed government guarantee).

C.9 The policies affected include: household property policies, strata policies, small business property policies, C.10 The compulsory nature of the proposed scheme does not change the fact that it would be accounted for as reinsurance held under AASB 17 because insurance risk is ceded to the ARPC.

Imposts for which the outcome is less clear

Withholding tax on foreign resident reinsurers

D.1 An insurer acquiring a reinsurance contract from a foreign resident reinsurer may need to address withholding tax.

D.2 The typical method for determining withholding tax is 10% of premiums paid to a foreign resident reinsurer[14], multiplied by the company tax rate of (say) 30% = 3% of premiums.

D.3 The insurer needs to forward the withholding tax to the ATO using a tax return specific to that purpose and using a TFN obtained for that purpose.

D.4 One view is that the insurer is simply acting as a collector of income tax (or a substitute for income tax) for the government because the amount collected relates to particular transactions and is the amount 'paid' to government (albeit together with other taxes).

D.5 The alternative view is that, in effect, of the total reinsurance premium payable by the ceding insurer, 97% is paid to the reinsurer and 3% to the ATO. There is no additional cost to the ceding insurer, merely a direction to allocate reinsurance premiums in a particular manner. Hence, withholding taxes are fulfilment cash flows of the ceding insurer (i.e., 3% of the total reinsurance premium) as is the payment of the remaining 97% to the reinsurer. This view might also be considered consistent with the fact that withholding taxes are 'paid' at year end with other entity taxes (which are expenses/revenues of the insurer).

D.6 In terms of the indicators identified in the introductory section of this paper, withholding tax can be analysed as follows:

Indicators the insurer is a mere conduit for the flow of levies to Government (Section A)		
Computed at a transactional level	Yes – except there may be multiple contracts with a foreign reinsurer	
Based on a fixed %	Yes – although as a shortcut to identifying tax on profit	
Remitted on a periodic basis to Government		No – remitted with other taxes annually
Indicators levies are costs of issuing insurance contracts/carrying on insurance business (Section B)		
Computed at an entity level		No – based on transactions with foreign reinsurers
Remitted through estimates or instalments		No – based on premium, although as a shortcut for tax on reinsurer's profit
Paid in relation to longer time periods	Yes – remitted with other taxes annually	

14 Technically, it is an income tax (rather than a withholding tax) on the 10% profit assumed by the ATO to be made by the reinsurer. This paper does not address the accounting by the reinsurer, which would need to determine whether to account on a gross basis (and recognise revenue for 100% of the premium it notionally receives and tax withheld under IAS 12 *Income Taxes*) or on a net basis (and recognise revenue for the 97% of the premium it actually receives and ignore the tax impacts).

D.7 Treating the withholding taxes as fulfilment cash flows of the ceding insurer might also be supported on the basis that it is a cost specifically chargeable to the policyholder under the terms of the contract/legislation in the context of AASB 17.B65(m).

~~~~~
~~~~~