

## FinTax Hour Insurance

# Recent tax updates for the Insurance sector

# Critical amendments / clarifications

## Deemed supply of service – clarification

- Deemed supply - Agreeing to the obligation to refrain from an act or to tolerate an act or a situation, or to do an act
- Taxability of liquidated damages clarified
- Notice pay recovery or payment of bond by employee – not taxable
- Cancellation of services – taxable, unless such charges are compensatory / liquidated damages

## Section 194R of Income Tax

- Amendment in Income Tax, where insurer will deduct TDS on perquisites
- Could have a bearing on GST where such perquisite / benefit is provided to insurance intermediaries, where insurer is liable to pay GST under reverse charge

## Declaration on invoice / document

- Insurance companies are exempted from generation and issue of e-invoice
- Following declaration to be added on the invoice / any other document issued in lieu of invoice:  
“I/We hereby declare that though our aggregate turnover in any preceding financial year from 2017-18 onwards is more than the aggregate turnover notified under sub-rule (4) of rule 48, we are not required to prepare an invoice in terms of the provisions of the said sub-rule.”

# Critical amendments / clarifications

## Exemption withdrawn on health-care services

- Services provided by clinical establishment by providing room on rent (excluding ICU/ICCU/NCU), the value of which is exceeding INR 5,000/- per day to a person receiving health care services is liable to GST at the rate of 5%
- Could have an impact on the cost, considering eligibility to claim ITC

## Exemption withdrawn on services by IRDAI

- Exemption on services provided by the Insurance Regulatory and Development Authority of India to insurers, has been withdrawn

# Judicial precedents

## Service tax collected from Insurance agents

### Facts of the case

- The commission payable to insurance agents was inclusive of tax
- The commission was paid after deducting Service Tax and TDS
- The deduction of Service Tax was due to applicability of reverse charge
- This deduction was viewed as an illegal recovery of Service Tax, and thus, the revenue sought that the amount recovered should be paid

### Decision

- Illegal recovery of Service Tax implies that the tax collected has not been paid
- There's nothing in law, which prohibits a person to collect tax already paid
- If the contractual arrangement entitles the recipient to collect the Service Tax already paid, there's no contravention of the law
- The Department has not alleged that the Service Tax has not been paid under RCM
- Demand cannot sustain

## Valuation

### Facts of the case

- The taxpayer incurred certain expenses such as training, sales and business promotion expenses
- Such expenses were not included in the value of taxable supply, on which RCM was paid

### Decision

- Consideration includes any amount payable for taxable service
- It can be argued that training expenses should have been incurred by the service provider
- The requirement for inclusion is that any amount that the expense should be borne by the service provider
- Since these expenses were not incurred by the Service provider, the same would not be includible in value of services, for payment of tax under reverse charge

# Judicial precedents

## CENVAT Credit on pooling arrangement

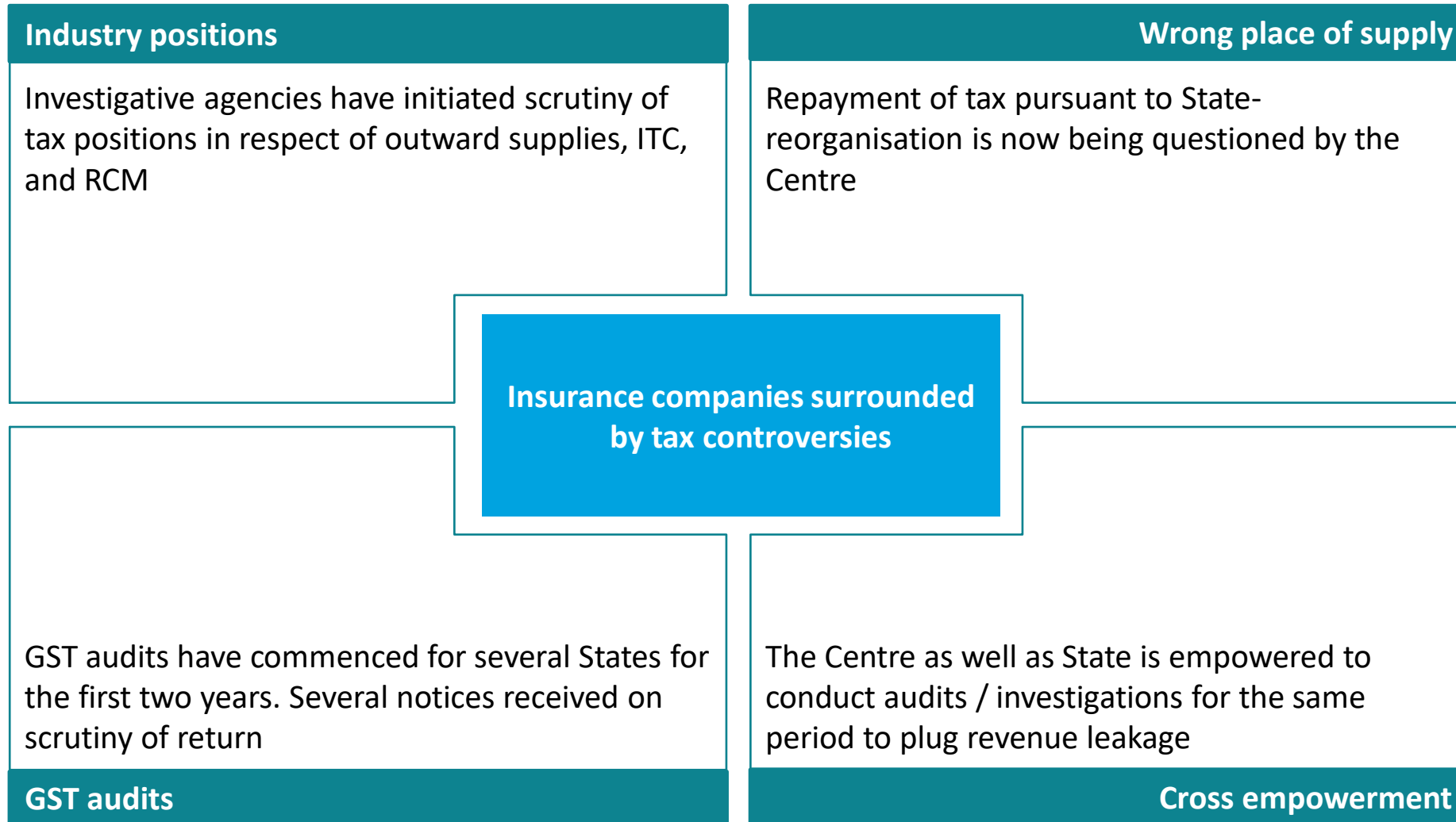
### Facts of the case

- The taxpayer had availed CENVAT Credit in respect of invoices issued by another insurance company, with whom they had a pooling arrangement
- It was alleged that CENVAT Credit will not be allowed since the expense did not qualify as an eligible 'input service'
- Since pooling mechanism was not a regulatory mandate, the High Court precedent on ITC eligibility for re-insurance service, would not apply

### Decision

- Creation of Insurance pool was pursuant to the directions issued by IRDA
- All general insurance companies were directed to collectively participate in a pooling arrangement to share insurance business underwritten
- In adherence to the directions, the insurance companies entered into an agreement to create the insurance pool
- These directives mandated insurance companies to create a pool, and was not a voluntary act
- Pooling system is nothing but a form of re-insurance
- CENVAT Credit was thus, permitted

# Tax controversies



## Polling question 1



**Do you anticipate that the number of audits and investigations under GST and the complexity thereof will increase/decrease?**

- Significantly increase
- Increase
- Will remain the same
- Decline







## Non-Life Insurance

### Interest on compensation awarded by MACT not taxable

#### Facts

- Pursuant to directions, the Insurance Company (IC) deposited amount awarded along with interest (including separate cheque for TDS) with Motor Accident Claims Tribunals (MACT).
- Miscellaneous application disposed directing the IC to deposit TDS with the Income-tax Department (ITD).
- Post depositing TDS with ITD, the IC filed correction statement in the year of award with interest which resulted in demand under section 201(1A).
- IC's application for waiver of interest under section 201(1A) rejected.

#### Decision

- Compensation under the Motor Vehicle Act is on account of loss of earning capacity and is not by way of earning or profit
- Interest awarded in motor accident claim from the claim date to award date is not exigible to tax.
- TDS provisions would not govern taxability.
- Interest paid for delay in depositing the awarded amount, would not form part of the compensation and, would be interest income exigible to tax under the normal provisions.

### No TDS on ceding commission paid by foreign reinsurer

#### Facts

- India branch of foreign reinsurer paid ceding commission to Indian insurance companies
- The AO held that the portion of reinsurance premium payable to reinsurance company retained by the Indian insurance companies is commission paid to them on which tax is deductible under section 194D.

#### Decision

- 'Cedant commission' is share of the reinsurance company in the nature of manpower cost, third party administration cost, etc. which is actually reimbursement of expenses
- Ceding commission is not paid for soliciting or procuring insurance business.
- TDS not required under section 194D.

# Judicial precedents

## Insurance broker (TDS liability and PE status)

### Facts

- Insurance premium received by IRDA-licensed Indian composite broker from Indian Cedant paid to a Singapore-based broker, which was in turn remitted to various non-resident reinsurers
- The AO held the Indian broker to be an assessee-in-default for non-deduction of tax at source on amount paid to Singapore-based broker and also to be its Dependent agent PE

### Decision

- The Indian broker only reflected brokerage as its income; sum received from Indian Cedant was held in 'Client Money Account' and reflected in the balance sheet as 'Reinsurance Premium payable to Reinsurers'
- Article 5(8) not fulfilled as the Indian broker had no authority to conclude contracts on behalf of the Singapore-based broker nor did it secure order only on behalf the Singapore-based broker
- The Indian Broker and the Singapore-based broker acted independently, on principal-to-principal basis – so Article 5(9) not attracted

## Life insurance (Computation of Taxable income)

### Facts

- The life insurance company filed tax return declaring loss which was computed by aggregating its reporting under shareholders account and policy holders account as prescribed under IRDAI
- The Assessing Officer treated the surplus under shareholders account as income from business and taxed at normal rates

### Decision

- The Taxpayer was engaged in only life insurance business and was not carrying on any other business
- Surplus with deficit as per shareholder's account was to be aggregated with surplus with deficit in policyholder's account for determining profit or loss under section 44
- Identical question considered by the Bombay High Court which is pending before the Supreme Court

Notice issued in SLP filed against Karnataka High court order, to be tagged with Bombay High Court

# Other updates



## Other updates

### **CBDT Circular No. 12 of 2022 dated 16 June 2022 (Section 194R Guidelines)**

- **Q4** - Tax is required to be deducted by the person in the name of recipient entity where the usage by owner/director/employee/relative is by virtue of their relationship with the recipient entity and in substance the benefit/perquisite has been provided by the person to the recipient entity
- **Q7** – Tax to be deducted on reimbursement of out-of-pocket expenses if the invoice is in the name of service provider
- **Q8** – No TDS on dealer conference to educate dealers. However, TDS applicable on conference attended by select dealers

### **Notification S.O. 3035(E) dated 4 July 2022 (Amendment to the Insurance Act, 1938)**

- Certain provisions of Insurance Act not to apply in Special Economic Zone and International Financial Services Centre

### **EXPOSURE DRAFT (2 August 2022) Insurance Regulatory and Development Authority of India (Expenses of Management of Insurers transacting life insurance business) Regulations, 2022**

### **EXPOSURE DRAFT (1 August 2022) - Insurance Regulatory and Development Authority of India (Expenses of Management of Insurers transacting General or Health Insurance business) Regulations, 2022**

Key Changes proposed:

- Compliance with limits of Expenses of Management (EoM) to be on an overall, aggregated basis for Par, Non-Par and Linked business and not on segmental basis (Life Insurance).
- Single Limit of EoM (General and Health Insurance)
- Additional allowance for: (Both)
  - Insurers with duration of business up to 10 years
  - Incremental rural sector and specified schemes
  - Expenses on Insurtech, Ind AS implementation and insurance awareness

**Amendment to section 37 vide Finance Act, 2022**

## Polling question 2



**Do you believe the implementation of the provisions of section 194R is routine incremental TDS compliance?**

- Yes, as we have identified the exact activities/ expenses, etc. which are covered by the new provisions
- No, as the new provisions leave a lot of room for interpretation
- Not sure
- Do not know



# Judicial precedents



## Life Insurance company

### Intragroup services

#### Facts of the case

- The taxpayer is engaged in the business of life insurance and annuity.
- International Transaction under dispute- Receiving of intragroup services in the nature of technical, administrative and training support services.
- Consideration- Actual costs incurred by associated enterprises ('AEs') in rendering the services without any mark up.
- Tax authorities determined arm's length consideration for such services to be NIL due to the following reasons-
  - Detailed documentation for proof of services received by the taxpayer were not submitted.
  - None of the benefits are tangible and real.

#### Decision

- Filing of voluminous correspondence, reports etc., not a proper way of discharging of taxpayer 's burden to establish the ALP.
- Reiterated manner of determination of the arm's length price for intra-group services.
- Matter remanded back to AO/TPO for fresh consideration.

### Applicability of Transfer pricing ('TP') provisions

- Taxpayer contended that TP provisions are not applicable to life insurer (which is governed by specific mode of computation of income under section 44 of the Act).
- Delhi Tribunal upheld the lower authority's decision and observed that TP provisions are applicable to life insurer.
- Delhi High court Admitted appeal of the taxpayer on applicability of TP provisions.
- Matter pending to be heard before the High Court.

# Judicial precedents



## UK Tribunal Ruling- Captive Insurer

### Facts of the case

- The taxpayer is a large retail chain selling consumer goods in UK.
- The taxpayer's group had a captive insurer based out of Isle of Man that offered insurance to the customers of the taxpayer indirectly.
- There is a third party company in the middle, which first offered insurance to the customers of the taxpayer and later on reinsured the risk with captive insurer.
- There was no direct contractual relationship between taxpayer and captive insurer.
- A large proportion of profits accumulated with captive insurer in Isle of Man.

### Decision

- The tribunal rejected taxpayer's contentions that the transfer pricing provisions do not apply in the absence of direct contractual relationship between taxpayer and captive insurer.
- Observed that super profits were available with the captive insurer, however the profits arose in the first place because of strong brand, point of sale advantage possessed by the taxpayer.
- Held profit split method as most appropriate method.
- Routine return on capital calculated using capital asset pricing model should be attributed to the captive insurer.
- All the residual profit should be allocated to the taxpayer as a reward to the intangibles it possessed by way of **commission**.

# Other updates



## Other updates

### Captive Insurance

- OECD TP Report on financial transaction dated February 2020 includes TP considerations for captive insurance.
- While captive insurance models are not prevalent in India, however IRDAI (vide press release dated 7 April 2022) in a welcome move is looking to encourage entry of captive insurers in Indian Insurance sector.

### Benefits of Captive Insurance model

- Captive Insurer is an insurance undertaking all of whose insurance business is to provide insurance for risks of its group entities.
- This model allows companies to consolidate and manage complex business risks within the group.
- This also helps in stabilizing overall premium paid by group entities.

### Practical guidelines for Insurance/ Reinsurance companies-

Recently, Indian Insurance industry is facing increased audit exposure by tax authorities.

Reference can be drawn from Australian Taxation Office's ('ATO') published findings dated June 2020 which outlined **key recommendations for taxpayers in insurance/ reinsurance industry to strengthen transfer pricing documentation-**

- Actuarial reports can be relied on to support transfer pricing outcomes
- Identify appropriate internal comparable agreements
- Compare relevant profit level indicator such as combined ratio against those of independent comparable companies
- Detailed explanation of business reasons where taxpayers have incurred sustained losses specially where the taxpayer has ceded risk to its offshore related parties via retrocession arrangements
- Additional assurance by highlighting that taxpayer's reinsurance arrangement have been reviewed by regulatory bodies (i.e. IRDAI in India)

## Polling question 3



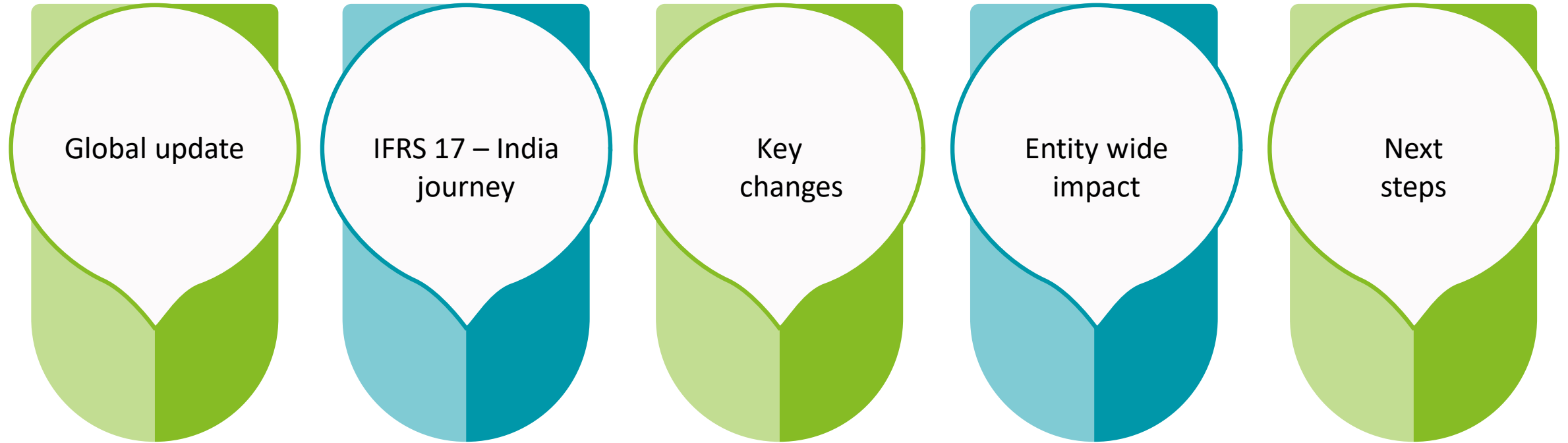
**Should transfer pricing provisions apply to life insurance companies as their taxable income is basis the actuarial valuation, as per the First Schedule to the Act?**

- Yes, as income and expenses between related party transactions should be at arms' length
- No, as there are no adjustments that can be made to the book income
- May be





# Agenda for discussion



## IFRS 17 – Global context

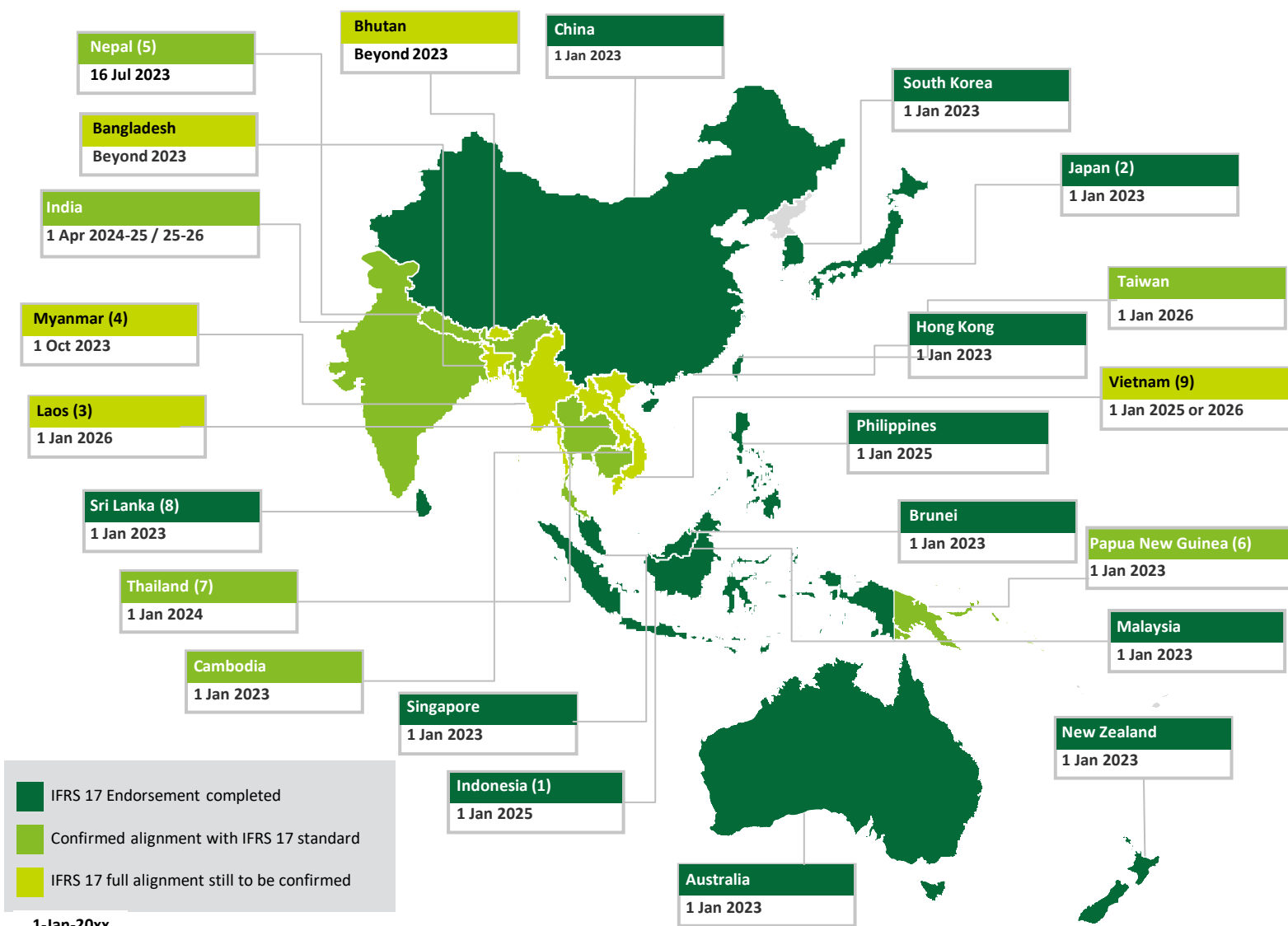
“IFRS 17 on Insurance Contracts is the first common global insurance accounting standard which is to be globally adopted effective 1 January 2023.”

“Insurers are required to prepare and report first IFRS 17 financial statement beginning from 1 January 2023, with comparatives for the financial year 2022.”





# IFRS 17 APAC updates

## Adoption Status and Effective Dates in the Asia-Pacific region



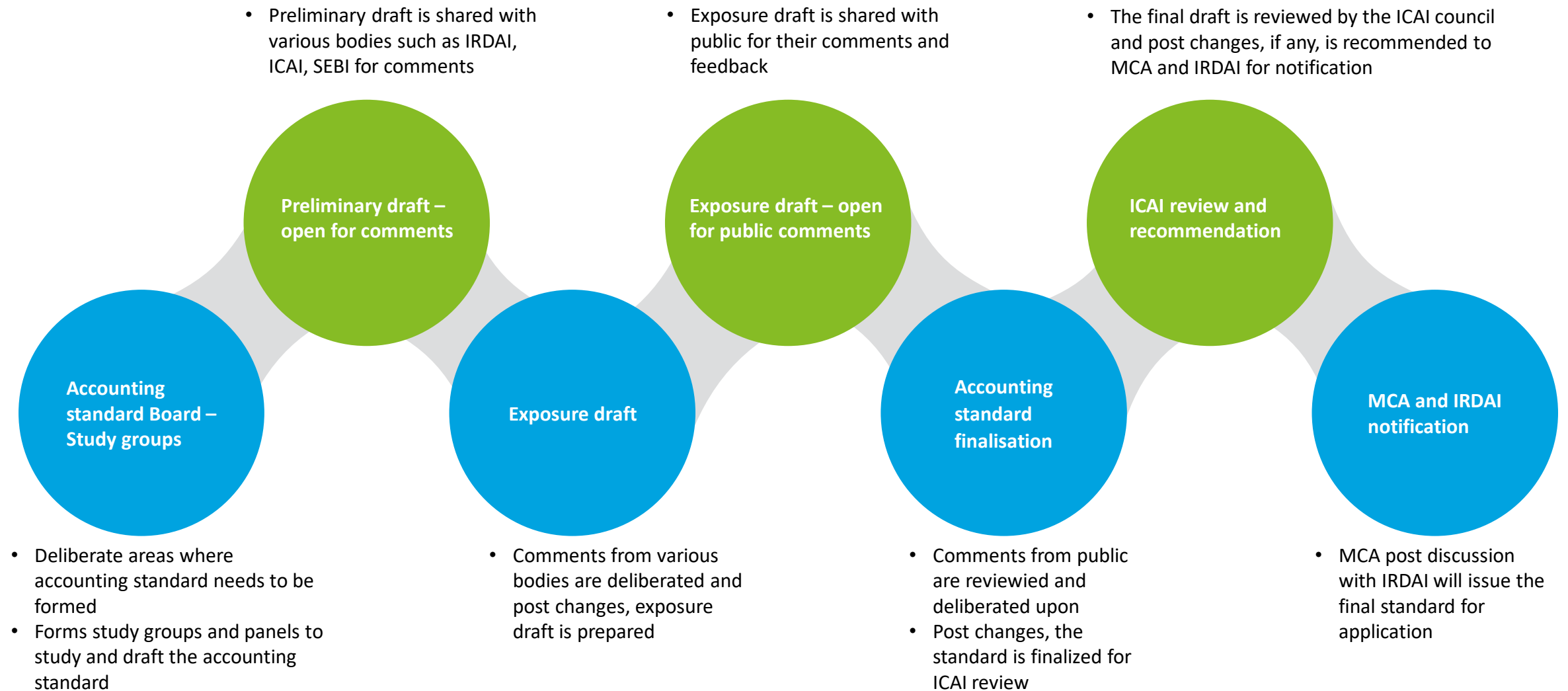
### Other Countries:

 **European Union**  
IFRS 17 Endorsement for the EU is complete and aligned with IASB effective date 1 January 2023. Optional exemption regarding the annual cohort requirements is permitted.

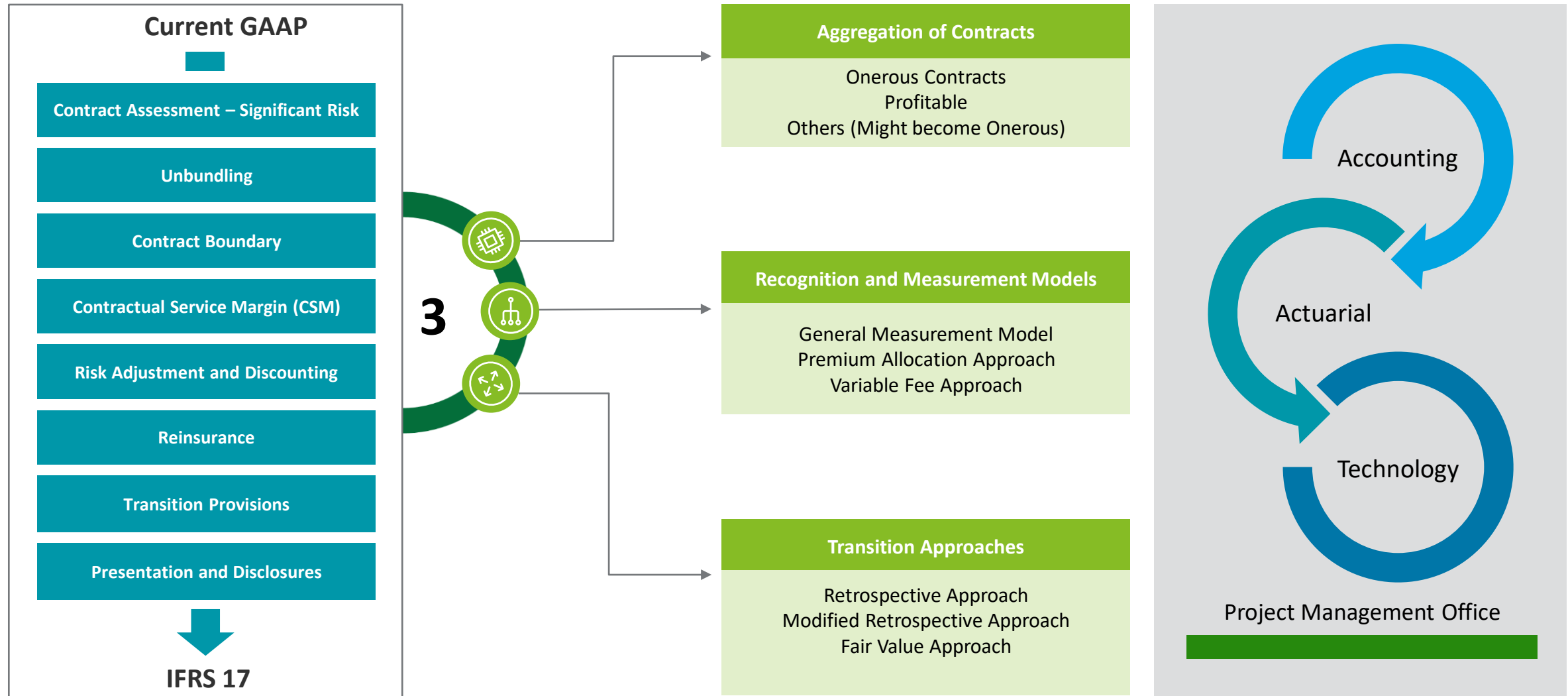
 **United States**  
Partial alignment with IFRS 17 requirements through US GAAP's LDTI. Effective date varies between 2022-2025.

- (1) Indonesia - The application of PSAK 74: Insurance Contracts in Indonesia will take effect on 1 January 2025 with earlier application permitted.
- (2) Japan - Eligible listed companies in Japan are permitted to apply IFRS as designated by the FSA in the consolidated financial statements
- (3) Laos - Ministry of Finance has issued notifications extending the transition period for the implementation of IFRSs for another 5 years from 2021 to 2025. Full IFRS implementation is required from 2026 onwards.
- (4) Myanmar – Due to impact of military coup, alignment with the 2020 IFRS Handbook including IFRS 17 is on hold and currently would not be applicable to Myanmar entities until further notice.
- (5) Nepal – Considering the preparedness of local industry, Insurance Regulator and practitioners, the 256<sup>th</sup> meeting of Council has deferred NFRS 17 effective date to 16 July 2023.
- (6) Papua New Guinea - It is expected the standard will be adopted in full per the requirements of the IASB and on the same effective date, which is 1 January 2023.
- (7) Thailand – The Thai Financial Reporting Standard no.17 (TFRS 17) is expected to be effective one year later than the IFRS 17 effective date, i.e. 1 January 2024.
- (8) Sri Lanka - SLFRS 17 was adopted by CA Sri Lanka in year 2017 and it will be effective from 1 January 2023 but might be extended until 1 January 2025. Early adoption of the standard is also permitted.
- (9) Vietnam - Insurers with holding companies overseas applying IFRS aligned with the IASB can apply IFRS 17 at the same time of the group (i.e. 1 January 2023)

# IFRS 17 - Implementation journey for India

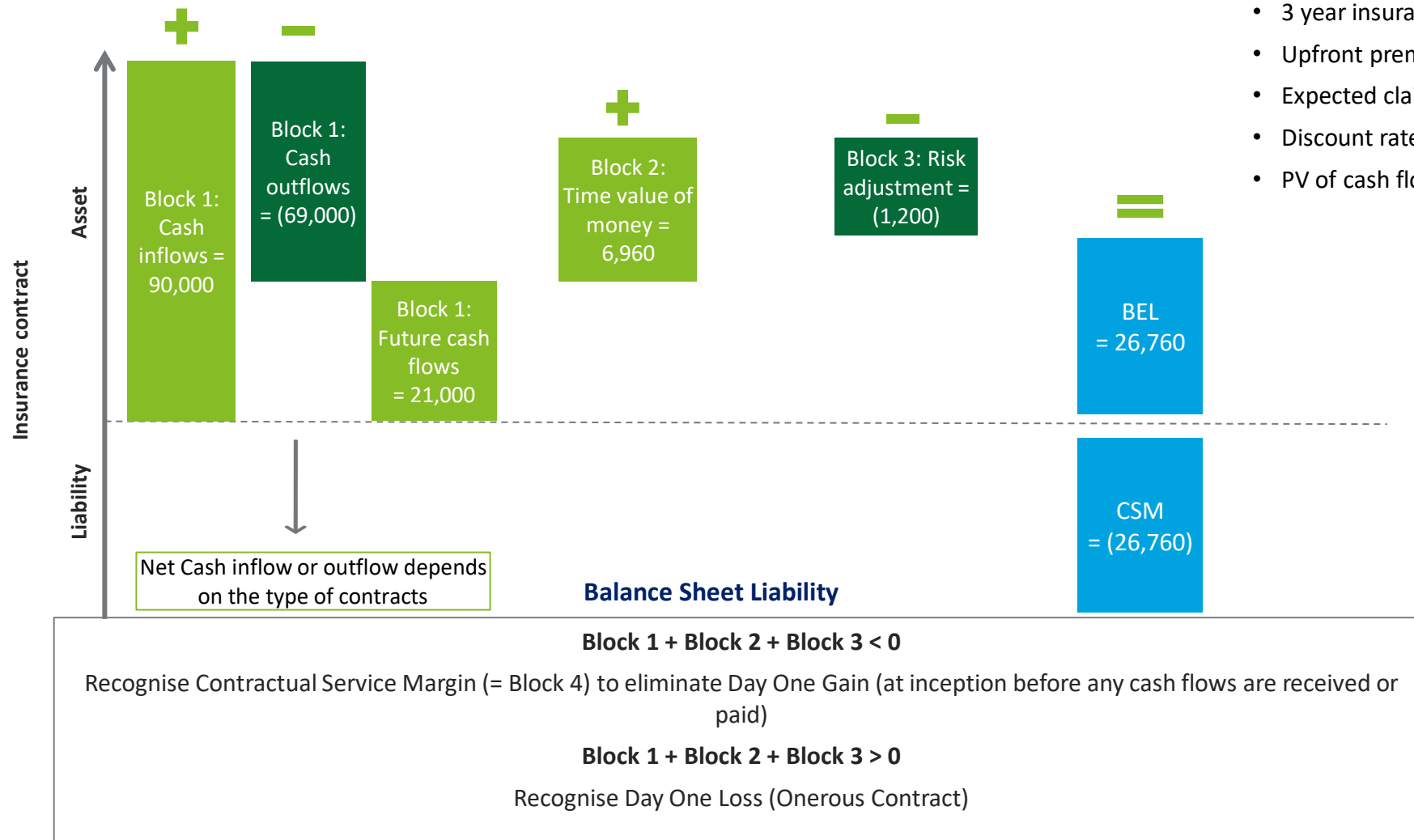


# IFRS 17 - Key changes



# General Measurement Model ('GMM')



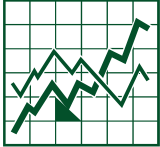








## Overview measurement



- 3 year insurance contract
- Upfront premium of Rs. 90,000
- Expected claims and commission of Rs. 69,000
- Discount rate of 5%
- PV of cash flows = Rs. 27,960

# Collateral impact of IFRS 17 implementation



 <p><b>Financial statements</b></p>	<p><b>Budgets and forecasts, GL systems</b></p> 	 <p><b>MD&amp;A and Non-GAAP measures</b></p>
<p><b>Accounting Resources/ Capabilities</b></p> 	 <p><b>Income and capital tax base</b></p>	<p><b>Compensation plans</b></p> 
 <p><b>Treasury and financial risk management</b></p>	<p><b>Audit Committee Knowledge, governance</b></p> 	
<p><b>Debt covenants and financing</b></p> 	 <p><b>M&amp;A strategy</b></p>	 <p><b>Internal and disclosure controls</b></p>

# What should you do next?

Start early, start small and keep it simple



Understand the impact of IFRS 17 and changes on your business



Understand the impact on your profit profiles, accounts and KPIs



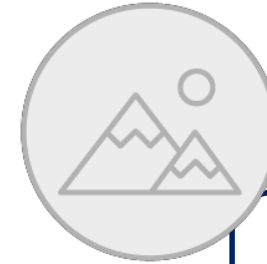
Understand the impact on Data, System, and Process



Make a strategic decision around timing of adoption



Complete a business case and secure budget



Educate senior management



## Polling question 4



**What will be the biggest challenge for companies in implementing IFRS 17?**

- Availability of trained resources
- High cost of vendor solutions and implementation
- Disruption to daily business operations
- All of the above
- None of the above



We look forward to seeing you in the next **FinTax Hour** webinar!

## **Capital markets**

**Date:** 14 September 2022

**Time:** 11:30 a.m. IST

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