



Australian Government

Commonwealth Grants Commission

2010 REVIEW

INSURANCE TAX

**COMMISSION POSITION PAPER
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BACKGROUND

- 1 In 2005, the Heads of Treasury undertook a review of horizontal fiscal equalisation. A conclusion of that review was that Commission processes could be simplified. The 2010 Review terms of reference ask the Commission to simplify its assessments, provided to do so is consistent with the principle of equalisation.
- 2 We consider that simplification and equalisation can both be achieved and that simplification will improve the reliability and robustness of the processes and the acceptability of the outcomes. Both objectives can best be achieved through a rigorous application of the assessment guidelines. These guidelines require the 2010 Review assessment methods to:
 - establish a conceptual case for the assessment;
 - support the conceptual case with evidence, which is both comparable and reliable;
 - develop a reliable assessment method; and
 - demonstrate such an assessment would be material¹.
- 3 Our intention is to develop these methods jointly with States. For that reason, we have chosen an iterative process. This approach provides States with opportunities to contribute to the development of the final assessments.
- 4 The first iteration of the Insurance tax assessment was presented in staff discussion paper 2007/03 *Proposed Methods for Revenue Assessments*. Staff proposed:
 - assessing compulsory motor vehicle third party (CTP) insurance and general and life insurance taxes together; and
 - assessing capacity using insurance premiums. Premiums raised from forms of insurance not normally taxed by States would be excluded.
- 5 Most States supported the proposed assessment.
- 6 This Commission position paper represents the second iteration of the Insurance Tax assessment. It sets out our preliminary decisions on the assessment. These decisions provide the basis on which the Insurance Tax assessment will be taken forward in consultation with States.
- 7 The paper reflects comments provided by the States during State visits and in State submissions received up until 15 August 2008. Comments received after this date will be considered alongside comments received from States in response to this paper.

¹ For a category to be deemed material, the average expense or revenue is greater than \$50 per capita, or the assessment is likely to redistribute more than \$30 per capita for any State.

PROPOSED ASSESSMENT

Overview

- 8 In discussion paper 2007/03-S, staff proposed that the 2010 Review equalisation budget contain an Insurance tax category comprising revenues from general and life insurance and CTP insurance.
- 9 Staff proposed:
- assessing motor CTP insurance and general and life insurance taxes together; and
 - assessing capacity using total insurance premiums less premium revenue from:
 - employer’s liability insurance. The average policy is not to tax employers’ insurance premiums;
 - reinsurance. The average policy is not to tax reinsurance premiums; and
 - fire insurance levies. These levies would be assessed within the Miscellaneous revenue category.

State views

- 10 Most States supported these proposals. However, some States said CTP insurance should be assessed separately because States taxed it at a lower rate than the other forms of insurance.

Commission view

- 11 The Commission’s position is to:
- have an Insurance tax category and include revenue raised from general and life insurance and CTP insurance in that category; and
 - assess capacity using total insurance premiums less premium revenue from the forms of insurance not normally taxed by States (employer’s liability insurance and reinsurance premiums) and fire insurance levies.
- 12 An investigation was undertaken into the issue some States raised about whether a separate assessment should be made for CTP insurance.

INVESTIGATION OF A SEPARATE ASSESSMENT OF CTP INSURANCE

Proposal

- 13 In discussion paper 2007/03-S, staff proposed assessing CTP insurance and general and life insurance together.

State views

- 14 New South Wales, Tasmania and the ACT said that as a lower rate of tax applied to CTP insurance, its capacity should be assessed separately. Tasmania and the ACT asked the

Commission to confirm whether separate assessments of CTP insurance and general and life insurance would produce an outcome that was materially different from a combined assessment.

Analysis

- 15 The Commission has investigated the materiality of separately assessing CTP insurance premiums. Table 1 shows that CTP insurance revenue is a small component (less than 10 per cent) of a combined insurance revenue category.

Table 1 CTP insurance revenue as a proportion of combined insurance revenue

Year	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aust
2002-03	0	16.2	0.1	12.7	17.2	9.7	0	0	8.7
2003-04	0	15.6	0.1	14.6	18.1	8.9	0	0	9.2
2004-05	0	15.9	0.1	13.8	18.6	9.2	0	0	9.4
2005-06	0	16.0	0.1	12.2	18.4	9.7	0	0	8.8
2006-07	0	16.4	0.1	12.2	17.3	8.7	0	0	8.5
5 year average	0	16.0	0.1	13.1	17.9	9.2	0	0	8.9

Source: 2008 Update, Working Papers, Volume 2, Insurance taxation.

- 16 In the 2008 Update, Insurance tax was assessed in two components:
- a CTP insurance component was assessed using CTP insurance premiums; and
 - a general and life insurance component was assessed using premiums from general and life insurance (excluding CTP premiums) less premiums from employers' liability insurance, premiums from reinsurance and revenue from insurance levies.
- 17 Table 2 shows how much these separate assessments redistributed, compared to an equal per capita assessment. The table also shows how much a combined assessment would have redistributed. The difference between the two approaches is less than \$10 per capita for any State and hence does not produce a materially different outcome.

Table 2 Financial impact of assessing all insurance together, 2008 Update

Redistribution	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aust
Combined assessment (\$m)	-175.4	30.7	66.7	30.2	10.9	20.1	9.6	7.2	175.4
Separate assessment (\$m)	-188.2	27.1	76.2	27.4	14.4	22.8	12.1	8.2	188.2
Difference (\$m)	12.8	4.2	-9.5	2.8	-4.1	-2.8	-2.5	-1.0	19.8
Difference (\$pc)	1.9	0.8	-2.3	1.3	-2.6	-5.6	-7.4	-4.6	0.9

Source: 2008 Update, Table E-3, page 113 and Commission simulation.

Commission view

- 18 On materiality grounds, the Commission's decision is to assess CTP insurance and general and life insurance together.

PRELIMINARY ASSESSMENT

- 19 The Commission's preliminary decision is to include revenue raised from CTP insurance and general and life insurance and to assess capacity using total insurance premiums less:

- premiums from employers' liability insurance;
- reinsurance premiums; and
- fire insurance levies.

- 20 Table 3 sets out the assessment for 2006-07.

CONCLUSION

- 21 The Commission's decision is to:

- assess CTP insurance and general and life insurance together;
- assess capacity using total insurance premiums less premium revenue from:
 - employer's liability insurance. The average policy is not to tax employers' insurance premiums;
 - reinsurance. The average policy is not to tax reinsurance premiums; and
 - fire insurance levies. These levies are to be assessed within the Miscellaneous revenue category.

Table 3 Insurance tax, 2006-07

	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	Aust
A. Population (persons)	6 855 811	5 167 516	4 135 619	2 082 041	1 576 644	491 648	336 691	212 802	20 858 772
B. Insurance premiums (\$m)									
C. Employers' liability premiums (\$m)									
D. Reinsurance premiums (\$m)									
E. Fire insurance levies (\$m)									
F. Assessed revenue base (\$m) [F = B – C – D – E]	9 133.1	5 577.0	4 477.7	2 197.2	1 789.3	391.3	298.2	191.0	24 054.8
G. Actual revenue (\$m)	598.4	726.5	418.1	335.4	243.7	38.0	34.5	23.1	2 417.7
H. Average tax rate (%) [$H_{Aust} = G_{Aust} / F_{Aust}$]									10.05
I. Assessed revenue (\$m) [I = F * H_{Aust}]	917.9	560.5	450.0	220.8	179.8	39.3	30.0	19.2	2 417.7
J. Assessed revenue per capita (\$pc) [J = I / A]	133.89	108.47	108.82	106.07	114.07	80.00	89.02	90.21	115.91
K. Category factor [K = J / J_{Aust}]	1.1552	0.9358	0.9389	0.9151	0.9841	0.6902	0.7681	0.7783	1.0000

Source: Premium data from Australian Prudential Regulatory Authority (APRA) is confidential and not shown in the above table. Actual revenue data provided by State Treasuries, classified to the 2010 Review category structure by the Commission.