Australian Government

Commonwealth Grants Commission

# 2020 REVIEW

# INSURANCE TAX

# STAFF DRAFT ASSESSMENT PAPER
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# CONTENTS

# INSURANCE TAX

1 The paper provides the Commission staff proposals for the assessment of Insurance tax revenue for the 2020 Review.

## 2015 REVIEW APPROACH

2 The Insurance tax category comprised revenue from duties on various forms of insurance, as well as insurance based fire and emergency services levies (FESLs). The duties are imposed on insurance companies and passed on to consumers.

3 Table 1 shows that States raised $5.3 billion from insurance tax in 2016-17.

**Table 1 Insurance tax revenue, 2016-17**

| | NSW | Vic | Qld | WA | SA | Tas | ACT | NT | Total |
|---|---|---|---|---|---|---|---|---|---|
| | $m | $m | $m | $m | $m | $m | $m | $m | $m |
| Insurance tax | 1 985 | 1 218 | 828 | 661 | 479 | 104 | 20 | 43 | 5 339 |

Source: State provided data.

### How was revenue capacity assessed?

4 States imposed duties on three main forms of insurance in the following ways.

- ***General insurance.*** All States imposed a fixed rate of duty on general insurance premiums (such as homeowner, motor vehicle, fire, public and product liability, and professional indemnity). The rate varied between 6% and 11%.[1] Three States (New South Wales, Queensland and Tasmania) applied concessional rates to certain classes of general insurance. Some classes of general insurance were exempt in one or more States.
- ***Compulsory third party (CTP) motor vehicle insurance***. Victoria and Western Australia imposed a single rate of duty on CTP premiums, while Queensland, South Australia and Tasmania imposed a flat fee.[2]
New South Wales, the ACT and the Northern Territory did not tax CTP insurance.

1 The ACT abolished general insurance duty from 1 July 2016. The fixed rate for the other States now varies between 9% and 11%, with three States continuing to impose concessional rates on certain types of general insurance.

2 CTP premiums were exempt from duty in Tasmania, but a flat fee was imposed on the issuance of the certificate. Victoria and Western Australia taxed CTP insurance at the same rate as general insurance.

- ***Life insurance.*** Five States imposed duty on the sum insured. South Australia imposed duty on the annual premiums. Western Australia and Victoria did not impose duty.[3]

5 Revenue capacity was assessed using data from the Australian Prudential Regulation Authority (APRA) on the total premiums paid for general insurance in each State.[4] Those data included premiums paid in relation to CTP insurance in States where it was privately underwritten.[5] To ensure comparability across States, the APRA data were supplemented by data from public insurers on total CTP insurance premiums in States where CTP insurance was publicly underwritten.[6]

6 APRA was unable to provide life insurance data by State. Life insurance premiums were, therefore, not included in the revenue base. Revenue from life insurance duties could not easily be removed from the category, but data from four States suggested it represented less than 5% of insurance tax revenue. On practicality grounds, the Commission decided to leave revenue from life insurance duty in the category and assess it using the general insurance revenue base.

### *Adjustments to the revenue base*

7 ***Workers' compensation premiums.*** The Commission made a further adjustment to the APRA data to exclude premiums relating to workers' compensation insurance. Those premiums represented about 27% of total general insurance premiums in 2012-13. However, the duty raised was only 2% of all insurance duties. Only Queensland and South Australia imposed duty on workers' compensation insurance premiums – Queensland did so at a concessional rate of 5% and South Australia exempted insurance in relation to employees under 25 years of age. A separate assessment of workers' compensation duties was not material at the $30 per capita threshold. Therefore, the Commission assessed workers' compensation duties equal per capita (EPC) in the Other revenue category.

8 ***Premiums paid to public insurers.*** Public insurers are controlled, or wholly owned, by State governments. They mainly provide CTP insurance, workers' compensation insurance, builders' warranty insurance and insurance for government agencies. Public insurers are not regulated by APRA and premiums paid to them are not included in the APRA data. The Commission supplemented the APRA data with data from public insurers on total premiums paid for CTP insurance and builders'

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3 Two States have abolished life insurance duty since the 2015 Review: the ACT from 1 July 2016 and the Northern Territory from 1 July 2015.

4 The APRA data covered general insurers in the private sector. These were insurers regulated by APRA. The data did not include premiums for reinsurance or private health insurance. Those forms of insurance were not liable for insurance tax in any State.

5 At the time of the 2015 Review, CTP insurance was privately underwritten in three States and publicly underwritten in five. South Australia moved to a privately underwritten CTP scheme from 1 July 2016.

6 A separate assessment of duty on CTP insurance was not material at the $30 per capita threshold.

warranty insurance.[7] Workers' compensation premiums paid to public insurers were not included in the revenue base, since workers' compensation duties were assessed in the Other revenue category. Premiums paid in relation to insurance for government agencies were not included in the revenue base, since any duty on those premiums was an internal budget transfer.[8]

9 ***Fire and emergency services levies.*** New South Wales and Tasmania imposed fire and emergency services levies on insurance companies. The levies are generally passed on to consumers. The Commission assessed these levies in the category, since they were raised on a similar basis to other insurance taxes.[9]

10 Premium data provided to APRA by insurance companies included insurance based FESLs.[10] To ensure that New South Wales and Tasmania were not assessed to have a higher insurance tax capacity due to their policy choice to impose insurance based FESLs, the FESL revenue was removed from the APRA premium data. Insurance based FESLs were, therefore, assessed using the general insurance revenue base.

11 Table 2 shows the derivation of the revenue base for the Insurance tax category in 2016-17.

**Table 2 Derivation of revenue base, insurance tax, 2016-17**

| | NSW | Vic | Qld | WA | SA | Tas | ACT | NT | Total |
|---|---|---|---|---|---|---|---|---|---|
| | $m | $m | $m | $m | $m | $m | $m | $m | $m |
| Premiums — APRA | 13 996 | 7 219 | 7 262 | 4 081 | 2 888 | 702 | 776 | 471 | 37 395 |
| Premiums — public insurers | 61 | 1 794 | 84 | 687 | 0 | 139 | 0 | 85 | 2 849 |
| Less workers' compensation premiums (privately underwritten) | 179 | 11 | 3 | 873 | 12 | 158 | 171 | 129 | 1 535 |
| Less insurance based FESL | 785 | 0 | 0 | 0 | 0 | 17 | 0 | 0 | 802 |
| Revenue base | 13 092 | 9 002 | 7 343 | 3 895 | 2 876 | 666 | 606 | 427 | 37 906 |

Source: Premium data from APRA and public insurers. FESL data provided by States.

7 Data were sourced from public insurers' annual reports. Three States had publicly underwritten builders' warranty insurance schemes. Builders' warranty insurance was privately underwritten in the other States and included in the APRA data.

8 This would not be the case for duty on premiums paid by Public Non-financial Corporations (PNFCs) other than those in health and urban transport. We did not have data to separately identify premiums paid by PNFCs.

9 Property based FESLs were included in the Land tax category, while vehicle based FESLs were included in Motor taxes.

10 This treatment is consistent with Australian accounting standard *AASB 1023*.

## GST redistribution

12 Table 3 shows the extent to which the assessment moved the GST distribution away from an EPC distribution in the 2018 Update. It shows GST revenue was redistributed from States with an above average revenue raising capacity (New South Wales, South Australia and the Northern Territory) to States with a below average revenue capacity (Victoria, Queensland, Western Australia, Tasmania and the ACT).

**Table 3 GST redistribution, Insurance tax, 2018 Update**

| | NSW | Vic | Qld | WA | SA | Tas | ACT | NT | Redist |
|---|---|---|---|---|---|---|---|---|---|
| Dollars million | -126 | 121 | 16 | 9 | -46 | 23 | 4 | -2 | 174 |
| Dollars per capita | -16 | 19 | 3 | 3 | -26 | 44 | 9 | -9 | 7 |

Source: 2018 Update.

## ISSUES AND ANALYSIS

13 This assessment does not need to be changed. It is achieving HFE. However, it could be simplified by treating insurance based FESLs, life insurance and workers' compensation insurance consistently. Revenue from these three sources could be assessed:

- using the general insurance revenue base (as is currently the case with insurance based FESLs and life insurance)
- EPC (as is currently the case for workers' compensation).

14 Neither of these treatments would be materially different to the current assessment. If the Commission were to assess these EPC, it could do so in a separate component within the category.

15 The Commission does not have data on life insurance tax revenue for the States that currently impose the tax. It would need data from those States if it were to move life insurance tax to an EPC component. On practicality grounds, life insurance tax revenue is currently assessed using the general insurance revenue base. Commission staff propose that that treatment should be continued. Treatment of the other two revenues is considered below.

## Treatment of insurance based FESLs

16 Two States (New South Wales and Tasmania) levy insurance based FESLs. Other States impose FESLs on property or motor vehicles. The Commission staff view is that the treatment of FESLs on the three bases should be considered as a single issue. A fuller discussion of the proposed treatment of FESLs can be found in the Draft Assessment for Land Tax.

17 Under its approach to average policy adopted in the 2015 Review, the Commission combined revenues that were taxed on the same basis. The hypothecation of FESL revenue to fire and emergency services was not a factor in how the Commission assessed revenue capacity. The Commission assessed insurance based FESLs in the Insurance tax category, since they were raised on a similar basis to other insurance taxes.

18 As the Commission is retaining this approach to average policy in the 2020 Review, Commission staff propose to continue to assess insurance based FESLs in the Insurance tax category.

## Treatment of duty on workers' compensation insurance

19 Two States (Queensland and South Australia) impose duty on workers' compensation premiums. Queensland taxes these premiums at a concessional rate of 5% and South Australia allows an exemption for workers' compensation in relation to employees under the age of 25.[11]

20 Workers' compensation premiums represent some 20% of all insurance premiums, but the duty raised on these represents less than 2% of total insurance tax revenue. Including workers' compensation premiums in the revenue base is likely to misrepresent States' revenue raising capacities.

21 A separate assessment of workers' compensation duty is not material at the $30 per capita threshold. Workers' compensation duty is raised on a similar basis to other insurance taxes. Assessing the revenue raised with the general insurance revenue base is not materially different from assessing it EPC. On simplicity grounds, Commission staff propose to leave the revenue from workers' compensation duty in the insurance tax category and assess it using the general insurance revenue base.

## Recommendations

Staff propose to recommend the Commission:

- retain the 2015 Review insurance tax assessment, but include workers' compensation duty in the category and assess it using the general insurance base.

## Other issues considered

22 ***Elasticity adjustment.*** The Commission has engaged a consultant to provide advice on whether it should consider reinstating elasticity adjustments and, if so, for which categories. The question whether an elasticity adjustment could be assessed in the Insurance tax category will be addressed by that consultancy.

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11 Queensland applied a tax rate of 9% to most classes of general insurance in 2015-16.

# CONCLUSION AND WAY FORWARD

23 Commission staff propose to retain the 2015 Review Insurance tax assessment, including the treatment of insurance based FESLs. Staff propose that, for simplicity, revenue from workers' compensation duty be left in the insurance category and assessed using the general insurance revenue base, rather than being assessed EPC in Other revenue as in the 2015 Review.

## Proposed assessment structure

24 Table 4 shows the proposed assessment structure for Insurance tax in the 2020 Review.

**Table 4 Proposed Insurance taxes category structure, 2020 Review**

| Component | Disability | Influence measured by disability |
|---|---|---|
| Insurance tax | Value of total premiums for taxable forms of insurance | Recognises the additional revenue capacity of States with a greater level of insured risk, as shown by total premiums for taxable forms of insurance. |