

TAXMANN®'S

Special Issue

CORPORATE PROFESSIONALS TODAY

A WEEKLY ON GST | INCOME TAX | COMPANY LAW | ACCOUNTS & AUDIT

ISSN 0975-9948

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www.taxmann.com

VOLUME 57 ■ ISSUE 13 ■ JULY 29, 2023 TO AUGUST 4, 2023

PRICE : ₹ 250

TOTAL NO. OF PAGES 72

Insurance Sector Under the Scrutiny of GST

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1. Overview

The implementation of the Goods and Services Tax Act (hereinafter referred as "GST") has brought about significant changes in the Tax landscape for Insurance Sector. GST is a comprehensive Indirect Tax levied on the supply of Goods and Services, which aims to replace a complex network of multiple Taxes. Whereas the Insurance Sector, being an important component of the global economy, has undergone significant changes since the implementation of GST. However, GST has streamlined the Tax structure by replacing multiple Taxes with a Unified System, simplifying compliance and reducing the administrative burden for insurers/policymakers¹.

This article will explore the key aspects such as Taxability on Insurance Companies, ITC eligibility², Taxation on premium³, compliance requirements and challenges with respect to revenue leakage. By gaining insights into these areas, Insurance Industry can ensure compliance, optimize their Tax obligations, and navigate the GST landscape with confidence. This article was created utilising secondary data and the exploratory research process.

2. Taxability on Insurance sector

Under the GST regime, insurance services⁴ are considered as "Financial Services", Insurance Services, including Life Insurance, General Insurance, and Reinsurance⁵, these services are subject to GST and are Taxable as "Supply of Services" under section 7(1) of the CGST Act, 2017⁶. The GST rates applicable to Insurance Services may vary based on the type of insurance and the coverage provided. Currently, the standard GST rate for Insurance Services is set at 18%⁷.

This means that Insurance Sector are required to register under GST and fulfil their Tax obligations accordingly. The GST framework applies a destination-based consumption tax model, where Taxes are levied at each stage of the supply chain, ultimately borne by the end consumer.

One of the essential features of GST is the availability of **Input Tax Credit (ITC)**⁸. ITC allows businesses to claim credit for the GST paid on inputs, *i.e.*, goods and services used in the furtherance of business. Insurance Company can also claim ITC⁹ on their inputs, such as office supplies, infrastructure, and other services procured for their operations. Therefore, maintaining proper records¹⁰ of input tax paid and received invoices is crucial to support ITC claims during audits.

Section 17(4) of the CGST Act, 2017 pertains to the restriction on claiming Input Tax Credit (ITC) for certain goods or services; this provision outlines situations where ITC cannot be claimed by registered persons engaged in the General Insurance Business¹¹.

3. Premiums and Settlements

Insurance companies typically collect premiums from policyholders. Under the GST regime, these Premiums are subject to Tax at a specific rate.¹² The rate may vary depending on the type of Insurance, such as Life Insurance, Health Insurance, or General Insurance. GST is levied on the entire premium amount received by the Insurance Company. The Tax liability arises at the time of receipt of premium or when an invoice is issued, whichever is earlier. The Insurance Sector is responsible for collecting and remitting the GST to the Government.

When it comes to claim settlements or Indemnity Payments made by Insurance Company, GST is not applicable, the reason behind this is that the Insurance Claim is Actionable Claim¹³ which is outside the purview of GST as per Schedule-III¹⁴, it is to be treated as

Capital Gain if the requirements of section 45(1A)¹⁵ are satisfied. However, any fees or charges associated with claim processing or administrative services may be subject to GST.

4. Compliances

Insurance Sector is required to comply with various GST compliance. If their annual turnover exceeds the threshold, which may vary, they are bound to register for GST¹⁶. Registration enables them to collect and deposit GST on premium charged from policyholders, they must maintain proper books of account, invoices¹⁷ to support their GST filings and shall retain them until the expiry of seventy-two months from the due date of furnishing of annual return for the year pertaining to such accounts and records.¹⁸

The Tax liability should be accurately calculated, and the appropriate Tax should be remitted within the prescribed timelines¹⁹. Insurance Companies are also required to file regular GST returns²⁰, such as GSTR-1 (outward supplies²¹)²², and GSTR-9 (annual return)²³ etc. These returns provide a consolidated view of the company's GST transactions, including the premium received, ITC availed, and Tax paid.

5. Fake Invoices

Integrity and transparency are fundamental pillars of any Tax System, and the Insurance Industry is no exception. Under section 31 of the CGST Act²⁴, 2017 outlines the provisions relating to the issuance of invoices by a registered person. According to this section, every registered person is required to issue a Tax invoice for the supply of goods or services. Invoices serve as crucial documents for various purposes. They are essential for claiming input Tax Credits, maintaining accurate Financial Records, facilitating audits, and resolving disputes between parties. However, some unscrupulous Insurance companies are taking advantage of loopholes within the

system by not complying with Section 31 of the CGST Act, they issue fake commission²⁵ invoices for Insurance Agents²⁶ to deceive revenue departments. This fraudulent activity not only undermines the Tax system but also poses ethical and legal risks for both insurers²⁷ and agents²⁸.

Investigations revealed that these insurers were actually paying commission beyond IRDAI's permissible limit²⁹ to their corporate agents in the garb of expenses related to marketing and brand activation. The norms with regard to payment of commission to agents and intermediaries have been modified by the insurance regulator IRDAI with effect from April 1, 2023.³⁰ The modified norms prescribe an overall limit for management expenses, including commission related expenditure that an insurer can incur.

Fake commission invoices refer to invoices generated by Insurance Company, falsely claiming the payment of commissions to Insurance Agents. These invoices are created to manipulate Financial Records and deceive Revenue Departments, leading to the wrongful reduction of Taxable income and the evasion of Taxes.

The Maharashtra Authority for Advance Ruling in *Jotun India Pvt. Ltd.*, In re [2019] 110 taxmann.com 184/76 GST 691/2019 (29) GSTL 778 (AAR-Maharashtra) has ruled that "The applicant has brought nothing on record to show that they are Insurance Company and registered with such authorities. Hence it appears that the applicant is creating this fiction of providing health insurance to their employees only to avail 100% ITC of payments made to the insurance companies. Therefore, considering the provision of section 7 of CGST Act, 2017 and ARA Ruling No.: *Pasco India Pune Processing Centre (P.) Ltd.*, In re [2019] 102 taxmann.com 21/2019 (21) GSTL 351 (AAR-Maharashtra), Dated 7th September, 2018, there is no supply of services and also credit cannot be claimed of GST paid on such medical Insurance Policy"³¹.

6. Consequences of Fake Invoices

- (a) By understating Taxable Income, Insurance Companies can evade Taxes, resulting in substantial losses to the Revenue Department. This revenue leakage hinders public welfare initiatives and infrastructure development.
- (b) This deceptive practice erodes trust between Insurers, Agents and Policyholders, thereby damaging the reputation of the entire Industry.
- (c) Insurance Company and individuals involved may face penalties, fines, and even criminal charges for Tax evasion and fraud.³²

7. Conclusion

Insurance Company need to be aware of their Tax obligations, including the eligibility and utilization of Input Tax Credit (ITC). Proper documentation and record-keeping practices are essential to determine the eligibility of ITC and claim it accurately. Additionally, Insurance Company must take care of Taxation on the premium collected from Policyholders³³. GST is applicable on the entire premium amount received, and it is the responsibility of Insurance Companies to collect and remit the Tax to the Government. Clear invoicing practices and accurate computation of Tax liability are essential for compliance with GST provisions.

However, despite the implementation of section 31 under CGST Act, the issue of generating fake invoices continues to persist, particularly within the Insurance Sector. Addressing this issue requires a collaborative effort between revenue departments, Insurance Regulators and industry stakeholders. By implementing stronger auditing procedures, imposing tougher penalties and promoting ethical guidelines, the Insurance Industry can root out this deceptive practice. Upholding transparency and integrity will not only protect Tax revenue but also instil public confidence and enhance the reputation of the Industry.

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1. Section 2(9) of The Insurance Act, 1938 define the definition of "Insurer".
2. Section 16 of the CGST Act, 2017.
3. GST on insurance premium is 18% (9% SGST + 9% CGST) as per GST rates issued by cbic-gst.gov.in (heading 9971 (financial and related services)).
4. Section 2(102) of The CGST Act, 2017 define the definition of "Services".
5. Section 2(16b) of The Insurance Act, 1938 define the definition of "Reinsurance".
6. Section 7(1) of the CGST Act, 2017 states the provision regarding "Scope of Supply".
7. GST on insurance premium is 18% (9% SGST + 9% CGST) as per GST rates issued by cbic-gst.gov.in (heading 9971 (financial and related services)).
8. Section 2(63) of The CGST Act, 2017 define the definition of "Input Tax Credit" & Section 16 of CGST Act, 2017 states the "Eligibility and conditions for taking input tax credit".
9. Section 41 of CGST Act, 2017 which states the provision regarding "Availment of ITC".
10. Section 14 of The Insurance Act, 1938 states the "Record of policies and claims."
11. Section 2(6b) of The Insurance Act, 1938 define the definition of "General Insurance Business." Read with Section 17(5)(ab) of CGST Act, 2017, Subs. by s. 9, *ibid.* for clauses (a) and (b) (w.e.f.1-2-2019).
12. GST on insurance premium is 18% (9% SGST + 9% CGST) as per GST rates issued by cbic-gst.gov.in (heading 9971 (financial and related services)).
13. Section 2(1) of the CGST Act, 2017 defines the definition of "Actionable Claims".
14. Schedule III(6) of CGST, 2017 states the "Activities or Transactions which shall be treated neither as a Supply of Goods nor a Supply of Services".
15. Section 45(1A) of Income-tax Act, 1961.
16. Section 22 of CGST Act, 2017 which states the provision related to "Persons liable for registration".
17. Section 2(66) of The CGST Act, 2017 define the definition of "Invoices".
18. Section 35 of CGST Act, 2017, read with Accounts and Records Rules on "cbic-gst.gov.in".
19. Section 9 of CGST Act, 2017 states the provision regarding "Levy and collection".
20. Section 2(97) of The CGST Act, 2017 define the definition of "Return".
21. Section 2(83) of The CGST Act, 2017 define the definition of "Outward Supply".
22. Section 37 of CGST Act, 2017 which states the provision regarding "Furnishing details of outward supplies."
23. Section 44 of CGST Act, 2017.
24. Section 31 of CGST Act, 2017 states the provision regarding "Tax Invoice".
25. Regulation 3(c) of Insurance Regulatory and Development Authority of India (Payment of Commission) Regulations, 2023 define the definition of "Commission".
26. Section 2(10) of The Insurance Act, 1938 define the definition of "Insurance Agent".
27. Section 2(9) of The Insurance Act, 1938 define the definition of "Insurer".
28. Section 2(5) of The CGST Act, 2017 define the definition of "Agent".
29. Regulation 5 of Insurance Regulatory and Development Authority of India (Payment of Commission) Regulations, 2023.
30. Insurance Regulatory and Development Authority of India (Payment of Commission) Regulations, 2023 F.No. IRDAI/Reg/2/190/2023.
31. 2019 SCC ONLINE MAH AAR GST 77.
32. Sections 122, 123 and 124 of the CGST Act, 2017 states provision regarding "Offences and Penalties".
33. Section 2(2) of The Insurance Act, 1938 define the definition of "Policyholder".