

Clarification regarding Service Tax on re-insurance Commission

Circular No. 120(a)/2/2010-ST, dated 16-4-2010

In terms of Section 101A (Part IV-A) of the Insurance Act, 1938, every insurer dealing in insurance business is required to re-insure a specified percentage of sum assured with another insurance company.

2. The insurance company pays premium to the reinsuring company for this service. However, a part of such premium is deducted and kept by the insurance company for meeting the administrative expenditure. In other words, the insurance company and the re-insurance company jointly bear the expenses for running the insurance/reinsurance business. This shared expense is commonly known as 'commission' though strictly it is not in the nature of a commission. It may be pertinent to mention that the customer/beneficiary deals only with the insurance company and may not even be aware of the role of re-insurer and the backroom operations between the insurance company and the reinsurer.

3. As per the provision of the Finance Act, 1994, insurance as well as reinsurance are subject to service tax. The Board has received representations that notices have been issued demanding service tax on the amounts deducted by the insurance company (in other words paid by the reinsurance company) on the ground that it is the consideration for the insurance company providing business auxiliary service (BAS) to the re-insuring company. The notices alleged that the insurance companies are promoting the business of re-insurers thereby providing them the BAS.

4. The issue has been examined. As explained in para 2 above, the arrangement between the insurance company and the reinsurer is only sharing of expenses and there is no service provided by the insurance company to the re-insurer for a consideration. Since the policy holder may not even be aware of the operations of the re-insurer, it cannot be said that the payment made by the re-insurer to the insurance company is for its business promotion or a service on behalf of the re-insuring company (i.e. Business Auxiliary Service). In fact, it is the reinsurer which provides insurance service to the insurance company. As both the insurance company and reinsurer pay service tax on the entire amount of premium charged by them, the question of charging service tax under any other taxable service does not arise.

5. The Board desires that all pending cases on this subject may be decided keeping in view the above clarification.