



INDIA

International Comparison of Insurance Taxation
March 2007



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International Comparison of Insurance Taxation

March 2007

India – General Insurance

1 Definition

Definition of property and casualty insurance company

Accounting

Under the Insurance Act, 1938, 'Indian insurance company' means any insurer being a company:

- (a) which is formed and registered under the Companies Act, 1956 (1 of 1956);
- (b) in which the aggregate holdings of equity shares by a foreign company, either by itself or through its subsidiary companies or its nominees, do not exceed 26% paid-up equity capital of such Indian insurance company;
- (c) whose sole purpose is to carry on general insurance business.

General insurance business means fire, marine or miscellaneous insurance business, whether carried out singly or in combination with one or more of them.

[Note Third proviso to Section 2C(1) of the Insurance Act, 1938 {inserted by the Insurance Regulatory and Development Authority (IRDA) Act, 1999} prohibits persons other than an Indian Insurance Company to begin to conduct insurance business. The said proviso is reproduced below:

'Provided also that no insurer other than an Indian Insurance Company shall begin to carry on any class of insurance business in India under this Act on or after the commencement of the IRDA Act, 1999']

Taxation

No separate definition provided in tax legislation.



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India – General Insurance

2 Commercial Accounts/ Tax and Regulatory Returns

Basis for the company's commercial accounts and regulatory returns

Accounting

Insurance Regulatory and Development Authority (Preparation of Financial Statements & Auditor's Report of Insurance Companies) Regulations, 2002

All mandatory Accounting Standards issued by Institute of Chartered Accountants of India to be adhered to subject to the following:

- (i) Accounting Standard 3 (AS 3), Cash Flow Statements – Cash Flow Statement shall be prepared only under the Direct Method.
- (ii) Accounting Standard 13 (AS 13), Accounting for Investment is not applicable.
- (iii) Accounting Standard 17 (AS 17) – Segment Reporting – shall apply even though insurance companies are not currently publicly traded.

Relevant/Applicable provisions of the Companies Act, 1956

Taxation

Accounting profits subject to adjustments under tax laws, for items including provisions, reserves for unexpired risks and depreciation form the basis of determining taxable income.

Regulatory return

Investment returns, solvency margin returns, actuarial returns and other returns are required to be filed by the insurer either quarterly or annually as prescribed under the relevant regulations.

N/A



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India – General Insurance (continued)

Tax return

Annual return of income to be filed by 31 October every year. The said return is also required to include information relating to fringe benefit tax payable by the company. The applicable reporting period is the immediately preceding financial year i.e. uniform tax year that begins on 1 April, XI and ends on 31 March, X2.

Annual return of net wealth to be filed by the above date wherever the taxable net wealth exceeds INR 1.5 million.

Withholding tax returns are also required to be filed on a quarterly basis. The applicable reporting period in this regard is the financial year, accordingly the first quarterly return is required to be filed for the quarter ended 30 June within the reporting deadline of 15 July.

③ Technical Reserves/ Equalisation Reserves

Unearned premium reserves (UPR)

Accounting

A reserve for unearned premium is created as the amount representing that part of the premium written, which is attributable to, and to be allocated to, the succeeding accounting periods and the amount is determined by the relevant provisions of the Insurance Act, 1938.

Taxation

No separate tax deduction for UPR is allowed, however a deduction for reserves for unexpired risks is allowable as discussed below.



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Unpaid claims reported	Unpaid claims are disclosed under claims outstanding as required by Insurance Regulatory and Development Authority (Preparation of Financial Statements & Auditor's Report of Insurance Companies) Regulations, 2002.	Though the tax laws do not contain a specific provision for tax deduction for such reserves, unpaid claims debited to the revenue accounts may be allowable as a deduction.
Claims incurred but not reported (IBNR)	Claims incurred but not reported (IBNR) is disclosed as claims outstanding as required by Insurance Regulatory and Development Authority (Preparation of Financial Statements & Auditor's Report of Insurance Companies) Regulations, 2002.	No specific tax deduction for such reserves is available under tax laws.
Unexpired risks	Same as unearned premium reserves.	Specific provisions are contained in the tax laws for reserves for unexpired risks as follows: <ul style="list-style-type: none">• Fire or engineering insurance which also provides insurance for terrorism risks – 100% of the net premium income of such business.• Fire or misc. insurance (other than above) – 50% of net premium income of such business• Marine insurance (including export credit insurance) – 100% of net premium income of such business.



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General contingency/solvency reserves	N/A	No specific tax deduction for such reserves is available under tax laws.
Equalisation/catastrophe reserves	Catastrophe reserve is made in accordance with norms prescribed by the Insurance Regulatory and Development Authority. Appropriations for Catastrophe reserve is made from the Revenue Account (Form B-RA).	No specific tax deduction for such reserves is available under tax laws.



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India – General Insurance (continued)

4 Expenses/Refunds

Acquisition costs

Accounting

Acquisition costs are costs that vary with and are primarily related to the acquisition of new and renewal insurance contracts. Such costs are expensed in the year in which they are incurred.

Taxation

Though the tax laws do not contain a specific provision for deduction of such expenses, acquisition costs debited to the revenue accounts are allowable as a deduction.

Loss adjustment expenses on unsettled claims (claims handling expenses)

Loss adjustment expenses (claims handling expenses) are incidental to processing of claims and are accounted under claims incurred in revenue account.

Though the tax laws do not contain a specific provision for deduction of such expenses, claims handling expenses debited to the revenue accounts are allowable as a deduction.

Experience-rated refunds

N/A

N/A

Investments

5 Gains and losses on investments

Accounting

In respect to government securities and other held to maturity securities, long-term gain/loss on transfer/sale of securities is the difference between the sale price and the net amortised cost/book value and is accounted for in either revenue account or profit and loss account on the basis of the ratio of shareholders fund and technical reserves.

Taxation

Gains/losses on investments held for insurance business are treated as revenue and considered in computation of total income.

Gains/losses on investments held as capital assets may be subject to lower tax rates as capital gains. Capital gains arising from sale of listed securities held for more than 12 months (being shares of an Indian company or units of mutual fund) are exempt from tax provided the sale is through a stock exchange in India and the transaction has been subject to a nominal securities transaction tax (STT).

Please note that such exempt capital gains are also subject to minimum alternative tax (MAT) provisions (discussed later).



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Investment reserves	Provision for diminution in value of investments other than temporary is accounted for.	If investments are held for the insurance business, a provision for diminution in value of such investments may be deductible, so long as the market valuation is readily ascertainable. Provision for diminution in value of investments held as capital assets shall not be allowed as a deduction.
Investment income	Investment income is recognised on accrual basis. Dividend income is recognised when the right to receive is established. Investment income is allocated to revenue account (Form B – RA) and to profit and loss account (Form B – PL) in the ratio of technical reserves and shareholders funds.	Included in taxable income. However, dividends from an Indian company which have been subject to a dividend distribution tax are not double taxed in the hands of shareholders (insurance company) and are exempt under Section 10(34) of the tax code.
6 Reinsurance Reinsurance premiums and claims	Accounting Reinsurance premium and commission is recognised over the period of risk. Reinsurance benefit to insurers for claims is accounted for when intimated and is accounted for in the same period as the related claims.	Taxation Tax treatment generally follows accounting treatment.
7 Mutual Companies Mutual companies (all profits returned to members)	Accounting No mutual company exists	Taxation No special treatment as mutual companies are presently not in existence in India in the general insurance sphere.



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India – Other Tax Features

8 Further corporate tax features

Loss carry-overs

Taxation

Permitted up to a maximum of eight years, subject to continuity of substantial ownership (>51%) test

Foreign branch income

Included in taxable income, as all resident insurance companies are taxed on worldwide income. However, a credit for foreign taxes may be available in India, subject to tax treaty provisions.

Domestic branch income

Calculated under ordinary rules based on branch accounts.

Corporate tax rate

The normal tax rate is 33.66% (incl. surcharge and educational cess).

Other tax features

9 Premium taxes

Taxation

No specific income tax on premiums. However, premiums collected are subject to a Service Tax of 12.24% (including education cess of 2%).

Capital taxes

Wealth tax is levied at the rate of 1% on certain specified assets (motor vehicles, jewellery, specified immovable property) owned by a company and valued in excess of Rs 1.5 million at the last day of the financial year net of any associated liabilities.

Captive insurance companies

N/A



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India – Other Tax Features (continued)

Minimum Alternative Tax (MAT)

For companies whose tax payable under normal tax provision is less than 10% of book profits, a mat of 10% is levied on book profits. The effective MAT rate for a domestic company is 11.22% (including surcharge and education cess). A credit of such tax paid under MAT provisions by a company w.e.f. financial year 2005-06 shall be allowed against the tax liability that arises in the subsequent seven years under the normal provisions of the Act.

Dividend Distribution Tax

Dividend income is exempt in the hands of the shareholders. However, a dividend distribution tax of 12.5% (plus surcharge and education cess) is levied on companies declaring dividend. Effective dividend distribution tax rate on companies is 14.03%.

Fringe Benefits Tax (FBT)

An additional tax termed as 'Fringe benefits tax' has been introduced beginning financial year 2005-06. It provides for the levy of an additional corporate tax of 30% (plus applicable surcharge and education cess) in the hands of the employer on the value of fringe benefits provided to the employees other than perquisites on which tax is paid/payable by the employee.



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India – Life Insurance

1 Definition

Definition of Life Insurance companies

Accounting

Under the Insurance Act, 1938, 'Indian insurance company' means any insurer being a company:

- (a) which is formed and registered under the Companies Act, 1956 (1 of 1956);
- (b) in which the aggregate holdings of equity shares by a foreign company, either by itself or through its subsidiary companies or its nominees, do not exceed 26% of paid-up equity capital of such Indian insurance company.
- (c) whose sole purpose is to carry on life insurance business.

Life insurance business means the business of effecting contracts of insurance upon human life, including any contract whereby the payment of money is assured on death (except death by accident only) or the happening of any contingency dependent on human life and any contract which is subject to payment of premium for a term dependent on human life and includes:

- a) granting of disability, double- or triple-indemnity accident benefits;
- b) granting of annuities;
- c) granting of superannuation allowance.

Taxation

No separate definition provided in tax legislation.



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India – Life Insurance (continued)

Life insurance business may be linked business or non-linked business. Under linked business, the benefits payable depend upon the value of assets available with the insurer and under non-linked business, the benefits are payable, irrespective of the value of assets. Similarly, there may be participating business or non-participating business, meaning thereby, the policyholders may or may not have the right to participate in the profits of the business. It may be mentioned that for each kind of business mentioned above, separate revenue accounts need to be prepared by the life insurer. [Note Third proviso to Section 2C(1) of the Insurance Act, 1938 {inserted by the Insurance Regulatory and Development Authority (IRDA) Act, 1999} prohibits persons other than an Indian insurance company to begin to transact insurance business. The said proviso is reproduced below:
'Provided also that no insurer other than an Indian insurance company shall begin to carry on any class of insurance business in India under this Act on or after the commencement of the IRDA Act, 1999'.]



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India – Life Insurance (continued)

2 Commercial Accounts/ Tax and Regulatory Returns

Basis for the company's commercial accounts

Accounting

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(ii) Accounting Standard 13 (AS 13), Accounting for Investment is not applicable;
(iii) Accounting Standard 17 (AS 17) – Segment Reporting – shall apply even though insurance companies are not currently publicly traded.

Taxation

N/A

Regulatory return

Investment returns, solvency margin returns, actuarial returns and other returns are required to be filed by the insurer either quarterly or annually as prescribed under the relevant regulations.

N/A



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India – Life Insurance (continued)

Tax return

Annual income tax return to be filed by 31 October every year. The said return is also required to include information relating to Fringe Benefit Tax payable by the company. The applicable reporting period is the immediate preceding financial year i.e. uniform tax year, which begins on 1 April, XI and ends on 31 March, X2.

Annual net wealth tax return to be filed by the above date wherever the taxable net wealth exceeds INR 1.5 million.

Withholding tax returns are also required to be filed on a quarterly basis. The applicable reporting period in this regard is the financial year. Accordingly, the first quarterly return is required to be filed for the quarter ended 30 June within the reporting deadline of 15 July.

3 General approach to calculation of income

Allocation of income between shareholders and policyholders

Accounting

Premium, income on investments made out of policyholders funds, and all expenses directly related to insurance business should be classified under the policyholders revenue account.
Income on investment made from shareholders funds and all expenses not directly related to insurance business is accounted for the under shareholders profit and loss account.

Taxation

Life insurance companies are taxed on a 'total income' basis, including overall profit from underwriting and investment income. In effect, the taxable income is the net income credited to the shareholders account and the profit allocated to the shareholders on participating and non-participating policies.



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India – Life Insurance (continued)

4 Calculation of investment return

Calculation of investment income and capital gains

Accounting

Substantial portion of funds are invested in government securities and treasury bonds. Investments are also made in Bonds and Equities. Interest income is recognised on accrual basis and is accounted under revenue account (technical account) or profit and loss account as applicable.

Taxation

Generally taxed as ordinary income from the business of life insurance.

5 Calculation of underwriting profits or total income

Actuarial reserves

Accounting

The actuarial liability on a policy is calculated based on the 'gross premium method,' which represents the present value of expected future outlay, including benefits and expenses, as reduced by the present value of expected future premium and related income.

The reserves for group business are calculated as the risk premium for the unexpired term of the policy with an allowance for expenses and a margin for adverse deviations.

For unit-linked business, unit reserves represent the value of the units attached to policies. Non-unit reserves are set up for mortality and morbidity risks associated with unit-linked business and are calculated using the 'gross premium methods.'

Taxation

Calculated under the Insurance Act and approved by the appointed actuary. An increase in actuarial reserves is deductible while a decrease in actuarial reserves is taxable.



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India – Life Insurance (continued)

Acquisition costs

Acquisition costs are costs that vary with and are primarily related to the acquisition of new and renewal insurance contracts. Such costs are expensed in the year in which they are incurred and are not to be capitalised.

Follows accounting. Accordingly, such expenses are tax deductible in year incurred.

Gains and losses on investments

In respect to government securities and other held to maturity securities, long-term gain/loss on transfer/sale of securities is the difference between the sale price and the net amortised cost/book value and is accounted as policyholders income under Form A-RA or shareholders income under Form A-PL as applicable.

The profit or loss on the actual sale of a listed security includes the accumulated changes in fair value previously recognised in the 'fair value charge account.' This amount is recycled to the appropriate revenue or profit and loss amount.

Follows accounting. Investment gains or losses (realised or unrealised) that have been charged to the policyholders or shareholders account in accordance with prescribed accounting regulations would be eligible for a tax deduction.



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India – Life Insurance (continued)

Reserves against market losses on investments	For impairments other than temporary in the value of investment at the balance sheet date, the amount of loss is recognised as an expense in the revenue account (Form A-RA) or profit and loss account (Form A – PL). Unrealised gains/losses due to changes in the fair value of listed equity shares flow through the fair value change account and are carried forward to the balance sheet. Unrealised gains and losses in unit-linked business are recognised in the respective scheme's revenue account (Form A – RA)	Follows accounting.
Dividend income	Dividend income is recognised when the right to receive is established.	Dividends from an Indian company that have been subject to a dividend distribution tax are not double taxed in the hands of shareholders, (life insurance company) and are exempt under Section 10(34) of the tax code.
Policyholder bonuses	Included in the revenue account.	Generally, tax-deductible in the form of actuarial reserves or benefit payments.
Other special deductions	None.	None.
⑥ Reinsurance Reinsurance	Accounting Reinsurance premium and commission is recognised over the period of risk. Reinsurance benefits to insurers for death claims are accounted for when intimated and accounted for in the same period as the related claims.	Taxation There are no separate rules in the tax code for taxation of a reinsurance company. Tax treatment of premiums ceded or claims received follows the accounting treatment in the books of the insurer.



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India – Life Insurance (continued)

7 Mutual companies/Stock companies Accounting

Mutual companies

No mutual company exists.

Taxation

There are no separate rules in the tax code for taxation of a mutual insurance company, it is taxed as any other life insurance company. Currently, there are no pure mutual insurance companies in India as most private life insurance companies are equity joint ventures between Indian and foreign promoters.

LIC, which is India's largest life insurer and owned wholly by the Government, operates virtually like a mutual insurer as it is funded almost entirely by policyholders funds and distributes over 90% of surplus as bonuses to policyholders.

Minimum Alternative Tax (MAT)

With an object to bring zero tax companies under tax net, MAT at 10% (plus applicable surcharge and education cess) of book profits is levied on companies whose tax payable under normal income-tax provisions is less than 10% of book profits.

The effective MAT rate for a domestic company is 11.22% (including surcharge and education cess). A credit of such tax paid under MAT provisions by a company w.e.f. financial year 2005-06 shall be allowed against the tax liability that arises in subsequent seven years under the normal provisions of the Act.



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India – Life Insurance (continued)

Dividend Distribution Tax

Dividend income is exempt in the hands of the shareholders. However, a dividend distribution tax at 12.5% (plus surcharge and education cess) is levied on companies declaring dividend. Effective dividend distribution tax rate on companies is 14.03%.

Fringe Benefits Tax (FBT)

An additional tax termed as 'Fringe benefit tax' has been introduced with effect from financial year 2005-06. It provides for levy of an additional tax at 30% (plus applicable surcharge and education cess) in the hands of the employer on the value of fringe benefits provided to the employees other than perquisites on which tax is paid /payable by the employee.



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India – Other Tax Features

8 Further corporate tax features

Loss carry-overs

Taxation

Permitted to be carried forward up to a maximum of eight years subject to continuity of substantial ownership (>51%) test

Foreign branch income

Included in taxable income, as all insurance companies being Indian companies are tax resident in India and are chargeable to tax on worldwide income. However, an exemption/tax credit for foreign taxes suffered, may be available in India, subject to tax treaty provisions.

Domestic branch income

Calculated under ordinary rules based on branch accounts.

Corporate tax rate

Effective tax rate is 14.03% (12.50% plus 10% surcharge plus 2% education cess).

9 Policyholder taxation

Deductibility of premiums

Taxation

Individuals may deduct premiums paid, subject to the overall maximum limit of INR 100,000 (per person/per year) provided under Section 80C of the Income Tax Act 1961.

The employer may deduct payments of key man life insurance premiums.

Interest build-up

Generally not taxable.

Proceeds during lifetime

Generally not taxable (Receipts under a keyman insurance policy are taxable and/or a policy which was established after 1 April, 2003, and premiums payable for any of the years during which the term of policy exceeds 20% of the actual capital sum assured)



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India – Other Tax Features (continued)

Proceeds on death

Not taxable [receipts under a keyman insurance policy are taxable]

10 Other tax features

Premium taxes

Taxation

Life insurance premiums generally attract a 12.24% service tax (including education cess of 2%) on the risk portion. Insurers in some cases may be in a position to opt for the composite scheme where service tax is payable on 1% (plus education cess) of the gross amount of premium, without a distinction being made between risk and investment portions.

Capital taxes

Wealth tax is levied at the rate of 1% on certain specified assets (motor vehicles, jewellery, specified immovable property) owned by a company and valued in excess of Rs 1.5 million at the last day of the financial year, net of associated liabilities, if any.

Captive insurance companies

No separate rules for captives.



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