HMRC - IPT07300 - Bad Debt Relief

Bad debt relief under the special accounting scheme

There are no specific provisions for bad debt relief in IPT. However, where insurers write a premium into their books and account for tax in the expectation that they will receive a premium (under the special accounting scheme) and subsequently do not receive that premium (and cancel the policy and reverse the accounting entry), they may claim a tax credit (see IPT07680).

Where a broker receives a premium on behalf of an insurer, and the broker subsequently fails to pay that premium to the insurer, the insurer is still required to account for the tax. This is because where a premium is received by another person on behalf of an insurer, it is treated as received by the insurer. Where the insurer is using the special accounting scheme, they must write the premium if they have not already done so, and must account for the tax (see IPT07715, where the relevant legal provision, Section 72(7) of the Finance Act 1994, is reproduced).

If a cheque, standing order etc., presented by the insured is dishonoured, there is no payment. But where a broker’s cheque, forwarding premiums already paid by the insured, is dishonoured (for example due to lack of funds), the insurer is still treated as having received the premium. That is for the reasons explained immediately above. Where payment from the insured to the broker, or payment from the insured direct to the insurer, is stolen in the post there is no payment.

This approach, of holding insurers liable for the tax when payment has been made by the insured, mirrors general industry practice, which in turn is based on the general law of agency. Where a client has paid a premium to a broker, or other agent acting on behalf of the insurer, the client is covered by the insurance that has been paid for, even if the broker fails to pass the premium to the insurer. The insurer is said to be ‘on risk’ in such situations, and cannot avoid his liability.

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Bad debt relief under the basic cash receipt scheme

Where an insurer uses the cash receipt method and deals directly with the insured (i.e. payment is not made through a broker) there is effectively automatic bad debt relief: no receipt of cash by the insurer means there is no tax point and thus no requirement to account for tax. However, as explained immediately above, where a broker receives a premium on behalf of an insurer using the cash receipt scheme and the broker subsequently fails to pay that premium to the insurer, the insurer is still required to account for the tax.

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