HMRC - IPT08485 - Tax Treatment Of Add-Ons

There are two necessary steps to take in order to determine the tax treatment of an add-on product. These are:

identify whether the product is insurance or some other service;

identify the chargeable amount.

Is the product insurance, or some other service?

The distinction between a contract of insurance and a contract for other services is important for several reasons, including taxation. In many cases it will be clear into which of the two categories a particular contract falls.

Paragraph 3.3 of Notice IPT1, although drawn up primarily to distinguish between insurance and guarantees, offers some useful guidance. The basic rule is that if the service provided does not match the description of insurance services in paragraph 3.3, it is not likely to be a supply of insurance (even if it is labelled ‘insurance’ by the supplier and accepted by the customer as such - the nature of the supply is determined by legal criteria, not by the label given). Authorised insurers are generally unable to do anything other than underwrite insurance business: therefore if the service is provided by an authorised insurer and not someone else it will almost certainly be insurance.

Examples of such services provided by insurers are breakdown recovery services written under Class 18, Schedule 1, Part 1 of the FSMA (Regulated Activities Order) 2001 (RAO) or a legal services help-line written under Class 17, Schedule 1, Part 1 of the RAO.

There are some exceptions such as pension fund management or surety, which can be provided by insurers. If you are in any doubt, contact the UoE or Deductions & Financial Services Team (see IPT08100) for guidance.

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What is the chargeable amount?

IPT will be due on that part of the gross premium which relates to the add-on insurance and which is due to the insurer offering the add-on insurance under the contract of insurance.

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Example 1

As part of a motor breakdown recovery insurance, each policyholder has a card which entitles him / her to call on a breakdown recovery service (supplied by a separate company), which will tow the car to a garage or the policyholder’s home. The cost to the insurer of the breakdown recovery service is £15 per policyholder. This cost is incorporated into the overall cost of the breakdown recovery insurance premium charged to the policyholder.

Regarding the supply by the separate company of the breakdown recovery service, there are three possibilities:

The supplier of the breakdown recovery service is not offering insurance (see paragraph 3.3 of Notice IPT 1). The supply of the breakdown recovery service is to the insurer. The supplier of the motor breakdown service does not have to account for IPT on his service (because it is not insurance) even though the cost of it (to the insurer) is included in the insurance premium charged to the policyholder by the insurer. The motor breakdown service does not become a supply of ‘insurance’ any more than does, for example, the supply of stationery received by the insurer, the cost of which may be incorporated into the premium. This is the situation described at d. in IPT08480.

The separate company is an authorised insurer providing the services under a Class 18 contract of insurance. There are two supplies of direct insurance to the policyholder: one of motor breakdown insurance by the Class 18 insurer, and one of the remaining cover by the other insurer. The policyholder will either have a single contract to which both insurers are party, or two contracts. The premium charged by each insurer will bear IPT, and each insurer is liable to account for IPT on their share of the premium. This is the situation described at b. in IPT08480.

An insurer providing the Class 18 motor breakdown insurance is providing insurance to the primary insurer (see c. in IPT08480). The primary insurer undertakes to ensure that the breakdown service is provided to the policyholder in certain circumstances. The primary insurer becomes liable to pay for the breakdown services, and he lays off the cost of this to a second insurer for a premium of £15 per policyholder. The second insurer procures the breakdown services in order to meet his obligations under the insurance contract with the primary insurer. The insurance premium paid by the direct insurer to the secondary insurer is subject to IPT, as is the premium paid by the policyholder to the primary insurer.

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