Simplify tax laws to improve insurance penetration

Governments around the world generally agree on the issue of incentivising buying of insurance policies, both life and non-life, through tax laws for achieving the twin objectives of promoting social security and mobilising long-term funds for economic development.

There are many ways of using taxation as a tool for achieving these goals, the simplest being allowing the premium amount as deductible from the total taxable income while computing tax liability of an individual or a legal entity

The other method is to exempt claims proceeds from any kind of tax, be it maturity or death claim amount, for life policies and the amount paid to indemnify loss of goods, property or any physical asset due to accident, fire theft or natural disaster, etc. In our country, a large segment of people look at insurance as a sure tool of escaping taxes on their income and, at the same time, are motivated to opt for insurance for long-term savings and for providing financial security to their family or business.

Over a period of time, tax implications and the exemption rules have become complicated and, at the same time, there have been uncertainties every year about how the tax treatment is going to be like following the Budget exercise by the government every year. The imposition of the service tax has further complicated tax issues and the perpetual uncertainties about the Direct Taxes Code has literally confused not only the buyers of a policy, but also the sellers.

Tax issues in insurance have far-reaching implications. When somebody decides to buy any insurance policy, he commits himself to its terms and conditions for a very long term. The existing tax law is also one of the factors influencing his decision and he would expect all such conditions to remain the same till he keeps renewing his policy in chain.

The tendency to fiddle with such rules frequently is, therefore, fraught with serious consequences, which may not only hamper growth, but also harm the interest of customers.

So far as tweaking with the slab of income for levying tax or the revision in tax rates are concerned, the industry should not have any concerns as these matters are decided in view of the total economic scenario and are subject to the government's discretion; but changing the basic structure of taxation may hamper growth of the industry. The following factors, therefore, may be considered by the policymakers:

The tax law should encourage people to buy adequate insurance cover. This would attract larger per capita fund and assist capital formation for development of the economy. Premium up to an amount of R1 lakh should be allowed for deduction from the taxable income.

To keep the rules simple, the ceiling should be exclusively for insurance premium and this should not be diluted by including other investments under the same umbrella. Such investments can be taken care separately.

This provision may attract a large number of customers and also ensure heavy flow of fund into the sector through the route of single premium, especially of those HNIs who want insurance, but want to avoid hassles of timely and regular premium payment for a very long period. It would be strategically wise to continue with the existing clause of Section 10(10D) for exempting proceeds of maturity or death claims. Other existing or new rules may continue as it is.

The medical premium for health policies should continue under Section 80D, but the ceiling of just R15,000 should be relaxed to any amount that is paid as premium. The restriction on amount of premium should be the effect of actuarial considerations and not of a common line drawn to have check on very high loss of revenue due to such deductions. Nobody would pay very high premium only to get this benefit. On the other hand, such liberalisation would encourage people to go for adequate coverage.

If a company pays premium to protect the value of its property through various non-life insurance schemes, it enjoys tax relief as all such premium are considered as business expense and, as a consequence, to the extent of the premium amount, the company’s net income is reduced for calculating tax liability.

A similar privilege should be extended to individuals if they pay premium for protecting life of self or family members against accident and other hazards and if they buy householders’ policies. This will go a long way in popularising the concept of insuring anything that has financial value around an individual.

Since the premium flow from individuals to non-life insurers outside the health segment is negligible, the loss of revenue to the government if the aforesaid suggestion is accepted will be of no consequence. But this may boost the premium income of the non-life insurers in a very big way, providing the society a scientific method of indemnifying loss to the few unfortunate individuals due to reasons beyond their control. If insurance replaces the government's occasional announcement of ex-gratia amount due to political or humanitarian ground, the government too would be protected against unexpected expenditure.

I think this initiative may help non-life insurers to achieve penetration level of 1%, which has been eluding the industry perpetually (life insurance penetration, not long back, peaked to 4.5%).

Keeping tax rules as simple as possible, so that individuals can compute their liabilities and permissible rebate themselves and plan their savings and tax payment efficiently, should be the essence of rules and law in this regard. Many people fail to take advantage of the government’s policies only because they are not able to hire somebody to assist them and the complexities and hassles involved force them to skip their obligations for paying taxes.

Energising the insurance sector

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