

# Decision impact statement

## Commissioner of Taxation v Hannover Life Re of Australasia Ltd

<b>Court citation/s:</b>	[2024] FCAFC 23 [2023] FCA 680
<b>Venue/s:</b>	Full Federal Court of Australia Federal Court of Australia
<b>Venue reference no/s:</b>	NSD 816/2023 NSD 288/2021
<b>Judge/AAT member name/s:</b>	Derrington, Thawley and Hespe JJ Stewart J
<b>Judgment date:</b>	4 March 2024 22 June 2023
<b>Appeals on foot:</b>	No
<b>Decision outcome:</b>	Partly favourable to the Commissioner

## Impacted advice



This decision has no impact on any related advice or guidance.

## Summary

This Decision impact statement outlines the ATO's response to this decision, which concerns the extent to which the taxpayer, a life insurer, is entitled to goods and services tax (GST) input tax credits for its acquisitions, when they make input taxed supplies of life insurance, as well as GST-free supplies of acquiring reinsurance.

All legislative references in this Decision impact statement are to the *A New Tax System (Goods and Services Tax) Act 1999* (GST Act), unless otherwise indicated.

## Brief summary of facts

Hannover Life Re of Australasia Ltd (Hannover) is a registered life insurance company. It is a wholly owned subsidiary of Hannover Rück SE (Hannover Rück), a non-resident company that operates a global reinsurance business.

Hannover's business consists of 3 categories (with each category allocated to a separate statutory fund for *Life Insurance Act 1995* purposes), all of which are financial supplies for GST purposes:

- (1) supplying life insurance policies to policyholders resident in Australia (input taxed supplies)
- (2) supplying reinsurance for life insurance policies issued by other Australian life insurers (input taxed supplies), and

- (3) supplying reinsurance for life insurance policies issued by non-resident New Zealand life insurers (GST-free supplies).

Hannover and Hannover Rück entered into numerous quota-share reinsurance agreements (reinsuring the risk of life insurance) for Category 1 above. They also entered into retrocession agreements (reinsuring the risk of reinsurance) for Categories 2 and 3 above. In both cases Hannover Rück accepted a specified percentage of the risk and reward of the relevant life insurance policies or reinsurance issued by Hannover.

An example of such a reinsurance agreement arose in the 'Greenstone arrangement'. A third party, Greenstone, distributed and administered certain life insurance policies (Greenstone life insurance policies) supplied by Hannover to resident policyholders. Hannover acquired reinsurance from Hannover Rück relating to these Greenstone life insurance policies. Under the terms of that reinsurance, Hannover Rück received a reinsurance premium equal to 75% of Hannover's premium income and was liable to Hannover for 75% of the claims liabilities and general expenses for the Greenstone life insurance policies.

It was not in dispute that, for GST purposes, the acquisition of reinsurance and retrocession from Hannover Rück was a financial supply (at the relevant time under subregulation 40.05.09(1) of the *A New Tax System (Goods and Services Tax) Regulations 1999*) made by Hannover (an 'acquisition-supply'), and that supply was GST-free (and therefore not input taxed under subsection 9-30(3) of the GST Act). These reinsurance and retrocession supplies will be referred to as 'GST-free reinsurance supplies'.

An entity is only entitled to input tax credits to the extent it acquires things for a creditable purpose under section 11-15. Acquisitions are not acquired for a creditable purpose to the extent that they relate to making input taxed supplies – paragraph 11-15(2)(a). If an acquisition is partly creditable the amount of the input tax credit is calculated under section 11-30.

The issue in dispute was the extent of creditable purpose for 2 categories of acquisitions:

- 'Greenstone' acquisitions, which were acquisitions of distribution and administration services supplied by Greenstone to assist Hannover in the supply of the Greenstone life insurance policies.
- 'Overhead' acquisitions, consisting of acquisitions such as rent, which Hannover had apportioned across all 3 of its statutory funds, rather than treating them as only relating to a particular life insurance or reinsurance product line or activity. This allocation of costs to its statutory funds was carried out by Hannover in the annual expense apportionment required under the *Life Insurance Act 1995*. The creditable purpose of overheads relating to New Zealand Category 3 supplies was not in dispute.

The Commissioner contended that the acquisitions related to input taxed supplies. Hannover contended that they partly related to the GST-free reinsurance supplies.

Hannover's proposed revenue-based apportionment method for the purposes of section 11-30 for the overhead acquisitions meant that those acquisitions were acquired for a creditable purpose, to the extent that risk was ceded to Hannover Rück under the GST-free reinsurance supplies.

## Issues decided by the Courts

### Creditable purpose of distribution and administrative services

At first instance in *Hannover Life Re of Australasia Ltd v Commissioner of Taxation* [2023] FCA 680 (*Hannover FCA*), Stewart J concluded that the Greenstone acquisitions were wholly related to making input taxed supplies of life insurance to Hannover's Australian policyholders, and the Greenstone acquisitions did not have a relevant relationship to the GST-free reinsurance supply for the purposes of paragraph 11-15(2)(a).<sup>1</sup>

The relevant factors in reaching this conclusion were that the services supplied by Greenstone were specifically referable to the Greenstone life insurance policies. The cessation of risk arose under the reinsurance agreement (not under the agreement with Greenstone), and the reinsurance effected no change in the relationship between Hannover and its policyholders.<sup>2</sup> That conclusion was not affected by the fact that, but for the GST-free reinsurance supplies entered into with Hannover Rück, the relevant input taxed supplies could not have been made. Consequently, Hannover was not entitled to input tax credits for the Greenstone acquisitions.<sup>3</sup>

While Hannover did not cross-appeal in relation to the Greenstone acquisitions, the Full Court observed that the primary judge's conclusions that those acquisitions related solely to the making of supplies that would be input taxed, and related in no real way to the GST-free reinsurance supplies were 'not contentious'.<sup>4</sup>

### Creditable purpose of overhead acquisitions

At first instance, the Commissioner was unsuccessful in respect of the application of paragraph 11-15(2)(a) to the overhead acquisitions. Stewart J held that those acquisitions related indifferently to all activities of the enterprise<sup>5</sup>, and had a relevant relationship to the GST-free reinsurance supplies.<sup>6</sup> Subject to one modification not presently relevant, Hannover's proposed apportionment method under section 11-30 was held to be fair and reasonable.<sup>7</sup>

The Commissioner appealed the first instance decision in relation to the overhead acquisitions.

The Full Court considered that the primary judge had to undertake an evaluative exercise, to make a judgment about the application of paragraph 11-15(2)(a) to the overhead acquisitions.<sup>8</sup>

The Full Court considered that determining the extent to which an acquisition relates to making input taxed supplies under paragraph 11-15(2)(a) also requires an assessment of whether there is real and substantial connection between that acquisition and any GST-free [or taxable] supplies.<sup>9</sup>

In addition to Stewart J's point at first instance that Hannover's unchallenged evidence that the overheads were not directly attributable to particular activities or product lines<sup>10</sup> must be accepted, the Full Court found that there was evidence that

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<sup>1</sup> *Hannover FCA* at [70].

<sup>2</sup> *Hannover FCA* at [70].

<sup>3</sup> *Hannover FCA* at [71].

<sup>4</sup> *Commissioner of Taxation v Hannover Life Re of Australasia Ltd* [2024] FCAFC 23 (*Hannover FCAFC*) at [8].

<sup>5</sup> *Hannover FCA* at [89].

<sup>6</sup> *Hannover FCA* at [82].

<sup>7</sup> *Hannover FCA* at [101].

<sup>8</sup> *Hannover FCAFC* at [30].

<sup>9</sup> *Hannover FCAFC* at [23].

<sup>10</sup> *Hannover FCA* at [87] and [89].

indicated that various administrative, legal and financial resources were applied to the various GST-free reinsurance supplies during Hannover's operations.<sup>11</sup> The Full Court concluded that the overhead acquisitions related to both input taxed and GST-free supplies, as the Commissioner had not identified any error in the primary judge's findings<sup>12</sup>, that the acquisitions were undifferentiated, or related indifferently to all supplies made by the enterprise.<sup>13</sup>

The Full Court noted that the 'wholly by and through' expression used in *Rio Tinto Services Limited v Commissioner of Taxation* [2015] FCAFC 117 (*Rio Tinto*) was an expression of a factual conclusion, and the statute requires a judgment about the relationship between an acquisition and the making of supplies.<sup>14</sup>

In relation to the apportionment method under section 11-30, the Full Court did not consider it relevant to assess if the method was fair and reasonable based on a hypothetical scenario where 100% of the risk was reinsured. The Full Court confirmed the primary judge's conclusion that the apportionment method was only to apply to this specific known case, where there was 75% of the risk reinsured.<sup>15</sup>

## ATO view of decision

The Commissioner accepts the decision regarding the taxpayer's input tax credit entitlement for the overhead acquisitions was open to the Full Court, based on the primary judge's factual evaluation of the evidence before the Court at first instance.

### Determining extent of creditable purpose

The Commissioner's approach to section 11-15 is consistent with the Full Court's observations on the statutory operation of section 11-15.<sup>16</sup>

These decisions confirm that the application of section 11-15 is focused on the precise nature of the relationship between an acquisition and the supplies made by the entity.<sup>17</sup> The fact that an input taxed supply is interdependent, and cannot be made without a GST-free or taxable supply also being made<sup>18</sup>, or that other supplies may arise automatically as a result of the making of an input taxed supply, will not in itself determine the creditable purpose of the relevant acquisition.<sup>19</sup>

In relation to acquisitions that do not relate solely to input taxed supplies, the Full Court confirmed the Commissioner's position, consistent with *Ronpibon Tin NL v Commissioner of Taxation (Cth)* [1949] HCA 15 and *Rio Tinto*, that it is an error to assume that because an acquisition does not relate specifically to one supply it must therefore relate indifferently to all supplies.<sup>20</sup> Further, as observed by the Full Court, where an acquisition relates to more than one type of supply, the extent of the relationship between the different classes of supplies is a question of fact.<sup>21</sup>

### Creditable purpose of overhead acquisitions

The Commissioner considers that the primary judge's conclusions in relation to the 'overhead' acquisitions consisted of an evaluative factual judgment of Hannover's

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<sup>11</sup> *Hannover* FCAFC at [31].

<sup>12</sup> *Hannover* FCAFC at [32].

<sup>13</sup> *Hannover* FCA at [76], [79] and [89].

<sup>14</sup> *Hannover* FCAFC at [28].

<sup>15</sup> *Hannover* FCAFC at [39]; *Hannover* FCA at [96].

<sup>16</sup> *Hannover* FCAFC at [19].

<sup>17</sup> *Hannover* FCAFC at [28].

<sup>18</sup> *Hannover* FCA at [70-71].

<sup>19</sup> *Hannover* FCA at [70] and [86]; *Hannover* FCAFC at [25].

<sup>20</sup> *Hannover* FCAFC at [31].

<sup>21</sup> *Hannover* FCAFC at [19].

unchallenged evidence before the Court, relating to the nature of the overhead acquisitions, and how Hannover had allocated those acquisitions across its 3 categories of life insurance and reinsurance products.<sup>22</sup>

When applying section 11-15 to their own circumstances, the Commissioner expects taxpayers to evidence that they have precisely identified the relevant acquisition<sup>23</sup>, and undertaken a factual enquiry into the connection between their own specific acquisitions and supplies, to determine if, and the extent to which, an acquisition relates to one or more different classes of supplies. Taxpayers should not assume that the same outcome will follow merely because their circumstances have some similarities to this case.

The mere fact that an acquisition may be labelled an 'overhead' or has a description or label similar to the individual overhead acquisitions in this case, does not necessarily mean that the acquisition relates to all supplies made by an entity, nor that it is undifferentiated such that it relates indifferently to all supplies. For example, it will be a question of fact whether something described as an 'advertising expense' relates only to specific supplies or relates to all supplies made by an enterprise.<sup>24</sup>

The Commissioner's views on identifying acquisitions that do not directly relate to a specific type of supply (being overheads or enterprise costs) are set out in paragraphs 136 to 148 of Goods and Services Tax Ruling GSTR 2008/1 *Goods and services tax: when do you acquire anything or import goods solely or partly for a creditable purpose?*

### **Apportionment methods for the purposes of section 11-30**

The Commissioner considers that the primary judge's observations in relation to the impacts where a life insurer can be seen as a 'mere conduit' for its reinsurer<sup>25</sup>, in a hypothetical example where 100% of the risk is reinsured, are *obiter*. These observations were not necessary to decide the matter<sup>26</sup>, and the Full Court did not confirm these particular observations.<sup>27</sup> In circumstances where the facts and evidence support a conclusion that particular acquisitions are partly creditable under section 11-15, the Commissioner considers that the application of an apportionment method for the purposes of section 11-30 must also be consistent and produce a partly creditable extent of creditable purpose for those acquisitions.

While the Commissioner accepts that there may be more than one methodology that is fair and reasonable in any given factual circumstance, the Commissioner does not consider that the fact a specific apportionment method was allowed in this case represents an endorsement of the method as fair and reasonable in other circumstances.

The Commissioner's views on when apportionment methods, including revenue-based methods, are fair and reasonable are set out in:

- Goods and Services Tax Ruling GSTR 2006/3 *Goods and services tax: determining the extent of creditable purpose for providers of financial supplies*, and
- Goods and Services Tax Ruling GSTR 2006/4 *Goods and services tax: determining the extent of creditable purpose for claiming input tax*

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<sup>22</sup> *Hannover FCA* [87] and [89].

<sup>23</sup> *Hannover FCA* at [67].

<sup>24</sup> *Hannover FCA* at [89].

<sup>25</sup> *Hannover FCA* at [95].

<sup>26</sup> *Hannover FCA* at [96].

<sup>27</sup> *Hannover FCAFC* at [36–39].

*credits and for making adjustments for changes in extent of creditable purpose.*

## Comments

We invite you to advise us if you feel this decision has consequences we have not identified. Please forward your comments to the contact officer.

**Date issued:** 15 May 2024

**Contact officer details have been removed as the comments period has expired.**

**Legislative references**

ANTS(GST)A 1999 9-30(3)  
ANTS(GST)A 1999 11-5  
ANTS(GST)A 1999 11-5(2)  
ANTS(GST)A 1999 11-15(2)(a)  
ANTS(GST)A 1999 11-30  
ANTS(GST)R 1999 40-05.09(1)  
Life Insurance Act 1995

**Case references**

Commissioner of Taxation v Hannover Life Re of Australasia Ltd [2024] FCAFC 23;  
2024 ATC 20-895  
Hannover Life Re of Australasia Ltd v Commissioner of Taxation [2023] FCA 680;  
117 ATR 1; 2023 ATC 20-870  
Rio Tinto Services Limited v Commissioner of Taxation [2015] FCAFC 117; 235 FCR  
159; 2015 ATC 20-525  
Rio Tinto Services Ltd v Commissioner of Taxation [2015] FCA 94; 98 ATR 390;  
2015 ATC 20-489  
Ronpibon Tin NL v Commissioner of Taxation (Cth) [1949] HCA 15; 78 CLR 47;  
[1949] ALR 785; 8 ATD 431

**Relevant rulings**

GSTR 2006/3; GSTR 2006/4; GSTR 2008/1

**ATO references**

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