

2011

EXPOSURE DRAFT

GST-FREE HEALTH SUPPLIES

EXPLANATORY MEMORANDUM

(Circulated by the authority of the
Deputy Prime Minister and Treasurer, the Hon Wayne Swan MP)

Chapter 1

GST-free health supplies

Outline of chapter

1.1 The attached Schedule amends the *A New Tax System (Goods and Services Tax) Act 1999* (GST Act) to ensure that certain supplies made to insurers in settling insurance claims under both private health insurance policies and taxable insurance policies are GST-free where the underlying supply to the insured (policy holder or third party) is GST-free under Subdivision 38-B of the GST Act.

1.2 The proposed amendments further clarify that supplies made under a compulsory third party (CTP) scheme are GST-free supplies where the underlying supply of health related goods or services to the individual is GST-free under Subdivision 38-B of the GST Act.

1.3 The proposed amendments also ensure that certain supplies made by health care providers to a Commonwealth, State or Territory government entity are GST-free where the underlying supply of health related goods or services to the individual is GST-free under Subdivision 38-B of the GST Act.

1.4 Moreover, the proposed amendments allow the supplier and a recipient to agree that a supply is not a GST-free supply, but is instead a taxable supply.

1.5 The provisions will take effect from 1 July 2012.

Context of amendments

1.6 Under Subdivision 38-B of the GST Act, certain health related supplies are GST-free, including most supplies of medical services (section 38-7), hospital treatment (section 38-20) and other health services (section 38-10).

1.7 In some instances, these supplies are made under multi-party arrangements where a health care provider supplies GST-free health related goods or services to a person and the health care provider receives a payment from an insurer or a government entity.

1.8 The Full Federal Court decision in *Commissioner of Taxation v Secretary to the Department (Victoria)* [2010] FCAFC 84 (*Department of Transport*), handed down on 9 July 2010, considered an arrangement entered into by the Victorian Department of Transport with taxi operators for the provision of subsidised taxi services to disabled passengers.

1.9 The Commissioner had denied the Department's claim for input tax credits in respect of the subsidy payments on the basis that there was no taxable supply between the taxi operator and the Department. The Full Federal Court held that a taxable supply was made by a taxi operator to the Victorian Department of Transport, and as a result, the Department was entitled to an input tax credit in relation to the GST component of the payment of the subsidy to the taxi operator.

1.10 Whilst the specific facts of the case related to a government funding arrangement, the Court took a considerably broader approach in characterising multi-party arrangements than that previously taken by the Commissioner. In particular, the decision has the potential to impact on certain multi-party arrangements involving supplies to individuals of GST-free health related goods and services made in settlement of claims made under GST-free private health insurance and taxable insurance policies, under compulsory third party (CTP) schemes and in relation to certain government health funding arrangements.

1.11 Prior to the decision, the Commissioner generally treated these affected arrangements as involving a single GST-free supply with the payment from the third party being consideration for that supply (GSTR 2006/9 'Goods and services tax: supplies'). The effect of the decision is that in certain circumstances there would now be two supplies by health care providers – one GST-free supply to the individual actually receiving the GST-free health related goods and services, and a taxable supply to the third party making the payment.

1.12 This creates compliance issues and administrative costs for health care providers and affected third parties as it requires them to account for a taxable supply when previously they did not need to. These entities would also need to alter their arrangements and put systems in place to account for GST on these supplies.

1.13 The amendments are intended to avoid these unintended outcomes and to ensure that certain supplies of health related goods and services continue to be GST-free when they involve multi-party payment arrangements.

1.14 When originally announced, retrospective amendment of the GST law to 1 July 2000 was considered appropriate. However, retrospective application is no longer considered necessary because

certain supplies previously treated as taxable will now be treated as GST-free. Retrospective application would result in compliance costs to alter the GST treatment for these past supplies. In addition, entities will be protected from paying any underpaid GST if they have relied on the ATO's ruling (GSTR 2006/9) to treat supplies as non-taxable. As no GST will have been paid in acquiring these supplies, the insurer or other third party acquirer will not be disadvantaged by prospective application.

Summary of new law

1.15 The attached Schedule inserts new section 38-60 to ensure that the supply of a service to make a supply to an individual is GST-free under Subdivision 38-B where the underlying supply to the individual is also GST-free under Subdivision 38-B and the supply is to:

- an insurer in settling a claim under a GST-free health or taxable insurance policy;
- an operator of a CTP scheme under a CTP scheme; or
- an Australian government agency.

1.16 The result in all these cases is that there is no separate taxable supply made by the health care provider to the insurer, operator of the CTP scheme or Australian government agency.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
A supply to an insurer of a service of making a supply of GST free health related goods or services to an individual for settling claims under an insurance policy is GST free.	A supply by a health care provider of a service of making a supply of GST-free health related goods or services to an individual that is paid for by an insurer, operator of a CTP scheme or a Commonwealth, State or Territory government entity is a taxable supply.
A supply to an operator of a CTP scheme of a service of making a supply of GST-free health related goods or services under a CTP scheme is GST free.	As above.
A supply to an Australian	As above.

government agency of a service of making a supply of GST-free health related goods or services to an individual is GST-free.	
The health care provider will be able to agree with the insurer, operator of the CTP scheme or Australian government agency to treat the service of making the supply of the GST-free health related goods and services as a taxable supply.	No equivalent.

Detailed explanation of new law

Private health insurance

1.17 If a supply by a health care provider to an insured person is GST-free under Subdivision 38-B of the GST Act (the underlying supply), then a supply of the service of making the underlying supply by the health care provider to an insurer in the course of settling insurance claims under a private health insurance policy is GST-free. [*Schedule #, item 1, subsection 38-60(1)*]

Example 1.1

Peter purchases private health insurance from a health insurer and pays an annual contribution. The health insurer has a pre-existing agreement with a physiotherapist where services are supplied to individuals for the purposes of settling claims made under insurance policies that it issues. The agreement outlines how the parties will act when the physiotherapist treats the identified individuals. The agreement also establishes the obligation on the health insurer to pay the physiotherapist if the physiotherapist provides services to the identified individuals and a mechanism by which such payments are to be authorised.

Peter injures his knee playing sport and requires physiotherapy. Peter contacts the health insurer advising of his injury. The health insurer refers Peter to the physiotherapist who supplies physiotherapy services to Peter. The supplies of the physiotherapy services are GST-free under subsection 38-10(1). The health insurer pays the physiotherapist for the services under the terms of the pre-existing agreement.

Peter's physiotherapist makes a GST-free supply to the health insurer under subsection 38-60(1). This is because:

- the supply made by the physiotherapist is a supply of a service to an insurer;
- the service is the physiotherapist making one or more supplies of services to an individual (Peter);
- the supplies made by the physiotherapist to Peter are GST-free under Subdivision 38-B; and
- the supplies are made for settling one or more claims under an insurance policy of which the health insurer is an insurer.

Note that the outcome in this example would be the same even if the health insurer and physiotherapist had no pre-existing agreement but instead the insurer contracted with the physiotherapist to provide the services.

Workers' compensation, compulsory third party schemes and other insurance

1.18 If a supply by a health care provider to an individual is GST-free under Subdivision 38-B of the GST Act (the underlying supply), then a supply of the service of making the underlying supply by the health care provider to an insurer for settling a claim under either a general insurance policy or a health insurance policy is GST-free. *[Schedule #, item 1, subsection 38-60(1)]*

1.19 If a supply by a health care provider to an individual is GST-free under Subdivision 38-B of the GST Act (the underlying supply), then a supply of the service of making the underlying supply by the health care provider to an insurer or operator of a CTP scheme under a workers' compensation or CTP scheme is GST-free. *[Schedule #, item 1, subsection 38-60(2)]*

Government health funding arrangements

1.20 If a supply by a health care provider to an individual is GST-free under Subdivision 38-B of the GST Act (the underlying supply) then a supply of the service of making the underlying supply by the health care provider to an Australian government agency is GST-free. *[Schedule #, item 1, subsection 38-60(3)]*

Example 1.2

An Australian government agency implements a program to fund specified health services for individuals that satisfy specific criteria. The program establishes a framework under which the Australian

government agency agrees to pay participating health service providers for services supplied to individuals that satisfy specific criteria.

Eligible individuals are issued a program card which may be presented to the health service provider, in which case they are not charged a fee for the services performed. Upon supplying the service to the eligible individual, the health service provider notifies the Australian government agency in accordance with the established framework and the Australian government agency makes a payment to the health service provider for which it is liable.

Lorraine satisfies the eligibility criteria under the program and is issued a program card by the Australian government agency. Lorraine attends her local doctor's surgery to receive treatment for a medical condition. The treatment is GST-free under subsection 38-7(1). The doctor is a participant in the program. The doctor is also registered for GST. Lorraine presents her program card and is not charged a fee. The doctor notifies the Australian government agency in accordance with the established framework that she has made a supply to Lorraine. The Australian government agency pays the doctor \$100 in respect of the service the doctor supplied to Lorraine.

The supply made by the doctor to the Australian government agency is GST-free under subsection 38-60(3) as:

- the supply made by the doctor is a supply of a service to an Australian government agency;
- the service is the doctor making one or more supplies of services to an individual (Lorraine); and
- the supply made by the doctor to Lorraine is GST-free under Subdivision 38-B.

As the supply the doctor makes to the Australian government agency is GST-free, the doctor does not have to pay GST for the supply. The Australian government agency cannot claim an input tax credit for the acquisition it makes from the doctor as the supply made by the doctor was not a taxable supply (see paragraph 11-5(b)).

If the supply made by the doctor to Lorraine was not a GST-free supply under Subdivision 38-B, then the supply by the doctor to the Australian government agency would not be a GST-free supply.

Option to treat as taxable

1.21 Some entities have a variety of arrangements with health care providers where a range of supplies are made to individuals. Depending on the nature and terms of the particular arrangement, some supplies will be GST-free and some will be taxable. Health care providers and the recipient of the supply (the insurer, operator of the CTP scheme or Australian government agency) will be able to agree to treat them as taxable. *[Schedule #, item 1, subsection 38-60(4)]*

1.22 It is expected that providing this option will reduce compliance costs, with no adverse effects to the individual receiving these goods and services. A similar mechanism currently exists in relation to supplies of medical aids and appliances and goods declared by the Minister for Health to be GST-free.

Application provisions

1.23 The amendments made by this Schedule apply in relation to supplies of services to insurers, operators of CTP schemes or Australian government agencies made on or after 1 July 2012. New subsection 38-60(4) will apply in relation to agreements made before, on or after 1 July 2012. This will allow agreements to be made in respect of supplies that will be made on or after 1 July 2012. *[Schedule #, item 5]*

Consequential amendments

1.24 Subsections 78-118(1) and 78-118(2) of the GST Act are amended to ensure that insurance policies under a portfolio transfer are covered by the amendments by specifying that both subsection 38-60(1) and Division 78 apply to portfolio transfers under the section. *[Schedule #, item 2, subsection 78-118(1); item 4, paragraph 28-118(2)(a)]*

1.25 Similarly, a note is inserted at the end of subsection 78-118(1) of the GST Act to clarify that subsection 38-60(1) provides that certain supplies to insurers are GST-free. *[Schedule #, item 3, subsection 78-118(1)]*