

2010

EXPOSURE DRAFT

TAX LAWS AMENDMENT BILL (5) 2010

EXPLANATORY MATERIAL

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Treasurer, the Hon Wayne Swan MP)

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Glossary

The following abbreviations and acronyms are used throughout this explanatory material.

<i>Abbreviation</i>	<i>Definition</i>
ITAA 1997	<i>Income Tax Assessment Act 1997</i>
ITA Regulations	<i>Income Tax Assessment Regulations 1997</i>
RSA provider	Retirement Savings Account Provider
RSA Regulations	<i>Retirement Savings Accounts Regulations 1997</i>
SIS Regulations	Superannuation Industry (Supervision) Regulations 1994
TMC	terminal medical condition

Chapter #

Deductions in relation to benefits for terminal medical conditions

Outline of chapter

- 1.1 Schedule # to this exposure draft extends the benefits in section 295-460 of the *Income Tax Assessment Act 1997* (ITAA 1997) to include terminal medical condition (TMC) benefits. The benefits in section 295-460 are benefits in relation to which complying superannuation funds and retirement savings account (RSA) providers can claim a deduction.
- 1.2 This measure will have effect from 16 February 2008.
- 1.3 All legislative references in this chapter are to the ITAA 1997 unless otherwise stated.

Context of amendments

The 'terminal medical condition' condition of release

1.4 In February 2008, the *Superannuation Industry (Supervision) Regulations 1994* (SIS Regulations) were amended to allow for the release of benefits to a member in the event of a TMC. This provision became effective from 16 February 2008.

1.5 A TMC is defined in the SIS Regulations as existing in relation to a person at a particular time if the following circumstances exist:

- two registered medical practitioners have certified, jointly or separately, that the person suffers from an illness, or has incurred an injury, that is likely to result in the death of the person within a period (the certification period) that ends not more than 12 months after the date of the certification;
- at least one of the registered medical practitioners is a specialist practicing in an area related to the illness or injury suffered by the person; and

- for each of the certificates, the certification period has not ended.

1.6 Identical definitions of 'terminal medical condition' are contained in the *Income Tax Assessment Regulations 1997* (ITA regulations), which applies to the ITAA 1997, and the *Retirement Savings Accounts Regulations 1997* (RSA Regulations).

Insurance provided through superannuation funds

1.7 Superannuation funds commonly take out death and disability insurance policies to insure their risk for a liability they may incur to their members.

1.8 Superannuation funds obtaining insurance for this purpose is consistent with the key objective of superannuation. That is, to provide benefits to members in retirement or, in the event of the member's death, to the member's beneficiaries.

1.9 Currently, a complying fund which provides certain death, disability superannuation benefits (in the case of a member's permanent incapacity) and temporary incapacity benefits can claim a deduction related to the cost of providing these benefits. The quantum of the deduction can be calculated based on either a premiums basis or by using a formula based on actual costs. An RSA provider can claim a deduction relating to the provision of these benefits on a premiums basis.

1.10 There are no associated deductions available in respect of TMC benefits.

Budget announcement

1.11 The Treasurer announced in the 2010 Budget that amendments would be made to extend the range of benefits that are deductible by complying superannuation funds and RSA providers to include TMC benefits.

Summary of new law

1.12 Schedule # to this exposure draft amends the ITAA 1997 to allow complying superannuation funds and RSA providers to deduct the cost of providing TMC benefits to members.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
Complying superannuation funds and RSA providers are able to claim deductions for insurance policies or some of the cost of providing benefits relating to the death, permanent incapacity, temporary incapacity, and TMC conditions of release.	Complying superannuation funds and RSA providers are able to claim deductions for insurance policies or some of the cost of providing benefits relating to the death, permanent incapacity and temporary incapacity conditions of release, but not those relating to the TMC condition of release.

Detailed explanation of new law

1.13 Currently, deductions are allowable for insurance policies to cover liabilities to pay benefits relating to the death, permanent incapacity and temporary incapacity conditions of release, but not those relating to the TMC condition of release. These amendments to the ITAA 1997 allow complying superannuation funds and RSA providers to claim a deduction for the cost of providing TMC benefits.

1.14 A new paragraph is inserted into section 295-460 of the ITAA 1997 to include a benefit payable to a person because they have a terminal medical condition. *[Schedule 1, item 1, paragraph 295-460(aa)]*

1.15 The term 'terminal medical condition' is defined in section 995-1 of the ITAA 1997 and has the same meaning in this section as in regulation 303-10.01 of the ITA regulations. This definition is the same as the definition in the SIS regulations and the RSA regulations. (For more information please refer back to 'Context of amendments' paragraphs 1.4-1.6.). *[Schedule 1, item 1, paragraph 295-460(aa), section 303-10, regulation 303-10.01 of the ITA Regulations]*

1.16 The inclusion of TMC benefits in section 295-460 of the ITAA 1997, in effect, allows complying superannuation funds and RSA providers a deduction for the cost of providing these benefits to members. This section interacts with sections 295-465, 295-470 and 295-475 which specify how this deduction operates. *[Schedule 1, item 1, paragraph 295-460(aa)]*

Operation

1.17 Section 295-460 of the ITAA 1997 lists the benefits for which a deduction is available under several other sections.

1.18 Subsection 295-465(1) allows deductions relating to premiums paid for insurance policies by complying superannuation funds for a liability to provide benefits referred to in section 295-460.

1.19 Under item 5 of the table in subsection 295-465(1), funds can deduct specified amounts that are part of a premium that is wholly for the liability to provide benefits referred to in section 295-460. Under item 6, funds can deduct so much of premiums that are attributable to the liability to provide section 295-460 benefits. An actuary's certificate is required in order to apportion premiums under item 6.

Example 1.1

Maths Super fund takes out insurance in relation to its members in June 2008 for death cover which includes terminal illness cover. In its trust deed, Maths Super Fund specifically provides a liability on the trustee to pay a TMC benefit to members.

The premium paid by Maths Super Fund would be fully deductible under item 5 of subsection 295-465(1) of the ITAA 1997. The premium applies fully to a period after 16 February 2008 and any liability to provide benefits insured for would be after that date. The premium relates fully to benefits listed in section 295-460 for which deductions are available; it relates partly to a liability of the fund to provide TMC benefits to members (paragraph 295-460(aa)), and partly to a liability to provide death benefits (paragraph 295-460(a)).

1.20 Subsection 295-465(2) allows a complying fund to claim a deduction for an amount it could reasonably be expected to pay in an arms length transaction to obtain an insurance policy to cover that part of its current or contingent liabilities to provide benefits referred to in section 295-460 for which the complying fund does not have insurance coverage.

1.21 Section 295-470 allows a complying superannuation fund to choose to deduct an amount for a future liability to pay benefits referred to in section 295-460, using a formula based on the actual cost of providing the benefits which arise each year.

1.22 A fund can deduct amounts under either section 295-465 or section 295-470 but not both.

1.23 Section 295-475 allows an RSA provider to deduct premiums for insurance policies that are wholly for its liability to provide benefits referred to in section 295-460.

Consequential amendments

1.24 In order to ensure that a deduction for a TMC benefit can be claimed under subparagraph 295-470(1)(b)(i), this section is amended to include a reference to the new paragraph 295-460(aa). *[Schedule 1, item 2, paragraph 295-460(aa) and paragraph 295-470(1)(b)(i)]*

Application provision

1.25 These amendments apply in relation to a current or contingent liability of a complying superannuation fund to provide TMC benefits on or after 16 February 2008. This is appropriate as the TMC condition of release was introduced on this date meaning that no such benefit would have been provided prior to this. *[Schedule 1, item 3]*

1.26 In cases where insurance policies begin before and end after 16 February 2008, superannuation funds may require an actuary to determine what part of the premium is attributable to the period after that date and therefore deductible under item 6 of the table in subsection 295-465(1). However, subsection 295-465(3) requires an actuary's certificate be obtained before the date of lodgement of a fund's income tax return. This may be problematic for superannuation funds which did not require an actuary's certificate or obtained one which excluded TMC benefits when they made their lodgement. Accordingly, a transitional provision modifies the application of subsection 295-465(3) for superannuation funds in such a position that apply for an amendment of their assessment so that the fund may obtain an actuary's certificate prior to the request for reassessment. *[Schedule 1, items 3 and 4]*