


***TR 2010/D9 - Income tax: deductibility under subsection 295-465(1) of the Income Tax Assessment Act 1997 of premiums paid by a complying superannuation fund for an insurance policy providing Total and Permanent Disability cover in respect of its members***

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## Draft Taxation Ruling

Income tax: deductibility under subsection 295-465(1) of the *Income Tax Assessment Act 1997* of premiums paid by a complying superannuation fund for an insurance policy providing Total and Permanent Disability cover in respect of its members

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## What this Ruling is about

1. This draft Ruling is concerned with issues relating to the deductibility under subsection 295-465(1) of the *Income Tax Assessment Act 1997* (ITAA 1997)<sup>1</sup> of premiums paid by a complying superannuation fund for insurance policies which provide total and permanent disability (TPD) cover in respect of the fund’s members.

2. In particular this draft Ruling deals with:

- The Commissioner’s view on how subsection 295-465(1) together with paragraph 295-460(b) applies to such premiums.

<sup>1</sup> All legislative references are to the ITAA 1997 unless otherwise indicated.

- The relationship between the deductibility of the premiums and the rules for the provision of benefits by a complying superannuation fund to its members as set out in the *Superannuation Industry (Supervision) Act 1993 (SISA)* and the *Supervision Industry (Supervision) Regulations 1994 (SISR)*.
3. The relevant provisions applied in this draft Ruling are:
- Section 295-460;
  - Section 295-465; and
  - Section 995-1.
4. This draft Ruling does not explain the deductibility of premiums paid by a fund for life insurance policies on the death of a member,<sup>2</sup> premiums paid for temporary disablement policies<sup>3</sup> and premiums paid for terminal illness cover or the cost of self insurance.<sup>4</sup>
5. This draft Ruling also does not deal with the application of former section 279 of the *Income Tax Assessment Act 1936* (ITAA 1936) and the transitional provisions that extend the definition of ‘disability superannuation benefits’ for the purposes of subsection 295-465(1) of the ITAA 1997 for the 2007-2008 to 2010-2011 income years.<sup>5</sup>

## Definitions

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### ‘TPD insurance policy’

6. In this draft Ruling TPD insurance policy means an insurance policy purchased by the trustee of a complying superannuation fund from an insurance company to insure the fund’s liability against total and permanent disability the members of the fund may suffer. For the purpose of this draft Ruling a TPD insurance policy may, in addition to the insurance against the liability the fund may have for TPD benefits, insure against the fund’s liability to provide other benefits to or in respect of members, for example death benefits.

### ‘TPD benefits’

7. In this draft Ruling the term TPD benefits means benefits paid under the terms of a TPD insurance policy when an insured event occurs to a member.

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<sup>2</sup> Paragraph (a) of section 295-460.

<sup>3</sup> Paragraph (c) of section 295-460.

<sup>4</sup> Subsection 295-465(2).

<sup>5</sup> Section 295-466 of the *Income Tax (Transitional Provisions) Act 1997*.

**‘insured event’**

8. A TPD insurance policy will specify certain events the occurrence of which will give rise to the insurer’s liability and the insured’s right to claim a benefit under the policy.

9. For example, an insured event under a TPD insurance policy could include a member of the superannuation fund suffering an illness or injury such that it is unlikely the member will ever be able to perform the duties of any occupation, business, profession or employment for which the person is reasonably suited by education, training or experience.

**‘complying superannuation fund’**

10. In this draft Ruling the term complying superannuation fund means a complying superannuation fund within the meaning of section 45 of the SISA.<sup>6</sup>

**‘preserved benefits’**

11. In this draft Ruling the term preserved benefits has the meaning in Subdivision 6.1.2 of Part 6 of the SISR. A member’s preserved benefits in a regulated superannuation fund may only be cashed on or after the satisfaction by the member of a condition of release.

**‘condition of release’**

12. In this draft Ruling the term condition of release means a condition of release specified in Column 2 of Schedule 1 to the SISR.

## **Ruling**

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**Deductibility of premiums under subsection 295-465(1)**

13. The test in subsection 295-465(1) is whether the superannuation fund has a current or contingent liability to provide a ‘disability superannuation benefit’, which is referred to in paragraph 295-460(b), to its members.

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<sup>6</sup> Refer to the definition in subsection 995-1(1).

14. For an insurance premium on a TPD insurance policy paid by a complying superannuation fund to be deductible, subsection 295-465(1) requires a connection between that payment and a current or contingent liability of the fund to provide a 'disability superannuation benefit'<sup>7</sup> referred to in paragraph 295-460(b).

15. The premium paid for the TPD insurance policy may be wholly or partly in respect of the provision of 'disability superannuation benefits'. The extent to which a premium will be in respect of the fund's liability to provide 'disability superannuation benefits' is determined by reference to the nature and scope of the insured event(s).

16. The trustee of a complying superannuation fund will have a current or contingent liability to provide a benefit to or in respect of a fund member where, upon the happening of a specified event or the occurrence of a particular situation, an obligation upon the trustee to provide that benefit arises under or in accordance with the terms of the fund trust deed.

17. The likelihood of the insured event occurring does not affect the deductibility of premiums paid by the fund. This is made clear by the reference to contingent liability in subsection 295-465(1). Premiums will be deductible even though it is most likely that a payout may never be made under the policy because the insured event may not occur.

18. The critical variable to take into account in determining the extent to which an insurance premium paid by a complying superannuation fund for a TPD insurance policy is deductible is the degree of certainty of the requirements of the 'disability superannuation benefit' definition in subsection 995-1(1) being met as a consequence of an insured event happening.

### ***Sole purpose***

19. The sole purpose test in section 62 of the SISA prohibits trustees from maintaining a complying superannuation fund for purposes other than the provision of benefits specified in subsection 62(1) of the SISA. Consistent with the sole purpose test, subregulation 6.18(1) of the SISR provides that a member's preserved benefits in a complying superannuation fund may be cashed on or after the satisfaction by the member of a condition of release.

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<sup>7</sup> Defined in subsection 995-1(1) as follows:

a \*superannuation benefit if:

- (a) the benefit is paid to a person because he or she suffers from ill-health (whether physical or mental); and
- (b) 2 legally qualified medical practitioners have certified that, because of the ill-health, it is unlikely that the person can ever be \*gainfully employed in a capacity for which he or she is reasonably qualified because of education, experience or training.

20. The condition of release for permanent incapacity (item 103 of Schedule 1 to the SISR) is the relevant condition of release that a member must satisfy in order for a superannuation fund to provide a 'disability superannuation benefit' referred to in paragraph 295-460(b).

21. In circumstances where the degree of ill-health suffered by a member would result in the requirements of the 'disability superannuation benefit' definition in subsection 995-1(1) being satisfied, the member would at that point in time also satisfy the condition of release for permanent incapacity.

***Deduction for specified part of the premium under item 5 in the table in subsection 295-465(1)***

22. Item 5 in the table in subsection 295-465(1) will apply to allow a deduction for the whole of the premium paid under a TPD insurance policy where:

- (a) it is certain that the occurrence of an insured event specified in the policy will result in a fund liability, pursuant to the terms of the fund trust deed, to provide a 'disability superannuation benefit' to a member; and
- (b) it is certain that all insured events under the policy are only for the provision of section 295-460 benefits<sup>8</sup> that the superannuation fund has a liability pursuant to the trust deed to provide to the member (refer to Examples 4, 6 and 8 at paragraphs 60 to 66, 78 to 84 and 91 to 99 respectively of this draft Ruling).

23. Where a premium is paid to cover more than one insured event for permanent disability and:

- (a) it is certain that the occurrence of one or more of the insured events specified in the policy will result in a fund liability, pursuant to the terms of the fund trust deed, to provide a 'disability superannuation benefit' to a member; and
- (b) the policy specifies the part of the premium paid that relates to those particular insured events as identified in paragraph (a) of paragraph 23 of this draft Ruling; and
- (c) it is uncertain that the occurrence of other insured events specified in the policy will result in a fund liability, pursuant to the terms of the fund trust deed, to provide a 'disability superannuation benefit' to a member;

then item 5 in the table in subsection 295-465(1) will apply to allow a deduction for that specified part of the premium referred to in paragraph (b) of paragraph 23 of this draft Ruling.

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<sup>8</sup> Paragraph (a) of section 295-460 refers to 'a superannuation death benefit' and paragraph (c) of section 295-460 refers to a benefit paid due to a temporary inability to engage in gainful employment.

24. Item 6 in the table in subsection 295-465(1) may apply to allow a deduction for a portion of that part of the premium paid for the other insured events referred to in paragraph (c) of paragraph 23 of this draft Ruling (refer to paragraph 25 of this draft Ruling).

***Deduction for part of the premium under item 6 in the table in subsection 295-465(1) based on apportionment in accordance with an actuary's certificate***

25. Where it is uncertain whether the satisfaction of an insured event definition in a policy will result in a fund liability to provide a paragraph 295-460(b) benefit to a member, it will be necessary to apportion premiums paid by the fund under item 6 in the table in subsection 295-465(1) based upon an actuary's certificate obtained in accordance with subsection 295-465(3) (refer to Examples 1, 3 and 5 at paragraphs 32 to 37, 50 to 59 and 67 to 77 respectively of this draft Ruling).

26. The actuarial task is to determine that part of the premium paid by a fund that is attributable to the likelihood that, upon the happening of an insured event that gives rise to a payout under the policy, the fund will have a liability to provide a 'disability superannuation benefit' to a member.

***No deduction***

27. An insurance premium is not deductible at all if it is certain that the requirements of the 'disability superannuation benefit' definition will not be met as a consequence of any insured event occurring under the policy. Any such premium payment clearly has no connection to a current or contingent liability of a fund to provide a 'disability superannuation benefit' referred to in paragraph 295-460(b) (refer to Example 2 at paragraphs 38 to 49 of this draft Ruling).

***Alignment with definition of 'disability superannuation benefit'***

28. The insurance policy does not need to define total and permanent disability using the same words as, or by referring to, the definition of 'disability superannuation benefit' in subsection 995-1(1) for a deduction to arise under subsection 295-465(1). Where there is alignment between an insured event under the policy and the requirements for the provision of a 'disability superannuation benefit' by the fund, this will ensure that a deduction is available under item 5 in the table in subsection 295-465(1) for that part of a premium that is specified for such an event.

29. It is also not necessary for the definition of total and permanent disability in the policy to be the same as the wording in the fund's trust deed giving rise to the current or contingent liability to provide disability benefits in order for a deduction to arise under subsection 295-465(1). It will suffice if the occasion of the insured event gives rise to a liability under or in accordance with the terms of the fund trust deed to provide a 'disability superannuation benefit' to the member.

### ***Effect of superannuation fund trust deed***

30. The possibility and likelihood of a member electing not to receive a benefit that is otherwise payable under the terms of the trust deed will not in itself deny deductibility of that insurance premium. The likelihood of a member electing not to receive a benefit, where the permanent incapacity condition of release has been met and the payment if made would satisfy the 'disability superannuation benefit' definition requirements, does not affect whether the trustee has a contingent liability to provide the 'disability superannuation benefit' at the time the insurance premium is paid.

31. If the amount payable by the insurer under a policy in respect of a member is greater than the benefit permitted to be paid out by the fund under the trust deed in relation to permanent incapacity condition of release, there will need to be an apportionment of the premium. That part of the premium paid that relates to the excess will not be deductible under subsection 295-465(1) (refer to Example 7 at paragraphs 85 to 90 of this draft Ruling).

## **Examples**

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### ***Example 1: deduction for own occupation under item 6 in the table in subsection 295-465(1)***

32. A complying superannuation fund (the fund) purchases a TPD insurance policy from an insurance company (Insurance Co) to cover its liabilities to its members in the event of the members suffering total and permanent disability.

33. The terms of the fund's trust deed provide that the fund trustee may provide either a superannuation lump sum or a superannuation income stream to a member where the trustee believes the member, having suffered an illness or injury, would satisfy the permanent incapacity condition of release (as in force at that time under the SISA and SISR).



34. The premium paid is clearly specified in the policy. The TPD insurance policy provides own occupation cover and has the following clauses in relation to this cover:

- (a) The insured suffers from an injury or illness (whether physical or mental) and
  - (i) as a result of that illness or injury the insured has been unable to be gainfully employed in their own occupation continuously for a period of at least 6 months, and
  - (ii) taking into account medical and other professional evidence the insured is unlikely ever to be gainfully employed in their own occupation.
- (b) Own occupation means the occupation the insured predominantly performed in the 12 months prior to the injury or illness.

35. In considering the full range of insured events that could possibly give rise to a payout to the fund under the own occupation cover provided in the policy, it is not certain that the occurrence of an insured event will always result in a liability for the fund to provide a 'disability superannuation benefit' to the member. In this regard it is recognised that in some circumstances the member will not be able to perform their own occupation but will still be able to be engaged in other gainful employment for which they are reasonably qualified by education, training or experience.

36. In circumstances where an insured event that occurs under the own occupation cover leads to a payout to the fund but the member does not satisfy the requirements of a 'disability superannuation benefit' referred to in paragraph 295-460(b), the fund will have no current or contingent liability to provide a 'disability superannuation benefit to the member'. The insurance payout will therefore be retained in the fund until the member satisfies a condition of release, such as retirement.

37. As the own occupation cover held by the fund does not relate wholly to the fund's liability to provide a 'disability superannuation benefit' under paragraph 295-460(b), the premium will not be deductible under item 5 in the table in subsection 295-465(1). Accordingly, deductibility of the premium paid by the fund will fall for consideration under item 6 in the table in subsection 295-465(1). This will require an actuary to certify that portion of the premium paid to Insurance Co that is attributable to the fund's liability to provide a 'disability superannuation benefit' referred to in paragraph 295-460(b).

***Example 2: deduction for any occupation and own occupation under item 5 in the table in subsection 295-465(1)***

38. After several years, the fund wishes to change its existing insurance policy with Insurance Co by exercising an option to vary the terms of cover (from those held in Example 1 at paragraphs 32 to 37 of this draft Ruling) in its next policy.

39. The new policy provides any occupation cover plus an own occupation cover option. The add-on of the own occupation option cover to the any occupation cover under this new policy is intended to extend the any occupation cover to replicate the full range of circumstances that would give rise to a payout under the previous policy.

40. The total premium payable under the insurance policy covers the cost of both the any occupation cover and the own occupation cover option, with the two amounts being separately specified within the policy.

41. Insurance Co's any occupation cover in the new policy has the following clauses:

The insured suffers from an injury or illness (whether physical or mental) and

- (a) as a result of that illness or injury the insured has been unable to be gainfully employed in any occupation continuously for a period of at least 6 months, and
- (b) taking into account medical and other professional evidence the insured is unlikely ever to engage in gainful employment for which they are reasonably qualified by education, training or experience.

42. Own occupation cover retains its definition from the insurance policy that was in place in Example 1 at paragraphs 32 to 37 of this draft Ruling in the previous year.

43. Under the terms of the policy the fund will receive only one payout upon the happening of an insured event, even if an insured event occurs that would satisfy both the any occupation and the own occupation cover. A payout received by the fund under the any occupation cover will reduce the member's entitlement to the own occupation benefit by the same amount. Conversely, a payout received by the fund under the own occupation cover will reduce the member's entitlement to a future any occupation benefit by the same amount.

44. The any occupation cover within the policy is consistent with the fund's current or contingent liability, under the terms of the fund trust deed, to provide a 'disability superannuation benefit'. The fund will only receive a payout under this cover if the occurrence of the insured event results in the member being unlikely to ever engage in gainful employment for which the member is reasonably qualified by education, training or experience.

45. It is therefore certain that the occurrence of an insured event under the any occupation cover would also give rise to a liability under the fund trust deed for the trustee to provide a 'disability superannuation benefit' to the member at that time.

46. In this case, the premium separately specified within the policy for any occupation cover is fully deductible under item 5 in the table in subsection 295-465(1), being wholly for the fund's liability to provide a 'disability superannuation benefit' referred to in paragraph 295-460(b). This is the case even though the definition of the any occupation cover in the policy does not use the same words as those for the requirements for the provision of a 'disability superannuation benefit' in subsection 995-1(1) (refer to paragraphs 28 to 29 of this draft Ruling).

47. Under the terms of the policy's own occupation cover the fund will only receive a payout in respect of a member if the occurrence of the insured event results in the member being unlikely ever to engage in their own occupation. Accordingly, where a claim under the policy only arises under the own occupation cover, the member will not have satisfied the policy conditions in relation to the any occupation cover as it is likely that the member could still engage in other gainful employment for which they are reasonably qualified by education, training or experience. In these circumstances the occurrence of the insured event giving rise to a payout under the own occupation cover will not also result in the member satisfying the 'disability superannuation benefit' definition referred to in paragraph 295-460(b).

48. The premium paid for the add-on of own occupation cover therefore has no connection with the fund's liability to provide benefits referred to in paragraph 295-460(b). Accordingly, the premium separately specified in the policy as being paid for own occupation cover is not deductible under subsection 295-465(1).

49. By altering the structure of the TPD insurance policy from an own occupation cover to any occupation cover with an own occupation add-on, the policy now specifies the premium paid in respect of each type of cover. This removes the need for the fund to obtain an actuary's certificate in order to claim the deductible portion of its insurance premium.

***Example 3: deduction for own occupation and loss of limbs and/or sight under item 6 in the table in subsection 295-465(1)***

50. A complying self managed superannuation fund (the fund) purchased a TPD insurance policy from an insurance company (Insurance Co) to cover its liability in the event of its members becoming totally and permanently disabled.

51. The terms of the fund's trust deed require the trustee, at the request of the member, to pay a benefit to that member where the trustee reasonably believes that due to accident or illness the member is totally and permanently disabled leaving them unlikely ever to be able to engage in any regular remunerative work for which they are reasonably suited by education, training and experience.

52. The fund's TPD insurance policy with Insurance Co contains own occupation and loss of limbs and/or sight combined cover.

53. Under the terms of the policy own occupation cover is defined as follows:

- (a) as a result of accident or injury, the insured is completely unable to work at their own occupation continuously for a period of at least 4 months and after considering medical and other evidence are unlikely ever to be able to do so again.
- (b) own occupation means the occupation the insured was engaged in at the time of the insured application for this insurance.

54. Loss of limbs and/or sight cover is defined in the policy as:

The insured has suffered the total and permanent loss of:

- (a) the use of both hands,
- (b) the use of both feet,
- (c) the use of one hand and one foot,
- (d) the use of one hand or one foot and the sight in one eye, or
- (e) the sight in both eyes.

55. Under the terms of the TPD insurance policy, the fund will receive only one payout even if the occurrence of an insured event would satisfy more than one of the defined types of cover. A payout received by the fund under the loss of limbs and/or sight cover will reduce the amount of any payout entitlement under own occupation cover by that same amount.

56. In considering the full range of insured events that could possibly give rise to a payout to the fund under the own occupation cover and loss of limbs and/or sight cover provided under the terms of the policy with Insurance Co, it is not certain that the occurrence of an insured event will result in a liability for the fund to provide a 'disability superannuation benefit' to a member. It is recognised that in some circumstances a member, having suffered an accident or illness, whether or not resulting in loss of limbs and/or sight, will not be able to perform their own occupation. However they may otherwise still be able to be engaged in gainful employment for which they are reasonably qualified by education, training or experience.

57. In some circumstances where an insured event that occurs under the own occupation or loss of limbs and/or sight cover leads to a payout to the fund by the insurer, the fund will have no liability to provide a 'disability superannuation benefit' to the member as at that time the relevant conditions have not been met. Any insurance payout will therefore be retained in the fund until the member satisfies a condition of release, such as retirement.

58. As the own occupation and loss of limbs and/or sight cover held by the fund does not relate wholly to the fund's liability to provide a 'disability superannuation benefit' under paragraph 295-460(b), the premium for the TPD insurance policy with Insurance Co will not be deductible under item 5 in the table in subsection 295-465(1).

59. Accordingly, deductibility of the premium paid by the fund will fall for consideration under item 6 in the table in subsection 295-465(1). This will require an actuary's certificate pursuant to subsection 295-465(3).

***Example 4: deduction for any occupation and domestic duties under item 5 in the table in subsection 295-465(1)***

60. A complying superannuation fund (the fund) purchases a TPD insurance policy from an insurance company to cover its liability in the event its members become totally and permanently disabled.

61. The terms of the fund's trust deed provide that the fund trustee may provide either a superannuation lump sum or a superannuation income stream to a member where the trustee believes the member, having suffered an illness or injury, would satisfy the permanent incapacity condition of release (as in force at that time under Superannuation Law).

62. The TPD insurance policy includes any occupation and domestic duties cover. A single premium paid for this combined cover is specified in the policy. The any occupation cover is defined as:

The insured suffers from an injury or illness (whether physical or mental) and

- (a) as a result of that illness or injury the insured has been unable to be gainfully employed in any occupation continuously for a period of at least 6 months, and
- (b) taking into account medical and other professional evidence the insured is unlikely ever to engage in gainful employment for which they are reasonably qualified by education, training or experience.

63. Domestic duties cover is defined as:

If the insured has the sole occupation of maintaining a family home and they suffer an illness or injury and:

- (a) the illness or injury wholly prevents them from engaging in any normal domestic duties for at least 3 consecutive months, and

- (b) since becoming ill or injured they have been under the regular care and attention of a medical practitioner for that illness or injury, and
- (c) in the insurer's opinion, as a result of the illness or injury the insured is incapacitated to such a degree they are unlikely to ever again be able to engage in domestic duties or engage in any occupation.

64. It is certain that the occurrence of an insured event under the any occupation cover would give rise to a liability under the fund trust deed for the trustee to provide a 'disability superannuation benefit' to the member.

65. It is accepted that the occurrence of an insured event under the domestic duties cover would give rise to a liability under the fund trust deed for the trustee to provide a 'disability superannuation benefit' to the member, as it would be unlikely that a member with this level of disability would ever be gainfully employed in a capacity for which they were reasonably qualified because of education, experience or training.

66. Accordingly the single premium specified within the policy for any occupation and domestic duties cover is fully deductible under item 5 in the table in subsection 295-465(1) as the premium is wholly for the fund's liability to provide a 'disability superannuation benefit' referred to in paragraph 295-460(b). This is the case even though the definition of the domestic duties cover in the policy does not use the same words as those for the requirements for the provision of a 'disability superannuation benefit' in subsection 995-1(1) (refer to paragraphs 28 to 29 of this draft Ruling).

***Example 5: deduction for any occupation and loss of limbs and/or sight under item 6 in the table in subsection 295-465(1)***

67. A complying superannuation fund (the fund) purchases a TPD insurance policy to cover its liabilities to its members in the event they become totally and permanently disabled. The TPD insurance policy includes any occupation and loss of limb and/or sight combined cover.

68. The terms of the fund's trust deed authorises the trustee to pay out a superannuation lump sum or superannuation income stream where the member meets a condition of release in accordance with the SISR. A benefit may be paid by the trustee if the payment does not change the fund's status as a complying superannuation fund under the SISA.

69. Any occupation is defined under the fund's policy as:

The insured has been unable to engage in any occupation, profession or business as a result of the insured's injury or sickness:

- (a) for at least 6 consecutive months, and
- (b) the insured is unlikely ever again to engage in any occupation, profession or business for which they are reasonably qualified as result of education, experience or training.

70. Loss of limbs and/or sight is defined in this policy as:

The insured has suffered the total and permanent loss of:

- (a) the use of both hands,
- (b) the use of both feet,
- (c) the use of one hand and one foot,
- (d) the use of one hand or one foot and the sight in one eye, or
- (e) the sight in both eyes.

71. A single premium is paid under the policy for both the any occupation and loss of limb and/or sight cover. The policy does not specify how much of the premium relates to each cover. The fund will receive two separate payouts under the policy in circumstances where an insured event occurs that will satisfy both the any occupation and loss of limb and/or sight policy definitions. A payout received by the fund under the any occupation cover will not reduce the fund's entitlement to a loss of limbs and/or sight payout and vice versa.

72. It is certain that the occurrence of an insured event under the any occupation cover would also give rise to a liability under the fund trust deed for the trustee to provide a 'disability superannuation benefit' to the member.

73. In considering the insured events that could possibly give rise to a payout to the fund under the loss of limbs and/or sight cover it is not certain that the occurrence of an insured event will always result in a liability for the fund to provide a 'disability superannuation benefit' to a member.

74. It is recognised that in some circumstances a member, having suffered an accident or injury resulting in loss of limbs and/or sight, will not be able to engage in any occupation, profession or business for which they are reasonably qualified as result of education, experience or training. In these circumstances, a liability will arise under the fund trust deed for the trustee to provide a 'disability superannuation benefit' to the member.

75. However in other circumstances, despite the loss of limbs and/or sight, the member may still be able to be engaged in gainful employment for which they are reasonably qualified by education, training or experience. Therefore, the cost to the fund of obtaining loss of limbs and/or sight cover does not relate wholly to the fund's liability to provide a 'disability superannuation benefit' under paragraph 295-460(b).

76. Since the premium paid by the fund for each type of cover is not specified separately in the policy, no deduction is allowed under item 5 in the table in subsection 295-465(1). Therefore, the premium paid has to be apportioned in accordance with item 6 in the table in subsection 295-465(1).

77. The part of the premium that relates to the provision of any occupation cover will be fully deductible. However, only a portion of the part of the premium that relates to the provision of loss of limb and/or sight cover will be deductible, and an actuary will need to certify that portion of the premium that is attributable to the insured events that will result in a liability for the fund to provide a 'disability superannuation benefit' to a member. This portion of the part of the premium that is certified by the actuary will also be deductible.

***Example 6: deduction for any occupation and loss of independence under item 5 in the table in subsection 295-465(1)***

78. A complying superannuation fund (the fund) purchases a TPD insurance policy to cover its liabilities to its members in the event of them becoming totally and permanently disabled.

79. The terms of the fund's trust deed require the trustee, at the request of the member, to pay a benefit to that member where the trustee reasonably believes that due to accident or illness the member is totally and permanently disabled leaving them unlikely ever to be able to engage in any regular remunerative work for which they are reasonably suited by education, training and experience.

80. The TPD insurance policy includes any occupation and loss of independence cover. A single premium paid for this combined cover is specified in the policy. The any occupation cover is defined as:

The insured suffers from an injury or illness (whether physical or mental) and

- (a) as a result of that illness or injury the insured has been unable to be gainfully employed in any occupation continuously for a period of at least 6 months, and
- (b) taking into account medical and other professional evidence the insured is unlikely ever to engage in gainful employment for which they are reasonably qualified by education, training or experience.

81. Loss of independence cover is defined under the policy as:

The insured has lost independence if, as a result of sickness or injury, they are totally and irreversibly unable to do two or more of the following groups of daily activities without physical help from someone else:

- (a) bathing or showering,
- (b) dressing,
- (c) moving from place to place, in and out of bed, and in and out of a chair,
- (d) eating and drinking, or
- (e) using the toilet.



82. It is certain that the occurrence of an insured event under the any occupation cover would give rise to a liability under the fund trust deed for the trustee to provide a 'disability superannuation benefit' to the member.

83. It is accepted that the occurrence of an insured event under the loss of independence cover would give rise to a liability under the fund trust deed for the trustee to provide a 'disability superannuation benefit' to the member, as it would be unlikely that a member with this level of disability would ever be gainfully employed in a capacity for which they were reasonably qualified because of education, experience or training.

84. Accordingly, the single premium specified within the policy for any occupation and loss of independence cover is fully deductible under item 5 in the table in subsection 295-465(1), being wholly for the fund's liability to provide a 'disability superannuation benefit' referred to in paragraph 295-460(b). This is the case even though the definitions of both the any occupation cover and the loss of independence cover in the policy do not use the same words as those for the requirements for the provision of a 'disability superannuation benefit' in subsection 995-1(1) (refer to paragraphs 2 to 29 of this draft Ruling).

***Example 7: deduction for any occupation under item 6 in the table in subsection 295-465(1)***

85. A complying superannuation fund (the fund) purchases a TPD insurance policy from an insurance company to cover its liability to its members in the event of the members suffering total and permanent incapacity. The policy contains any occupation cover. The premium paid for this cover is specified in the policy.

86. Any occupation is defined in the policy as:

As a result of the insured's injury or sickness, the insured has been unable to engage in any occupation, profession or business:

- (a) for at least 6 consecutive months, and
- (c) the insured is unlikely ever again to engage in any occupation, profession or business for which they are reasonably qualified as result of education, experience or training.

87. Under the terms of the trust deed, in order for a member to receive a 'disability superannuation benefit' from the fund, the member has to be receiving constant medical care from a certified medical practitioner for a minimum of six consecutive months.

88. This trust deed requirement is stricter than the SISR 'permanent incapacity' condition of release. Therefore, the occurrence of some of the insured events that give rise to payouts under the policy may not give rise to a liability under the fund's trust deed to provide a 'disability superannuation benefit' to the member. In such circumstances the payout received by the fund may be retained in the fund until the trust deed conditions are satisfied, even if the member has satisfied the conditions for payment of a 'disability superannuation benefit'.

89. Under subsection 295-465(1), the fund can only deduct an amount of premium paid for TPD insurance which relates to the fund's current or contingent liability to provide a 'disability superannuation benefit' referred to in section 295-460. Where the fund holds insurance that does not relate wholly to the fund's liability to provide a section 295-460 benefit under the terms of its trust deed, deduction of the premium will fall for consideration under item 6 in the table in subsection 295-465(1).

90. To claim a deduction under item 6 in the table in subsection 295-465(1) an actuary will need to certify that portion of the premium that is attributable to the insured events that will result in a liability for the fund to provide a section 295-460 benefit.

***Example 8: deduction for any occupation and death benefit under item 5 in the table in subsection 295-465(1)***

91. A complying superannuation fund (the fund) purchases an insurance policy to cover its liabilities to its members in the event of their death or if they become totally and permanently disabled.

92. The terms of the fund's trust deed require the trustee to pay a benefit in relation to a member on the member's death.

93. The terms of the fund's trust deed also require the trustee, at the request of the member, to pay a benefit to that member where the trustee reasonably believes that due to accident or illness the member is totally and permanently disabled leaving them unlikely ever to be able to engage in any regular remunerative work for which they are reasonably suited by education, training and experience.

94. The insurance policy includes death benefit and any occupation cover. A single premium paid for this combined cover is specified in the policy.

95. The death benefit cover is defined under the policy as providing a benefit on the death of the person insured, being the member of the superannuation fund.

96. The any occupation cover is defined under the policy as:  
The insured suffers from an injury or illness (whether physical or mental) and
- (a) as a result of that illness or injury the insured has been unable to be gainfully employed in any occupation continuously for a period of at least 6 months, and
  - (b) taking into account medical and other professional evidence the insured is unlikely ever to engage in gainful employment for which they are reasonably qualified by education, training or experience.
97. It is certain that the occurrence of the insured event under the death benefit cover would give rise to a superannuation death benefit under paragraph 295-460(a).
98. It is also certain that the occurrence of an insured event under the any occupation cover would give rise to a liability under the fund trust deed for the trustee to provide a 'disability superannuation benefit' referred to in paragraph 295-460(b) to the member.
99. Accordingly the single premium specified within the policy for the death benefit and any occupation cover is fully deductible under item 5 in the table in subsection 295-465(1), as the premium is wholly for the fund's liability to provide benefits referred to in section 295-460.

## Date of effect

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100. When the final Ruling is issued, it is proposed to apply from 1 July 2011 and later income years.
101. However, the Ruling will not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Ruling (see paragraphs 75 to 77 of Taxation Ruling TR 2006/10).

## **Appendix 1 – Explanation**

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**❶** *This Appendix is provided as information to help you understand how the Commissioner’s preliminary view has been reached. It does not form part of the proposed binding public ruling.*

### **Background**

102. Superannuation funds commonly take out insurance policies in respect of their liability to provide benefits to members. Often these policies will be a type of group policy, whereby a single policy provides coverage in respect of all of the members of the fund or an identified sub-class of those members. In other cases the policies will be taken out in respect of an individual member.

103. The term total and permanent disability (TPD) will be defined in the insurance policy. There are currently a wide range of definitions of totally and permanently disabled used in insurance policies for the purposes of determining when a benefit will be payable under the policy.

104. TPD cover is often sold as an add-on to term life insurance policies that provide a payment on death of the insured. Alternatively, TPD cover can be provided under a separate insurance policy. Some trauma insurance products also include TPD as one of the insured events.

### **Legislative history – the ITAA 1936**

105. Former section 279 of the ITAA 1936 allowed a deduction for a premium paid (in whole or in part) in respect of a current or contingent liability of a superannuation fund to provide death or disability benefits for the members of the fund.

106. The definition of ‘death or disability benefit’ in former section 267 of the ITAA 1936 included at paragraph (b) ‘a benefit provided to the member in the event of the permanent disability of the member’.

107. The term ‘permanent disability’ was not defined. Consequently, insurers and superannuation funds interpreted the term according to its ordinary meaning, resulting in a wide range of TPD definitions in insurance policies taken out by funds on behalf of their members.

108. Our understanding is that industry practice was to claim a full deduction for TPD premiums regardless of whether a policy covered any occupation, own occupation, loss of independence, home duties, or loss of limb and/or sight benefits.

109. This view focuses on the insurer’s liability to the fund rather than the fund’s liabilities to members.

110. The provisions regarding deductibility of TPD insurance premiums were rewritten and transferred from former section 279 of the ITAA 1936 to Division 295 of the ITAA 1997 with effect from the 2007-2008 income year.

### ***Transitional provisions***

111. In response to concerns raised by the superannuation and insurance industry that the ATO view of the deductibility of TPD insurance premiums did not accord with industry practice, the Minister for Financial Services, Superannuation & Corporate Law announced an intention to amend the tax law to provide transitional relief to complying superannuation funds for income tax deductibility of TPD insurance premiums.<sup>9</sup>

112. These amendments to the tax law have now been enacted and ensure that complying superannuation funds could deduct in full the insurance premiums commonly regarded as TPD policy premiums for the income years from 2004-05 to 2010-11.

### ***Division 295***

113. Division 295 (of which sections 295-460 and 295-465 form a part) contains special rules in relation to the taxation of complying superannuation funds.

114. Under subsection 295-465(1), a complying superannuation fund can deduct the proportion of premiums it pays for insurance policies that are wholly or partly for current or contingent liabilities of the fund to provide benefits referred to in section 295-460 for its members.

115. Section 295-460 is concerned with particular types of benefits a superannuation fund may provide to a member (in the case of a 'disability superannuation benefit') or another person (in the case of a superannuation death benefit).

116. The premium paid for a TPD insurance policy may be deductible under item 5 or item 6 in the table in subsection 295-465(1).

117. Under item 5 in the table in subsection 295-465(1) the fund can deduct the part of the premium that is specified in the policy as being wholly for the liability to provide benefits referred to in section 295-460.

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<sup>9</sup> Bowen C (Minister for Financial Services, Superannuation and Corporate Law) 2009, *Transitional Relief for Superannuation Funds: Deductibility of Disability Benefit Premiums*, media release, Canberra, 13 October.

118. Under item 6 in the table in subsection 295-465(1) the fund can deduct so much of other insurance premiums as are attributable to the liability to provide benefits referred to in section 295-460.

119. Subsection 295-465(2) provides that a complying superannuation fund can also deduct the amount it could reasonably be expected to pay in an arm's length transaction to obtain an insurance policy to cover it for that part of its current or contingent liabilities to provide benefits referred to in section 295-460 for which it does not have insurance coverage.

120. The trustee of the relevant fund must obtain an actuary's certificate before the date of lodgement of the fund's income tax return for the income year in order to deduct an amount referred to in item 6 in the table in subsection 295-465(1) or in subsection 295-465(2).

### **Deductibility of premiums under subsection 295-465(1)**

121. Subsection 295-465(1) states that a complying superannuation fund can deduct in an income year:

...the proportions specified in this table of premiums it pays for insurance policies that are (wholly or partly) for current or contingent liabilities of the fund to provide benefits referred to in section 295-460 for its members.

122. Paragraph (b) of section 295-460 refers to a 'disability superannuation benefit' as being one of the benefits to which section 295-465 applies.

123. A 'disability superannuation benefit' is defined in subsection 995-1(1) to mean a superannuation benefit where:

- (a) the benefit is paid to a person because he or she suffers from ill-health (whether physical or mental); and
- (b) 2 legally qualified medical practitioners have certified that, because of the ill-health, it is unlikely that the person can ever be \*gainfully employed in a capacity for which he or she is reasonably qualified because of education, experience or training.

124. The term 'gainfully employed' is also defined in subsection 995-1(1) as meaning:

employed or self employed for gain or reward in any business, trade, profession, vocation, calling, occupation or employment.

125. There has been no judicial consideration of the meaning of the term ‘disability superannuation benefit’ as defined in subsection 995-1(1). This draft Ruling does not deal with the circumstances that would result in satisfaction of the requirement that ‘a person is unlikely to ever be gainfully employed in a capacity for which he or she is reasonably qualified because of education, experience or training’. However, by way of background the following comments from Court and Superannuation Tribunal decisions involving permanent disability claims may be of some assistance:

- it is not a question of whether the person can perform their current occupation, it is whether they are reasonably qualified to perform any ‘gainful employment’ by reason of education, training or experience.<sup>10</sup>
- transferable skills may enable a person to undertake work, even if it is different work.<sup>11</sup>
- consideration needs to be given as to whether it is reasonable in the circumstances that the person would be able to obtain employment.<sup>12</sup>
- in considering whether the person is reasonably qualified, it is whether at the time of assessment they have the skills to do the proposed work not whether they can be retrained.<sup>13</sup>

126. An insurance premium is consideration provided by or on behalf of the insured to the insurer in return for the insurer undertaking to pay the insured a sum of money or an equivalent benefit on the happening of a specified event, the occurrence or timing of which is uncertain (*Prudential Insurance Company v. Commissioners of Inland Revenue* [1904] 2 KB 658).

127. In *Community Development Pty Ltd v. Engwirda Construction Co* (1969) 120 CLR 455, Owen J referred to *Sutherland (decd) v. Inland Revenue Commissioners* [1961] 3 All ER 855 where Lord Reid said the following in regard to the meaning of contingent liability:

...‘contingent liabilities’, which must mean sums, payment of which depends on a contingency, that is, sums which will only become payable if certain things happen, and which otherwise will never become payable.<sup>14</sup> ... The essence of a contingent liability must surely be that it may never become an existing legal liability because the event on which it depends may never happen.<sup>15</sup>

<sup>10</sup> See for example *Edwards v. The Hunter Valley Co-op Dairy Co Ltd* (1992) 7 ANZ Insurance Cases 61-113 and *White v. The Board of Trustees* [1997] 2 Qd R 659.

<sup>11</sup> *Alessi v. National Mutual Life Association of Australasia Ltd* (1982) 2 ANZ Insurance Cases 60-481.

<sup>12</sup> *Nile v. Club Plus Superannuation Pty Ltd and Anor* [2005] NSWSC 55.

<sup>13</sup> *Cavill Power Products Pty Ltd v. Royle* (1991) 42 IR 229.

<sup>14</sup> All ER at p 859.

<sup>15</sup> All ER at p 860.

128. Where a superannuation fund takes out an insurance policy in relation to its members, the relationship between the parties is complicated by the fact that the fund is the entity entering into the contract of insurance. The fund pays the premium and receives the payout on the insured event occurring to the member concerned.

129. At the time a superannuation fund pays an insurance premium for a policy in respect of one or more of its members, it is uncertain what the outcome will be. Specifically, it is uncertain as to whether the member will ever satisfy the requisite degree of ill-health for a 'disability superannuation benefit'. The possibility and likelihood of the insured event occurring does not deny the deductibility of premiums paid by the fund. This is made clear by the reference to 'contingent liability' in section 295-465. Premiums will therefore be deductible even though it is most likely that a payout may never be made under the policy because the insured event may not occur.

130. The trustee of a complying superannuation fund will have a current or contingent liability to provide a benefit to or in respect of a fund member where, upon the happening of a specified event or the occurrence of a particular situation, the terms of the fund trust deed impose an obligation upon the trustee to provide that benefit.

131. Whether a deduction can be claimed by a complying superannuation fund for a premium it pays for TPD insurance is not determined solely by the nature or scope of the events which will lead to a payout being made under the policy. However the events insured against do impact on the basis on which a deduction can be claimed under section 295-465 (refer paragraphs 143 to 172 of this draft Ruling).

132. For a TPD insurance premium paid by a complying superannuation fund to be deductible under subsection 295-465(1), the law requires a connection between the payment and the current or contingent liabilities of the fund to provide benefits referred to in section 295-460. The benefit must be a benefit contemplated by the sole purpose test.

133. Subsection 295-465(1) by referring to 'the proportions' and 'wholly or partly' explicitly contemplates that some insurance premiums may be attributable to insurance cover outside of the fund's liability to provide benefits referred to in section 295-460. The premium will not be deductible to the extent to which it is not in relation to a liability to provide a benefit referred to in section 295-460.



## **Sole purpose**

134. An integral feature of the superannuation regulatory regime<sup>16</sup> is the sole purpose test in section 62 of the SISA. Under the sole purpose test, a regulated superannuation fund must generally be maintained solely for the purpose of providing retirement and certain related benefits, including benefits payable on or after the occurrence of earlier contingencies such as death and permanent incapacity.

135. Section 295-460 sets out three types of benefits for which insurance premium deductions may be available under section 295-465: (a) a superannuation death benefit (b) a disability superannuation benefit and (c) a benefit for temporary inability to engage in gainful employment. The three types of benefits set out in section 295-460 can be contrasted with other types of superannuation member benefits that may be provided to members by complying superannuation funds, such as benefits provided by a fund to members on retirement or reaching age 65.

136. The general rules on payment of a member's benefits from a superannuation fund are set out in Division 6.2 of the SISR. Under Division 6.3 of the SISR, the payment of a member's benefits may be compulsory or voluntary.

137. Consistent with the sole purpose test, a complying superannuation fund can only provide a member's preserved benefits on or after the time when a member satisfies a condition of release (regulation 6.18 of the SISR). Schedule 1 to the SISR identifies the conditions of release for these purposes together with any restrictions that apply to the provision of benefits when certain release conditions have been met.

138. The provision of a 'disability superannuation benefit' to a member is determined by reference to the entitlements of the member under the trust deed, and more particularly, the operation of the conditions of release in Schedule 1 to the SISR. Accordingly, the matter of when and to what extent a member receives a benefit referable to the payout under an insurance policy is not determined solely by the occurrence of the insured event and the receipt of a payout by the trustee of the a fund under the insurance policy.

139. The permanent incapacity of a member is listed in item 103 of Schedule 1 to the SISR as one of the conditions of release under which a superannuation fund can provide a benefit to a member and is the relevant condition of release that would have to be satisfied in order for a superannuation fund to provide a 'disability superannuation benefit'.

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<sup>16</sup> under the SISA and the SISR.

140. Subregulation 6.01(2) of the SISR defines permanent incapacity in relation to a member as:

ill-health (whether physical or mental), where the trustee is reasonably satisfied that the member is unlikely, because of the ill-health, to engage in gainful employment for which the member is reasonably qualified by education, training or experience.

141. In our view the degree of ill-health that the trustee of a fund must be reasonably satisfied exists in order that a member meets the definition of permanent incapacity under subregulation 6.01(2) of the SISR is identical to that which two medical practitioners must certify for the payment of a 'disability superannuation benefit'.

142. It is possible that a trustee may be reasonably satisfied that the permanent incapacity condition of release under the SISR is met prior to the certification of the same by two medical practitioners as required under the definition of 'disability superannuation benefit'. However, it is difficult to contemplate a situation where two medical practitioners would not certify the satisfaction of the permanent incapacity condition of release where a fund trustee is reasonably satisfied that such a condition exists. While in strict terms there may be a need to take this matter into account in determining deductibility of insurance premiums, our view is that the practical impact is at most negligible.

***Deduction for specified part of the premium under item 5 in the table in subsection 295-465(1)***

143. An insurance premium payment for a TPD insurance policy is deductible under item 5 in the table in subsection 295-465(1) where the policy documentation specifies that part of the premium that is wholly for the liability to provide a 'disability superannuation benefit'.

144. Where an insurance premium or part of a premium is specified as being for an insured event that aligns with the 'disability superannuation benefit' definition the premium or relevant part of the premium will be fully deductible under item 5 in the table in subsection 295-465(1). In this case it is certain that where the insured event occurs the fund will have a liability to provide a 'disability superannuation benefit'. There is a necessary connection between the insurance premium paid and the liability of the fund to provide a section 295-460 benefit.

145. Where it is certain that the ‘disability superannuation benefit’ definition will be met following the occurrence of any of the insured events covered by an insurance policy, the premium will be fully deductible irrespective of whether the policy dissects the premium and identifies each part of the premium applying to the different insured events that are covered under the TPD insurance policy. This will also be the case where the policy covers other benefits contained in section 295-460.<sup>17</sup>

146. Where it is uncertain that the ‘disability superannuation benefit’ definition will be met following the occurrence of some insured events under the policy but the policy identifies those parts of the premiums paid that relate to events where it is certain that the condition of release will be met, item 5 in the table in subsection 295-465(1) will apply in relation to those parts of the premium that are specified as being wholly for a liability to provide section 295-460 benefits. Item 6 in the table in subsection 295-465(1) may apply to the remainder of the premium (refer to paragraphs 160 to 172 of this draft Ruling).

147. In the context of common TPD insurance policy cover, where the insured event comes under any occupation cover it will be certain that where such an event happens to a member the fund will have a liability to provide a ‘disability superannuation benefit’ to that member (refer to Example 2 at paragraphs 38 to 49 of this draft Ruling).

148. A policy providing any occupation cover defines disability in terms of the person being unlikely to be able to ever perform the duties of any occupation, business, profession or employment for which the person is reasonably suited by education, training or experience.

149. This definition is based on the same conditions required to establish permanent incapacity under subregulation 6.01(2) of the SISR, which we consider to be equivalent to the ‘disability superannuation benefit’ definition in subsection 995-1(1).

150. The definition of the any occupation insured event may vary in different TPD insurance policies, but we consider that this variation would not affect our view on the deductibility of premiums provided the variation is not significantly different to the condition set out in paragraph 148 of this draft Ruling.

151. There is insurance coverage for other insured events in TPD insurance policies which adopt narrower and often more specific objective event conditions. However, the key requirement to be considered when determining whether the premium for this type of insurance cover is deductible is still whether there is certainty that a ‘disability superannuation benefit’ will be provided if the event occurs.

152. The most common example is the insured event for ‘loss of independence’ cover contained in some TPD insurance policies.

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<sup>17</sup> Paragraph (a) of section 295-460 refers to a ‘superannuation death benefit’ and paragraph (c) of section 295-460 refers to a benefit paid due to a temporary inability to engage in gainful employment.

153. A policy providing loss of independence cover will define disability as the total and permanent inability to perform at least 2 out of 5 activities of daily living without assistance. The 5 activities of daily living include washing, dressing, feeding, continence and mobility.

154. The degree of disability required to meet the definition of loss of independence would mean that it is unlikely that a member with this level of incapacity will ever be gainfully employed in a capacity for which they are reasonably qualified because of education, experience or training. Accordingly, a benefit payable under a loss of independence cover would usually satisfy the definition of a 'disability superannuation benefit' in subsection 995-1(1).

155. The home or domestic duties cover in TPD insurance policies is another example of insurance cover where it is considered that the 'disability superannuation benefit' definition would be met for most policies providing this kind of benefit.

156. A policy providing home or domestic duties cover will generally define disability in terms of the person being unlikely to be able to ever perform normal home or domestic duties. In some cases the policy may also impose a requirement that the member also be unlikely to ever be able to engage in any occupation for which they are reasonably suited by education training or experience in order for a home or domestic duties benefit to be payable.

157. Home or domestic duties may be defined in insurance policies as including activities such as cleaning the person's home, shopping for food and household items, meal preparation and laundry duties. Insurance policies may also include the inability to undertake activities such as looking after dependant children or providing full time care for invalid family members under the home or domestic duties cover.

158. The degree of disability required in relation to the home or domestic duties cover would in most cases mean that it is unlikely that a member with this level of incapacity will ever be gainfully employed in a capacity for which they are reasonably qualified because of education, experience or training. Accordingly, a benefit payable under a home or domestic duties cover would in most cases satisfy the definition of a 'disability superannuation benefit' in subsection 995-1(1).

159. However, depending on the definition of home or domestic duties in the insurance policy, it is possible in limited cases that a person will meet the definition of home or domestic duties in a TPD insurance policy while at the same time not satisfying the definition of a 'disability superannuation benefit' in subsection 995-1(1). Where this is the case, the deduction will be considered under item 6 in the table in subsection 295-465(1).

***Deduction for part of the premium under item 6 in the table in subsection 295-465(1) based on apportionment in accordance with an actuary's certificate***

160. As stated at paragraph 133 of this draft Ruling, subsection 295-465(1) contemplates that there may be a portion of the insurance premiums paid by the fund which will not be for a fund's liability to provide benefits referred to in section 295-460. Under item 6 in the table in subsection 295-465(1), a fund can deduct so much of other insurance premiums as are attributable to the liability to provide benefits referred to in section 295-460.

161. Where it is uncertain whether any insurance payout will be reflected in a liability to pay a 'disability superannuation benefit' to a member, deductibility of the premium will be considered under item 6 in the table in subsection 295-465(1).

162. In these circumstances, this uncertainty will be reflected in the possibility that the benefits attributable to an insurance payout made by the insurer to the fund on meeting the insured event have the potential to be retained within the fund until a condition of release is subsequently met. The premium for the insurance coverage is therefore considered to only partly relate to the fund's liability to provide benefits listed in section 295-460.

163. In the context of TPD insurance policies, the standard own occupation definitions focus on the capacity of a member to continue in the particular employment that he or she was last engaged in at the time of the relevant injury or illness.

164. Under an own occupation policy, a payout could be made to the fund because the insured event has occurred but the member may still be able to engage in another occupation. A policy providing own occupation cover generally defines disability in terms of the person being unlikely to be able to perform the usual and customary duties of the occupation, business, profession or employment that they were engaged in when they suffered the illness or injury. Own occupation cover is usually provided in relation to a person engaged in a professional occupation or undertaking senior management duties.

165. In the case where the member would not satisfy the 'disability superannuation benefit' definition in subsection 995-1(1) or the permanent incapacity condition of release under subregulation 6.01(2) of the SISR, the payment will be retained in the fund until a condition of release such as the retirement of the member is satisfied.

166. However, if the member is assessed as being unlikely to engage in any occupation for which they are reasonably qualified by education, training or experience, it follows that the member is unlikely to engage in the occupation that they were last engaged in at the time of the injury or illness. In this case, a payout may be made to the fund under an own occupation policy in circumstances where the member of the fund satisfies the permanent incapacity condition of release under subregulation 6.01(2) of the SISR and a benefit can then be paid to the member under that condition (refer to Example 1 at paragraphs 32 to 37 of this draft Ruling).

167. It is therefore uncertain whether a 'disability superannuation benefit' under paragraph 295-460(b) will arise as a result of the occurrence of the insured event under an own occupation policy.

168. In these circumstances the insurance premiums are only partly deductible and it is necessary to apportion the premiums under item 6 in the table in subsection 295-465(1) in accordance with the extent to which the premium is attributable to the provision of a 'disability superannuation benefit' as certified by an actuary.

169. A policy for loss of limbs and/or sight cover is also an example of a policy where apportionment of the premiums may be necessary.

170. A policy providing loss of limbs and/or sight cover will generally insure against the total and permanent loss of either the use of 2 limbs, the sight of both eyes, or the use of one limb and the sight of one eye.

171. The question of whether payouts under the loss of limbs and/or sight cover will lead to a 'disability superannuation benefit' will among other things depend on the nature of the occupation for which the relevant member is reasonably qualified.

172. Due to the uncertainty of the 'disability superannuation benefit' conditions being met, it is necessary to apportion the premiums under item 6 in the table in subsection 295-465(1).

#### *Actuary's certificate*

173. It is common for a complying superannuation fund to enter into a TPD insurance policy that seeks to adequately cover the risk of the fund providing both section 295-460 benefits (including 'disability superannuation benefits') and also benefits not covered by section 295-460. This means that the fund's insurance policy will cover a number of insured events in respect of its members.

174. Where the premiums for each type of insured event are not separately identified, subsection 295-465(3) requires that an actuary's certificate be obtained in order for the part of the premium that relates to section 295-460 benefits to be deductible under item 6 in the table in subsection 295-465(1). The actuary's certificate must be obtained prior to lodging the return and claiming the apportioned deduction. An actuary is defined in subsection 995-1(1) for these purposes as a 'Fellow or Accredited Member of the Institute of Actuaries of Australia'.

175. The actuarial task is to determine that part of the premium paid by a fund that is attributable to the fund's liability to provide a benefit referred to in section 295-460.

176. The actuary will also need to take into account the potential for overlap in event definitions and how this is dealt with in any payouts under the policy. For example, a fund providing permanent disability benefits may take out an insurance policy that provides benefits in relation to significant loss of limbs or sight events and also any occupation benefits (Refer to Example 5 at paragraphs 67 to 77 of this draft Ruling).

### ***No deduction***

177. An insurance premium is not deductible at all if it is certain that none of the insured events covered by that particular premium payment would result in a liability of the fund to provide a 'disability superannuation benefit'.

178. Any such premium payment clearly has no connection to a current or contingent liability of a fund to provide a 'disability superannuation benefit' according to paragraph 295-460(b).

### ***Alignment with definition of 'disability superannuation benefit'***

179. It is not necessary for the definition of insured events in a TPD insurance policy to exactly align with the definition of a 'disability superannuation benefit' in subsection 995-1(1) in order for a deduction to arise under subsection 295-465(1).

180. The relationship identified in subsection 295-465(1) is between insurance premiums paid by a fund and that fund's liabilities to provide 'disability superannuation benefits' to its members.

181. The recognition in subsection 295-465(1) that premiums may be paid for policies that are wholly or partly for current or contingent fund liabilities to provide section 295-460 benefits supports this position.

182. However, alignment between an insured event and section 295-460 benefit requirements will ensure that a deduction is available under item 5 in the table in subsection 295-465(1) for that part of a premium that is specified for such an event.

### ***Effect of superannuation fund trust deed***

183. In some circumstances, upon the happening of the specified event or the occurrence of a particular situation, the terms of the fund trust deed may, rather than requiring the trustee to provide the benefit, give to the member the right to make an election to receive that benefit.

184. The possibility and likelihood of a member electing not to receive a benefit in circumstances where an insured event has occurred and the member has satisfied both the permanent incapacity condition of release and the requirements of the 'disability superannuation benefit' definition referred to in paragraph 295-460(b) will not in itself deny deductibility of any premium paid for that insurance. This is due to the fact that, despite the possibility and likelihood of a member electing not to receive a benefit, the trustee has a contingent liability to provide the 'disability superannuation benefit' at the time the insurance premium is paid.

185. Each superannuation fund has its own governing rules (that is the trust deed). The trust deed will in most cases contain rules regarding the payment of benefits to members for TPD. The trustee must ensure that these rules are not wider than those provided for in the SISR. However, the governing rules of the fund may be narrower than those provided for in the SISR.

186. Whilst it is not expected to occur in many cases, there may be additional limitations imposed by trust deeds or fund rules on the ability of a fund trustee to provide paragraph 295-460(b) benefits to fund members. If the benefit payable by the insurer under a policy in respect of a member is greater than the benefit permitted to be paid out by the fund under the trust deed in relation to a 'disability superannuation benefit', there will need to be an apportionment of premium payments to the extent those payments relate to the excess. To the extent that the premium relates to this excess, the premium will not be deductible under subsection 295-465(1) (refer to Example 7 at paragraphs 85 to 90 of this draft Ruling).



## Appendix 2 – Your comments

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187. You are invited to comment on this draft Ruling. Please forward your comments to the contact officer by the due date.

188. A compendium of comments is also prepared for the consideration of the relevant Rulings Panel or relevant tax officers. An edited version (names and identifying information removed) of the compendium of comments will also be prepared to:

- provide responses to persons providing comments; and
- publish on the Australian Taxation Office website at [www.ato.gov.au](http://www.ato.gov.au).

Please advise if you do not want your comments included in the edited version of the compendium.

<b>Due date:</b>	<b>14 February 2011</b>
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## **Appendix 3 – Detailed contents list**

189. The following is a detailed contents list for this Ruling:

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## References

*Previous draft:*

Not previously issued as a draft

*Related Rulings/Determinations:*

TR 2006/10

*Subject references:*

- Complying superannuation funds
- Self managed superannuation funds
- Superannuation benefits
- Superannuation Funds- death or disability premiums
- Deduction & Expenses

*Legislative references:*

- ITAA 1997
- ITAA 1997 Div 295
- ITAA 1997 295-460
- ITAA 1997 295-460(a)
- ITAA 1997 295-460(b)
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- Alessi v. National Mutual Life Association of Australasia Ltd (1982) 2 ANZ Insurance Cases 60-481
- Cavill Power Products Pty Ltd v. Royle (1991) 42 IR 229
- Community Development Pty Ltd v. Engwirda Construction Co (1969) 120 CLR 455
- Edwards v. The Hunter Valley Co-op Dairy Co Ltd (1992) 7 ANZ Insurance Cases 61-113
- Nile v. Club Plus Superannuation Pty Ltd and Anor [2005] NSWSC 55
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- White v. The Board of Trustees [1997] 2 Qd R 659

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- Bowen C (Minister for Financial Services, Superannuation and Corporate Law) 2009, Transitional Relief for Superannuation Funds: Deductibility of Disability Benefit Premiums, media release, Canberra, 13 October

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