



CR 2001/16 - Income Tax: The assessability of bonuses received on the termination of the V and T Investment Bond Fund for investments held for less than 10 years

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 This document has changed over time. This is a consolidated version of the ruling which was published on *31 December 2000*



Class Ruling

Income Tax: The assessability of bonuses received on the termination of the V and T Investment Bond Fund for investments held for less than 10 years

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Preamble

*The number, subject heading, and the **What this Class Ruling is about** (including **Tax law(s)**, **Class of persons** and **Qualifications** sections), **Date of effect**, **Withdrawal**, **Arrangement** and **Ruling** parts of this document are a 'public ruling' in terms of Part IVAAA of the **Taxation Administration Act 1953**. CR 2001/1 explains Class Rulings and Taxation Rulings TR 92/1 and TR 97/16 together explain when a Ruling is a public ruling and how it is binding on the Commissioner.*

What this Class Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the 'tax law(s)' identified below apply to the defined class of persons, who take part in the arrangement to which this Ruling relates.

Tax law(s)

2. The tax law(s) dealt with in this Ruling are:
- Subsections 26AH(2), 26AH(4), 26AH(6) of the *Income Tax Assessment Act 1936* ('ITAA 1936').

Class of persons

3. The class of persons to whom this Ruling applies is:
- Investors in the V and T Investment Bond Fund (also known as the Flexible Insurance Fund) who have held the investment for less than 10 years at the date of the termination of the Fund.

Qualifications

4. The Commissioner makes this Ruling based on the precise arrangement identified in this Ruling.

5. The class of persons defined in this Ruling may rely on its contents provided the arrangement described below at paragraphs 10 to 11 is carried out in accordance with the details of the arrangement provided in this Ruling.

6. If the arrangement described in this Ruling is materially different from the arrangement that is actually carried out:

- (a) this Ruling has no binding effect on the Commissioner because the arrangement entered into is not the arrangement on which the Commissioner has ruled, and
- (b) this Ruling may be withdrawn or modified.

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Date of effect

8. This Ruling applies from 31 December 2000. However, the Ruling does 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 21 and 22 of Taxation Ruling TR 92/20).

Withdrawal

9. This Ruling is withdrawn and ceases to have effect after 31 December 2001. The Ruling continues to apply, in respect of the tax law(s) ruled upon, to all persons within the specified class who enter into the specified arrangement during the term of the ruling. Thus, the Ruling continues to apply to those persons, even following its withdrawal, for arrangements entered into prior to withdrawal of the Ruling. This is subject to there being no change in the arrangement or in the persons' involvement in the arrangement.

Arrangement

10. The V and T Investment Bond Fund (also known as the Flexible Insurance Fund) is a Benefit Fund of the Vic and Tas Friendly Society Ltd. It contains monies of members investing in Insurance Bonds. The policies issued by the Fund are eligible policies within the meaning of section 26AH(1) (ITAA 1936).

11. Following a member resolution at a Special General Meeting on 15 December 2000, the Fund is to be terminated by 30 June 2001. Investors in the Fund will be entitled to receive payment of their entitlements in the Fund on termination. A substantial minority of investors have held Investment Bonds with the Fund for less than 10 years and therefore bonuses received by them on the termination of the Fund are assessable under section 26AH of the *Income Tax Assessment Act 1936* either in full, or partially if held for more than 8 but less than 10 years. Some investors may reinvest their full entitlement from the Bond Fund in a like product with another Friendly Society or Life Company by either:

- (a) receiving their entitlements and reinvesting them personally; or
- (b) by directing the Vic and Tas Friendly Society Ltd to reinvest their entitlements.

12. The Commissioner has been requested to provide his opinion as to whether this will be treated as a continuation of the original investment under subsection 26AH(2), as opposed to the investors receiving an amount or being taken to have received an amount under subsection 26AH(4).

Ruling

13. The reinvestment by a taxpayer (the subject of this Ruling) in a like product with another Friendly Society or Life Company is not a continuation of the eligible policy for the purposes of subsection 26AH(2).

14. A taxpayer who receives his or her entitlements and reinvests them personally has received an amount for the purposes of subsection 26AH(6).

15. A taxpayer who directs the Vic and Tas Friendly Society Ltd to reinvest his or her entitlements is taken to have received an amount for the purposes of subsection 26AH(4).

16. In either case, the assessable income of the taxpayer will include an amount received as a bonus on termination of the Fund under subsection 26AH(6) as follows:

- If the bonus is received during the first 8 years: assessable in full.
- If received during 9th year: two thirds assessable.
- If received in the 10th year: one third assessable.

(**Note:** A section 160AAB rebate of 33% is available to investors for an amount included in assessable income under section 26AH.)

Explanations

If the investors' entitlements in the Fund were transferred directly into a similar product with another Friendly Society or Life Company

17. Subsection 26AH(6) of the *Income Tax Assessment Act* includes bonuses **received** under short term Life Policies in the taxpayers assessable income if they are received within 10 years of the date of the commencement of risk of the policy. These bonuses are reversionary bonuses which are only received on surrender or completion of the policy and are not assessable under any other provision of the ITAA 1936.

18. Subsection 26AH(4) expands the definition of "received" in subsection 26AH(6) to include amounts reinvested or otherwise dealt with on his behalf or as he directs.

19. Subsection 26AH(2) provides that no amount shall be taken to have been reinvested or otherwise dealt with on behalf of the taxpayer or as he directs in connection with the issue of the paid up policy if a paid up policy is issued in lieu of an eligible policy and the paid up policy shall be a continuation of the eligible policy.

20. The term 'paid up policy' is not defined in the ITAA but is defined in section 96 of the *Life Insurance Act 1945* with a similar provision in section 209 of the *Life Insurance Act 1995*.

Section 96 provides that:

"Where a policyowner who desires to discontinue further premium payments on a policy on which not less than 3 years' premiums have been paid in cash makes application to the Company for a paid up policy-

- (a) the company shall vary the policy so as to provide for the payment, in lieu of the amount originally payable, of an amount not less than the amount determined in

accordance with the rules set out in Part 1 of the Sixth Schedule and

- (b) the policy as so varied shall be taken, for the purposes of that Part of that schedule, to be a paid up policy.

21. In Tax Ruling IT 2346 which considers the taxation of Life Insurance Bonuses under section 26AH, the term ‘paid up policy’ in section 26AH(2) is referred to as applying to a situation where insurance premiums are discontinued as in the Life Insurance Act definition. It states at paragraph 14 that:

“where a policyholder decides to discontinue premium payments and is issued with a paid up policy in lieu of the original policy, sub section 26AH(2) operates to deem the paid up policy to be a continuation of the existing policy.”

The definition of “paid up” policy in the ITAA36 is the same as that in the Life Insurance Act.

22. The term paid up policy in the Life Insurance Act applies to paid up policies issued by the same Life Company that has issued the eligible policy, not another Company issuing a replacement policy to a former policyholder of another Life Insurance Company.

23. A paid up policy issued by another Friendly Society or Life Company will not be a continuation of an existing eligible policy under subsection 26AH(2) of the *Income Tax Assessment Act 1936* (ITAA 1936).

24. If Vic and Tas Friendly Society has already issued a “paid up policy” in lieu of an eligible policy, a policy issued by another Life Company as a “replacement” for that paid up policy is not issued in lieu of an eligible policy. A paid up policy is specifically deemed to be a continuation of an eligible policy by subsection 26AH(2) but is not, of itself, an eligible policy under the definition in subsection 26AH(1).

If the investors’ entitlements were paid to the investor on termination of the Fund and the amount subsequently reinvested in a like product

25. If the investors’ entitlements are received by the investors after the termination of the Fund, there is an actual receipt of an amount under subsection 26AH(6) and therefore questions about deemed receipt under subsection 26AH(4) are not relevant. A paid up policy issued by another Life Company or Friendly Society will not be a continuation of an existing policy under subsection 26AH(2) of ITAA 1936.

Detailed contents list

26. Below is a detailed contents list for this Class Ruling:

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Commissioner of Taxation23 May 2001

Previous draft:

Not previously issued in draft form

Legislative references:

- ITAA 1936 26AH

- ITAA 1936 26AH(1)

Related Rulings/Determinations:

IT 2346

- ITAA 1936 26AH(2)

- ITAA 1936 26AH(4)

- ITAA 1936 26AH(6)

Subject references:

- Short-term life assurance policies

- Life Insurance Act 1945 96

- Life Insurance Act 1995 209

ATO References

NO T2001/007797

BO

FOI number: I 1025076

ISSN: 1445 2014