

TD 2000/D7 - Income tax: what is the method of calculating the capital value of purchased pensions not payable for life for the purposes of the reasonable benefit limits (RBLs)?

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This document has been finalised by TD 2000/29.

Draft Taxation Determination

Income tax: what is the method of calculating the capital value of purchased pensions not payable for life for the purposes of the reasonable benefit limits (RBLs)?

Preamble

Draft Taxation Determinations (DTDs) present the preliminary, though considered, views of the Australian Taxation Office. DTDs should not be relied on; only final Taxation Determinations represent authoritative statements by the Australian Taxation Office.

1. A pension is regarded as purchased when the rules providing for the pension are based on an identifiable lump sum amount. For example, the purchase price of an allocated pension is the account balance on the 'commencement day' of the allocated pension. The 'commencement day' is defined in section 140C of the *Income Tax Assessment Act 1936* as the first day of the period to which the first payment of the pension relates.
2. The method for calculating the capital value of a fixed term pension when the entitlement is a defined benefit is set out in Draft Taxation Determination TD 2000/D6. For these purposes, a pension is a defined benefit if it is not fully determined by the purchase price, but is determined by reference to factors such as salary before retirement, years of service or the governing rules of the fund.
3. Under subsection 140ZO(2) of the *Income Tax Assessment Act 1936*, the Commissioner must determine in writing a method for calculating the capital value of a superannuation pension that is not payable for life. Allocated pensions come within subsection 140ZO(2) as they are not payable for life. In addition, purchased pensions not payable for life, including pensions which satisfy the standards of subregulation 1.06(7) of the Superannuation Industry (Supervision) Regulations (SISR), come within subsection 140ZO(2).
4. The formula used to determine the capital value of all purchased pensions that are not payable for life is:

$$\text{Capital Value} = \text{Purchase Price} - (\text{Undeducted Contributions} + \text{Concessional Component} + \text{Invalidity Component})$$

where:

Purchase Price is the purchase price of the pension. Where the fund has underlying assets that provide for the pension, the assets must be valued at their net market value on the commencement

day of the pension. It is this value that must be reported to the ATO. In recognition of the costs involved for superannuation funds in obtaining valuations, the ATO will accept the most recent valuation obtained within the last 12 months of the commencement day of the pension. This would include valuations obtained for other statutory purposes.

Undeducted Contributions is the amount of the undeducted contributions as defined in subsection 27A(1).

Concessional Component is the amount of the concessional component as defined in subsection 27A(1).

Invalidity Component is the amount of the post-June 1994 invalidity component as defined in subsection 27A(1).

5 For RBL reporting purposes, the components of the purchase price must be calculated by reference to the amount of the purchase price and eligible service period of the pension at the commencement day. In effect, the purchase price is treated as a notional Eligible Termination Payment (ETP).

6 The capital value calculated in paragraph 4 is used to determine whether a pension not payable for life (whether a fixed term pension or an allocated pension), paid to a person is within the person's lump sum or pension RBLs.

Example 1

On 30 May 2000 Andrew, then aged 70, commences to receive a pension which has a purchase price of \$600,000. It includes undeducted contributions of \$20,000, concessional component of \$25,000 and a post-June 1994 invalidity component of \$10,000.

Andrew's life expectancy determined by reference to the relevant prescribed Life Tables prepared by the Australian Government Actuary is 12.8 years. Andrew's pension is therefore payable for a fixed term of 13 years and meets the requirements of subregulation 1.06(7) (SISR). The capital value of the pension is:

$$\begin{aligned}\text{Capital Value} &= \$600,000 - (\$20,000 + \$25,000 + \$10,000) \\ &= \$545,000\end{aligned}$$

Example 2

The Cross Superannuation Fund has two members, Alister and Caroline, and has assets of \$200 000 valued at historical cost that will provide pensions. Based on historical cost, Alister and Caroline have member accounts of \$150,000 and \$50,000 respectively.

Alister retires in February and commences to receive an allocated pension. The net market value of the fund's assets underlying Alister's pension is \$300,000. The purchase price of Alister's pension reported to the ATO is therefore \$300,000. This includes undeducted contributions of \$50,000. The capital value of the pension is:

$$\begin{aligned}\text{Capital Value} &= \$300,000 - (\$50,000 + \$0 + \$0) \\ &= \$250,000\end{aligned}$$

Example 3

Caroline, from example 2, decides to retire in September of the same year. Providing no later valuations have been obtained, the superannuation fund can use the valuation of the fund's assets that was originally obtained when Alister retired in February. At that time the net market value of assets underlying Caroline's allocated pension was \$100,000. At the date the pension commenced Caroline's account included \$20,000 undeducted contributions.

The capital value of the pension is:

$$\begin{aligned}\text{Capital Value} &= \$100,000 - (\$20,000 + \$0 + \$0) \\ &= \$80,000\end{aligned}$$

Your comment

7. We invite you to comment on this Draft Taxation Determination. We are allowing 4 weeks for comments before we finalise the Determination. If you want your comments considered, please provide them to us within this period.

Comments by Date: 12 May 2000
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Commissioner of Taxation

12 April 2000

Previous draft:

Not previously issued in draft form

Related Rulings/Determinations:

Draft TD 2000/D6

Subject references:

- eligible termination
- fixed term pensions;
- payments;
- pension capital value;
- reasonable benefit limits;
- superannuation pensions;
- superannuation funds;

Legislative references:

ITAA 140ZO(1);

ITAA 140ZO(2);

ATO references:

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