


TD 2013/D7 - Income tax: in what circumstances is an asset of a complying superannuation fund a segregated current pension asset under section 295-385 of the Income Tax Assessment Act 1997?

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Draft Taxation Determination

Income tax: in what circumstances is an asset of a complying superannuation fund a segregated current pension asset under section 295-385 of the *Income Tax Assessment Act 1997*?

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Ruling

1. An asset of a complying superannuation fund will be invested, held in reserve or otherwise being dealt with¹ for the sole purpose of enabling a fund to discharge liabilities payable in respect of superannuation income stream benefits² ('the relevant sole purpose'), where the whole asset is so invested, held or dealt with.³ To meet the requirements of paragraph 295-385(3)(a) or subsection 295-385(4) of the *Income Tax Assessment Act 1997* (ITAA 1997):

- an asset cannot be partly invested, held or dealt with partly for the relevant sole purpose and partly for another purpose; and
- part of an asset cannot be invested, held or dealt with for the relevant sole purpose, and another part of the asset invested, held or dealt with for another purpose.

¹ The meaning of 'invested, held in reserve or otherwise being dealt with' is discussed at paragraphs 64 to 67 in the Explanation section of this Determination.

² Under subsection 295-385(4) of the ITAA 1997. Paragraph 295-385(3)(a) has the same requirements: see paragraph 44 in the Explanation section of this Determination.

³ An asset held for the relevant sole purpose will be a segregated current asset when the additional requirements of paragraphs 295-385(3)(b) or 295-385(4)(b) of the ITAA 1997 are met.

2. That is the case for all types of assets that are capable of being a segregated current pension asset if invested, held or dealt with for the relevant sole purpose. Section 295-385 of the ITAA 1997 applies at the level of each single, discrete, indivisible asset at law, including:

- a bank account, being a single chose in action at law;⁴
- a share in a company, being a single chose in action at law;
- a unit in a trust, that is a discrete identifiable equitable interest;
- a legal title to a real property or a legal title to a lot in a strata title; and
- any other discretely identifiable item of legal or equitable property or right or interest that is an asset for the purposes of section 295-385 of the ITAA 1997.

3. Whether an asset is invested, held in reserve or otherwise being dealt with for the relevant sole purpose of enabling a fund to discharge liabilities in respect of superannuation income stream benefits is an objective question determined by examining all the facts and circumstances, particularly the allocation, application or distribution of the income from the asset. The purpose will be evidenced by records of the trustee, such as resolutions, accounting records, financial statements, investment strategies or policies, actuarial reports or certificates, bank account statements and share holding statements.

4. If a particular asset is a segregated current pension asset for only part of an income year, only the income that is received from the asset at the time that it is a segregated current pension asset will be exempt from income tax under section 295-385 of the ITAA 1997.⁵

5. Subsection 295-385(6) of the ITAA 1997 provides that assets held for the relevant sole purpose in respect of prescribed pensions under subsection 295-385(4) are not segregated current pension assets to the extent that the market value of the assets exceeds the account balance supporting the benefit. For each of the assets identified as being an asset contributing to the excess of the market value over the account balance, none of the income received from that asset will be exempt under section 295-385 of the ITAA 1997. However, section 295-390 may be applied to exempt a proportion of the income from such an asset.

6. Some receipts or outgoings⁶ that require apportionment or attribution between current pension liabilities and other liabilities⁷ will of necessity be paid to or from a single bank account. Where such amounts are paid to or from a segregated bank account held for the relevant sole purpose, in order to maintain segregation of the bank account the fund will have to make a transfer or set off between the fund's segregated bank account and its general bank account within a reasonable time.⁸

⁴ Due to the legal nature of a bank account being a single chose in action, a complying superannuation fund will need a separate bank account held for the relevant sole purpose, and another bank account held for other or general purposes, to segregate the bank account held for the relevant sole purpose. See further paragraphs 56 to 58 of the Explanation section of this Determination.

⁵ Paragraph 295-385(3)(a) and subsection 295-385(4) of the ITAA 1997 refer to an asset being a segregated current pension asset 'at a time' if it is being held for the relevant sole purpose 'at that time'. See further paragraph 55 in the Explanation section of this Determination.

⁶ For example a taxation refund or a taxation payment, or a dividend paid by a company in respect of which some of the shares held are segregated current pension assets and some are not.

⁷ That is, current pension liabilities, being liabilities (contingent or not) in respect of superannuation income stream benefits that are payable by the fund at a time, as distinguished from all other liabilities.

⁸ Twenty eight days would generally be considered a reasonable time.

7. Some essential incidental expenses payable by a complying superannuation fund may relate to the operation of the fund generally and may not be subject to apportionment. Payment of such essential incidental expenses from a segregated bank account will not prevent it from being a segregated current asset held for the relevant sole purpose.

8. Under section 295-385 of the ITAA 1997 there is no requirement to segregate assets in respect of each individual member of a complying superannuation fund who is in receipt of superannuation income stream benefits. Section 295-385 of the ITAA 1997 only requires segregation of the current pension assets as a whole, from the other assets of the fund, for the income from segregated assets to be able to be exempt from income tax.⁹

9. In the case of a complying superannuation fund which only has members in receipt of pensions prescribed for the purposes of subsection 295-385(4) of the ITAA 1997,¹⁰ where the value of the fund's assets does not exceed the value of current pension liabilities, it follows that all of the assets are segregated. In these circumstances, the apportionment approach under section 295-390 of the ITAA 1997 cannot be applied.

10. If an asset is purported to be segregated shortly before disposal, and then disposed of in circumstances where a capital gain is claimed to be exempt income, it will be a question of fact having regard to all the circumstances as to whether it was invested or otherwise being dealt with for the sole purpose of enabling the fund to discharge liabilities in respect of superannuation income stream benefits, and whether the anti-avoidance provisions in Part IVA of the *Income Tax Assessment Act 1936* (ITAA 1936) would apply in connection with the obtaining of a tax benefit, being an amount not being included in the assessable income of the fund.¹¹

Example 1: Segregated bank account and general bank account maintained

11. A complying superannuation fund has a bank account at call with a balance of approximately \$100,000 from time to time, and a one year term deposit with a balance of \$200,000. Both investments are solely for investing and holding money to enable the fund to discharge current pension liabilities in respect of the superannuation income stream benefits of Mr Barley and Mrs Barley. The combined value of their pension benefits is \$600,000.

12. The fund holds another bank account with a balance of \$250,000 in respect of the superannuation benefits of Mr Gargery and Ms Pirrip, who are yet to retire and are still in the accumulation phase. The fund also holds a real property rented as commercial premises, and shares in listed companies.

13. The records of the trustee of the fund record the purpose for which each bank account, the term deposit, the real property, and the shares are held. The accounting records and financial statements of the fund also deal with them on the basis that they are held for different purposes.

⁹ However, trustees of a fund could choose to segregate assets in respect of individual members where it is otherwise within their powers to do so.

¹⁰ See regulation 295-385.01 of the *Income Tax Assessment Regulations 1997*.

¹¹ The Explanatory Memorandum to the Taxation Laws Amendment (Superannuation) Bill 1989 that enacted section 273A of the ITAA 1936 stated: "While section 273A would allow assets to be transferred to and from the segregated current pension assets portfolio to meet movements in the level of current pension liabilities and changes in investment returns, it would be contrary to the intention of section 282B for assets to be transferred into the segregated current assets portfolio to avoid the imposition of capital gains tax. The general anti-avoidance provisions of Part IVA of the Principal Act stand as a barrier against any arrangements for asset transfers for capital gains tax avoidance". Section 295-385 of the ITAA 1997 is a 'rewrite' of section 273A of the ITAA 1936: see paragraph 42 in the Explanation section of this Determination.

14. Each bank account and the term deposit is legally a single separate asset. As separate bank accounts are maintained for the current pension liabilities and the other liabilities of the fund, the bank account supporting the current pension liabilities is a segregated current pension asset for the purposes of section 295-385 of the ITAA 1997, and interest earned from it will be exempt from income tax under subsection 295-385(1). That is also the case for the term deposit.

Example 2: Failure to segregate a single bank account

15. A complying superannuation fund has a bank account at call with a balance of approximately \$100,000 from time to time, maintained solely for investing and holding money to enable the fund to discharge current pension liabilities in respect of superannuation income stream benefits of two of its members.

16. The fund holds another bank account with a balance of \$250,000 in respect of the superannuation benefits of two other members, who are yet to retire and are still in the accumulation phase.

17. The trustees of the fund decide to close one of the bank accounts and transfer the moneys into the remaining bank account.

18. As a result, the remaining bank account is not a segregated current pension asset, as the bank account, being a single asset, is only partly held to enable the fund to discharge liabilities in respect of superannuation income stream benefits payable at that time, and is partly for other purposes.

19. This is the case, despite the fund keeping its own accounting records in an attempt to identify which portion of the bank account's interest relates to the notional account balance supporting current pension liabilities.

Example 3: Dividend payment to segregated bank account, and transfer of part of the amount to general bank account within 28 days

20. A complying superannuation fund has two bank accounts. Bank Account 1 is a segregated current pension asset and as such is used to meet current pension liabilities. Bank Account 2 is held in respect of liabilities other than current pension liabilities.

21. The fund holds 10,000 shares in Hubble Ltd, of which 3,000 are segregated current pension assets. The shares are uncertificated and the fund is the registered shareholder on the stock exchange electronic sub-register maintained by Hubble Ltd. The fund keeps appropriate records to identify and trace the 3,000 segregated shares and the other 7,000 shares.

22. Hubble Ltd pays a dividend of \$1 per share, and makes a single payment of \$10,000 to Bank Account 1 by electronic funds transfer in respect of the 10,000 shares held by the fund.

23. The fund transfers \$7,000 to Bank Account 2 within 28 days of receiving the dividend. As \$7,000 was transferred from Bank Account 1 within a reasonable time, that bank account continues to be a segregated current pension asset.

Example 4: Incidental payments from a segregated bank account

24. A complying superannuation fund has two members, both of whom have retired and are in receipt of a current pension from the fund. Among other assets, the fund holds a single bank account, being a segregated current pension asset and used to fund part of the pension payments.

25. The fund makes necessary incidental payments (such as for its annual supervisory levy) from that bank account.

26. As such payments are both incidental and necessary, the bank account is still being maintained for the relevant sole purpose, and remains a segregated current pension asset.

Example 5: Segregation of particular identified assets

27. A complying superannuation fund has two members who are being paid pensions. Neither pension is a prescribed pension under the regulations for the purposes of subsection 295-385(4) of the ITAA 1997. Subsection 295-385(3) applies and an actuary's certificate is required when the fund trustee decides to use the segregated assets method.

28. The fund has two other members who have not retired and whose accounts are in accumulation phase. As at 1 July 2013 the fund trustee holds the following assets:

- a commercial real property on a single title valued at \$950,000 from which rent is received.
- 30,000 shares in Panks Ltd valued at \$20 each for a total of \$600,000, from which dividends are received. The shares are uncertificated and the fund is the registered shareholder on the stock exchange electronic sub-register maintained by Panks Ltd.
- 80,000 units in a listed property trust, the Casby Unit Trust valued at \$5.00 each for a total of \$400,000, from which distributions are received.
- a bank account with a balance of \$10,000 for the two members receiving pensions.
- a bank account with a balance of \$5,000 for the two members in the accumulation phase.

The trustee keeps appropriate records to identify and trace the uncertificated shares and units.

29. There are no other accounts for the two members receiving pensions. An actuary has determined that the amount of the current pension liabilities for the fund is \$900,000.

30. The commercial real property on a single title cannot be a segregated current pension asset for the purposes of section 295-385 of the ITAA 1997, because its market value exceeds the amount required to support the liabilities in respect of the superannuation income stream benefits payable to the two members. The bank account held for the two members receiving pensions is a segregated current pension asset under section 295-385 of the ITAA 1997, and the interest derived from it will be exempt from income tax under subsection 295-385(1).

TD 2013/D7

31. In respect of the shares and units, any combination of shares and units not exceeding a total market value of \$890,000 (for example 30,000 shares valued at \$600,000 and 58,000 units valued at \$290,000) can be held as segregated current pension assets, provided appropriate evidence is kept to demonstrate which shares and units are segregated.¹² The records of the trustee of the fund will need to record the purpose for which each asset is held, and the accounting records and financial statements of the fund will need to deal with them on the basis that they are held for different purposes.

Example 6: Effect of subsection 295-385(6)

32. A complying superannuation fund has three members. Two of the members have retired and are each in receipt of a pension from the fund. One member is still in accumulation phase.

33. Each of the two members has a pension account balance of \$60,000, meaning the fund has current pension liabilities of \$120,000.

34. The fund has total assets of \$250,000, comprised of two legal titles to real property to the value of \$100,000 and \$80,000, and a bank account with a balance of \$70,000.

35. As subsection 295-385(6) of the ITAA 1997 provides that an asset cannot be a segregated current pension asset to the extent that the market value exceeds the account balance supporting the benefit, only one of the above mentioned assets can be a segregated current pension asset. Attempting to segregate a second asset would contribute to the market value of the assets used to support the pensions being in excess of the current pension account balances¹³.

36. Although this limits the amount of exempt income calculated under section 295-385 of the ITAA 1997, section 295-390 may be used to apportion the income from assets which are not segregated current pension assets, so that a proportion of the income will be exempt.

Date of effect

37. When the final Determination is issued, it is proposed to apply from 1 July 2014. However, the Determination 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 Determination (see paragraphs 75 to 76 of Taxation Ruling TR2006 /10).

Commissioner of Taxation

7 August 2013

¹² See paragraphs 61 and 62 in the Explanation section of this Determination concerning identifying and tracing shares and units.

¹³ As an alternative, more bank accounts could be opened and the balance of the original bank account spread across multiple accounts, so as to potentially accommodate segregation of one or more of the new accounts with lower balances.

Appendix 1 – Explanation

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: Exempt income under Subdivision 295-F

38. Subdivision 295-F of the ITAA 1997 provides that the ordinary and statutory income of a complying superannuation fund may be exempt from income tax in two different circumstances:

- (i) where the income is derived from segregated current pension assets under section 295-385 (segregation); or
- (ii) where the income is apportioned under section 295-390 ('apportionment').

39. Segregation and apportionment can both be applicable to exempt different amounts of income of a complying superannuation fund in the same income year. For example some assets might be segregated for the discharge of part of the liabilities in respect of income stream benefits under section 295-385, and a proportion of the income received from the remainder of the assets might be exempt in accordance with the apportionment calculation under section 295-390 of the ITAA 1997.

Segregation

40. Subsection 995-1(1) of the ITAA 1997 states that 'segregated current pension assets' has the meaning given by section 295-385 of the ITAA 1997, which has two definitions of the term in subsections (3) and (4). Under subsections 295-385(3) and (4), assets of a complying superannuation fund are segregated current pension assets in two circumstances. Both subsections 295-385(3) and (4) provide that assets are segregated current pension assets at a time if the assets are invested, held in reserve or otherwise being dealt with at that time for the sole purpose of enabling the fund to discharge all or part of its liabilities (contingent or not) as they become due, in respect of superannuation income stream benefits.¹⁴ Each subsection has a respective different additional requirement, as follows:

- (i) Subsection 295-385(3) applies where the trustee obtains an actuary's certificate before the date of lodgement of the fund's income tax return for the income year to the effect that the assets and the earnings expected to be made from them would provide the amount required to discharge in full all or part of the fund's liabilities (contingent or not) in respect of superannuation income stream benefits payable by the fund as they fall due.

¹⁴ Although the wording of paragraph 295-385(3)(a) and subsection 295-385(4) is different in certain respects, these differences do not result in any differences in meaning or application between the two subsections: see further paragraph 44 in the Explanation section of this Determination.

- (ii) Subsection 295-385(4) applies in respect of superannuation income stream benefits prescribed in the regulations (three types of pensions have been prescribed: allocated pensions, market linked pensions, and account-based pensions, within the meaning of the Superannuation Industry (Supervision) Regulations 1994)¹⁵ that are payable by the fund at that time, subject to the exceptions in subsections (5) and (6).¹⁶

Apportionment

41. Where assets are not segregated under section 295-385 of the ITAA 1997, section 295-390 of the ITAA 1997 provides that a proportion of the income of a complying superannuation fund can be exempt from tax, calculated under a statutory formula based on the evidence of the fund's assets and liabilities stated in an actuary's certificate.

Section 295-385 of the ITAA 1997 and sections 273A and 282B of the ITAA 1936

42. Section 295-385 of the ITAA 1997 is a 'rewrite' of sections 273A and 282B of the ITAA 1936.¹⁷ (And section 295-390 of the ITAA 1997 is a rewrite of section 283 of the ITAA 1936). Section 295-385 was inserted into the ITAA 1997 by the *Tax Laws Amendment (Simplified Superannuation) Act 2007*. Paragraph 3.1 of the Explanatory Memorandum to the relevant Bill stated:

3.1 Schedule 1 to this Bill incorporates the provisions of Part IX of the *Income Tax Assessment Act 1936* (ITAA 1936) that deal with the taxation of superannuation entities into the *Income Tax Assessment Act 1997* (ITAA 1997). The rewritten provisions in Division 295 of the ITAA 1997 do not change the law as it currently operates under Part IX of the ITAA 1936.¹⁸

¹⁵ As at the date of issue of this Draft Determination: see regulation 295-385.01 of the *Income Tax Assessment Regulations 1997*.

¹⁶ Subsection 295-385(5) of the ITAA 1997 requires that at all times during the income year the liabilities of the fund (contingent or not) to pay superannuation income stream benefits were liabilities in respect of prescribed superannuation income stream benefits. Subsection 295-385(6) provides that assets supporting a superannuation income stream benefit prescribed by the regulations are not segregated to the extent that the market value of the assets exceeds the account balance supporting the benefit.

¹⁷ The Explanatory Memorandum to Tax Laws Amendment (Simplified Superannuation) Bill 2006 General Outline and financial impact, page 1: "The Tax Laws Amendment (Simplified Superannuation) Bill 2006 (this Bill) and supporting Bills ... rewrite the superannuation taxation law into the *Income Tax Assessment Act 1997* (ITAA 1997) to present a clear picture of the taxation of superannuation".

¹⁸ The Explanatory Memorandum to Tax Laws Amendment (Simplified Superannuation) Bill 2006 paragraph 3.1. See also: paragraph 3.14; Finding Table 1 – New law to old law; and Finding Table 2 – Old law to new law. Further, section 1-3 of the ITAA 1997 provides that the ITAA 1997 contains provisions of the ITAA 1936 in rewritten form, and if the ITAA 1936 expressed an idea in a particular form of words and the ITAA 1997 appears to have expressed the same idea in a different form of words in order to use a clearer or simpler style, the ideas are not taken to be different just because the different form of words were used. See also section 15AC of the *Acts Interpretation Act 1901* to the same effect in respect of Commonwealth legislation generally.

43. Specifically, subsection 295-385(3) is a rewrite of subsection 273A(1), and subsection 295-385(4) is a rewrite of subsection 273A(2). Former section 273A of the ITAA 1936 stated:

273A(1) Assets of a complying superannuation fund are segregated current pension assets of the fund at a particular time in a year of income for the purposes of this Part if:

- (a) the assets are invested, held in reserve or *otherwise being dealt with* at that time by the fund for *the sole purpose of enabling* the fund to discharge the whole or part of its current pension liabilities as they *become due*; and

....

273A(2) Assets of a complying superannuation fund are also segregated current pension assets of the fund at a particular time in a year of income for the purposes of this Part *if* the assets are invested, held in reserve or *otherwise being dealt with* at that time by the fund for the *sole purpose of enabling* the fund to discharge the whole or part of the current pension liabilities, as they *become due*, in respect of pensions that are prescribed by the regulations for the purposes of this section. [Emphasis added]

44. Paragraph 295-385(3)(a) of the ITAA 1997 contains the phrases: 'otherwise dealt with', 'solely to enable the fund' and 'as they fall due'. Subsection 295-385(4) of the ITAA 1997 contains the phrases: 'otherwise *being dealt with*', 'for the *sole purpose of enabling* the fund' and 'as they *become due*'. In respect of both of the definitions of segregated current pension asset in subsections 295-385(3) and (4) of the ITAA 1997, section 273A of the ITAA 1936 used the phrases: 'otherwise being dealt with', 'for the sole purpose of enabling' and 'as they become due'.

45. Having regard to the Explanatory Memorandum, both subsections 295-385(3) and (4) of the ITAA 1997 should be interpreted on the basis that they have the same meaning, and that meaning is derived from the phrases 'otherwise being dealt with', 'for the sole purpose of enabling', and 'as they become due' as used in section 273A of the ITAA 1936 and subsection 295-385(4) of the ITAA 1997.¹⁹

Ordinary and statutory income that is exempt to the extent that it would otherwise be assessable income and it is from segregated assets

46. Section 295-385 of the ITAA 1997 is headed 'Income from assets set aside to meet current pension liabilities'.²⁰ Under subsection 295-385(1) the ordinary income and statutory income of a complying superannuation fund for an income year is exempt from income tax to the extent that:

- it would otherwise be assessable income; and
- it is from segregated current pension assets.

47. The introduction of subsection 295-385(1) of the ITAA 1997 uses the words 'is exempt *to the extent that*' in providing that income from segregated current assets is exempt from tax, whereas section 282B of the ITAA 1936 provided that: 'Any amount of normal assessable income derived by a complying superannuation fund from assets that, when the income is derived, are segregated current pension assets, *is exempt from tax*'. [Emphasis added]

¹⁹ Had any change in meaning been intended by the change to the words, it would have been expected to been mentioned specifically in the Explanatory Memorandum.

²⁰ Under Division 950 of the ITAA 1997 headings to sections that are operative provisions are part of the Act.

48. In section 282B of the ITAA 1936 no question of apportionment of income from segregated assets arose, as the phrase ‘is exempt from tax’ was used rather than the phrase ‘is exempt from tax to the extent that’. Section 295-385 of the ITAA 1997 is a rewrite of that provision that does not change the law as it previously operated, as discussed above. Therefore the change of the phrase ‘is exempt from tax’ in section 282B of the ITAA 1936 to ‘is exempt from income tax to the extent that’ in subsection 295-385(1) of the ITAA 1997, does not change the meaning, or produce the result that part of an asset can be segregated, or an asset can be partly segregated, under paragraph 295-385(1)(b) of the ITAA 1997.

49. This interpretive approach is supported by the overall context and operation of Subdivision 295-F of the ITAA 1997.²¹ If part of an asset could be segregated, or an asset could be partly segregated, for the purposes of section 295-385 of the ITAA 1997, the apportionment provisions in section 295-390 of the ITAA 1997 would have limited operation or scope.

Identifying the asset and the sole purpose

50. The term ‘asset’ is not defined in the ITAA 1997 and therefore it takes its ordinary meaning having regard to the context in which it is used.²² The *Macquarie Dictionary* (Fifth Edition) defines ‘asset’ to mean ‘*an item of property; an economic resource*’. Similarly, the *LexisNexis Concise Australian Legal Dictionary* (Fourth Edition) defines an asset to be:

an item, whether tangible or intangible, having economic value to its owner which, if not already in the form of money, can be converted into money to the owner’s benefit.

51. It is consistent with these definitions to conclude that an asset must be a discrete identifiable item, whether tangible or intangible. Regard is to be had to the nature of the asset rather than any proprietary rights comprising the asset or that exist in relation to the asset’s income producing capabilities.

52. It is the entire asset that must be segregated if the asset is to meet the requirements of subsections 295-385(3) or (4) of the ITAA 1997 as a segregated current pension asset. What is the entire asset will depend on the nature of the asset in question. See further paragraphs 56 to 63 below in relation to bank accounts, shares, units in trusts and real property.

²¹ See *Commissioner of Taxation v. Unit Trend Services Pty Ltd* [2013] HCA 161 at [47]; *Federal Commissioner of Taxation v. Consolidated Media Holdings Ltd* [2012] HCA 55; and *Project Blue Sky Inc v. Australian Broadcasting Authority* (1998) 194 CLR 355 at 381 [69]; [1998] HCA 28.

²² Statutory definitions related to ‘asset’ are consistent with this approach. Under subsection 10(1) of the *Superannuation Industry (Supervision) Act 1993*: “asset means any form of property and, to avoid doubt, includes money (whether Australian currency or currency of another country)” (see also the definition of ‘acquirable asset’ in section 67A of that Act). ‘CGT asset’ is defined in section 108-5 of the ITAA 1997 as “any kind of property” or “a legal or equitable right that is not property” and also includes part of an asset. Examples of CGT assets stated are ‘land and buildings’ and ‘shares in a company and units in a trust’. See also SMSFR 2012/1.

53. The sole purpose requirement in subsections 295--385(3) and (4) of the ITAA 1997 also requires that the asset only be invested, held or otherwise dealt with for the relevant purpose, and not partly for any other purpose. In *Ryde Municipal Council v. Macquarie University*²³ Gibbs ACJ referred to the decision of Windeyer J in *Randwick Corporation v. Rutledge* (1959) 102 CLR 54 and approved the following statement from that case:

When such words [as 'exclusively' or 'solely'] 'are present, it is a question of fact whether the land is being used for any purpose outside the stipulated purpose... As Kitto J. said in *Lloyd v. Federal Commissioner of Taxation* (48), such words confine the use of the property to the purpose stipulated and prevent any use of it for any purpose, however minor in importance, which is collateral or independent, as distinguished from incidental to the stipulated use.

54. As an asset is required to be invested, held or otherwise dealt with for the sole purpose of discharging superannuation income stream benefit liabilities, it is not possible to meet this requirement if an asset, and the income from that asset, is serving more than one purpose.

55. If an asset is a segregated current pension asset for only part of an income year, only the income of the complying superannuation fund that is received from the asset at the time that it is a segregated current pension asset will be exempt from income tax under section 295-385 of the ITAA 1997. Subsections 295-385(3) and (4) refer to assets being segregated 'at a time' if they are held for the relevant sole purpose at that time. The purpose for which the asset is held at the time income is received will determine whether or not the asset is segregated and the income is exempt. If income is received at a time an asset is segregated, it will be from a segregated current asset for the purposes of subsection 295-385(1). If income is derived at a time an asset is not segregated it will not be exempt under subsection 295-385(1).

Bank Accounts

56. A deposit with a bank is a single loan from the customer to the bank.²⁴ The balance of the money in the bank account standing to the customer's credit is an accruing debt that the bank owes to the customer²⁵ that arises out of one continuing contract between the customer and the bank.²⁶ A new contract is not created with each separate deposit;²⁷ where deposits have been made to an account over time they form one blended fund, the parts of which have no longer any distinct existence.²⁸ The bank is free to use the money as its own and, once deposited, the customer has parted with all control over the money. The bank is simply obliged to return an equivalent amount of money by paying the same sum as that deposited, upon demand of the customer.²⁹ The moneys in the account are treated as one single debt, and the debt and the right of the customer to request payment and withdraw their moneys, represent a single chose in action, not a composite or multiples.³⁰

²³ (1978) 139 CLR 633; (1978) 53 ALJR 179; (1978) 55 LGRA 373; (1978) 23 ALR 41; [1978] HCA 58.

²⁴ *Parker v. Marchant* (1843) 1 PH 356.

²⁵ *Walker v. The Bradford Old Bank Ltd* [1884] QBD 511.

²⁶ *Joachimson v. Swiss Bank Corp* [1921] 3 KB 110.

²⁷ *Hart (HMIT) v. Sangster* [1957] 1 Ch 329.

²⁸ *Devaynes v. Noble (Clayton's Case)* (1816) 1 Mer 529; (1816) 35 ER 781.

²⁹ *Foley v. Hill* [1848] 2 HLC 28.

³⁰ *Alcom Ltd v. Republic of Colombia* [1984] 1 AC 580; *Croton v R* (1976) 117 CLR 326.

57. The moneys standing to the credit of a bank account are one single chose in action being the accruing debt owed by the bank to the customer from time to time, and therefore one single asset for the purpose of section 295-385 of the ITAA 1997. The moneys standing to the credit of the account are incapable of being separated into multiple choses in action as they form one single fund once deposited. The fact that the bank account is held by, or in the name of, a trustee does not change that.

58. Due to the legal nature of a bank account being a single chose in action, a complying superannuation fund will often require two separate bank accounts in order to maintain one of them as a segregated bank account. A separate bank account will need to be held for the relevant sole purpose, and another bank account may need to be held for other or general purposes, to segregate the bank account held for the relevant sole purpose.

Shares

59. Each share in a company is a single separate chose in action, and therefore each share is an asset for the purposes of section 295-385 of the ITAA 1997. For the purposes of segregating shares under section 295-385 of the ITAA 1997 issues of identification and tracing arise.

60. Some shares issued in certificated form may be numbered on the paper share certificate or in the company register, and specific shares or parcels may be able to be identified and traced by that means. Listed shares are usually held in uncertificated form as part of an electronic clearing house register system.³¹ Listed uncertificated shares are not numbered and are not individually identifiable, unlike some certificated shares. Listed uncertificated shares will be held on an electronic sub-register maintained by either the electronic exchange trading clearing house, or by the company issuing the shares (or its registry service). The shareholder will receive a unique identification number either from an exchange participant (for example a broker) in respect of all shares held through that participant, or from the issuer of the shares (the company or its registry service) to identify their shareholdings.³² The balance of the shareholder's shareholding for each company will be shown for each identification number in statements issued by either the participant or the issuer. Uncertificated shares cannot be specifically identified.

61. Where uncertificated or certificated shares cannot be specifically identified, but appropriate accounting records are maintained of the acquisition and disposal of shares,³³ that will be sufficient to specifically identify shares to segregate them for the purposes of section 295-385 of the ITAA 1997. If appropriate acquisition and disposal records of shares are not maintained, the shares will not be segregated assets for the purpose of section 295-385 of the ITAA 1997, where the market value of a shareholding exceeds the amount (or the part of the amount remaining after accounting for other segregated assets) required to discharge liabilities (contingent or not), as they become due, in respect of superannuation income stream benefits. In the absence of unusual circumstances that might make it inappropriate, a first in first out (FIFO) rule will be an acceptable method of determining which shares have been disposed of.

³¹ For example the Australian Stock Exchange ('ASX') Clearing House Electronic Subregister System ('CHESS').

³² In the case of the ASX CHESS system, a holder identification number (HIN) from a market participant, and a security holder reference number (SRN) from a company or share registry.

³³ In accordance with TR 96/4 *Income Tax: valuing shares acquired as revenue assets*, paragraphs 13 to 16, and 26 to 48.

Unit Trusts

62. The same approach applies to identifying and tracing certificated and uncertificated units in a trust, to that set out for shares stated above.

Real property

63. Generally each title to real property is an asset for the purposes of section 295-385. In the case of residential or commercial real property it is a title to land including any building on it, or a title to a lot in a strata title, that comprises the asset for this purpose, rather than any lease agreement which secures the payment of rent. Where a single building or improvement is built on unconsolidated multiple titles to land, it will be a question of fact as to whether the individual titles to land are capable of being segregated assets, or whether a building on land on multiple titles is so integrated that it is not possible to segregate the individual titles to land.

‘Invested, held in reserve or otherwise dealt with’

64. Subsections 295-385(3) and (4) of the ITAA 1997 provide that assets of a complying superannuation fund are segregated assets at a time if ‘the assets are invested, held in reserve or otherwise dealt with’ for the requisite purpose.

65. An asset will be ‘invested’ for that purpose where the asset is held to receive income to enable the fund to discharge superannuation income stream benefits. For example a real property investment from which rent is applied to paying a pension; or a share investment, from which dividends are applied to paying a pension.

66. An asset will be ‘held in reserve’ for that purpose, where the asset is held for that purpose but is not producing income for a period of time. For example a rental property may be a segregated current pension asset held in reserve for that purpose when the property is vacant for a period in between tenancies while a new tenant is sought, or repairs are undertaken.

67. An asset will be ‘otherwise dealt with’ for that purpose, where the asset is held for that purpose in other circumstances to which the phrases ‘invested’, or ‘held in reserve’ are not applicable. For example shares that are lent under a securities lending agreement for a lending fee.

Consideration of subsection 295-385(6)

68. Subsection 295-385(6) is an exception to subsection 295-385(4) of the ITAA1997 in the case of prescribed superannuation income streams. Under subsection 295-385(6) of the ITAA1997 assets will not be segregated current pension assets to the extent that the market value of the assets exceeds the account balance supporting the benefit.

69. Subsection 295-385(6) of the ITAA1997 had no equivalent in Part IX of the ITAA1936 prior to 1 July 2007. Subsection 295-385(6) was inserted into Division 295 by a later amendment Act than that which enacted Division 295 of the ITAA 1997, although it also applied from the 2007-8 income year.³⁴ The Explanatory Memorandum to the Bill that introduced subsection 295-385(6) of the ITAA 1997 stated:

5.39 Under section 295-385 of the ITAA 1997, income of a complying superannuation fund that is derived from 'segregated current pension assets' (as defined in that section) is exempt from tax.

5.40 These amendments provide that assets supporting a superannuation income stream benefit which is being paid as an allocated pension, a market-linked pension or an account-based pension, are not considered segregated current pension assets to the extent that the value of those assets exceeds the value of the account balance supporting the income stream benefit. [*Schedule 5, item 5, subsection 295-385(6) of the ITAA 1997*]

5.41 The effect of this integrity change is that assets which are not included in a pension account balance will not be considered segregated current pension assets and therefore any income derived from those assets will not be exempt from tax.

70. Subsection 295-385(6) of the ITAA 1997 provides that assets held for the relevant sole purpose in respect of prescribed pensions under subsection 295-385(4) are not segregated current pension assets to the extent that the market value of the assets exceeds the account balance supporting the benefit. For each of the assets identified as being an asset contributing to the excess of the market value over the account balance, none of the income received from that asset will be exempt under section 295-385 of the ITAA1997. However, section 295-390 may be applied to exempt a proportion of the income from such an asset.

71. The use of the phrase 'to the extent' in the context of this provision does not apportion an asset as between being partly segregated and not segregated, or apportion a part of the total income received from all of the assets. Rather, it applies to apportion all of the assets considered as a whole, to ensure that some of those assets (each in its entirety) are identified and excluded from being treated as segregated current pension assets, to the extent of the excess of the market value of all of the assets over the account balance supporting the benefit. In circumstances where it is not apparent which of the assets represent the excess market value, it will be a matter for the trustees of a complying superannuation fund to identify which assets represent the excess.

72. Subsection 295-385(6) relies on an asset first being treated as a 'segregated current pension asset' under subsection 295-385(4), with both subsections referring to superannuation income stream benefits as prescribed by the *Income Tax Assessment Regulations 1997*. Similarly to subsection 295-385(5), subsection 295-385(6) operates to modify the result of subsection 295-385(4) of the ITAA 1997 .

73. This approach to subsection 295-385(6) of the ITAA 1997 is consistent with the sole purpose requirement in subsection 295-385(4). As previously discussed above in relation to subsection 295-385(1) of the ITAA 1997, if an apportionment approach was adopted in relation to particular assets for section 295-385, it would be contrary to the use of the word 'solely' in subsections 295-385(3) and (4), and would leave no room for the application of section 295-390, which applies an apportionment approach in cases where assets are not segregated.

³⁴ Division 295 [including section 295-385 subsections (1) to (5)] was enacted by *Tax Laws Amendment (Simplified Superannuation) Act 2007* Act No 9 of 2007; subsection 295-385(6) was inserted by *Tax Laws Amendment (2007 Measures No. 4) Act 2007* Act No 143 of 2007.

Appendix 2 – Your comments

74. You are invited to comment on this draft Determination including the proposed date of effect. Please forward your comments to the contact officer by the due date.

75. A compendium of comments is 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
- be published on the ATO website at www.ato.gov.au

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

Due date: 4 September 2013
Contact officer: Mladen Bajic
Email address: mladen.bajic@ato.gov.au
Telephone: (02) 9374 8096
Facsimile: (02) 9374 2693
Address: Australian Taxation Office
GPO Box 9977
Sydney NSW 2001

References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

SMSFR 2012/1; TR 96/4; TR 2006/10

Subject references:

- Exempt income of superannuation funds
- Segregated current pension assets
- Superannuation fund income

Legislative references:

- AIA 1901 15AC
- ITAA 1936 Pt IVA
- ITAA 1936 Pt IX
- ITAA 1936 273A
- ITAA 1936 273A(1)
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- ITAA 1936 282B
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- ITAA 1997 295-385
- ITAA 1997 295-385(1)
- ITAA 1997 295-385(1)(b)
- ITAA 1997 295-385(3)
- ITAA 1997 295-385(3)(a)
- ITAA 1997 295-385(3)(b)
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- ITAA 1997 295-385(6)
- ITAA 1997 295-390
- ITAA 1997 Div 950
- ITAA 1997 995-1(1)
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- SISA 1993 10(1)
- SISA 1993 67A
- *Tax Laws Amendment (2007 Measures No. 4) Act 2007* Act No 143 of 2007
- *Tax Laws Amendment (Simplified Superannuation) Act 2007* Act No 9 of 2007

Case references:

- *Alcom Ltd v. Republic of Colombia* [1984] 1 AC 580
- *Commissioner of Taxation v. Unit Trend Services Pty Ltd* [2013] HCA 161
- *Croton v. R* (1976) 117 CLR 326
- *Devaynes v. Noble* (1816) 1 Mer 529; (1816) 35 ER 781
- *Federal Commissioner of Taxation v. Consolidated Media Holdings Ltd* [2012] HCA 55
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- *Lloyd v. Federal Commissioner of Taxation* (1955) 93 CLR 645
- *Parker v. Marchant* (1843) 1 PH 356
- *Project Blue Sky Inc v. Australian Broadcasting Authority* (1998) 194 CLR 355
- *Randwick Corporation v. Rutledge* (1959) 102 CLR 54
- *Ryde Municipal Council v. Macquarie University* (1978) 139 CLR 633; (1978) 53 ALJR 179; (1978) 55 LGRA 373; (1978) 23 ALR 41; [1978] HCA 58
- *Walker v. The Bradford Old Bank Ltd* [1884] QBD 511

Other references:

- Explanatory Memorandum to the Tax Laws Amendment (Simplified Superannuation) Bill 2006
- Explanatory Memorandum to the Taxation Laws Amendment (Superannuation) Bill 1989
- LexisNexis Concise Australian Legal Dictionary (Fourth Edition)
- Macquarie Dictionary (Fifth Edition)

ATO references

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