



TR 92/7 - Income tax: Life Assurance Companies - Total Income

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Taxation Ruling

Income tax: Life Assurance Companies - Total Income

*This Ruling, to the extent that it is capable of being a 'public ruling' in terms of Part IVAAA of the **Taxation Administration Act 1953**, is a public ruling for the purposes of that Part. Taxation Ruling TR 92/1 explains when a Ruling is a public ruling and how it is binding on the Commissioner.*

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What this Ruling is about

1. This Ruling sets out the amounts derived by a life assurance company which are to be included in 'total income' for the purposes of sections 113, 111C and 116CF of the *Income Tax Assessment Act 1936*.

Ruling

Section 113

2. Total income for the purposes of section 113 includes all items of assessable income, premiums in respect of life assurance policies and exempt income. Therefore, the following amounts are included in total income for the purposes of section 113:

- . taxable contributions transferred under section 275;
- . profits on sale of assets assessed under section 25;
- . net capital gains included in assessable income;
- . gross sales of trading stock;
- . gross sales income of joint ventures;
- . foreign income exempt under sections 23AH or 112B;
- . imputation gross ups;
- . foreign income gross ups;

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- . exempt income referable to exempt policies (section 112A) and eligible non-resident policies (section 112C);
- . exempt income relating to current pension liabilities (section 110C);
- . superannuation premiums;
- . other life insurance premiums;
- . accident and disability premiums (net of unearned premiums provision);
- . management fees received;
- . interest on overdue premiums; and
- . interest, rent and dividends.

The above list is not exhaustive.

Section 111C

3. Total income for the purposes of section 111C includes the same amounts as for section 113.

Section 116CF

4. Total income for the purposes of section 116CF is the sum of the assessable income for each of the classes of assessable income of a life assurance company reduced by any net capital gains included in assessable income under section 116CD.

Date of effect

5. This Ruling sets out the current practice of the Australian Taxation Office and is not concerned with a change in interpretation. Consequently, it applies (subject to any limitations imposed by statute) for years of income commencing both before and after the date on which it is issued.

Explanations

Section 113

6. Section 113 specifies what deduction may be allowed in respect of 'expenditure incurred ... in the general management of the business'

of a life assurance company. The section is not concerned with 'expenditure exclusively incurred in gaining or producing assessable income', which is fully deductible. It is not concerned with expenditure 'exclusively incurred in gaining or producing income that is not assessable income' which is not deductible at all. And the section is not concerned with expenditure of a capital nature. So subsection 113(3) excludes from expenditure in the general management of a life assurance company's business expenditure of a capital nature, expenditure exclusively incurred in gaining or producing assessable income, and expenditure exclusively incurred in gaining or producing income that is not assessable income.

7. A life company, the sole or principal business of which is life assurance, must use the formula set out in subsection 113(2) to ascertain the deductible general management expenditure, unless the company elects to use subsection 113(1). The amount of the expenditure that is deductible is calculated under subsection 113(2) according to the formula:

$$\text{General management expenditure} \times \frac{\text{Assessable income}}{\text{Total income}}$$

8. While there is no definition of the term total income for the purposes of subsection 113(2), subsection 111(2) applies so that the term includes premiums in respect of life assurance policies.

9. There is no case law on the meaning of total income in this context. However, we consider that the term includes the following amounts in addition to premiums:

- . income that is subject to tax; and
- . exempt income.

This is consistent with the explanation of the meaning of total income included in the Explanatory Memorandum on the amendments of the law which inserted existing section 113 (the section was inserted by the *Income Tax and Social Services Contribution Assessment Act 1961* (Act No. 17)). The Explanatory Memorandum at page 13 states:

'Total income includes income from premiums and exempt income, as well as income that is subject to tax.'

10. A further issue is whether total income includes items of assessable income which are not income under ordinary concepts. We consider total income does include all items of assessable income, irrespective of whether they are income under ordinary concepts. The term 'total income' should be read in the context of the section in which it appears (see comments by Gibbs J in *Avondale Motors (Parts) Pty. Ltd. v. FC of T* 71 ATC 4101 at 4106; (1971) 2 ATR 312 at 317). For the purposes of subsection 113(2), assessable income is a

subset of total income. This interpretation ensures that the application of the formula in subsection 113(2) fulfils the purposes of the section, namely, to allocate general management expenses between assessable income and exempt income in order to determine the deductible amount of the expenses.

Transferred taxable contributions

11. Under section 275 of the Act, the liability for tax on taxable contributions may be transferred by a complying superannuation fund or approved deposit fund to a life assurance company. Subsection 275(2) sets out the consequences of an amount of taxable contributions being specified in a notice for transfer. Under paragraph 275(2)(a) the amount of taxable contributions transferred is included in the assessable income of the life company, while under paragraph 275(2)(b) the same amount is excluded from the assessable income of the fund.

12. There is an argument that the taxable contributions transferred to a life assurance company under section 275 are not 'income' under ordinary concepts and therefore should not be part of total income. However, having regard to the comments in paragraph 10 above, we consider that the taxable contributions transferred do form part of total income.

Gains on sale of assets

13. A life assurance company is, generally, assessed under subsection 25(1) on income arising on the disposal of investment assets. However, specific provisions in the Act treat gains relating to the complying superannuation and rollover annuity business (CS/RA class) of a company as capital gains for the purposes of the capital gains provisions of the Act. In both cases, the amount to be included in assessable income is reduced by applying the formula in subsection 112A(1), which exempts a portion of the gains relating to exempt policies, or the formula in subsection 112C(2), which exempts a portion of the gains relating to eligible non-resident policies.

14. The net gain (or profit) on disposal of an asset assessed under subsection 25(1) is to be included in total income. The decision in *Australasian Catholic Assurance Co. Ltd. v. FC of T* (1959) 100 CLR 502; 11 ATD 577 is authority for including the net rather than the gross amount from a disposal. Also, the amount of any 'overall 160Z gain' which is included in a class of assessable income by section 116CD is to be included in total income. In the case of trading stock sales and sales income of joint ventures, the term total income is to include the gross amount. (Deductions under subsection 51(1) for a

loss on disposal of an asset will not reduce the amount of total income.)

15. Also to be included in total income is the amount by which a gain on disposal of an asset has been reduced by applying the formula in subsection 112A(1) or subsection 112C(2) (i.e., the amount of the gain that is referable to exempt policies or eligible non-resident policies).

Foreign income

16. For assessments for the 1987-88 to 1989-90 income years, life assurance companies were exempt from tax under section 112B of the Act on so much of the foreign income as was not remitted to Australia. It follows that the amount of foreign income derived during any of those years of income which was exempt by section 112B, is to be included in total income in respect of the relevant year for the purposes of section 113.

17. Section 112B was repealed so as not to apply to assessments for the 1990-91 income year and all subsequent years. From the 1990-91 income year, sections 23AH, 112A, or 112C of the Act exempt from tax certain foreign income of a life assurance company derived in carrying on a business at or through a permanent establishment in a foreign country. Foreign income which is exempt under sections 23AH, 112A or 112C is to be included in total income.

Imputation gross up

18. By subsection 160AQT(1A), a life assurance company which receives a franked dividend in respect of an asset included in its insurance funds is to include in its assessable income the amount of the imputation credit attached to the dividend. Consistent with the treatment of section 275 amounts (see paragraph 12 above) the amount of the imputation credit included in assessable income should also be included in total income.

Foreign income gross up

19. Section 6AC of the Act ensures that the amount of foreign income of a taxpayer for the purposes of the Act is the gross amount before the payment of any foreign tax. The effect of the section is that amounts of foreign taxes that are deemed to have been paid (for example, underlying taxes) are included in assessable income. Consistent with the treatment of section 275 amounts (see paragraph 12 above) the amount of the foreign tax included in assessable income should also be included in total income.

Section 111C

20. Section 111C requires a life assurance company to reduce certain deductions otherwise allowable to take account of exempt income derived by the company. Subsection 111C(1) sets out the deductions to which the section applies, namely, deductions, other than deductions allowable under section 51 or 113, not related exclusively to the assessable income of the life company.

21. By subsection 111C(2), a deduction which satisfies subsection 111C(1) is allowable only to the extent calculated using the formula:

$$\text{Deduction} \times \frac{\text{Assessable income}}{\text{Total income}}$$

where:

Total income is the total of all the amounts that would be the assessable income of the company if no exempting provisions applied.

22. Based on the definition in subsection (2), total income for the purposes of section 111C includes all amounts of exempt and assessable income derived by a life assurance company.

Section 116CF

23. Under section 116CF, current year deductions and notional Part IIIA disposals deductions (as defined in section 110) of a life assurance company are allocated to the classes of assessable income of a life assurance company for the purposes of determining the components of taxable income under section 116CJ.

24. Subsection 116CF(2) allocates the non-exclusive current year deductions of a company, to classes of assessable income using the formula:

$$\text{Residual current deductions} \times \frac{\text{Income of class}}{\text{Total income}}$$

where:

Total income is the amount of the total assessable income of the company, excluding the amount of any net capital gains included in assessable income under section 116CD.

25. The definition of total income in subsection 116CF(2) is clear. Total income is the sum of the assessable income for each of the classes of assessable income of a life assurance company (as calculated under section 116CE) reduced by any net capital gains included in assessable income under section 116CD.

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- Australasian Catholic Assurance Co. Ltd. v. FC of T (1959) 100 CLR 502; 11 ATD 577
- Avondale Motors (Parts) Pty. Ltd. v. FC of T 71 ATC 4101; (1971) 2 ATR 312