CR 2008/16 - Income tax: amendments to Sensible Saver Life Assurance Policy issued by Zurich Australia Limited

Class Ruling

Income tax: amendments to Sensible Saver Life Assurance Policy issued by Zurich Australia Limited

Contents Para

This Ruling provides you with the following level of protection:

This publication (excluding appendices) is a public ruling for the purposes of the *Taxation Administration Act 1953*.

A public ruling is an expression of the Commissioner's opinion about the way in which a taxation provision applies, or would apply, to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

If you rely on this ruling, we must apply the law to you in the way set out in the ruling (unless we are satisfied that the ruling is incorrect and disadvantages you, in which case we may apply the law in a way that is more favourable for you – provided we are not prevented from doing so by a time limit imposed by the law). You will be protected from having to pay any underpaid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state how the relevant provision applies to you.

What this Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant provision identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

Relevant provision(s)

2. The relevant provision dealt with in this Ruling is:

- section 26AH of the *Income Tax Assessment Act 1936* (ITAA 1936).

All subsequent legislative references are to the ITAA 1936 unless otherwise indicated.

Class of entities

3. The class of entities to which this Ruling applies are the policyholders of the 'Sensible Saver Life Assurance Policy' (the Policy) issued by Zurich Australia Limited (Zurich) who were policyholders at the time the Policy was varied and at the time of variation have held the Policy for a period less then 10 years, or whose eligible period in respect of the Policy is less than 10 years.

4. In this Ruling, the entities belonging to this class are referred to as 'policyholders'.

Qualifications

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

6. The class of entities defined in this Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 14 to 28 of this Ruling.

7. If the scheme actually carried out is materially different from the scheme that is described in this Ruling, then:

- this Ruling has no binding effect on the Commissioner because the scheme entered into is not the scheme on which the Commissioner has ruled; and
- this Ruling may be withdrawn or modified.

Date of effect

9. This Ruling applies to the income year ending 30 June 2008. However, the Ruling continues to apply after this date to all entities within the specified class who entered into the specified scheme during the term of the Ruling, subject to there being no change in the scheme or in the entities involved in the scheme.

10. 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. Furthermore, the Ruling only applies to the extent that:

- it is not later withdrawn by notice in the *Gazette*; or
- the relevant provisions are not amended.

11. If this Ruling is inconsistent with a later public or private ruling, the relevant class of persons may rely on either ruling which applies to them (item 1 of subsection 357-75(1) of Schedule 1 to the *Taxation Administration Act 1953* (TAA)).

12. If this Ruling is inconsistent with an earlier private ruling, the private ruling is taken not to have been made if, when the Ruling is made, the following two conditions are met:

- the income year or other period to which the rulings relate has not begun; and
- the scheme to which the rulings relate has not begun to be carried out.

13. If the above two conditions do not apply, the relevant class of person may rely on either ruling which applies to them (item 3 of subsection 357-75(1) of Schedule 1 to the TAA).

Scheme

14. The scheme that is the subject of this Ruling is described below. The description is based on the following documents. These documents or relevant parts of them as the case may be, form part of and are to be read with this description. The relevant documents or parts of documents incorporated into this description are:

- the application for Class Ruling from Greenwoods & Freehills dated 27 September 2007;
- the Policy; and
- the Policy incorporating the amendments.

15. The Policy is an insurance bond that provides for a structured monthly savings program designed to enable the accumulation of investor funds. In addition, it permits insurance benefits, in the form of life insurance and total and permanent disablement benefits, to be incorporated into the Policy to create a comprehensive savings and security package.

16. The Policy allows for Zurich to change the terms and conditions of the policy – subject to written notice being given to policyholders.

17. The Policy provides policyholders with two investment options:

Capital Stable Portfolio

This investment option holds a minimum of seventy-five percent (75%) in fixed interest securities or cash and a maximum of twenty-five percent (25%) in Australian equities listed on a recognised Stock Exchange.

Managed Portfolio

This investment option holds a minimum of twenty-five percent (25%) in fixed interest securities or cash and a maximum of seventy-five percent (75%) in Australian and overseas equities and property trusts on a recognised Stock Exchange.

18. Under the Terms and Conditions (the terms) of the Policy the minimum Account Balance to be maintained is $500 per portfolio fund.

19. Where the minimum Account Balance is at least $1,000 after withdrawal or 60 Monthly Contributions have been made there are no withdrawal fees. If the Policy is terminated or the Account Balance is below $1,000 Zurich will debit fees against the Account Balance by applying a scaling process.

20. The following fees also apply to the Policy:

Administration Fees

A monthly administration fee is debited from the Account Balance.

Contribution Fee

A contribution fee is debited against the Account Balance when a lump sum deposit or a monthly contribution is received. Lump sum contributions will not incur any contribution fee if they are made after 1 April 2005. Monthly contributions made after 1 April 2005 will incur a contribution fee of 5% of all regular contributions.

Investment Management Fee

A percentage of the investment return is retained by Zurich as an investment management fee. The percentage as from 1 April 2005 is 50% on average daily account balances of $0 - $1,499 and 40% on balances greater than $1,500.

Switching Fee

A switching fee of $27 per switch applies for switches in excess of four switches in any 12 month period.

Variation to the Policy

21. Zurich proposes to vary the Policy to:

- provide additional investment options and crediting of earnings on a daily basis;
- alter the basis on which fees are determined; and
- change the basis on which the valuation of the Policy is communicated from a dollar value to valuing on a notional unitisation basis.

22. Policyholders will have the option of investing in the following new or varied funds, each with their own benchmarks and ranges:

Capital Stable

Invests mainly in fixed interest securities and cash with some exposure to growth assets such as Australian and international shares and property securities.

Balanced

Invests in a balanced mix of income and growth assets, which may include Australian and international shares, fixed interest securities, property securities, and cash.

Managed Growth

Invests in a mix of Australian and international shares, fixed interest securities, property securities and cash.

Managed Share

Invests in Australian companies, including property securities, with a smaller allocation to shares listed on foreign stock exchanges.

International Shares

Invests in a broad selection of companies listed on foreign stock exchanges.

Cash

Invests in Australian wholesale money markets including bank guaranteed, government guaranteed and corporate securities.

23. The minimum Account Balance to be maintained is increased to $1,000. The scaling fee imposed on termination of the Policy or where the Account Balances is below $1,000 is withdrawn.

24. The investment management fee structure is altered to levy a fee of 1.3% on the Cash fund, 1.95% on the International Shares fund and 1.8% on all other funds.

25. The switching fee of $27 is also withdrawn.

26. The terms of the Policy have also been amended to guarantee a bonus to any policyholder who becomes disadvantaged because of the changes to the Policy. The bonus is determined when the policyholder exits the policy.

27. The notional unitisation approach will mean that the value of the policy will be determined at least once a week instead of on the last day of the quarter.

Other matters

28. The following describes the major elements that remain the same:

- the policy is a life insurance policy having regard to paragraph 9(1)(f) and paragraph 9(1)(g) of the *Life Insurance Act 1995*;
- the policy is an 'eligible policy', as defined for the purposes of section 26AH*;*
- there is no intention as between Zurich and the policyholders to terminate or replace the existing Policies;
- no new policy numbers are to be issued by Zurich to the policyholders; and
- the policy is a non-participating policy.

Ruling

29. Section 26AH does not apply to have the policyholders include an amount in assessable income as a consequence of the variation to the Policy.

Commissioner of Taxation
5 March 2008

Appendix 1 – Explanation

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

30. The Policy is a life insurance policy, other than a funeral policy, and the date of commencement of risk is after 27 August 1982.

31. Section 26AH includes in the assessable income of a taxpayer amounts received as or by way of bonuses under a life assurance policy where the date of commencement of risk is after 27 August 1982 and the amounts are received within 10 years of the date of commencement of the risk of the policy.

32. Where the terms of a life insurance policy are amended with the result that a new policy has been created the old life insurance policy is taken to have been rescinded. Any bonus that would have accrued under the old policy, though not received but applied for the benefit of the policyholder in relation to the new policy, is deemed to have been received by the policyholder under subsection 26AH(4). Subsection 26AH(6) applies to include, subject the number of years the policy was held for, the bonus in the policyholder's assessable income.

33. However, section 26AH will not apply if the terms of a life insurance policy are merely varied.

34. The legal analysis of the effect of a variation of a contract is found in the distinction between a variation of a contract and a rescission of a contract.

35. In *Dan v. Barclays Australia Limited* (1983) 46 ALR 437 (*Dan's case*), Wilson and Dawson JJ said at 448:

> The distinction between rescission and variation is discussed in such cases as *Tallerman & Co Pty Ltd v. Nathan's Merchandise (Vic) Pty Ltd* (1956) 98 CLR 93; *Morris v. Baron and Co* [1918] AC 1 and *British and Benington Ltd v. NW Cachar Tea Co* [1923] AC 48. Variation of an existing contract, whilst it in one sense always gives rise to a new contract, does not always result in a substituted contract which, in order to operate, must necessarily rescind the contract which is varied. Variation may take the form of rescission of some terms of an existing contract but if that is to have the effect of rescission of the whole contract, the rescission must be express or by necessary implication and the determining factor must always be the intention of the parties as disclosed by contract when varied …

36. The High Court in *Dan's case* applied the principle expressed in *Tallerman & Co Pty Ltd v. Nathan's Merchandise (Vic) Pty Ltd* (1956) 98 CLR 93 that the 'determining factor must always be the intention of the parties as disclosed by the later agreement': at CLR 144.

37. The intention of the parties is therefore a critical and deciding factor in determining whether a variation to a contract brings about a termination. In *Commissioner of Taxation v. Sara Lee Household & Body Care (Australia) Pty Ltd* (2000) 201 CLR 520; [2000] HCA 35; (2000) ALR 346; 2000 ATC 4378; (2000) 44 ATR 370 the High Court, in determining whether an amendment agreement had the effect of terminating the original contract, applied the principle in *Dan's case* on the intention of the parties and concluded at CLR 534, HCA paragraph 25, ALR 352; ATC 4383; ATR 375 that:

> The manifest intention of the parties was not that the agreement … should be wholly rescinded and replaced by a new agreement, but that the rights and liabilities under … the agreement, should be varied in certain respects.

38. The parties to the Policy, namely Zurich and the policyholder have not expressed the intention for the Policy to be terminated. The intention is to vary the policy to enhance certain features of the policy.

39. An intention to terminate a contract will also be inferred where, because the terms in a subsequent agreement are inconsistent with the terms of the original agreement, the two agreements are not intended to coexist: *British & Beningtons Limited v. North Western Cachar Tea Company Limited* [1923] AC 48 at 62. The new Policy terms are not inconsistent with what had been provided in the original Policy. The Policy continues to provide investment options, although on a more expansive scale than previously, and allows for the policyholder to switch investments without incurring the additional fee that had been prescribed in the original Policy. The fee changes are allowed under the terms of the Policy and merely involve a restructure of the basis on which Zurich levies fees.

40. Furthermore, an intention to terminate the original contract is unlikely to be inferred where the parties have not abandoned their rights: *Concut Pty Ltd v. Worrell* [2000] HCA 64; (2000) 176 ALR 693. Zurich has, in this regard, ensured that any disadvantaged policyholder would be entitled to a bonus. This guarantees the policyholders' rights to the benefits under the original Policy are maintained.

41. The change of valuation of the Policy from a dollar value to a unitised value, in line with industry practice, while a departure from the previous practice does not bring the original Policy to an end. The change will result in valuations being determined by the unit price for each unit linked investment fund at least on a weekly basis rather than quarterly but this does not alter the essential character of the Policy.

42. The new terms proposed for the Policy are not considered to rescind the original Policy. None of the new terms is so substantial as to rescind the original Policy. The new terms merely vary the Policy.

43. Accordingly, section 26AH does not apply to include an amount in the policyholders' assessable income.

Appendix 2 – Detailed contents list

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

References

Previous draft:

Not previously issued as a draft

Subject references:

- investment linked policies
- life insurance policies

Legislative references:

- ITAA 1936 26AH
- ITAA 1936 26AH(4)
- ITAA 1936 26AH(6)
- Life Insurance Act 1995 9(1)(f)
- Life Insurance Act 1995 9(1)(g)
- TAA 1953
- TAA 1953 Sch 1 357-75(1)
- Copyright Act 1968

Case references:

- British and Beningtons Limited v. North Western Cachar Tea Company Limited [1923] AC 48
- Commission of Taxation v. Sara Lee Household & Body Care (Australia) Pty Ltd (2000) 201 CLR 520; [2000] HCA 35; (2000) ALR 346; 2000 ATC 4378; (2000) 44 ATR 370
- Concut Pty Ltd v. Worrell [2000] HCA 64; (2000) 176 ALR 693
- Dan v. Barclays Australia Ltd (1983) 46 ALR 437
- Morris v. Baron and Co [1918] AC 1
- Tallerman & Co Pty Ltd v. Nathan's Merchandise (Vic) Pty Ltd (1956) 98 CLR 93

ATO references

NO:	2008/2946
ISSN:	1445-2014
ATOlaw topic:	Income Tax ~~ Assessable income ~~ life insurance bonuses and policies