


TD 2000/D6 - Income tax: what is the method for valuing fixed term defined benefit pensions for the purposes of the reasonable benefit limits (RBLs)?

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This document has been finalised by TD 2000/28.

Draft Taxation Determination

Income tax: what is the method for valuing fixed term defined benefit pensions 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 fixed term pension is a defined benefit pension 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.
2. The capital value of a fixed term pension which is purchased is calculated using the method set out in Draft Taxation Determination TD 2000/D7. A pension is regarded as purchased where the rules providing for the pension are based on an identifiable lump sum amount, for example an allocated pension.
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. Defined benefit pensions payable for a fixed term, including pensions which satisfy the standards of subregulation 1.06(7) of the Superannuation Industry (Supervision) Regulations, come within subsection 140ZO(2).
4. The capital value of a fixed term pension when the entitlement is a defined benefit is calculated using the following formula:

$$\text{Capital Value} = \left[\text{Annual Value} \times \text{Fixed Term Valuation Factor} \right] - \text{Undeducted Purchase Price} + \text{Residual Capital Value}$$

where:

Annual Value is the amount worked out by multiplying:

- (a) the greatest number of payments of the pension that could be made in respect of the 12 month period beginning on the commencement day of the pension,
- by
- (b) the amount of the first regular payment of the pension.

Fixed Term Valuation Factor is the pension valuation factor set out in the Table of Pension Valuation Factors for Fixed Term Pensions attached to this Determination.

Undeducted Purchase Price is the undeducted purchase price of the pension as defined in subsection 140ZO(1).

Residual Capital Value is the present value of the residual future capital value of the pension calculated by using the formula:

$$\text{Residual Capital Value} = A / (1.1)^n$$

where:

- A** is the residual capital value of the pension. This is the dollar amount the fund expects will be paid as a lump sum after a fixed term of n years.
- n** is the number of years, or parts of a year, between the commencement day of the pension and the payment of the residual capital value.

5. The capital value calculated in paragraph 4 is used to determine whether a fixed term pension paid to a person is within the person's lump sum or pension reasonable benefit limits (RBLs), as appropriate.

6. Where the indexation rate or the term of the pension lies outside the range of values specified in the Table of Pension Valuation Factors attached, full details surrounding the particular fixed term pension should be provided to the ATO in order to determine the relevant valuation factor.

Example

Mark has decided to retire and take a fixed term pension. The pension is for a term of 20 years and will be indexed at 5% pa. The first regular monthly payment of the pension will be \$1,200 and will be paid on the first of each month. The annual value of the pension is $\$1,200 \times 12 = \$14,400$. It has an undeducted purchase price of \$80,000. There is no residual capital value.

For the purposes of applying the RBLs, the capital value of the pension is calculated as:

$$\begin{aligned} \text{Capital Value} &= (\$14,400 * 12.77) - \$80,000 + \$0 \\ &= \$103,888. \end{aligned}$$

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.

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Commissioner of Taxation

12 April 2000

Previous draft:

Not previously issued in draft form

Related Rulings/Determinations:

Draft TD 2000/D7

Subject references:

- fixed term pensions
- pension capital value
- reasonable benefit limits
- superannuation funds
- superannuation pensions

Legislative references:

ITAA140ZO(1)

ITAA 140ZO(2)

ATO references:

NO T2000/6193

BO

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ATTACHMENT
TABLE OF PENSION VALUATION FACTORS FOR FIXED TERM PENSIONS

Pension Term (years)	Indexation Rate								
	0.00%	1.00%	2.00%	3.00%	4.00%	5.00%	6.00%	7.00%	8.00%
1	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
2	1.82	1.84	1.85	1.87	1.89	1.91	1.92	1.94	1.96
3	2.61	2.64	2.68	2.72	2.75	2.79	2.83	2.87	2.91
4	3.33	3.38	3.44	3.50	3.57	3.63	3.70	3.77	3.85
5	3.98	4.06	4.15	4.24	4.34	4.44	4.54	4.65	4.76
6	4.57	4.68	4.81	4.93	5.06	5.20	5.35	5.50	5.66
7	5.11	5.26	5.41	5.58	5.75	5.93	6.12	6.32	6.54
8	5.60	5.78	5.97	6.18	6.39	6.62	6.87	7.12	7.40
9	6.04	6.26	6.49	6.74	7.00	7.28	7.58	7.90	8.24
10	6.45	6.70	6.98	7.27	7.58	7.91	8.27	8.66	9.07
11	6.81	7.11	7.42	7.76	8.12	8.51	8.93	9.39	9.88
12	7.15	7.48	7.83	8.22	8.63	9.08	9.57	10.10	10.68
13	7.45	7.82	8.22	8.65	9.12	9.63	10.18	10.79	11.46
14	7.73	8.13	8.57	9.05	9.57	10.14	10.77	11.46	12.23
15	7.98	8.42	8.90	9.42	10.00	10.64	11.34	12.12	12.98
16	8.21	8.68	9.20	9.77	10.41	11.11	11.88	12.75	13.71
17	8.42	8.92	9.48	10.10	10.79	11.55	12.41	13.36	14.43
18	8.60	9.14	9.74	10.41	11.15	11.98	12.91	13.96	15.14
19	8.78	9.35	9.98	10.69	11.49	12.38	13.39	14.54	15.83
20	8.93	9.53	10.21	10.96	11.81	12.77	13.86	15.10	16.51
21	9.07	9.70	10.41	11.21	12.11	13.14	14.31	15.65	17.18
22	9.20	9.86	10.60	11.44	12.40	13.49	14.74	16.17	17.83
23	9.32	10.01	10.78	11.66	12.67	13.82	15.15	16.69	18.47
24	9.43	10.14	10.94	11.87	12.92	14.14	15.55	17.19	19.10
25	9.52	10.26	11.10	12.06	13.16	14.44	15.93	17.67	19.72
26	9.61	10.37	11.24	12.24	13.39	14.73	16.30	18.14	20.32
27	9.69	10.47	11.37	12.40	13.60	15.01	16.65	18.60	20.91
28	9.76	10.56	11.49	12.56	13.80	15.27	16.99	19.04	21.49
29	9.83	10.65	11.60	12.70	13.99	15.52	17.32	19.47	22.06
30	9.89	10.73	11.70	12.84	14.17	15.75	17.64	19.89	22.62

Note: A pension that is indexed by reference to movements in the Consumer Price Index (CPI) is taken to have the indexation rate prescribed in Taxation Determination TD 96/33.