PR 2014/2 - Income tax: Challenger Care Annuity

Product Ruling

Income tax: Challenger Care Annuity

Contents Para

This publication provides you with the following level of protection:

This publication (excluding appendixes) 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 relevant 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, the Commissioner must apply the law to you in the way set out in the ruling (unless the Commissioner is satisfied that the ruling is incorrect and disadvantages you, in which case the law may be applied to you in a way that is more favourable for you – provided the Commissioner is 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.

No guarantee of commercial success

The Commissioner **does not** sanction or guarantee this product. Further, the Commissioner gives no assurance that the product is commercially viable, that charges are reasonable, appropriate or represent industry norms, or that projected returns will be achieved or are reasonably based.

Potential participants must form their own view about the commercial and financial viability of the product. The Commissioner recommends a financial (or other) adviser be consulted for such information.

This Product Ruling provides certainty for potential participants by confirming that the tax benefits set out in the **Ruling** part of this document are available, **provided that** the scheme is carried out in accordance with the information we have been given, and have described below in the **Scheme** part of this document. If the scheme is not carried out as described, participants lose the protection of this Product Ruling.

Terms of use of this Product Ruling

This Product Ruling has been given on the basis that the entity(s) who applied for the Product Ruling, and their associates, will abide by strict terms of use. Any failure to comply with the terms of use may lead to the withdrawal of this Product Ruling.

What this Ruling is about

1. This Product Ruling sets out the Commissioner's opinion on the way in which the relevant provisions identified in the Ruling section apply to the defined class of entities who take part in the scheme to which this Ruling relates. All legislative references in this Ruling are to the *Income Tax Assessment Act 1936* (ITAA 1936) unless otherwise indicated.

2. In this Product Ruling the scheme is an investment in a Challenger Care Annuity policy (Annuity) issued by Challenger Life Company Limited (Challenger) and offered under the Product Disclosure Statement dated 24 June 2013 (PDS).

3. This Product Ruling does not address:

(a) the taxation consequences of acquiring, holding and disposing or redeeming the Annuity, other than as per paragraphs 16 to 29 of this Product Ruling;

(b) the taxation consequences from disposing or otherwise ending the Annuity other than by way of commutation or upon death;

(c) the taxation consequences for an Annuity purchased using a directed termination payment within the meaning of the *Income Tax (Transitional Provisions) Act 1997* (IT(TP)A 1997);

(d) the taxation consequences for an Annuity purchased using personal injury compensation money, as per Division 54 of the *Income Tax Assessment Act 1997* (ITAA 1997);

(e) a Holder's eligibility to claim the Senior Australians and pensioners tax offset;

(f) the deductibility of the amount invested to purchase the Annuity;[1]

(g) the deductibility of adviser service fees; and

(h) the taxation consequences of borrowing funds to purchase the Annuity, including the deductibility of interest on funds borrowed to purchase the Annuity.

Class of entities

4. This part of the Product Ruling specifies which entities can rely on the Ruling section of this Product Ruling and which entities cannot rely on the Ruling section.

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[1] For the purposes of this Product Ruling, it is assumed at paragraph 29(e) that no portion of the amount invested to purchase the Annuity is deductible.

5. The class of entities who can rely on the Ruling section of this Product Ruling consists of those entities that are Australian residents for taxation purposes and are one of the following:

(a) an individual policy owner (not acting in a trustee capacity) who purchases the Annuity described in paragraphs 16 to 29 of this Product Ruling on or after 1 July 2013 and on or before 30 June 2016, referred to as a Holder in this Product Ruling; and

(b) the estate of a Holder, where the Holder dies within the withdrawal period.

6. The class of entities who can rely on the Ruling section of this Product Ruling does **not** include entities who:

(a) purchase the Annuity before 1 July 2013 or after 30 June 2016; or

(b) purchase the Annuity using a directed termination payment within the meaning of the IT(TP)A 1997, or personal injury compensation money that is subject to Division 54 of the ITAA 1997.

Superannuation Industry (Supervision) Act 1993

7. This Product Ruling does not address the provisions of the *Superannuation Industry (Supervision) Act 1993* (SISA). The Commissioner gives no assurance that the scheme is an appropriate investment for a superannuation fund. The trustees of superannuation funds are advised that no consideration has been given in this Product Ruling as to whether investment in this scheme may contravene the provisions of SISA.

Qualifications

8. The class of entities defined in this Product Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described in paragraphs 16 to 29 of this Ruling.

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

- this Product 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 Product Ruling may be withdrawn or modified.

Date of effect

10. This Product Ruling applies prospectively from 1 July 2013. It therefore applies only to the specified class of entities that enter into the scheme from 1 July 2013 until 30 June 2016, being its period of application. This Product Ruling will continue to apply to those entities even after its period of application has ended for the scheme entered into during the period of application.

11. However the Product Ruling only applies to the extent that there is no change in the scheme or in the entity's involvement in the scheme.

Changes in the law

12. Although this Product Ruling deals with the income tax laws enacted at the time it was issued, later amendments may impact on this Product Ruling. Any such changes will take precedence over the application of this Product Ruling and, to that extent, this Product Ruling will have no effect.

13. Entities who are considering participating in the scheme are advised to confirm with their taxation adviser that changes in the law have not affected this Product Ruling since it was issued.

Note to promoters and advisers

14. Product Rulings were introduced for the purpose of providing certainty about tax consequences for entities in schemes such as this. In keeping with that intention the Commissioner suggests that promoters and advisers ensure that participants are fully informed of any legislative changes after the Product Ruling has issued.

Ruling

15. Subject to paragraph 3 and the assumptions in paragraph 29 of this Ruling:

(a) An Annuity purchased by a Holder:

  (i) is not a 'qualifying security' as defined in subsection 159GP(1);

  (ii) is not a 'superannuation income stream' as defined in regulation 995-1.01 of the *Income Tax Assessment Regulations 1997* (ITAR); and

  (iii) is an 'annuity' as defined in subsection 27H(4).

(b) An Annuity purchased by a Holder is not a financial arrangement to which Division 230 of the ITAA 1997 applies.

(c) The regular payments made by Challenger to a Holder are assessable income under subsection 27H(1) to the extent that the regular payments exceed the 'deductible amount' in relation to the Annuity. The deductible amount is excluded from the assessable amount of the Annuity.

(d) The annual deductible amount in relation to the regular payments derived by a Holder is ascertained (subject to subsection 27H(3)) in accordance with the formula set out in subsection 27H(2) on the basis that:

  (i) the 'relevant share' in relation to the Annuity is 1;

  (ii) the 'undeducted purchase price' of the Annuity is the initial investment amount paid to purchase the Annuity;

  (iii) the 'residual capital value' in relation to the Annuity is nil; and

  (iv) the 'relevant number' in relation to the Annuity is the life expectation factor of the Holder, determined on the commencement date of the Annuity in accordance with official Australian Life Tables.

(e) Where the regular payments are not payable to a Holder for the whole of an income year, the deductible amount for that year will be reduced proportionately by the Commissioner pursuant to subsection 27H(3) based on the part of the year during which the regular payments are not paid.

(f) Any capital gain made by a Holder resulting from the regular payments made by Challenger is disregarded under section 118-300 of the ITAA 1997, and is not otherwise assessable as ordinary or statutory income under the *Income Tax Assessment Act*.

(g) Any capital gain made by a Holder resulting from the payment of the withdrawal value by Challenger to them upon commutation is disregarded under section 118-300 of the ITAA 1997. The payment of the withdrawal value in these circumstances is, however, included in the assessable income of the Holder to the extent that it exceeds the capital component of the Annuity. The capital component of the Annuity is calculated as the undeducted purchase price (as per paragraph 15(d)(ii) of this Ruling) less any deductible amounts previously applied to the regular payments from the Annuity, but not reduced to less than $0.

(h) Any capital gain made by a Holder's deceased estate resulting from the payment of the withdrawal value by Challenger to it upon death is disregarded under section 118-300 of the ITAA 1997. The payment of the withdrawal value in these circumstances is, however, included in the assessable income of the deceased estate to the extent that it exceeds the capital component of the Annuity. The capital component of the Annuity is calculated as the undeducted purchase price (as per paragraph 15(d)(ii) of this Ruling) less any deductible amounts previously applied to the regular payments from the Annuity, but not reduced to less than $0.

(i) Provided the scheme ruled on is entered into and carried out as described in this Ruling, the anti-avoidance provisions in Part IVA will not apply to a Holder or their estate.

Scheme

16. The scheme that is the subject of this Ruling is identified and described in the following documents:

- application for a Product Ruling as constituted by documents and information received on 18 December 2013 and 15 January 2014;
- Challenger Care Annuity Policy Document dated 24 June 2013;
- Challenger Care Annuity Product Disclosure Statement dated 24 June 2013; and
- Investor Certificate.

Note: certain information has been provided on a commercial-in-confidence basis and will not be disclosed or released under Freedom of Information legislation.

17. For the purposes of describing the scheme to which this Ruling applies, there are no other agreements, whether formal or informal, and whether or not legally enforceable, which a Holder or their estate, or any associate of a Holder or their estate, will be a party to, which are a part of the scheme.

18. All Australian Securities and Investments Commission (ASIC) requirements are, or will be, complied with for the term of the agreements.

Overview

19. The Annuity is a 'life policy' for the purposes of the Life Insurance Act 1995 (as per paragraph 9(1)(c) of that Act) which therefore satisfies the definition of a 'life insurance policy' under subsection 995-1(1) of the ITAA 1997, and is offered by Challenger in Australia to individuals over 18 years of age who:

- have Aged Care Assessment Team approval[2] that specifies that either 'low level' or 'high level' residential care is required; or
- live in an approved residential care facility.

20. Individuals who purchase the Annuity cannot do so using a 'roll-over superannuation benefit' (as defined in section 306-10 of the ITAA 1997), or jointly with another person.

21. To purchase the Annuity, a Holder is (among other things) required to execute and lodge the Application Form attached to the PDS with Challenger, together with an initial investment amount of at least $10,000 to buy the Annuity. No additional fees or charges are payable to Challenger by the Holder.

22. Upon acceptance of a valid application, the Holder is issued with the Policy Document (a legal contract between the Holder and Challenger) and an Investor Certificate by Challenger, setting out the relevant terms and conditions.

23. In exchange for the initial investment amount, the Annuity provides regular payments for the Holder's lifetime at an agreed frequency (monthly, quarterly, half-yearly or yearly, as chosen at the time the Annuity is purchased).

24. The amount of the regular payments is fixed and determined at the time the Annuity is purchased and will depend on a number of factors, including the amount of the initial investment, prevailing market rates and the Holder's life expectancy at the time of purchase.

25. The Annuity has a withdrawal period of 10 years from its commencement date during which time the Annuity has a withdrawal value, payable by Challenger as a lump sum if during this period the Holder either chooses to end their Annuity early or dies. After the end of the withdrawal period, the Annuity ceases to have a withdrawal value.

26. The Holder has the right to withdraw voluntarily from the Annuity (commute) within the withdrawal period and be paid the withdrawal value from Challenger. Calculation of the withdrawal value by Challenger in these circumstances will be in accordance with the terms of the Annuity and subject to a minimum level prescribed under the *Life Insurance Act 1995* and prudential standards enforced by the Australian Prudential Regulation Authority.

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[2] Or Aged Care Assessment Service approval in Victoria.

27. If the Holder commutes their Annuity at the end of the withdrawal period, the withdrawal value will be a guaranteed 100% of their initial investment. A partial commutation of the Annuity is not permitted.

28. Challenger will pay a withdrawal value equal to 100% of the initial investment amount to the Holder's estate where the Holder dies within the withdrawal period.

Assumptions

29. This Ruling is made on the basis of the following assumptions:

(a) a Holder is an individual Australian resident for taxation purposes and is not a taxation resident of a country with which Australia has concluded a double tax treaty;

(b) a Holder's deceased estate is an Australian resident trust estate as defined in subsection 95(2) and is not a resident trust estate of a country with which Australia has concluded a double tax treaty;

(c) a Holder will not purchase the Annuity using a directed termination payment within the meaning of the IT(TP)A 1997, or using personal injury compensation money that is subject to Division 54 of the ITAA 1997;

(d) all Holders are the original Holders who purchased the annuity from Challenger for their own benefit;

(e) no portion of the amount invested to purchase the Annuity is deductible;

(f) all dealings between a Holder, their estate and Challenger will be at arm's length; and

(g) the scheme will be executed in the manner described in the Scheme section of this Ruling and the scheme documentation referred to in paragraph 16 of this Ruling.

Commissioner of Taxation
26 February 2014

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.

Subsection 27H(4) – annuity

30. Subsection 27H(4) defines an 'annuity' to mean:

> an annuity, a pension paid from a foreign superannuation fund (within the meaning of the *Income Tax Assessment Act 1997*) or a pension paid from a scheme mentioned in paragraph 290-5(c) of that Act, but does not include:
>
> (a) an annuity that is a qualifying security for the purposes of Division 16E; or
>
> (b) a superannuation income stream (within the meaning of the *Income Tax Assessment Act 1997*).

31. This definition encompasses an annuity on ordinary concepts, as contemplated within various judicial authorities and discussed in Taxation Ruling IT 2480. An annuity on ordinary concepts is a contract under which a principal sum is converted into an income stream[3] of payments that are at least annual, fixed or variable in a way that is calculable, and which will continue to be paid for a fixed or determinable period.

32. The Holder's initial investment amount is applied to purchase the regular payments payable by Challenger under the terms of the Annuity, a contract between the Holder and Challenger. Those regular payments are a series of periodic payments (payable at least yearly), fixed at the time of purchase and (unless commuted earlier for the withdrawal value) continue for the life of the Holder. The Holder's ability to commute does not of itself result in the Annuity failing to be accepted as an annuity contract (paragraph 25 of IT 2480).

33. An Annuity purchased by a Holder therefore constitutes an annuity on ordinary concepts and, subject to the exclusions in paragraphs (a) and (b) of the definition (considered below at paragraphs 34 to 39 of this Ruling), constitutes an annuity as defined in subsection 27H(4).

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[3] The term 'income stream' is defined in Taxation Ruling TR 2013/5 in the context of a superannuation income stream payable by a superannuation fund trustee to a member as "a series of periodic payments that relate to each other over an identifiable period of time".

Division 16E – qualifying security

34. A 'qualifying security' is defined in subsection 159GP(1). For the purposes of determining whether an arrangement is a qualifying security, that arrangement must be a security, also defined in subsection 159GP(1) to mean:

(a) stock, a bond, debenture, certificate of entitlement, bill of exchange, promissory note or other security;

(b) a deposit at bank or other financial institution;

(c) a secured or unsecured loan; or

(d) any other contract, whether or not in writing, under which a person is liable to pay an amount or amounts, whether or not the liability is secured.

35. The Annuity is not considered to have sufficient debt like obligations to be a contract to which paragraph (d) of the definition of security in subsection 159GP(1) applies, nor does it fall within paragraphs (a), (b) or (c) of that definition. Therefore, the Annuity does not meet the definition of security under subsection 159GP(1) and, as such, is not a qualifying security for the purposes of Division 16E.

36. Additionally, an annuity will not be a qualifying security for the purposes of subsection 159GP(1) where it is an 'ineligible annuity', a term also defined in subsection 159GP(1) to mean an annuity issued by a life assurance company to or for the benefit of a natural person other than in the capacity of trustee of a trust estate. An Annuity issued by Challenger to a Holder (that is, a natural person other than in the capacity of trustee of a trust estate) is an ineligible annuity.

Superannuation income stream

37. A 'superannuation income stream' has the meaning given by the ITAR (subsection 307-70(2) of the ITAA 1997). Subregulation 995-1.01(1) of the ITAR defines superannuation income stream in relation to an annuity commenced after 19 September 2007 to mean an income stream that is taken to be an annuity for the purposes of the SISA in accordance with subregulation 1.05(1) of the *Superannuation Industry (Supervision) Regulations 1994* (SISR).

38. Subregulation 1.05(1) of the SISR provides a number of requirements that must be met for a benefit provided by a life insurance company to be taken to be an annuity for the purposes of the SISA. One of those requirements in respect of a benefit purchased on or after 1 July 2007 is that it is purchased with the whole or part of a roll-over superannuation benefit as defined in section 306-10 of the ITAA 1997, or the whole or part of a directed termination payment within the meaning of the IT(TP)A 1997.

39. As per paragraph 20 of this Ruling, a Holder cannot purchase the Annuity using a roll-over superannuation benefit as defined in section 306-10 of the ITAA 1997 and, as per paragraph 29(c) of this Ruling, it is assumed for the purposes of this Ruling that a Holder will not purchase the Annuity using a directed termination payment within the meaning of the IT(TP)A 1997. As such, the Annuity is not a superannuation income stream for a Holder.

Division 230 – taxation of financial arrangements

40. Division 230 of the ITAA 1997 sets out the tax treatment of gains or losses from a 'financial arrangement'. Generally, a financial arrangement is a cash settlable legal or equitable right to receive a financial benefit, or obligation to provide such benefit, or a combination of one or more such rights and/or obligations (subsection 230-45(1) of the ITAA 1997). A right to receive or obligation to provide a financial benefit can be 'cash settlable' under subsection 230-45(2) of the ITAA 1997 if the benefit is money, or if it is a right the taxpayer intends to satisfy or settle by receiving money, or if it is an obligation that the taxpayer intends to satisfy or settle by providing money.

41. The Annuity constitutes a financial arrangement for the purposes of Division 230 of the ITAA 1997 on the basis that a Holder and their estate have cash settlable rights to receive a financial benefit in the form of the regular payments and/or the withdrawal value, as applicable, and on the basis that the Holder has a cash settlable obligation to provide a financial benefit in the form of the initial investment amount.

42. Subject to exceptions under Subdivision 230-H, gains made from a financial arrangement are included in assessable income under subsection 230-15(1) of the ITAA 1997 and are not (to any extent) to be included in assessable income pursuant to any other taxing provision of the *Income Tax Assessment Act* (subsection 230-20(4) of the ITAA 1997), including section 27H.

43. However, where the rights and/or obligations under an arrangement are the subject of an exception under section 230-460 of the ITAA 1997, Division 230 of the ITAA 1997 does not apply in relation to gains or losses from a financial arrangement for any income year (subsection 230-460(1) of the ITAA 1997). Subsection 230-460(5) of the ITAA 1997 provides a specific exception as follows:

> A right or obligation under a *life insurance policy is the subject of an exception unless:
>
> (a) you are not a *life insurance company that is the insurer under the policy; and
>
> (b) the policy is an annuity that is a *qualifying security.

44. As the Annuity is a life insurance policy (as defined in subsection 995-1(1) of the ITAA 1997 and as per paragraph 19 of this Ruling) that is not a qualifying security (as defined in subsection 159GP(1) and discussed at paragraphs 34 to 36 of this Ruling), the exception in subsection 230-460(5) applies and Division 230 of the ITAA 1997 does not apply to any gains or losses derived from an Annuity purchased by a Holder.

Section 27H – assessability of regular payments

45. Paragraph 27H(1)(a) includes in the assessable income of a taxpayer of a year of income the amount of any annuity derived by the taxpayer during that year excluding, in the case of an annuity that has been purchased, any amount that is the deductible amount in relation to the annuity in relation to the year of income. The regular payments made by Challenger to a Holder are therefore assessable income under subsection 27H(1) to the extent that the regular payments exceed the deductible amount in relation to the Annuity.

46. The deductible amount is excluded from the assessable amount of the annuity and is tax free to the recipient because it represents the return to them of the amount paid to acquire the annuity. Subsection 27H(2) provides for the calculation of the deductible amount in relation to an annuity derived by a taxpayer during a year of income, subject to subsections 27H(3) and (3A), in accordance with the following formula:

$$\frac{A\ (B - C)}{D}$$

where:

A is the relevant share in relation to the annuity in relation to the taxpayer in relation to the year of income.

B is the amount of the undeducted purchase price of the annuity.

C is:

(a) if there is a residual capital value in relation to the annuity and that residual capital value is specified in the agreement by virtue of which the annuity is payable or is capable of being ascertained from the terms of that agreement at the time when the annuity is first derived - that residual capital value; or

(b) in any other case - nil; and

D is the relevant number in relation to the annuity.

47. The relevant share in relation to the Annuity (component A) for a Holder is 1.

48. The undeducted purchase price in relation to an Annuity (component B) that is purchased by a Holder is the whole of the purchase price of the Annuity (the initial investment amount), reduced by any portion of the initial investment amount that is an allowable deduction. As per paragraph 29(e) of this Ruling, it is assumed for the purposes of this Ruling that no portion of the initial investment amount is deductible.

49. The residual capital value in relation to an annuity is defined in subsection 27H(4) to mean the capital amount payable on the termination of the annuity. As the terms of the Annuity do not provide for any residual capital value in relation to the Annuity, it (component C) is nil.

50. Where an annuity is payable during the lifetime of a person and not thereafter, the relevant number in relation to that annuity in relation to a year of income is defined in subsection 27H(4) to mean the life expectation factor of the person. The relevant number in relation to the Annuity (component D) is therefore the life expectation factor of the Holder. The life expectation factor in relation to a person in relation to an annuity is defined in subsection 27H(4) to mean the number of years in the complete expectation of life of the person as ascertained by reference to the prescribed Life Tables[4] at the time at the beginning of the period to which the first payment of the annuity relates.

51. Where the Commissioner considers that the deductible amount ascertained in accordance with the formula in subsection 27H(2) is inappropriate, having regard to the terms and conditions applying to the annuity and to any other relevant matters, he may, subject to subsection 27H(3A), determine the deductible amount that applies pursuant to subsection 27H(3). In making a determination pursuant to subsection 27H(3), the Commissioner may have regard to the terms and conditions applying to the annuity, to a certificate supplied by an actuary and to any other matters considered relevant.

52. Paragraphs 16 to 24 of Taxation Ruling IT 2157 provide some guidelines as to the exercise of the discretion under subsection 27H(3). Applying those guidelines to the Annuity, the Commissioner may exercise the discretion under subsection 27H(3) where the regular payments are not payable for the whole of an income year, in which case the deductible amount ascertained under subsection 27H(2) will be inappropriate and reduced proportionately based on the part of the year during which the regular payments are not paid.

53. As the Annuity cannot be partly commuted, subsection 27H(3A) cannot have any application on the determination of the deductible amount in relation to the Annuity.

[4] For the purposes of the definition of ‘life expectation factor’ in subsection 27H(4) and with respect to annuities first commencing to be payable on or after 1 July 1993, regulation 9(d) of the *Income Tax Regulations 1936* prescribes the Australian Life Tables that are most recently published by the Australian Government Actuary before the year in which the annuity first commences to be payable.

Capital gain or loss from payments under the Annuity disregarded

54. Under subsection 108-5(1) of the ITAA 1997 a CGT asset is any kind of property or a legal or equitable right that is not property. The contractual rights of a Holder and their estate under the Annuity are legally enforceable rights and therefore a CGT asset according to the definition in subsection 108-5(1) of the ITAA 1997. Generally, the discharge or satisfaction of contractual rights give rise to a CGT event C2 (paragraph 104-25(1)(b) of the ITAA 1997).

55. Section 118-300 of the ITAA 1997 exempts certain capital gains and losses made in respect of a policy of insurance on the life of an individual or an annuity instrument. An annuity instrument is defined broadly in subsection 995-1(1) of the ITAA 1997 to mean an instrument that secures the grant of an annuity (whether dependent on the life of an individual or not).

Section 118-300 – regular payments

56. Item 3 of the table in subsection 118-300(1) of the ITAA 1997 provides that a capital gain or capital loss made from a CGT event happening in relation to a CGT asset that is an interest in rights under a life insurance policy or an annuity instrument is disregarded where that CGT event happens to the original beneficial owner of the policy or instrument.

57. The 'original beneficial owner' of any of the rights, or any interest in any of the rights, under a policy of life assurance is defined in Taxation Determination TD 94/31 to mean the first person who:

(i) at the time the policy is effected, holds such rights, or any interest in such rights, and

(ii) possesses all the normal incidents of beneficial ownership (for example, is entitled to the benefits of the policy proceeds and has the power of management and control over the policy as well as the power to transfer, grant as security, surrender or otherwise dispose of, the policy).

58. As an individual to whom the Annuity is first issued, a Holder is regarded as an original beneficial owner of a policy of insurance on the life of an individual or an annuity instrument. Pursuant to item 3 in the table in subsection 118-300(1) of the ITAA 1997, any capital gain or capital loss the Holder makes under section 104-25 of the ITAA 1997 from the receipt of regular payments by Challenger under the Annuity is therefore disregarded.

Section 118-300 – payment of withdrawal value

59. As a Holder is regarded as an original beneficial owner of a policy of insurance on the life of an individual or an annuity instrument, pursuant to item 3 in the table in subsection 118-300(1) of the ITAA 1997, they will disregard any capital gain or capital loss they make under section 104-25 of the ITAA 1997 from the receipt of the withdrawal value from Challenger upon commutation of the Annuity.

60. Item 4 of the table in subsection 118-300(1) of the ITAA 1997 provides that a capital gain or capital loss made from a CGT event happening in relation to a CGT asset that is an interest in rights under a life insurance policy or an annuity instrument is disregarded where that CGT event happens to an entity that acquired the interest in the policy or instrument for no consideration.

61. A Holder's deceased estate acquires, on the death of a Holder, an interest in the Annuity for no consideration and will therefore, pursuant to item 4 in the table in subsection 118-300(1) of the ITAA 1997, disregard any capital gain or capital loss they make under section 104-25 of the ITAA 1997 from the receipt of the withdrawal value from Challenger upon the Holder's death.

Assessability of withdrawal value

62. The receipt of the withdrawal value from Challenger by a Holder upon commutation of the Annuity, or a Holder's deceased estate on the death of a Holder is assessable income to the extent that it does not comprise a repayment of capital. The capital component of the withdrawal value in these circumstances is the undeducted purchase price of the Annuity less any deductible amounts previously applied to the regular payments from the Annuity, but not reduced to less than $0.

63. Any amount referred to in paragraph 62 of this Ruling which is included in the assessable income of a Holder's deceased estate shall, pursuant to subsection 101A(1) be deemed to be income to which no beneficiary is presently entitled.

Part IVA – anti-avoidance

64. Provided that the scheme ruled on is entered into and carried out as disclosed in this Ruling, it is accepted that the scheme is an ordinary commercial transaction and Part IVA will not apply.

Appendix 2 – Detailed contents list

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

References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

IT 2157; IT 2480; TD 94/31;
TR 2013/5

Subject references:

- capital gains tax
- income tax
- producing assessable Income
- product rulings
- public rulings
- securities
- taxation of financial arrangements

Legislative references:

- ITAA 1936
- ITAA 1936 27H
- ITAA 1936 27H(1)
- ITAA 1936 27H(1)(a)
- ITAA 1936 27H(2)
- ITAA 1936 27H(3)
- ITAA 1936 27H(3A)
- ITAA 1936 27H(4)
- ITAA 1936 95(2)
- ITAA 1936 101A(1)
- ITAA 1936 Pt III Div 16E
- ITAA 1936 159GP(1)
- ITAA 1936 159GP(1)(a)
- ITAA 1936 159GP(1)(b)
- ITAA 1936 159GP(1)(c)
- ITAA 1936 159GP(1)(d)
- ITAA 1936 Pt IVA
- ITR 1936 9(d)
- ITAA 1997 Div 54
- ITAA 1997 104-25
- ITAA 1997 104-25(1)(b)
- ITAA 1997 108-5(1)
- ITAA 1997 118-300
- ITAA 1997 118-300(1)
- ITAA 1997 Div 230
- ITAA 1997 230-15(1)
- ITAA 1997 230-20(4)
- ITAA 1997 230-45(1)
- ITAA 1997 230-45(2)
- ITAA 1997 Subdiv 230-H
- ITAA 1997 230-460
- ITAA 1997 230-460(1)
- ITAA 1997 230-460(5)
- ITAA 1997 306-10
- ITAA 1997 307-70(2)
- ITAA 1997 995-1(1)
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