



THE TAX INSTITUTE

THE MARK OF EXPERTISE

20 October 2014

Ms Jessica Mohr
Manager
Small Business and Indirect Taxes Unit
Small Business Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: TaxLawDesign@treasury.gov.au

Dear Ms Mohr,

Capital Gains Tax Exemption for Compensation and Insurance

The Tax Institute welcomes the opportunity to make a submission to Treasury in relation to *Tax and Superannuation Laws Amendment Bill: CGT exemption for compensation and insurance (Exposure Draft)*.

Legislative references in this submission are to the *Income Tax Assessment Act 1997* unless noted otherwise.

We welcome these amendments, which address one of the announced but unenacted measures from the previous government (Item 64 of the list of measures the current government announced that it would proceed with on 14 December 2013). Our submission proposes some amendments to the Exposure Draft, which would more fully address the relevant announcements.

References to "CGT asset"

Proposed sections 118-37(1)(ba) and 118-300(1A) use the term "CGT asset". The intent of these proposed sections is to ensure that where total and permanent disability or life insurance proceeds are received by a trustee of a trust (exempt under sections 118-37(1)(b) or 118-300(1)), the subsequent payment of the proceeds to the beneficiary are also exempt (where the relevant requirements are met).

Generally, the subsequent payment of the proceeds to the beneficiary would be in the form of a cash distribution and the Explanatory Memorandum suggests the intention is for these proposed sections to cover cash distributions. Proposed para 1.7 of the Explanatory Memorandum refers to "receives a distribution", and proposed para 1.19 refers to compensation "paid through" a trust.

In those circumstances, it is unfortunate that the term "CGT asset" is used, given the Commissioner's view that Australian currency is sometimes a CGT asset (ATOID 2003/166), but sometimes isn't (TD 2002/25). A phrase such as "amount or property" may be a more reasonable substitute for the term "CGT asset" and capture both cash and in specie distributions.

Application date

Items 2 and 6 of the Exposure Draft are proposed to apply from Royal Assent. These two items relate to proceeds received by a beneficiary of a trust that holds the policy – Item 6 contains the general exemption, and Item 2 excludes the moneys from CGT Event E4.

Proposed para 1.27 suggests there is no basis for retrospective application of these provisions, as there was no existing administrative practice on this issue. However this would seem to be inconsistent with 2012-13 Budget papers¹, and also the "Administrative treatment" QC 24454 issued by the Commissioner.² It also creates an unnecessary difference between the treatment of total and permanent disability and life insurance policies owned by trusts.

Item 64(a) of announced but unenacted measures

The measure in this Exposure Draft to ensure personal injury insurance proceeds received by a complying super fund are not subject to CGT nor section 6-5 as a fall back are welcome. It represents Item 64(b) of the announced but unenacted measures from the previous government.

It would be expeditious if the Exposure Draft could also cover the related Item 64(a) which the current Government also said it would proceed with. To this end, and as announced in the 2011-12 Budget papers³, it would be desirable if the same legislative clarity that section 6-5 cannot apply as a fall back could be provided for all life insurance policies held by complying superannuation entities that are currently exempt from CGT under item 5 of section 118-300 by repealing item 10 of section 295-85(4) in its entirety. This would be a step towards eliminating:

- for investment policies, the possibility of double 15% tax arising through the life insurance company paying tax on the proceeds of the sale of assets that support the policy, and the superannuation fund paying tax again on the same proceeds when it receives them from the life insurance company; and
- for risk policies, the possibility of tax at the superannuation fund level which, if tax applied, would abrogate the fundamental policy position from 1988 that, when superannuation funds became generally taxable on other earnings, they would still be able to provide the same level of insurance benefits without needing to increase the required contributions towards the premiums.

¹ 2012-13 Budget Papers - part 1: Revenue Measures page 20

² <https://www.ato.gov.au/General/New-legislation/In-detail/Direct-taxes/Income-tax-on-capital-gains/Extending-the-CGT-exemption-for-certain-compensation-payments-and-insurance-policies/>

³ 2011-12 Budget Papers – Revenue Measures page 18 dot point 3

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If you would like to discuss any of the above, please contact either me or Tax Counsel, Thilini Wickramasuriya, on 02 8223 0044.

Yours sincerely

A handwritten signature in black ink, appearing to read "M. Flynn", followed by a long, horizontal, slightly wavy line that extends to the right.

Michael Flynn
President