THE INSTITUTE OF ACTUARIES OF AUSTRALIA
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GUIDANCE NOTE 450 - COST OF DEATH AND DISABILITY BENEFITS - CERTIFICATES BY ACTUARIES UNDER SUB-SECTION 279(3) OF THE INCOME TAX ASSESSMENT ACT

APPLICATION

Actuarial certificates under Sub-section 279(3) of the Income Tax Assessment Act.

LEGISLATION

This Guidance Note deals with determination of the cost of death and disability benefits for purposes of Section 279 of the Income Tax Assessment Act.

FIRST ISSUED

December 1991.

CLASSIFICATION

Compliance with the provisions of this Guidance Note is mandatory.

1.PURPOSE

1 The purpose of this Guidance Note is to provide advice to members on the operation of certain parts of Section 279 of the Income Tax Assessment Act ("the Act") relating to tax deductions for the cost of providing death and disability benefits. Taxation Ruling IT2617 requires that an actuarial certificate under Sub-section 279(3) must include "confirmation that the valuation is consistent with any Guidance Notes issued by the Institute".

2.INTERPRETATION

1 Sub-sections 279(1) and 279(2) of the Act refer to "liability to provide death or disability benefits". The Institute's interpretation is that liability for this purpose excludes the funded retirement portion of these benefits.

2 To establish that a liability exists to provide death and disability benefits where no insurance has been effected it is necessary for either the benefit on death or disability to be defined or the unfunded element to be defined.

3.MAXIMUM "LIABILITY"

1 For the purposes of claiming a deduction under Sub -sections 279(1) or 279(2) the maximum amount of insurance, or notional insurance, for lump sum benefits, is:

(a) Defined Benefit Plan

Death/disability benefit	less	Accrued retirement benefit

(b) Accumulation Plan

Death/ disability benefit	less	Accumulated retirement benefit

unless the actuary certifies that a greater amount of insurance or notional insurance is required. In the case of a plan providing death or disability benefits in pension form an additional factor is required to allow for the lump sum value of the pension benefit. Accrued retirement benefit for this purpose is calculated in a manner consistent with the benefits provided by the plan, in particular the early retirement benefit.

2 Circumstances where a greater amount of insurance or notional insurance would be reasonable include plans where the aggregate of accrued retirement benefits or accumulated retirement benefits exceeds the value of plan assets. Theamount insured or notionally insured would commonly be calculated by deducting some form of discounted accrued retirement benefit from the death/disability benefit.

4.ARM'S LENGTH PREMIUM

1 Sub-section 279(2) provides that the arm's length premium in respect of the "liability" is an allowable deduction. In determining the underlying rates to be used in calculation of the "arm's length premium" it is not a requirement to seek quotations from insurers provided due consideration is given to the definition of "arm's length premium" under Sub -section 267(1) of the Act and the circumstances and experience of the complying superannuation fund. If the actuary has a significant level of doubt as to the rates to be used, quotations should be obtained and used in determining an arm's length premium. The underlying rates adopted should not include a profit sharing component.

2 In calculating the arm's length premium allowance should be made for changes in membership throughout the year of income on an appropriate basis.

5.APPORTIONMENT OF PREMIUM

1 Sub-section 279(1)(d) relates to bundled policies that are not whole of life or endowment policies. It is necessary to determine the part of the premium that is attributable to the liability to provide death and disability benefits. The basis of such apportionment should recognise the underlying premium basis and produce results consistent with those produced if the arm's length premium approach had been adopted.

6.USE OF SUB-SECTION 279(2)

1 Sub-section 279(2) can be applied where the "liability" to provide death or disability benefits "to some extent is not covered by an insurance policy". Use of Sub-section 279(2) is appropriate where a plan elects to self insure part or all of the unfunded portion of death or disability benefits, for example:

(a) where the plan does not insure the first $x of "liability" per member;

(b) all or certain members are not covered by insurance;

(c) stop loss arrangements are in place.

2 In addition, if the level of insurance for a plan is less than that specified under paragraph 3.1 above it would be possible for the plan to also seek a deduction under Sub-section 279(2) for self-insurance of the difference between the maximum specified in paragraph 3.1 and the actual amount of insurance. Where a plan has stop loss arrangements in place it would be appropriate to utilise Sub-section 279(2) and not claim a deduction for the stop loss premium or reduce the amount of the arm's length premium by the amount of the stop loss premium and claim a deduction for the stop loss premium.

7.ACTUARIAL CERTIFICATE

1 Whilst it is not necessary for an actuarial certificate required under Sub-section 279(3) to accompany the plan's tax return it is still necessary for the actuary to provide such a certificate to the Trustees. The certificate is required to be in a form approved by the Taxation Commissioner as detailed in Taxation Ruling IT2617.

2 In addition to the items specified in IT2617, where a deduction is being claimed under Sub-section 279(2), the actuarial certificate should provide the following information:

(a) data on which the certificate is based;

(b) the amount of the plan's "liability" to provide death or disability benefits not covered by an insurance policy, and the basis of determining that amount;

(c) a statement of the underlying rates used in the calculation of the arm's length premium and a brief explanation of the basis of determining these rates.

3 In addition to the items specified in IT2617, where a deduction is being claimed under Sub-section 279(1)(d) the actuarial certificate should provide the information required by (a) above and details of the basis of apportionment.

8.MISCELLANEOUS

1 The Guidance Note has been prepared on the assumption that the actuary undertaking the work is familiar with the operations of the plan through other work done for the plan. In practice this may not be so, in which case the actuary should have regard to the Code of Conduct, particularly Guidance Notes B.9 and B.10.

2 This Guidance Note was first issued in December 1991 and replaces a previous note from the Superannuation Committee dated 5 April 1990.

END OF GUIDANCE NOTE 450