



CR 2010/27 - Income tax: employment termination payment: Monadelphous Engineering Associates Pty Ltd

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Class Ruling

Income tax: employment termination payment: Monadelphous Engineering Associates Pty Ltd

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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.

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What this Ruling is about

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

Relevant provision

2. The relevant provision dealt with in this Ruling is section 82-130 of the *Income Tax Assessment Act 1997* (ITAA 1997).¹

Class of entities

3. The class of entities to which this Ruling applies is all common law employees who receive a payment under the scheme described in paragraphs 9 to 21 of this Ruling.

¹ All legislative references are to the ITAA 1997 unless otherwise indicated.

Qualifications

4. 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 9 to 21 of this Ruling.

5. 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- this Ruling may be withdrawn or modified.

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Date of effect

7. This Ruling applies from 1 July 2009 to 30 June 2013. The Ruling continues to apply after 30 June 2013 to all entities within the specified class who entered into the specified scheme during the term of the Ruling. However, the ruling will not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of the issue of the Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Scheme

8. The following description of the scheme is based on information provided by the applicant.

9. The conditions of employment for employees of Monadelphous Engineering Associates Pty Ltd (employer) working on the Pluto project (Project) are detailed in a Collective Agreement (Agreement).

10. Employees are to work standard project working hours of 10 hours per day from Monday to Saturday (that is, 60 hours per week from Monday to Saturday).

11. Clause 34 of the Agreement provides an employee entitlement called Pluto Special Leave (PSL).

12. Under subclause 34(1) of the Agreement, on commencement all employees of the Project will be placed on a four week work cycle for the purposes of accruing entitlements to rest and recreation (R&R) leave and PSL.

13. Subclause 34(3) of the Agreement, stipulates that PSL is an additional leave that accrues to employees including casual employees who work all Project working hours during their work cycle. PSL does not accrue during any period of R&R leave.

14. Subclause 34(4) of the Agreement specifies that where an employee qualifies for PSL at the end of their work cycle, they will accrue PSL as shown below:

Length of work Cycle	Required Project Working Hours	PSL Accrual
4 weeks	240	32 hours
5 weeks	300	50 hours
6 weeks	360	72 hours

15. Under subclause 34(5) of the Agreement, if an employee is absent from work without the authorisation of the employer in any week during the work cycle the employee shall accrue a reduced amount of PSL for that cycle calculated on a pro-rata basis with regard only to those weeks where there was no unauthorised absence.

16. Under subclause 34(6) of the Agreement, and subject to subclauses 34(7) and 34(8) of the Agreement, PSL accruals will not be affected for those on short absences from work that have received prior approval of the employer.

17. Under subclauses 34(7) and 34(8) of the Agreement, PSL does not accrue during any period an employee is absent from work, during that person's work cycle, that is due to any of the following:

- workers compensation for longer than two weeks;
- receiving a benefit under Income Protection Insurance;
- long service leave;
- annual leave;
- jury service leave;
- parental leave; or
- approved unpaid leave greater than one day.

18. Subclause 34(9) of the Agreement states the following:

At anytime an Employee may receive payment for PSL that they have accrued by choosing to:

- (a) receive payment for those R&R Leave Days that they would otherwise have taken as unpaid R&R Leave; or
- (b) Cash-in either all or part of their accrued PSL entitlement for an equivalent monetary benefit.

19. Under subclause 34(10) of the Agreement any unused PSL at the time of termination from the project shall be paid to the employee.

20. Subclause 34(11) of the Agreement provides that PSL shall be paid at the employee's ordinary hourly rate applying at the time the employee receives the payment for PSL.

21. The applicant states that PSL is in the nature of an employee incentive payment which is designed to keep workers on the Project, encourage the workforce to follow dispute procedures and not to take industrial strike action. The applicant also states that PSL is structured to encourage workers not to take unapproved leave.

Ruling

22. A payment made or to be made to an employee in accordance with the scheme described in paragraphs 9 to 21 of this Ruling is in consequence of termination of employment and is an employment termination payment under section 82-130.

Commissioner of Taxation

14 July 2010

Appendix 1 – Explanation

❶ *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.*

Employment termination payment

23. From 1 July 2007 a payment made to an employee is an employment termination payment if the payment satisfies all the requirements in section 82-130.

24. Section 995-1 states that:

employment termination payment has the meaning given by section 82-130.

25. Subsection 82-130(1) states:

A payment is an **employment termination payment** if:

- (a) it is received by you:
 - (i) in consequence of the termination of your employment; or
 - (ii) after another person's death, in consequence of the termination of the other person's employment; and
- (b) it is received no later than 12 months after the termination (but see subsection (4)); and
- (c) it is *not* a payment mentioned in section 82-135.

26. Section 82-135 provides that certain payments are not employment termination payments, including:

- superannuation benefits;
- payments for unused annual leave or unused long service leave (and any other similar leave);
- the tax-free part of a genuine redundancy payment or an early retirement scheme payment; and
- reasonable capital payments for personal injury.

27. All of the conditions under section 82-130(1) need to be satisfied in order for the payment to be treated as an employment termination payment.

The payment is made in consequence of the termination of the taxpayer's employment

28. The first condition to be met is that there must be an employment termination payment that is made in consequence of the termination of employment of the taxpayer.

29. It should be noted that the phrase in consequence of the termination of your employment is not defined in the legislation. However, both the Courts and the Commissioner have considered meaning of this phrase.

30. In Taxation Ruling TR 2003/13 the Commissioner considered the meaning of the phrase in consequence of as interpreted by the Courts. In paragraph 5 of TR 2003/13 the Commissioner states:

a payment is made in respect of a taxpayer in consequence of the termination of the employment of the taxpayer if the payment follows as an effect or result of the termination

31. As further stated by the Commissioner in paragraph 6 of TR 2003/13, there must be:

a causal connection between the termination and the payment, although the termination need not be the dominant cause of the payment. The question of whether a payment is made in consequence of the termination of employment will be determined by the relevant facts and circumstances of each case.

32. Also in paragraph 5 of TR 2003/13 the Commissioner notes that the Courts have considered the meaning of the words in consequence of in several cases. Of note are the decisions made by the Full Bench of the High Court in *Reseck v. Federal Commissioner of Taxation*² (*Reseck*) and the Full Federal Court in *McIntosh v. Federal Commissioner of Taxation*³ (*McIntosh*).

33. In *Reseck* Gibbs J stated:

Within the ordinary meaning of the words a sum is paid in consequence of the termination of employment when the payment follows as an effect or result of the termination. It is not my opinion necessary that the termination of the services should be the dominant cause of the payment.

While Jacobs J, in the same case, stated:

It was submitted that the words in consequence of import a concept that the termination of the employment was the dominant cause of the payment. This cannot be so. A consequence in this context is not the same as a result. It does not import causation but rather a following on.

34. In looking at the phrase 'in consequence of' the Full Federal Court in *McIntosh* considered the decision in *Reseck*. In doing so the Full Federal Court emphasised that a payment may be in consequence of the termination of employment even though the termination is not the dominant cause of the payment.

35. Brennan J considered the judgments of Gibbs J and Jacobs J in *Reseck* and concluded that their Honours were both saying that a causal nexus between the termination and payment was required, though it was not necessary for the termination to be the dominant cause of the payment.

² (1975) 133 CLR 45; 75 ATC 4213; (1975) 5 ATR 538.

³ (1979) 25 ALR 557; 79 ATC 4325; (1979) 10 ATR 13.

36. Suffice to say, the view of both Courts was that for a payment to be made in consequence of the termination of employment it had to follow on as a result or effect of the termination of employment. Additionally, while it is not necessary to show that termination of employment is the sole or dominant cause, a temporal sequence alone would not be sufficient.

37. The phrase 'in consequence of' and the decisions in *Reseck* and *McIntosh* were considered more recently by the Federal Court in *Le Grand v. Federal Commissioner of Taxation*⁴ (*Le Grand*), where Goldberg J stated:

I am satisfied that there is a sufficient connection between the termination of the applicant's employment and the payment to warrant the finding that the payment was made in consequence of the termination of the applicant's employment. I am satisfied that the payment was an effect or result of that termination in the sense that there was a sequence of events following the termination of the employment which had a relationship and connection which ultimately led to the payment.

38. Goldberg J concluded that the test for determining when a payment is made in consequence of the termination of employment is that which was expressed by Gibbs J in *Reseck*. Thus, for the payment to have been made in consequence of the termination of employment, the payment must follow as an effect or result of the termination of employment. As noted in both paragraphs 6 and 28 of TR 2003/13, there must be 'a causal connection between the termination and the payment even though the termination need not be the sole or dominant cause of the payment'.

39. Therefore if the payment follows as an effect or a result from the termination of employment, the payment will be made in consequence of the termination of employment for the purposes of subparagraph 82-130(1)(a)(i).

40. From the facts provided, the principal conditions of employment for employees of the employer working on the Project are detailed in the Agreement. The Agreement includes a provision for an entitlement called PSL at clause 34 of the Agreement. Under subclause 34(10) of the Agreement any unused PSL at the time of termination from the Project will be paid to the employee.

41. The payment of unused PSL is made in consequence of the termination of employment as the payment fund under subclause 34(10) of the Agreement follows on as an effect or a result of the termination of employment. The unused PSL is paid to employees when they terminate employment with the employer on the Project. There is a sufficient connection between the unused PSL payment and the termination of employment for the payment to be considered to be made in consequence of the termination of employment.

⁴ [2002] FCA 1258; (2002) 124 FCR 53; 2002 ATC 4907; (2002) 51 ATR 139.

42. This being the case, the condition under paragraph 82-130(1)(a) has been met.

The payment is made no later than 12 months after the termination of employment

43. The second condition for the payment to meet the criteria, as an employment termination payment is stated under paragraph 82-130(1)(b), is that the employment termination payment was paid to the taxpayer no later than 12 months after their employment was terminated.

44. On the basis that the unused PSL payments will be made to employees within 12 months of the termination of employment from the Project the condition under paragraph 82-130(1)(b) has been met..

The payment is not a payment specifically excluded under section 82-135

45. The third condition for the payment to meet the criteria, as an employment termination payment is stated under paragraph 82-130(1)(c), is that the payment must not be specifically excluded under section 82-135.

46. Section 82-135 provides that certain payments are not employment termination payments, including:

- superannuation benefits;
- payment for unused annual leave or unused long service leave (and any other similar leave);
- the tax-free part of a genuine redundancy payment or an early retirement scheme payment; and
- reasonable capital payments for personal injury.

47. On the basis of the information provided by the applicant, it is accepted that the PSL payments are not payments that are specifically excluded under section 82-135, therefore the condition under paragraph 82-130(1)(c) has been met.

48. As the PSL payments made to an employee in accordance with the scheme described in paragraphs 9 to 21 of the Ruling satisfy all the conditions under subsection 82-130(1), the payments are employment termination payments for the purposes of section 82-130.

Appendix 2 – Detailed contents list

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

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References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2003/13; TR 2006/10

Subject references:

- employment termination
- employment termination payments
- superannuation, retirement & employment termination

Legislative references:

- ITAA 1997
- ITAA 1997 82-130
- ITAA 1997 82-130(1)
- ITAA 1997 82-130(1)(a)
- ITAA 1997 82-130(1)(a)(i)
- ITAA 1997 82-130(1)(b)

- ITAA 1997 82-130(1)(c)

- ITAA 1997 82-135

- ITAA 1997 995-1

- TAA 1953

- Copyright Act 1968

Case references:

- Le Grand v. Federal Commissioner of Taxation [2002] FCA 1258; (2002) 124 FCR 53; 2002 ATC 4907; (2002) 51 ATR 139
- McIntosh v. Federal Commissioner of Taxation (1979) 25 ALR 557; 79 ATC 4325; (1979) 10 ATR 13
- Reseck v. Federal Commissioner of Taxation (1975) 133 CLR 45; 75 ATC 4213; (1975) 5 ATR 538

ATO references

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