


TD 93/D254 - Income tax: what is the income tax treatment of a deferred salary payment agreement?

 This cover sheet is provided for information only. It does not form part of *TD 93/D254 - Income tax: what is the income tax treatment of a deferred salary payment agreement?*

This document has been finalised by TD 94/243.

Draft Taxation Determinations (TDs) represent the preliminary, though considered, views of the ATO. Draft TDs may not be relied on; only final TDs are authoritative statements of the ATO.

Draft Taxation Determination

Income tax: what is the income tax treatment of a deferred salary payment agreement?

1. A deferred salary payment agreement refers to an employment contract where the employee agrees to forgo a portion of the normal annual salary for his or her position in return for paid leave in a later period.
2. Subsection 25(1) of the *Income Tax Assessment Act 1936* (ITAA) provides that the assessable income of a resident taxpayer shall include gross income derived directly or indirectly from all sources whether in or out of Australia.
3. Income from employment, such as salary, wages or other payments to employees for services rendered, is generally said to be derived only when received. That is, on a cash receipts basis.
4. Section 19 of the ITAA provides that there is "constructive receipt" when income is credited without restriction and made available to the taxpayer. For instance, if an amount is credited to an employee in the books of his employer and can be drawn by the employee at any time, it is derived at the time it was so credited and made available to the employee.
5. Section 19 does not apply to include the deferred salary component, payable under a deferred salary payment agreement, in the taxpayer's assessable income prior to payment provided the deferred amount is not applied, accumulated or invested for the benefit of the taxpayer. In these circumstances the amount is assessable when received.

Example 1:

A taxpayer enters into a five year employment contract with his/her employer. Under the contract, the taxpayer is paid a contracted salary equivalent to 80% of the normal annual salary for the position in each of the first four years. In the fifth year the taxpayer is entitled to paid sabbatical leave at the contracted salary amount.

The entitlement to paid sabbatical leave accrues over the period of the contract. Under the terms of the contract, the taxpayer does not have access to the accruing paid sabbatical leave until the fifth year or on earlier termination of the contract. The salary forgone is not invested or accumulated on the taxpayer's behalf.

The payment for the accrued sabbatical leave is assessable to the taxpayer in the year of payment, that is, in the fifth year or on early termination.

Example 2:

At the direction of the taxpayer, an employer pays the taxpayer 80% of his/her yearly salary for four years. The remaining 20% per annum is placed into a savings account on the employee's behalf. In the fifth year the taxpayer is in a position to take fully paid leave for a year by utilising the accumulated savings.

The provisions of section 19 of the ITAA would apply to such an arrangement. The taxpayer is entitled to receive the remaining 20% salary in each given year but directs the employer to place it into a savings account on his/her behalf. Therefore, the deferred salary is assessable to the taxpayer in each of the given years.

Commissioner of Taxation

30/9/93

FOI INDEX DETAIL: Reference No.

Related Determinations:

Related Rulings: TD 92/D155

Subject Ref: assessable income; deferred income; income derived; contract of employment

Legislative Ref: ITAA 25(1); ITAA 17; ITAA 19

Case Ref:

ATO Ref: CAN AC752/16

ISSN 1038 - 8982