


CR 2007/28 - Income tax: deductibility of employer contributions to the Australian Construction Industry Redundancy Trust

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Class Ruling

Income tax: deductibility of employer contributions to the Australian Construction Industry Redundancy Trust

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① 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, we must apply the law to you in the way set out in the ruling (unless we are satisfied that the ruling is incorrect and disadvantages you, in which case we may apply the law in a way that is more favourable for you – provided we are 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.

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(s)

2. The relevant provisions dealt within this Ruling are:

- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997); and
- section 8-1 of the ITAA 1997.

All legislative references in this Ruling are to the ITAA 1997 unless otherwise indicated.

Class of entities

3. The class of entities to which this Ruling applies is all employers who make contributions to the Australian Construction Industry Redundancy Trust (ACIRT) on behalf of workers who are members of ACIRT (members).

Qualifications

4. The Commissioner makes this Ruling based on the precise scheme identified in this Ruling.

5. 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 13 to 27 of this Ruling.

6. 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

8. This Ruling applies from 1 July 2006 to 30 June 2012. However, the Ruling continues to apply after this date to all entities within the specified class who entered into the specified scheme during the term of the Ruling, subject to there being no change in the scheme or in the entities involved in the scheme.

9. The Ruling does not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Ruling. Furthermore, the Ruling only applies to the extent that:

- it is not later withdrawn by notice in the *Gazette*; or
- the relevant provisions are not amended.

10. If this Class Ruling is inconsistent with a later public or private ruling, the relevant class of entities may rely on either ruling which applies to them (item 1 of subsection 357-75(1) of Schedule 1 to the *Taxation Administration Act 1953* (TAA)).

11. If this Class Ruling is inconsistent with an earlier private ruling, the private ruling is taken not to have been made if, when the Class Ruling is made, the following two conditions are met:

- the income year or other period to which the rulings relate has not begun; and
- the scheme to which the rulings relate has not begun to be carried out.

12. If the above two conditions do not apply, the relevant class of entities may rely on either ruling which applies to them (item 3 of subsection 357-75(1) of Schedule 1 to the TAA).

Scheme

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

14. ACIRT is an Australian resident trust fund governed by a trust deed (Trust Deed) which established the fund in Australia. The central management and control of the fund is in Australia.

15. The trustee of ACIRT is ACIRT Pty Ltd ACN 062330170 (the Trustee), an Australian resident company.

16. The trustee has appointed an administrator of ACIRT and an investment manager to manage the investments of ACIRT on behalf of the trustee.

17. ACIRT is an approved worker entitlement fund for fringe benefits tax (FBT) purposes from 26 February 2004.

18. Employers are obligated by various industrial awards and enterprise agreements (industrial instruments) to provide redundancy benefits for their workers. Employers can fund worker redundancy benefits that they are required to make by the payment of contributions to ACIRT.

19. An employer must apply to the trustee of ACIRT for admission to ACIRT and must complete a Deed of Adherence to participate in ACIRT.

20. ACIRT accepts contributions from employers, on a monthly basis, for each week of service in respect of which contributions are legally payable under an industrial instrument or the Deed of Adherence, to fund each worker's redundancy benefit. Under clause 4.1 of the Trust Deed, the amount to be contributed by the employer in respect of each worker is:

- the minimum contribution (as defined in the Trust Deed);
- an amount required to fund the workers redundancy benefit as provided in an industrial instrument;

- such higher contribution specified in the Deed of Adherence; or
- such contribution specified in the Deed of Adherence until the total amount as specified in the Deed of Adherence has been contributed.

21. As outlined in clause 5.1 of the Trust Deed, all contributions made to ACIRT by employers will be placed into separate member accounts identifying contributions for that member.

22. On becoming redundant, as defined in the Trust Deed, an employee is entitled to be paid a redundancy benefit of the amount held in the member's account.

23. In addition to receiving contributions from employers on behalf of workers, ACIRT earns income on the contributions it holds. After payment of fund expenses, ACIRT distributes all of the net income each year to members.

24. The net income available for distribution is divided amongst members in proportion to the members' account balances (subject to a minimum balance requirement).

25. The Trust Deed in Clause 19.4 contains a facility for reimbursement of the employer, where it has paid the redundancy amount to the member directly.

26. Members can transfer the benefits they have accumulated with another similar redundancy fund into ACIRT where such transfer is permitted by the other fund.

27. Members can transfer benefits from ACIRT to another approved worker entitlement fund.

Ruling

28. An employer who makes contributions for worker redundancy benefits to ACIRT under the Trust Deed can claim a deduction under section 8-1 for the amount of the contributions.

29. Where an employer pays an amount directly to a worker, which the worker is entitled to on redundancy under the Trust Deed, and then seeks reimbursement from ACIRT, the amount of the payment will be an allowable deduction under section 8-1.

30. A reimbursement received by an employer from ACIRT for an amount paid directly to a worker, which the worker is entitled to on redundancy under the Trust Deed, will be assessable income under section 6-5 at the time the amount is derived by the employer.

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.*

Application of section 8-1

31. Section 8-1 provides that you can deduct from your assessable income any loss or outgoing to the extent that it is incurred in gaining or producing assessable income or is necessarily incurred in carrying on a business for the purpose of gaining or producing assessable income and is not:

- capital, private or domestic in nature;
- incurred in gaining or producing exempt income; or
- prevented from being deductible by a provision of the ITAA 1997.

Positive limbs

Nexus to gaining and producing assessable income

32. Employers, in the course of carrying on their business activities, are obligated by various industrial instruments to provide redundancy benefits for their workers. Employers can fund these worker redundancy benefits that they are required to make by the payment of contributions to ACIRT.

33. If an employer chooses to fund their worker redundancy benefits via contributions to ACIRT, a Deed of Adherence is executed between the employer and ACIRT.

34. In addition to the employer's legal obligations under the relevant industrial instrument, the employer is also required to meet the obligations under the Deed of Adherence and the Trust Deed. The administrative provisions require the employer to make monthly contributions to ACIRT in respect of worker entitlements.

35. It is accepted that there is a nexus between the business activities being carried on by the employer and the employer's obligation to provide for worker redundancy benefits, such that payment of the contributions is incidental and relevant to the production of the assessable income of the business.

Incurring the amount

36. At the point at which an employer makes a contribution to the Trustee of ACIRT the amount is placed into member accounts and the amount is no longer available to the employer. This differs from the situation in *Walstern Pty Ltd v. Federal Commissioner of Taxation* [2003] FCA 1428; 2003 ATC 5076; (2003) 54 ATR 423 where there were no members of the trust. The contributions were not expenses incurred by the employer as they remained funds of the employer.

37. The fact that amounts may be returned to the employer under the Trust Deed when the employer is reimbursed for payments made directly to a worker (a factor which does not prevent ACIRT being an approved worker entitlement fund under section 58PB of the *Fringe Benefits Tax Assessment Act 1986*) does not affect whether the monthly contributions are incurred by the employer.

38. Even though the Trust Deed enables the employer to seek reimbursement in certain circumstances, the contributions to ACIRT are definite payments which the employer is required to make to meet the legal obligations under the industrial instruments or Deed of Adherence which arise in the course of carrying on their business activities. As such the employer incurs the expenditure on contributions when the liability to make the payment arises each month.

Conclusion

39. The employer's monthly contributions to ACIRT are outgoings necessarily incurred in carrying on a business for the purpose of gaining or producing assessable income for the purposes of section 8-1.

Negative limbs

Is the contribution revenue or capital in nature?

40. Whether the payment of contributions for worker redundancy benefits to ACIRT is revenue or capital in nature depends on the character of the payment when made by the employer. As stated in *GP International Pipecoaters Pty Ltd v. Federal Commissioner of Taxation* (1990) 90 ATC 4413 at 4419; (1990) 21 ATR 1 at 7:

The character of expenditure is ordinarily determined by reference to the nature of the asset acquired or the liability discharged by the making of the expenditure, for the character of the advantage sought by the making of the expenditure is the chief, if not the critical, factor in determining the character of what is paid: *Sun Newspapers Ltd. v. F.C. of T.* (1938) 61 C.L.R. 337 at p. 363.

41. In making the monthly contributions to ACIRT as required by clause 4.1 of the Trust Deed, the employer meets their immediate legal obligation under an industrial instrument or the Deed of Adherence.

42. The employer is making repetitive monthly contributions to discharge an immediate obligation and the obligation is directly connected to the income earning capacity of the business. Accordingly, the payment of the contributions is revenue in nature.

Payments by employer to employee

43. It is accepted that there is a nexus between the business activities being carried on by the employer and the employer's obligation to provide for worker redundancy benefits, such that payment of the worker redundancy benefits directly to a worker by an employer is incidental and relevant to the production of the assessable income of the business.

44. Accordingly the payment of a worker redundancy benefit directly to a redundant worker would be an allowable deduction under section 8-1 as an outgoing incurred in gaining or producing assessable income or in carrying on a business for that purpose.

Reimbursement of payment by employer

45. Where an employer has paid a worker their worker redundancy benefit directly, the employer may apply to ACIRT for a reimbursement of this amount. ACIRT may reimburse the employer for this amount under clause 19.4 of the Trust Deed.

46. Where an employer has claimed or will claim a deduction for a worker redundancy benefit paid directly to a redundant worker under section 8-1, the reimbursement of this expense must be declared as income. In these cases it is considered that the reimbursement is income received in the ordinary course of business and assessable under section 6-5 in the income year in which it is derived.

Appendix 2 – Detailed contents list

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References

Previous draft:

Not previously issued as a draft

Subject references:

- assessable recoupments
- deductions and expenses
- eligible termination payments
- income

Legislative references:

- ITAA 1997 6-5
- ITAA 1997 8-1
- FBTAA 1986 58PB
- Copyright Act 1968
- TAA 1953

- TAA 1953 Sch 1 357-75(1)

Case references:

- GP International Pipecoaters Pty Ltd v. Federal Commissioner of Taxation (1990) 90 ATC 4413; (1990) 21 ATR 1
- Sun Newspapers Ltd v. FC of T (1938) 61 CLR 337
- Walstern Pty Ltd v. Federal Commissioner of Taxation [2003] FCA 1428; 2003 ATC 5076; (2003) 54 ATR 423

ATO references

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