



Class Ruling

Income tax: Deferred Salary Payment Agreement for Sabbatical Leave Scheme by teachers at Lutheran Schools and Kindergartens in South Australia

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Preamble

*The number, subject heading, and the **What this Class Ruling is about** (including **Tax law(s)**, **Class of persons** and **Qualifications** sections), **Date of effect**, **Arrangement** and **Ruling** parts of this document are a 'public ruling' in terms of Part IVAAA of the **Taxation Administration Act 1953**. CR 2001/1 explains **Class Rulings** and **Taxation Rulings** TR 92/1 and TR 97/16 together explain when a **Ruling** is a public ruling and how it is binding on the Commissioner.*

What this Class Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the 'tax laws' identified below apply to the defined class of persons, who take part in the arrangement to which this Ruling relates.

Tax law(s)

2. The tax law(s) dealt with in this Ruling are:

- sections 26AC, 26AD and 101A of the *Income Tax Assessment Act 1936* (ITAA 1936);
- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- subsection 136(1) of the *Fringe Benefits Tax Assessment Act 1986* (FBTAA 1986); and
- section 12-35 of Schedule 1 to the *Taxation Administration Act 1953* (TAA 1953).

Class of persons

3. The class of persons to which this Ruling applies is full time and part time teachers at Lutheran Schools and Kindergartens in South Australia that are a party to the SA Lutheran Schools Enterprise Agreement 2003 (the Agreement).

Qualifications

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

5. The class of persons defined in this Ruling may rely on its contents provided the arrangement actually carried out is carried out in accordance with the arrangement described below at paragraphs 9 to 25 in this Ruling.

6. If the arrangement actually carried out is materially different from the arrangement that is described in this Ruling:

- (a) this Ruling has no binding effect on the Commissioner because the arrangement entered into is not the arrangement on which the Commissioner has ruled; and
- (b) this Ruling may be withdrawn or modified.

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Date of effect

8. This Ruling applies from 1 July 2003. However, 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 (see paragraphs 21 and 22 of Taxation Ruling TR 92/20).

Arrangement

9. The arrangement that is the subject of the Ruling is described below. This description is based on the following documents. These documents, or relevant parts of them, as the case may be, form part of and are to be read with this description. The relevant documents or parts of the documents incorporated into the description of the arrangements are:

- Application for Class Ruling dated 28 May 2003;
- e-mail dated 7 July 2003 from the applicant; and
- revised draft of the clause in the Agreement which relates to Sabbatical Leave, provided as part of the additional information on 7 July 2003.

10. The Lutheran Schools Association of SA, NT & WA Inc. is the governing body of various Lutheran Schools throughout Australia. The Agreement provides the basis for a scheme whereby full time and part time teachers at Lutheran Schools in South Australia that are a party to the Agreement, can enter into an agreement with their employer school to defer an entitlement to salary in return for the right to receive salary while taking sabbatical leave.

11. The sabbatical leave scheme is designed to help with the reduction in stress arising out of the teaching service. Participants in the scheme are expected to use the sabbatical leave to be reinvigorated. This could mean a course of study, trying a different job, or travel.

12. Teachers who have been employed within Lutheran Schools that are a party to the Agreement who wish to participate in the scheme require:

- a minimum of two years continuous service; and
- approval of the employer school which depends upon the needs and requirements of the school.

13. The sabbatical leave is funded by the employee who defers the payment of salary by either:

- reducing his or her normal annual salary by 20% and taking sabbatical leave in the fifth year; or
- reducing his or her normal annual salary by 10% and taking sabbatical leave in the tenth year.

14. Normal salary is defined as a teacher's normal fortnightly salary plus any associated teaching allowances.

15. The employee continues to work the normal agreed hours as specified in the Enterprise Agreement.

16. The period of leave will be for twelve months, from 1 February to 31 January of the subsequent year.

17. Participants in the scheme may withdraw at any time by notifying the employer in writing. Participation in the scheme will be suspended during any period of unpaid leave. Any period of unpaid leave will reduce contributions to the scheme and therefore proportionately reduce the accrued payment in the year of leave.

18. Once an employer has approved an application under the sabbatical leave clause of the Agreement, the employer cannot withdraw from the arrangement.

19. A participant may elect to suspend contributions for a period of less than twelve months, once during the accrual period. This will also reduce the accrued payment in the year of leave. The employer retains the discretionary authority to approve suspension for a period of twelve months at the request of the participant. Such a suspension will extend the taking of the year of leave by one year.

20. Teachers are able to maintain their participation in the scheme should they transfer their employment between Lutheran Schools that are a party to the Agreement.

21. The salary differential sacrificed by the employee will be remitted by the school, on a two or four weekly basis, to the Lutheran Schools Association of SA, NT & WA Inc. for management. The amount will be recognised by the schools as a future liability to pay the employee and provision will be made in the accounts of the employer school. Interest does not accrue to the employee on the amount for which the employer school has made provision. Neither the Lutheran Schools Association SA, NT & WA Inc. nor the employer schools will open individual bank accounts or similar investments on behalf of the employees.

22. All contributions to the scheme are guaranteed by the Lutheran Schools Association. Interest accrued will be utilised to offset the administrative costs of the fund.

23. The exact amount for which provision has been made will be paid to the employee:

(a) when sabbatical leave is taken:

- fortnightly during the year of taking the sabbatical leave;
- two payments equally spaced throughout the one year period of sabbatical leave; or
- one lump sum payment at the commencement of the sabbatical leave.

(b) earlier when one of the following events occurs:

- termination of employment; or
- the employee withdraws from the scheme.

24. Should the employee die before one of the events in the previous paragraph has occurred, the amount set aside as a provision will be paid to the personal representative of the deceased employee.

25. A participant in the scheme may defer the taking of sabbatical leave by agreement with the employer. If this occurs, the payment of salary arrangements shall continue unless there is agreement to suspend contributions as provided by the relevant sub-clause in the Agreement.

Ruling

26. The amount of salary which a teacher in the class of persons described in paragraph 3 of this ruling defers receiving in return for the right to receive income while taking sabbatical leave, is assessable income in the taxation year/s in which it is derived.

27. Each fortnightly amount of deferred salary paid to the teacher during the year of sabbatical leave is derived as income in the taxation year in which it is received.

28. Each of the two equally spaced amounts of deferred salary paid to the teacher during the year of sabbatical leave is derived as income in the taxation year in which it is received.

29. Where the deferred amount of salary is paid to the teacher as a lump sum it is derived as income in the taxation year in which it is received.

30. The assessable income of the legal representative of the estate of a deceased teacher includes all salary paid after the death of the employee. The salary paid after the death of the teacher is derived in the taxation year in which it is received by the legal representative.

Explanation

31. The Commissioner's view of the income tax treatment of deferred salary payment agreements is set out in Taxation Determination TD 93/242.

32. Teachers employed by Lutheran Schools and Kindergartens in South Australia that are a party to the SA Lutheran Schools Enterprise Agreement 2003, who enter the scheme described in the Arrangement part of this Ruling, have varied their employment contracts. In return for accepting a lesser salary for future employment services they will provide to the employer, they will have an entitlement to receive a salary while on sabbatical leave.

33. Subsection 6-5(1) ITAA 1997 provides that the assessable income of a taxpayer includes income according to ordinary concepts, which is called ordinary income. Subsection 6-5(2) provides that the assessable income of Australian residents includes ordinary income derived directly or indirectly from all sources.

34. Income from employment is generally derived only when received. Where an employee has entered into an agreement to have their salary discounted, it is the amount of discounted salary received that is assessable income and brought to account under subsection 6-5(1).

35. The income that the discounting of salary defers is not considered to be an amount that has been applied or dealt with in any way on behalf of, or at the direction of the employee. While the employer School recognises that it has a future obligation to make the payment, the employee does not have the right to draw on the amount until one of the events in paragraph 23 occurs. It is considered that subsection 6-5(4) does not apply.

36. If the employee dies before deriving all or some of the deferred salary, the amount so paid thereafter is the assessable income of the legal representative of the deceased employee's estate and is brought to account under section 101A of the ITAA 1936. The deferred salary is not in respect of annual leave or long service leave that would have been included in the assessable income of the employee by virtue of either section 26AC or 26AD of the ITAA 1936 if received by the employee before death. Therefore the exclusion of income that subsection 101A(2) provides does not apply.

37. Fringe Benefit is a widely defined term in subsection 136(1) of the FBTA 1986. Paragraph (h) of that definition specifically excludes a payment of salary or wages from being a fringe benefit. As the deferred salary will be salary when taken, the right to receive salary while on sabbatical leave is not a fringe benefit.

Pay as you go (PAYG) withholding

38. At the time of paying the deferred salary to the employee, whether paid fortnightly, as two equally spaced payments or as a lump sum, the Lutheran School or Kindergarten is an employer that is making a payment of salary to an employee. Section 12-35 of Schedule 1 to the TAA 1953 requires that the Lutheran School or Kindergarten withhold an amount from that payment of salary.

39. The legal representative of the deceased estate of an employee is not an employee of the Lutheran School or Kindergarten. The Lutheran School is not required to withhold an amount from a payment to the legal representative.

Detailed contents list

40. Below is a detailed contents list for this Class Ruling:

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Commissioner of Taxation

3 September 2003

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

CR 2001/1; TR 92/1; TR 92/20;
TR 97/16; TD 93/242

Subject references:

- deferred salary payment
- assessable income
- contract of employment
- deferred income
- income derived

CR 2003/75

Legislative references:

- ITAA 1936 26AC
 - ITAA 1936 26AD
 - ITAA 1936 101A
 - ITAA 1936 101A(2)
 - ITAA 1997 6-5
 - ITAA 1997 6-5(1)
 - ITAA 1997 6-5(2)
 - ITAA 1997 6-5(4)
 - TAA 1953 Part IVAAA
 - TAA 1953 Schedule 1, 12-35
 - FBTAA 1986 136(1)
 - FBTAA 1986 136(1)(h)
 - Copyright Act 1968
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ATO references

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