



Class Ruling

Income tax: early retirement scheme – Alcoa of Australia Limited

Contents	Para
LEGALLY BINDING SECTION:	
What this Ruling is about	1
Date of effect	8
Scheme	9
Ruling	30
Appendix 1:	
Explanation	33
Appendix 2:	
Detailed contents list	51

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, 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.

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 with this Ruling are:

- section 83-170 of the *Income Tax Assessment Act 1997* (ITAA 1997); and
- section 83-180 of the ITAA 1997.

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

Class of entities

3. The class of entities to which this Ruling applies is those Pinjarra Refinery operators who receive a payment under the scheme described in paragraphs 10 to 28 of this Ruling.

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 10 to 28 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 18 May 2011 to 31 March 2012. The Ruling continues to apply after 31 March 2012 to all entities within the specified class who entered into the specified scheme during the term of the Ruling. However, this Ruling will not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Scheme

9. The following description of the scheme is based on information provided by the applicant.
10. Alcoa of Australia Limited (the Company) is seeking approval for an early retirement scheme (ERS).
11. The class of persons to whom this scheme applies is all Pinjarra Refinery operators covered by the Alcoa World Alumina Australia Pinjarra Refinery AWU Enterprise Agreement 2011 (EBA).

12. The purpose of the scheme is to reduce the size of the operator workforce at its Pinjarra alumina refinery, south of Perth. As part of the restructuring of the non-core functions at the refinery these functions will be outsourced to contractor organisations with the aim of improving the refinery's cost competitiveness by achieving productivity gains.

13. The recently completed EBA included an agreement to outsource the work currently being undertaken in the cleaning, scaffolding and de-scaling departments at Pinjarra.

14. The maximum number of eligible employees that the employer will allow to retire under the scheme, will be limited.

15. Should the expressions of interest from the directly affected employees in the cleaning, scaffolding and de-scaling departments at the Pinjarra Refinery be less than the number of employees required to participate in the scheme, the Company will call for other employees at the Pinjarra site to express an interest in the scheme.

16. Following approval of the scheme, all eligible employees within the class will have until the end of June 2011 to express an interest in the scheme.

17. Offers will be made first to the directly affected employees in the cleaning, scaffolding and de-scaling departments at Pinjarra, then made to other employees on the basis of site seniority. All offers will be made by the end of July 2011.

18. Separation packages that are the subject of this ruling will not occur prior to 1 July 2011.

19. Once an offer is made an eligible employee will have between 2 and 6 months to terminate employment. All employees who retire under the scheme will terminate employment and receive the payment on a date determined by the employer based on their operational requirements but no later than 31 March 2012.

20. It is proposed the scheme will be implemented from 18 May 2011 to 31 March 2012.

21. Participation in the ERS is entirely voluntary.

22. Directly affected employees who do not wish to participate in the scheme will be relocated to other roles outside the three work areas.

23. There are no employees within the class that the employer will not allow to retire as part of the scheme.

24. All eligible employees under the ERS will be offered a separation package based on the agreed calculation prescribed in the EBA at clause 9 of Appendix 5 and shown as follows:

- (a) A minimum of four weeks notice shall apply, and generally the notice period shall be worked out by mutual agreement between the Company and the employee concerned.
- (b) An ex-gratia payment calculated in accordance with the following cumulative formula:
 - (i) first 5 years of continuous service – 3 weeks' pay for each completed year and pro-rata payment for any part thereof
 - (ii) sixth to tenth year of continuous service – 4 weeks' pay for each completed year and pro-rata payment for any part thereof
 - (iii) eleventh and subsequent years of continuous service – 4.5 weeks' pay for each completed year and pro-rata payment for any part thereof.
- (c) For the purposes of this clause, 'a weeks' pay' shall be defined as annual rate of pay (superannuation salary) divided by 52.1667;
- (f) All payments made under this clause are to be calculated on the base salary amount (that is, superannuation salary).

25. In addition, employees will receive any unused annual leave and long service leave entitlements, however they do not form part of the payment made under the scheme.

26. The ex-gratia payment is in excess of any superannuation and any other benefits to which eligible employees would otherwise be entitled.

27. The Payments made under the ERS are at arm's length.

28. The retirement of employees under the ERS will occur before they turn 65 years of age.

29. There is no agreement in place between the employee and the Company, or between the Company and another person to employ the employee after retirement.

Ruling

30. The early retirement scheme to be implemented by Alcoa of Australia Limited is an early retirement scheme for the purposes of section 83-180.

31. Accordingly, so much of the payment received by an employee that exceeds the amount that could be reasonably be expected to be received by the employee in consequence of voluntary termination of his or her employment at the time of the retirement will be an early retirement scheme payment.

32. In addition, so much of the early retirement scheme payment as falls within the threshold calculated in accordance with section 83-170 is not assessable income and is not exempt income.

Commissioner of Taxation

18 May 2011

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.*

33. Where a scheme satisfies the requirements of section 83-180 that scheme will be an 'early retirement scheme'.

34. Subsection 83-180(3) states that:

A scheme is an **early retirement scheme** if:

- (a) all the employer's employees who comprise such a class of employees as the Commissioner approves may participate in the scheme; and
- (b) the employer's purpose in implementing the scheme is to rationalise or re-organise the employer's operations by making any change to the employer's operations, or the nature of the work force, that the Commissioner approves; and
- (c) before the scheme is implemented, the Commissioner, by written instrument, approves the scheme as an early retirement scheme for the purposes of this section.

These three conditions will now be considered.

All employees within a class approved by the Commissioner may participate in the scheme

35. In order to satisfy the first condition, the scheme must be offered to all employees in a class approved by the Commissioner under paragraph 83-180(3)(a).

36. The class of employees to whom early retirement will be offered is set out in paragraph 11 of this Ruling.

37. The Commissioner considers that this is an appropriate class of persons for the scheme to be offered to. In approving this class of employees the Commissioner has considered the nature of the rationalisation or re-organisation of the operations of the employer. It is therefore considered that these employees meet the requirements of an approved class of employees for the purposes of paragraph 83-180(3)(a).

The employer's purpose in implementing the scheme is to rationalise or re-organise the employer's operations in a way approved by the Commissioner

38. The proposed scheme must be implemented by the employer with a view to rationalising or re-organising the operations of the employer as described in paragraph 83-180(3)(b).

39. Paragraphs 12 and 13 of this Ruling describe the nature of the rationalisation or re-organisation of the employer's operations. In approving the Scheme, the Commissioner has had regard to the changes in the operations and nature of the workforce of the employer. It is therefore considered the scheme is to be implemented by the employer with a view to rationalising or re-organising the operations of the employer for the purposes of paragraph 83-180(3)(b). Accordingly, the second condition for approval has been met.

The scheme must be approved by the Commissioner prior to its implementation

40. The Scheme is proposed to operate for a period from 18 May 2011 to 31 March 2012. Approval was granted prior to implementation therefore, for the purposes of paragraph 83-180(3)(c), the third condition is satisfied.

41. The scheme will be in operation for 10 months. This is considered to be appropriate in this case due to the circumstances of the restructure and for those employees that will be given the option of early retirement under the scheme.

Other relevant information

42. Under subsection 83-180(1) so much of the payment received by an employee, because the employee retires under an early retirement scheme, as exceeds the amount that could reasonably be expected to be received by the employee in consequence of the voluntary termination of his or her employment at the time of termination is an early retirement scheme payment.

43. It should be noted that, in order for a payment to qualify as an early retirement scheme payment, it must also satisfy the following requirements (as set out in subsections 83-180(2), 83-180(5) and 83-130(6)):

- the retirement occurred before the employee turned age 65 or such earlier date on which the employee's employment would have terminated under the terms of employment because of the employee attaining a certain age or completing a particular period of service (as the case may be);
- if the employee and the employer are not dealing with each other at arm's length (for example because they are related in some way) the payment does not exceed the amount that could reasonably be expected to be made if the retirement was made at arm's length;

- at the time of retirement there was no arrangement between the employee and the employer, or between the employer and another person, to employ the employee after the retirement;
- the payment must not be made in lieu of superannuation benefits;
- it is not a payment mentioned in section 82-135 (apart from paragraph 82-135(e)).

44. The term 'arrangement' is defined in subsection 995-1(1) as meaning 'any arrangement, agreement, understanding, promise or undertaking, whether express or implied, and whether or not enforceable (or intended to be enforceable) by legal proceedings'.

45. From 1 July 2007 an early retirement scheme payment that falls within the specified limit is referred to as the 'tax-free' amount and will not be assessable income and will not be exempt income.

46. For the 2010-11 income year, the tax-free amount is limited to \$8,126 (base amount) plus \$4,064 (service amount) for each whole year of completed employment service to which the early retirement scheme payment relates. It should be noted that 6 months, 8 months or even 11 months do not count as a whole year for the purposes of this calculation. In accordance with section 960-285, the base amount and service amount limits will be indexed in line with average weekly ordinary time earnings for each income year.

47. The total of the amount received on the termination of employment calculated in accordance with paragraph 24 of the facts may qualify as an early retirement scheme payment.

48. The total of the payments in paragraph 46 will be measured against the limit calculated in accordance with formula mentioned in paragraph 45 to determine the 'tax-free' amount of the early retirement scheme payment.

49. The 'tax-free' amount will:

- not be an employment termination payment; and
- not be able to be rolled-over into a superannuation fund.

50. Any payment in excess of this limit will be an employment termination payment and split up into tax free and taxable components. The tax free component of an employment termination payment includes the pre-July 83 segment of the payment. The tax free component is not assessable income and is not exempt income.

Appendix 2 – Detailed contents list

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

	Paragraph
What this Ruling is about	1
Relevant provision(s)	2
Class of entities	3
Qualifications	4
Date of effect	8
Scheme	9
Ruling	30
Appendix 1 – Explanation	33
All employees within a class approved by the Commissioner may participate in the scheme	35
The employer's purpose in implementing the scheme is to rationalise or re-organise the employer's operations in a way approved by the Commissioner	38
The scheme must be approved by the Commissioner prior to its implementation	40
Other relevant information	42
Appendix 2 – Detailed contents list	51

References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10

Subject references:

- early retirement scheme payment
- employment termination

Legislative references:

- Copyright Act 1968
- TAA 1953
- ITAA 1997

- ITAA 1997 82-135
- ITAA 1997 82-135(e)
- ITAA 1997 83-170
- ITAA 1997 83-180
- ITAA 1997 83-180(1)
- ITAA 1997 83-180(2)
- ITAA 1997 83-180(3)
- ITAA 1997 83-180(3)(a)
- ITAA 1997 83-180(3)(b)
- ITAA 1997 83-180(3)(c)
- ITAA 1997 83-180(5)
- ITAA 1997 83-180(6)
- ITAA 1997 960-285
- ITAA 1997 995-1(1)

ATO references

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