


CR 2010/58 - Income tax: treatment of transfer payments to employees of Country Energy following the sale of Country Energy Gas Pty Ltd (Gas Networks)

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Class Ruling

Income tax: treatment of transfer payments to employees of Country Energy following the sale of Country Energy Gas Pty Ltd (Gas Networks)

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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, 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 identified below applies to the defined class of entities, who take part in the scheme to which this Ruling relates.

Relevant provision(s)

2. The relevant provision dealt with in this Ruling is section 82-130 of the *Income Tax Assessment Act 1997* (ITAA 1997). All subsequent references in this Ruling are to the ITAA 1997 unless otherwise stated.

Class of entities

3. The class of entities to whom this scheme applies is employees of Country Energy who, at the time of the sale of Country Energy Gas Pty Ltd (Gas Networks):

- cease employment with Country Energy;
- accept an offer to take up employment with the purchaser of Gas Networks; and
- receive a 'transfer payment' from Country Energy under the scheme described in paragraphs 10 to 25 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 in accordance with the scheme described in paragraphs 10 to 25 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 December 2010 to 30 November 2012. This Ruling continues to apply after 30 November 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. Country Energy is a leading Australian energy services provider owned by the NSW Government.
11. The scheme is to be known as 'Income tax: treatment of transfer payments to employees of Country Energy following the sale of Country Energy Gas Pty Ltd (Gas Networks)'.
12. Country Energy operates Australia's largest electricity distribution network, extending across 95% of NSW and into parts of Queensland, Victoria and the Australian Capital Territory.
13. In addition to electricity, services provided by Country Energy include natural and bottled gas, and water and energy management.
14. Country Energy provides reticulated natural gas services to customers through its 100% owned subsidiary Gas Networks.
15. While Gas Networks is a sound asset and is earning a commercial return, it represents only 2% of Country Energy's total asset base, and there are no plans to grow Gas Networks in competition with the private sector. As a result, a decision was made to offer Gas Networks for sale to the private sector.
16. The sale will allow Country Energy to focus on its core business of delivering electricity to families and businesses across regional NSW.
17. The purchaser of Gas Networks will be determined by way of a tender process. The sale of Gas Networks will be structured as a sale of shares in that company to the preferred bidder.
18. Country Energy currently employs approximately 4,500 staff of which approximately 20 employees will be affected by the sale. These affected employees are currently employed by Country Energy, but their normal duties are substantially gas related. In this regard, while they work predominantly in the business conducted by Gas Networks they are not employees of that company.
19. For the majority of employees who choose to transfer it is expected that following the execution of the Sale and Purchase Agreement with the preferred bidder, employees will be given the option to transfer and receive an offer of employment that will give them a fixed time period of not less than two to three weeks to make their decision.
20. The majority of these employees are employed on the terms of the Country Energy Enterprise Agreement 2009 (NSW) and the Country Energy Managers and Specialist Agreement 2009 (NSW). The remaining employees are employed under separate contracts.

21. Upon the sale of Gas Networks, all permanent (full or part-time) employees with more than one year's service with Country Energy, who accept an offer to take up employment with the purchaser of Gas Networks, will receive a transfer payment from Country Energy.

22. The transfer payment reflects compensation for certain public sector employment conditions that will be lost following cessation of employment with Country Energy such as:

- No forced redundancies and voluntary redundancy provisions;
- Access to redeployment provisions, including salary maintenance (a period up to 12 months on full salary if an employee's position is made redundant) and professional career transition support with external providers and priority assignment of eligibility for vacancies within the public sector;
- Paid maternity leave provisions;
- Sick leave provisions;
- Extended leave (long service leave) provisions;
- Broader range of paid leave and leave without pay provisions;
- Mandatory flexible working hours arrangements;
- Access to provisions regarding the management of conduct and performance;
- Access to provisions regarding the advertising, eligibility, selection and appointment to positions; and
- Access to Government and Related Appeal Tribunal – ability to dispute promotions and disciplinary action

23. For a period of up to 12 months after the sale, Country Energy may be engaged to provide some transitional services (such as operations, maintenance, billing and other various administration tasks) to the purchaser of Gas Networks under a Transitional Services Agreement. Employees who provide these services will continue to be employed by Country Energy. However, it is possible that up until the end of the Transitional Service Agreement, the purchaser of Gas Networks may make offers of employment to these employees. Any of these employees who subsequently cease employment with Country Energy and transfer to the purchaser will also be entitled to a transfer payment.

24. The transfer payment will be determined as set out in the table below:

Length of Service	Transfer payment Week's ordinary time base rate of pay
1 year or more, but less than 2 years	7.5
2 years or more, but less than 3 years	13.125
3 years or more, but less than 4 years	18.75
4 years or more, but less than 5 years	22.5
5 years or more, but less than 6 years	26.25
6 years or more	30

25. The transfer payment will be paid at the earliest possible time after completion of the sale of Gas Networks and be received within 12 months of the termination of employment.

Ruling

26. The proposed transfer payment made in accordance with the scheme described in paragraphs 10 to 25 of this Ruling is in consequence of the termination of employment. Unless the employee is covered by a determination exempting them from the 12 month rule, the payment must be received within 12 months of the employee's termination of employment to qualify as an employment termination payment under section 82-130.

Commissioner of Taxation

27 October 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

27. Section 995-1 states that an employment termination payment has the meaning given by section 82-130.

28. 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 that termination (but see subsection (4)); and
- (c) it is not a payment mentioned in section 82-135.

29. Section 82-135 lists payments that are not employment termination payments. These include (among others):

- superannuation benefits;
- unused annual leave or long service leave payments; and
- the tax free part of a genuine redundancy payment or an early retirement scheme payment.

30. For a transfer payment to constitute an employment termination payment, all the conditions in section 82-130 must be satisfied. Failure to satisfy any of the three conditions under subsection 82-130(1) will result in the payment not being considered an employment termination payment.

Is there a termination of employment?

31. Paragraph 9 of Income Taxation Ruling IT 2152 Income tax: retiring allowances paid to employees upon restructuring of a business, states:

Where a company or other employer ceases carrying on a business which has been transferred to an associated entity, it will be accepted that the employees of the company have had their employment terminated. This will apply in cases similar to the *Paklan Case* where it is clear that the business in question has been transferred to another entity and it is also clear that the employee’s employment has, in fact, been terminated...

32. The facts in *Paklan Pty Ltd (in liq) v Federal Commissioner of Taxation*¹ (*Paklan*) can be summarised as follows:

- The taxpayers were directors and shareholders of a company (the old company) which carried on business as consulting engineers.
- On 30 June 1977 the old company ceased to carry on business and the next day sold the business to another company (the new company) also controlled by the taxpayers.
- The new company commenced carrying on the business from the same premises and subject to the same arrangements for occupancy as the old company.
- All the old company's employees, including the taxpayers, became employees of the new company.
- Six months later, it was decided to pay a lump sum to former directors. The payments were actually made a year after the company ceased business and out of outstanding fees received after the business had ceased.

33. The taxpayers in *Paklan* did not succeed in having the lump sums in question treated as a 'payment in consequence of termination' as they were paid under circumstances, and at a time, too remote from the termination. However, the Full Federal Court did not dispute the fact that employment had terminated when the old company had ceased business on 1 July 1977.

34. The facts in Board of Review *Taxation Case Q118*² are similar to those in *Paklan* and again involved the sale of a company's business as a going concern to a new company. All the employees of the old business were transferred across to the new company. The Board of Review did not dispute the fact that employees of the old company had ceased to be employees of the old company immediately before taking up employment with the new company.

35. Board of Review *Taxation Case K76*³ involved a taxpayer who ceased work with a subsidiary company due to a corporate restructure and immediately re-commenced work with the parent company on the same terms and conditions. It was held by the Board of Review that the taxpayer's employment with the subsidiary company had been terminated.

¹ (1983) 67 FLR 238; 83 ATC 4456; (1983) 14 ATR 457.

² (1983) 27 CTBR (NS) 312; (1983) 83 ATC 610.

³ (1978) 23 CTBR (NS) 24; 78 ATC 703.

36. The relevant facts in respect of the sale of Gas Networks indicate that employees of Country Energy affected by the sale will be able to elect whether to remain employed in the NSW Government public sector or to transfer to the purchaser of Gas Networks on completion of the sale.

37. Employees who take up positions with the purchaser of Gas Networks will cease employment with Country Energy. Therefore, there is a termination of their employment with Country Energy.

Is the making of the transfer payment ‘in consequence of the termination of employment’?

38. A payment can be considered to be in consequence of termination where it follows from the termination, or the termination is a condition precedent to the payment. In *Reseck v. Federal Commissioner of Taxation*⁴ (*Reseck*) Justice Gibbs said:

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 in my opinion necessary that the termination of the services should be the dominant cause of the payment.

39. In the same case, Justice Jacobs said that ‘in consequence of’ did not import causation but rather a ‘following on’.

40. The decision in *Reseck* was considered by the Full Federal Court in *McIntosh v. Federal Commissioner of Taxation*⁵ (*McIntosh*). The case concerned a taxpayer who became entitled to a payment subsequent to his retirement. In finding that the payment was in consequence of the taxpayer’s termination, Justice Brennan said:

...if the payment is made to satisfy a payee’s entitlement, the phrase ‘in consequence of retirement’ requires that the retirement be the occasion of, and a condition of, entitlement to the payment. A sufficient causal nexus between the payment and the retirement is thus established.

41. The phrase ‘in consequence of’ and the decisions in *Reseck* and *McIntosh* were also considered more recently by the Federal Court in *Le Grand v. Federal Commissioner of Taxation*⁶ (*Le Grand*).

⁴ (1975) 133 CLR 45; 75 ATC 4213; (1975) 5 ATR 538.

⁵ (1979) 45 FLR 279; 79 ATC 4325; (1979) 10 ATR 13.

⁶ [2002] FCA 1258; (2002) 124 FCR 53; 2002 ATC 4907; (2002) 51 ATR 139.

42. *Le Grand* involved a payment to the taxpayer as a result of accepting an offer of compromise in respect of claims brought by him against his former employer, in relation to the termination of his employment. The taxpayer had made claims for common law damages for breach of the employment agreement and for statutory damages for misleading and deceptive conduct to procure the taxpayer's employment with the employer. The payment was found to be in consequence of the taxpayer's termination. Justice Goldberg said:

I do not consider that the issue can simply be determined by seeking to identify the 'occasion' for the payment. The thrust of the judgments in *Reseck* and *McIntosh* is rather to the effect that payment is made 'in consequence' of a particular circumstance when the payment follows on from, and is an effect or result, in a causal sense, of the circumstance. ... there need not be identified only one circumstance which gives rise to a payment before it can be said that the payment is made 'in consequence' of that circumstance. ... it can be said that a payment may be made in consequence of a number of circumstances and that, for present purposes, it is not necessary that the termination of the employment be the dominant cause of the payment so long as the payment follows in the causal sense referred to in those judgments, as an effect or result of the termination.

43. In paragraphs 5 and 6 of TR 2003/13 Income tax: eligible termination payments (ETP): payments made in consequence of the termination of any employment: meaning of the phrase 'in consequence of', the Commissioner, after considering the judgments referred to in paragraphs 38 to 42 of this Ruling, stated:

... 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. In other words, but for the termination of employment, the payment would not have been made to the taxpayer. The phrase requires 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.

44. In the present case, notwithstanding that the transfer payment is payable only to those affected Country Energy employees who take up employment with the purchaser of Gas Networks, the transfer payment is payable only on the condition that employees have terminated their employment with Country Energy. The payment follows as an effect or result of the termination and the payment would not have been made to the employees but for the termination of their employment with Country Energy.

45. The following aspects of the arrangement reinforce the characterisation of the transfer payment as an employment termination payment (as distinct from, for example, a transfer or sign-on fee):

- the payment will be made by Country Energy;

- the payment is calculated by reference to each employee's years of service with Country Energy; and
- there are no obligations imposed on the employees to continue their employment with the purchaser of Gas Networks for any particular period after commencement of the employment with the purchaser.

46. Further, the transfer payment will be paid at the earliest possible time after completion of the sale of Gas Networks and be received within 12 months of the termination of employment. The timing of the payments further strengthens the connection between the transfer payments and the termination of employment.

47. The transfer payment is only payable on the condition that employees have terminated their employment with Country Energy. No entitlement to the payment arises prior to this event. Although the transfer payment is payable to those who take up employment with the purchaser of Gas Networks, it more directly relates to the termination of employment with Country Energy.

48. In view of the above, the transfer payment is in consequence of the termination of employment. Unless the employee is covered by a determination⁷ exempting them from the 12 month rule, the payment must be received within 12 months of the employee's termination of employment to qualify as an employment termination payment under section 82-130.

⁷ See subsection 82-130(4).

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:

IT 2152; TR 2003/13;
TR 2006/10

Subject references:

- eligible termination payments
- employment termination
- superannuation business line
- superannuation retirement & employment termination

Legislative references:

- ITAA 1997
- ITAA 1997 82-130
- ITAA 1997 82-130(1)
- ITAA 1997 82-130(4)
- ITAA 1997 82-135
- ITAA 1997 995-1
- TAA 1953
- Copyright Act 1968

Case references:

- Taxation Case K76 (1978) 23 CTBR (NS) 24; 78 ATC 703

- Taxation Case Q118 (1983) 27 CTBR (NS) 312 ; 83 ATC 610
- Le Grand v. Commissioner of Taxation [2002] FCA 1258; (2002) 124 FCR 53; 2002 ATC 4907; (2002) 51 ATR 139
- McIntosh v. Federal Commissioner of Taxation (1979) 45 FLR 279; 79 ATC 4325; (1979) 10 ATR 13
- Paklan Pty Ltd (in liq) v Federal Commissioner of Taxation (1983) 67 FLR 328; 83 ATC 4456; (1983) 14 ATR 457
- Reseck v. Federal Commissioner of Taxation (1975) 133 CLR 45; 75 ATC 4213; (1975) 5 ATR 538

Other references:

- Country Energy Enterprise Agreement 2009 (NSW)
- Country Energy Managers and Specialist Agreement 2009 (NSW)

ATO references

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