

CR 2013/56 - Income tax: treatment of transfer payments to employees of NSW Roads & Maritime Services following the outsourcing of road maintenance operations to a private operator

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Class Ruling

Income tax: treatment of transfer payments to employees of NSW Roads & Maritime Services following the outsourcing of road maintenance operations to a private operator

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ⓘ 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

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 which this scheme applies are all relevant New South Wales Roads and Maritime Services (RMS) maintenance employees who:

- cease employment with RMS;

- accept an offer to take up new employment with the successful tenderer(s); and
- receive a 'transfer payment' from RMS described in paragraphs 8 to 26 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 8 to 26 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.

Date of effect

7. This Ruling applies from the issue date of this ruling to 30 June 2015. This Ruling continues to apply after 30 June 2015 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

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

9. The New South Wales (NSW) State Government on behalf of NSW Roads and Maritime Services (RMS) is seeking advice on whether a proposed transfer payment to be made to employees of RMS, pursuant to the outsourcing of the road maintenance operations would constitute an employment termination payment.

10. The scheme is to be known as 'Income tax: treatment of transfer payments to employees of NSW Roads & Maritime Services following the outsourcing of road maintenance operations to a private operator'.

11. The NSW Government spends around \$900 million each year on maintenance of RMS managed roads across the State.

12. Road maintenance is undertaken successfully by the private sector in many jurisdictions nationally and internationally.

13. The purpose of RMS following such examples and outsourcing road maintenance operations is to separate the task of road maintenance from the other services provided by RMS with the aim of delivering better services at a lower cost and with greater innovation.

14. The strategy is based on a recommendation from the NSW Commission of Audit to implement a competitive tender scheme for road maintenance in the Sydney area. The aim is to achieve a road maintenance solution, which provides value for money and optimum service, by involving the private sector in the delivery of maintenance, and setting clear performance outcomes.

15. Under the proposed outsourcing of road maintenance and construction, the NSW Government intends to tender and award several new Stewardship Maintenance Contracts in the Sydney area. This will have the effect of outsourcing the maintenance operations currently provided internally by RMS to private sector organisation(s).

16. RMS's objectives for this outsourcing are:

- increase contestability of road maintenance services in the Sydney Region;
- improve customer, network and asset outcomes;
- improve total asset management decision making; and
- reduce the total cost of managing and maintaining assets.

17. RMS's objective for the proposed tendering process is to identify Service Providers(s) with the capability to meet the objectives outlined above and to provide the services across the contested zones in a safe, efficient, reliable and cost-effective manner.

18. The transfer of all road maintenance and improvement works is to be structured through a tendering process with new contracts to be awarded for the Sydney West and Sydney South Zones respectively. Part of the works in the Sydney North zone are currently undertaken by the private sector. This new procurement process will also include the balance of the works in the Sydney North Zone

19. Request for proposals for Sydney West and Sydney South Zones will be sought from the shortlisted tenders. Contracts will then be executed with the private sector organisations that are selected as the preferred providers to undertake the works.

20. The successful tenderer(s) will employ a number of wages and salaried staff from the teams within RMS that currently perform this work. These staff will terminate their employment with RMS and become employees of the new private sector providers on new contract of employment.

21. RMS currently employs approximately 1,100 road maintenance staff in Sydney, of which approximately 702 (affected employees) are in positions that will become excess to RMS's needs as result of the contract for outsourcing of road maintenance operations. Under the arrangements, the Service Provider(s) will be required to offer employment to all affected wage employees. The Service Provider(s) may offer employment to affected salaried staff at their discretion.

22. Any permanent (full or part-time) employee with more than one year's service with RMS, whose position becomes excess as a result of an outsourcing contract as described in this Ruling, and who terminates their employment with RMS and accepts an offer to take up employment with the Service Provider(s) will receive a transfer payment. This payment will be made concurrently with the final payment they receive at the conclusion of their employment with RMS.

23. It is intended that the terms of transfer for staff who choose to transfer to the successful tenderer(s) will include:

- continuation of employment guaranteed for 2 years;
- continuation of existing superannuation arrangements;
- accrued annual leave and long service leave entitlements (except to the extent employees are able to and elect to cash out leave entitlements) and accrued sick leave entitlements will be recognised by the successful tenderer(s); and
- a transfer payment based on the employee's length of service.

24. The 'transfer payment' reflects compensation for certain public sector employment conditions that will be lost following cessation of employment with RMS such as:

- voluntary redundancy provisions;
- access to redeployment provisions, professional career transition support with external providers and priority assignment of eligibility for vacancies within the public sector;
- paid maternity leave provision;
- sick leave provision;
- extended leave (long service leave) provisions;
- broader range of paid leave and leave without pay provisions;
- 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 NSW Industrial Relations Commission to dispute promotions and disciplinary action.
25. The transfer payment will be made by RMS.
26. The 'transfer payment' will be calculated by reference to each employee's years of service as set out in the table below:

Length of service	Transfer payment Week's ordinary time base rate of pay
Less than one year	0
1 year or more, but less than 2 years	7.5
2 years and more but less than 3 years	13.125
3 years and more but less than 4 years	18.75
4 years and more but less than 5 years	22.5
5 years and more but less than 6 years	26.25
6 years or more	30

Ruling

27. The proposed transfer payment made in accordance with the scheme described in paragraphs 8 to 26 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

31 July 2013

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

28. A payment made to an employee is an employment termination payment if the payment satisfies all the requirements in section 82-130 of the *Income Tax Assessment Act 1997* (ITAA 1997), and is not specifically excluded under section 82-135 of the ITAA 1997.

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

30. 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.

31. 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.

32. The proposed transfer payment is not a payment mentioned in section 82-135 of the ITAA 1997.

33. For a transfer payment to constitute an employment termination payment, all the conditions in subsection 82-130(1) of the ITAA 1997 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.

34. To qualify as an employment termination payment subsection 82-130(1) of the ITAA 1997 requires the payment must be received by the person within 12 months of termination. Any termination payments received outside of the 12 months will be assessable at the person's marginal tax rates (section 83-295), unless the person is covered by a determination exempting them from the 12 month rule (subsection 82-130(4)).

Is there a termination of employment?

35. Paragraph 9 of 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...

36. Furthermore, paragraph 2 of Taxation Determination TD 93/140 *Income tax: if a company ceases carrying on a business which has been transferred to an associated entity, will a payment made by that company to a former employee be an eligible termination payment as defined in subsection 27A(1) of the Income Tax Assessment Act 1936?* confirms the view expressed in IT 2152 that employees of an entity ceasing business have had their employment terminated.

37. The facts in *Paklan Pty Ltd and others v. Federal Commissioner of Taxation (Cth)*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.

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

- 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.

38. 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 to 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.

39. The facts in *Case Q118*² were 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.

40. *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.

41. The relevant facts in respect of RMS indicate that employees who take up positions with the successful tenderer(s) will cease employment with RMS. Therefore, there is a termination of employment for the purposes of subsection 82-130(1) of the ITAA 1997.

Is the making of the transfer payment 'in consequence of the termination of employment'?

42. 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.

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

44. The decision in *Reseck* was considered by the Full Federal Court in *McIntosh v. Federal Commissioner of Taxation*⁵ (*McIntosh*).

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

³ (1978) 78 ATC 703; (1978) 23 CTBR (NS) 24

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

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.

45. 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*).

46. *Le Grand* involved a payment by 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.

47. The Commissioner of Taxation has issued Taxation Ruling TR2003/13 Income tax: *eligible termination payments (ETP): payments made in consequence of the termination of any employment: meaning of the phrase 'in consequence of'*.

⁵ (1979) 45 FLR 279; (1979) 79 ATC 4325; (1979) 10 ATR 13; (1979) 25 ALR 557

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

48. In paragraphs 5 and 6 of TR 2003/13, the Commissioner, after considering the judgments referred to in paragraphs 42 to 47 of this Ruling, states:

... 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.

49. In the present case, whilst the transfer payment is payable only to the relevant transferring employees who take up employment with the successful tenderer(s), the transfer payment is payable only on the condition that the employees have terminated their employment with RMS. 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 RMS.

50. 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 RMS;
- the payment is calculated by reference to each transferring employee's years of service with RMS; and
- there are no obligations imposed on the relevant transferring employees to continue their employment with the successful tenderer(s) for any particular period after commencement of the employment.

51. The transfer payment is only payable on the condition that employees have terminated their employment with RMS. Although the transfer payment is payable to those who take up employment with the successful tenderer(s), it more directly relates to the termination of employment with RMS.

52. In view of the above, the transfer payment is in consequence of the termination of employment and is therefore an employment termination payment under section 82-130 of the ITAA 1997. 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

53. 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; TR 93/140

Subject references:

- employment termination
- eligible termination payments
- superannuation business line
- superannuation retirement & employment termination
- Sydney CBD ATO

Legislative references:

- Copyright Act 1968
- ITAA 1997
- ITAA 1997 82-130
- ITAA 1997 82-130(1)
- ITAA 1997 82-130(4)
- ITAA 1997 82-135
- ITAA 1997 83-295
- ITAA 1997 995-1
- TAA 1953

Case references:

- Case K76 (1978) 78 ATC 703; (1978) 23 CTBR (NS) 24
- Case Q118 (1983) 83 ATC 610; (1983) 27 CTBR (NS) 312
- Le Grand v. Federal Commissioner of Taxation [2002] FCA 1258; (2002) 124 FCR 53; (2002) 2002 ATC 4907; (2002) 51 ATR 139
- McIntosh v. Federal Commissioner of Taxation (1979) 45 FLR 279; (1979) 79 ATC 4325; (1979) 10 ATR 13; (1979) 25 ALR 557
- Paklan Pty Ltd and others v. Federal Commissioner of Taxation (1983) 14 ATR 457; (1983) 67 FLR 238; (1983) 83 ATC 4456
- Reseck v. Federal Commissioner of Taxation (1975) 133 CLR 45; (1975) 75 ATC 4213; (1975) 5 ATR 538

ATO references

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