


# ***CR 2014/44 - Income tax: treatment of transfer payments made to employees of Newcastle Port Corporation***

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## Class Ruling

# Income tax: treatment of transfer payments made to employees of Newcastle Port Corporation

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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(s) identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

### Relevant provisions

2. The relevant provisions dealt with in this Ruling is:

- section 82-130 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 82-135 of the ITAA 1997; and
- section 995-1 of the ITAA 1997.

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

## Class of entities

3. The class of employees to whom this scheme applies is all employees of Newcastle Port Corporation (NPC), who, at the time of sale of the Special Purpose Vehicle entity (the SPV) to the new purchasers:

- were allocated to perform the work for the SPV
- cease employment with NPC
- accept an offer to take up employment with the new purchaser of SPV, and
- receive a transfer payment from NPC under the scheme described in paragraph 15 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 9 to 22 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

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7. This Ruling applies from 21 May 2014 to 30 June 2015. The 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

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

9. Newcastle Port Corporation (NPC) currently owns and manages Port of Newcastle including the land on which Port of Newcastle is situated, the assets and employees currently working in Port of Newcastle.

10. New South Wales (NSW) Treasury intends to transact the businesses of Port of Newcastle to the private sector. The transaction is intended to be effected by way of a 98-year lease of Port of Newcastle.

11. In order to effect the transaction, NPC will create a new Special Purpose Vehicle entity called the Trustee for the Port of Newcastle Unit Trust (referred to as the SPV). Assets of businesses to be sold will be transferred into the SPV. Third party purchasers will then purchase 100% of the units in the SPV on 30 May 2014 (the Transaction Date).

12. NPC employees who are required to run the businesses being sold will remain as employees of NPC and be allocated to perform work for the SPV, knowing that it is NPC's intention to sell the SPV to the new owners.

13. The new owners have been identified. Consequently, NPC employees who were allocated to perform work for the SPV will be given, prior to the Transaction Date, the choice of:

- (a) continuing employment with NPC; or
- (b) upon transaction completion, terminating employment with NPC and commencing employment with the new purchasers of the SPV.

14. No employees will be forced to terminate their employment with NPC.

15. Payments will be made to employees whose employment with NPC is terminated and following the sale of the SPV, commence new employment with the new purchasers. These payments are hereafter referred to as transfer payments. The amount received by the terminating employee will depend on their years of service with NPC as follows:

<b>Continuous Length of Service</b>	<b>Transfer Payment Weeks of Pay</b>
One year or more but less than two years	7.5
Two years or more but less than three years	13.125
Three years or more but less than four years	18.75
Four years or more but less than five years	22.5
Five years or more but less than six years	26.25
Six years or more	30

16. The transfer payment to be made to the transferring employee will be made by NPC.

17. Upon commencing employment with the new purchasers of the SPV, any accrued entitlements of an employee (such as accrued annual leave and long service leave) will be recognised by the new purchasers, to the extent they were not cashed out when the employee terminated their employment with NPC.

18. Voluntary redundancies are not intended to be offered to employees terminating under the above arrangements.

19. The new purchasers are to ensure that no employee who was allocated to perform work for the SPV, under the above arrangement, will be made forcibly redundant within an agreed two year period after commencing employment with the new purchasers.

20. The names of the prospective buyers have been advised.

21. Employees who remain in employment with NPC and later take up employment with the new purchasers outside of the sale transaction will not be entitled to receive the transfer payment.

22. The transfer payment will be paid at the earliest possible time after the Transaction Date and be received within 12 months of the termination of employment.

## Ruling

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23. The proposed transfer payments made in accordance with the Scheme are made 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.

## 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

24. A payment made to an employee is an employment termination payment if the payment satisfies all the requirements in section 82-130 and is not specifically excluded under section 82-135.

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

26. 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 persons 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.

27. 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;
- the tax free part of a genuine redundancy payment or an early retirement scheme payment.

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

29. Even where all the conditions in subsection 82-130(1) have been satisfied, generally, to qualify as an employment termination payment, the payment must be received by the person within 12 months of termination.<sup>1</sup> Generally any termination payments received outside of the 12 months will be assessable at the person's marginal tax rates,<sup>2</sup> unless the person is covered by a determination exempting them from the 12 month rule.<sup>3</sup>

<sup>1</sup> paragraph 82-130(1)(b)

<sup>2</sup> section 83-295

<sup>3</sup> subsection 82-130(4)

## Is there a termination of employment?

30. 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...

31. Furthermore, at 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.

32. The facts in *Paklan Pty Ltd and others v. Federal Commissioner of Taxation*<sup>4</sup> (*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 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; and
- 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.

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<sup>4</sup> (1983) 67 FLR 328; (1983) 83 ATC 4456; (1983) 14 ATR 457

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 to the termination. However, the Full Federal Court did not dispute the fact employment had terminated when the old company had ceased business on 1 July 1977.

34. The facts dealt with by the Board of Review in *Case Q118*<sup>5</sup> 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.

35. The Board of Review decision *Case K76*,<sup>6</sup> 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.

36. The relevant facts in respect of the sale of the SPV indicate that employees of NPC affected by the sale will be able to elect whether to remain employed with NPC or to transfer to the new purchasers on completion of the sale.

37. Employees who take up positions with the new purchasers of the SPV will cease employment with NPC. Therefore, there is a termination of their employment for the purposes of subsection 82-130(1).

### **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*<sup>7</sup> (*Reseck*) Justice Gibbs of the High Court 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'.

<sup>5</sup> (1983) 83 ATC 610; (1983) 27 CTBR (NS) 312

<sup>6</sup> (1978) 78 ATC 703; (1978) 23 CTBR(NS) 24

<sup>7</sup> (1975) 75 ATC 4213; (1975) 133 CLR 45; (1975) 49 ALJR 370; (1975) 6 ALR 642; (1975) 5 ATR 538; [1975] HCA 38



40. The decision in *Reseck* was considered by the Full Federal Court in *McIntosh v. Federal Commissioner of Taxation*<sup>8</sup> (*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. Commissioner of Taxation*<sup>9</sup> (*Le Grand*).

42. *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.

43. The Commissioner of Taxation issued Taxation Ruling 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'*. In paragraphs 5 and 6 of TR 2003/13, the Commissioner stated:

5. ... 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.

<sup>8</sup> (1979) 79 ATC 4325; (1979) 25 ALR 557; (1979) 45 FLR 279; (1979) 10 ATR 13

<sup>9</sup> (2002) 195 ALR 194; (2002) 2002 ATC 4907; (2002) 51 ATR 139; (2002) 124 FCR 53; [2002] FCA 1258

6. 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 NPC employees who were allocated to perform work for the SPV and accepted employment with the new purchasers of the SPV, the transfer payment is payable only on the condition that employees have terminated their employment with NPC. 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 NPC.

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 is made by NPC
- the payment is calculated by reference to each employee's years of service with NPC, and
- there are no obligations imposed on the employees to continue their employment with the purchaser of the SPV for any particular period after commencement of the employment with the new purchaser.

46. The transfer payment will be paid by NPC at the earliest possible time after completion of the sale of the SPV to the new purchasers and be received within 12 months of the termination of employment, unless the employee is covered by a determination exempting them from the 12 month rule. 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 NPC. No entitlement to the payment arises prior to this event. Although the transfer payment is payable to those who take up employment with the new purchasers of the SPV, it more directly relates to the termination of employment with NPC.

48. In view of the above, the transfer payment 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.

## **Appendix 2 – Detailed contents list**

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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 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 83-295
- ITAA 1997 995-1
- TAA 1953
- Copyright Act 1968
- Fair Work Act 2009

### *Case references:*

- Case K76 78 ATC 703; (1978) 23 CTBR(NS) 24
- Case Q118 83 ATC 610; (1983) 27 CTBR (NS) 312
- Le Grand v. Commissioner of Taxation (2002) 124 FCR 53; [2002] FCA 1258; 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 and others v. Federal Commissioner of Taxation (1983) 67 FLR 328; 83 ATC 4456; (1983) 14 ATR 457
- Reseck v. Federal Commissioner of Taxation [1975] HCA 38; (1975) 133 CLR 45; 75 ATC 4213; (1975) 5 ATR 538

### ATO references

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