


CR 2016/24 - Income tax: Essential Energy Transformation Early Retirement Scheme

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Class Ruling

Income tax: Essential Energy Transformation Early Retirement Scheme

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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 provisions 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 in 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 whom this scheme applies is those employees of Essential Energy who receive a payment under paragraph 12, subject to paragraph 14, of this Ruling.

Qualifications

4. The Commissioner makes this Ruling based on the precise scheme identified in this Ruling. The class of entities defined in the Ruling may rely on its contents provided the scheme actually carried out is carried out in accordance with the scheme described under the heading *Scheme*.

5. If the scheme actually carried out is materially different from the scheme that is described in this Ruling, then:

- the Ruling has no binding effect on the Commissioner because the scheme entered into is not the scheme on which the Commissioner has ruled, and
- the Ruling may be withdrawn or modified.

Date of effect

6. This Ruling applies from 4 May 2016 to 31 December 2017. The Ruling continues to apply after 31 December 2017 to all entities within the specified class who entered into the specified scheme during the term of the Ruling. However, the 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 the Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Scheme

7. The scheme will be titled the '**Essential Energy Transformation Early Retirement Scheme**', hereafter referred to as the Scheme.

8. Essential Energy is a New South Wales (NSW) state-owned corporation, responsible for building, operating and maintaining Australia's largest electricity network, delivering essential services to more than 800,000 homes and businesses across 95% of NSW and parts of southern Queensland and northern Victoria.

9. The Australian Energy Regulator (AER) in its 2014-19 final determination dated 30 April 2015 has reduced Essential Energy's revenue by 25%, operating expenditure by 30% and capital expenditure by 7%. This, together with the development of disruptive technologies, such as battery storage and changes in consumer usage patterns, means that Essential Energy must undergo major re-organisation in order to deliver efficiency and productivity requirements from the AER determination as well as addressing market pressures.

10. As a result of the above developments, Essential Energy has approximately 1,395 unfunded positions costing \$15 million per month.

11. Accordingly, Essential Energy has initiated a *Transformational Program* to change its business model. A key component of this program is to rationalise and re-organise the business so that a range of functions in the organisation can be efficiently and effectively performed using streamlined practices requiring fewer employees.

12. The class of employees to whom the Scheme applies is all full-time and part time employees covered by the *Essential Energy Enterprise Agreement 2013* (or its successor), and employees employed under the Essential Energy individual employment agreements/contracts of employment who occupy a position that is to be backfilled by a 'reform-affected employee'.

13. A 'reform-affected employee' is an employee who occupies or has occupied a position that is determined to be no longer required by Essential Energy, or whose position can be backfilled by a 'reform-affected employee' (as defined in this paragraph).

14. The following employees are specifically excluded from participating in the Scheme:

- casual employees
- employees on short-term fixed contracts, and
- employees who have participated in either the Graduates', Apprentices', Trainee Engineering Officers', or Cadets' Development Programs since 1 January 2012.

15. The Scheme will operate on staggered timeframe basis as follows:

- Eligible employees will be invited to express an interest in participating in the Scheme.
- Eligible employees who express interest will be provided with an indicative payout figure.
- Eligible employees who submit an expression of interest will be notified of the outcome.
- All eligible employees who accept the offer to retire under the Scheme will terminate their employment within the duration of the Scheme. However, the actual date of termination will be negotiated with each individual employee based on operational requirements but will be no later than 31 December 2017.

16. All eligible employees who retire under the Scheme will receive a separation payment of:

- four weeks' notice payment (five if over 45 years of age)
- eight weeks' early acceptance payment, plus
- two weeks' payment for each completed year of service.

The total separation payment is not to exceed 52 weeks, inclusive of Payment in Lieu of Notice and any Early Acceptance Payment.

17. Part-time employees will receive a pro-rated separation payment based on the above.
18. All eligible employees who accept the offer to retire under the Scheme will terminate their employment no later than 12 months after an offer to retire under the Scheme and prior to 31 December 2017.
19. In addition, all employees terminated under the Scheme will receive their statutory entitlements, however they will not form part of the payment made under the Scheme.
20. Participation in the Scheme is entirely voluntary.
21. Essential Energy reserves the right to refrain from allowing an employee, or up to 40% of safety-critical employees, whichever of the two numbers is higher, from each of its organisational units to retire under the Scheme.
22. 'Safety-critical work force categories' are those work force categories with field-based staff, and those work force categories involved in setting and/or monitoring safety compliance requirements.
23. The payment made under the Scheme is in excess of any superannuation and any other benefits to which eligible employees would otherwise be entitled.
24. Any employee who terminates their employment other than under the proposed Scheme, will not be entitled to receive the Scheme payment.
25. The retirement of employees who receive a payment under the Scheme will occur before they turn 65 years of age.
26. Payments made to eligible employees who are 65 years or older will not be eligible for the tax-free base limits under the Scheme.
27. Payments made under the Scheme will be at arm's length.
28. There is no agreement in place between any eligible employee and Essential Energy, or between Essential Energy and another person to employ the eligible employee after retirement under the Scheme.

Ruling

29. The *Essential Energy Transformation Early Retirement Scheme* is an early retirement scheme for the purposes of section 83-180.

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

31. 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

4 May 2016

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.*

32. A scheme will be an early retirement scheme if it satisfies the requirements of subsection 83-180(3) or (4).

33. 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 are now considered.

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

34. 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).

35. The class of employees to whom early retirement will be offered under the Scheme is set out in paragraph 12, subject to paragraph 14 of this Ruling.

36. 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

37. 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).

38. The nature of the rationalisation or re-organisation of the employer's operations are described above under the heading *Scheme*. In approving the Scheme, the Commissioner has had regard to the changes in the operations and nature of the work force 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).

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

39. The Scheme is proposed to operate for a period from 4 May 2016 to 31 December 2017. The approval to be provided by the class ruling will have been granted prior to implementation therefore, for the purposes of paragraph 83-180(3)(c), this condition is satisfied.

40. The Scheme will be in operation for approximately 21 months. This is considered appropriate due to the circumstances of the re-organisation.

41. As all the conditions for approval under subsection 83-180(3) have been met, consideration of subsection 83-180(4) is not required.

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 their 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 83-180(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 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, and
- 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. 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 2015-16 income year, the tax-free amount is limited to \$9,780 (base amount) plus \$4,891 (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.

47. For the 2016-17 income year, the base amount is \$9,936 and the service amount is 4,969.

48. The total of the amount received on the termination of employment calculated in accordance with paragraph 16 of this Ruling may qualify as an early retirement scheme payment.

49. The total payment calculated in accordance with paragraph 16 of this Ruling will be measured against the limit in accordance with the formula mentioned in paragraph 46 and paragraph 47 of this Ruling to determine the tax-free amount of the early retirement scheme payment.

50. The tax-free amount will:

- not be an employment termination payment (ETP), and
- not be able to be rolled-over into a superannuation fund.

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

52. The taxable component of the ETP will be taxed at various rates depending on the person's age.

53. It should be noted the 'whole of income' cap does not apply to any part of the early retirement scheme payment.

Appendix 2 – Detailed contents list

54. 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:

TR 2006/10

Legislative references:

- 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
 - ITAA 1997 82-135
 - ITAA 1997 82-135(e)
 - ITAA 1997 83-170
 - ITAA 1997 83-180
 - ITAA 1997 960-285
 - ITAA 1997 995-1(1)
 - TAA 1953
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ATO references

NO: 1-7GW0XK6

ISSN: 2205-5517

ATOlaw topic: Income tax ~~ Assessable income ~~ Employment related
~~ Employment termination payment – early retirement
scheme

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