

IT 2255 - Income tax : assessment of eligible termination payments - certain payments where no entitlement to long service leave exists

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TAXATION RULING NO. IT 2255

INCOME TAX : ASSESSMENT OF ELIGIBLE TERMINATION
PAYMENTS - CERTAIN PAYMENTS WHERE NO ENTITLEMENT TO
LONG SERVICE LEAVE EXISTS.

F.O.I. EMBARGO: May be released

REF H.O. REF: 85/2803-9 DATE OF EFFECT: Immediate

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F.O.I. INDEX DETAIL

REFERENCE NO:	SUBJECT REFS:	LEGISLAT. REFS:
I 1205932	ELIGIBLE TERMINATION PAYMENTS PAYMENTS IN LIEU OF LONG SERVICE LEAVE	26AD 27A

OTHER RULINGS ON TOPIC: IT 2157, IT 2168, IT 2256

PREAMBLE

Advice has been sought as to whether certain employment termination payments constitute eligible termination payments for the purposes of Subdivision AA of Division 2 of Part III of the Income Tax Assessment Act (the Act). The payments in question are those made under early retiring or redundancy arrangements to employees who are not eligible for long service leave, or a pro rata long service payment under a State or Territory law or award. If the payments are eligible termination payments, a secondary question arises as to whether the payments qualify for concessional taxing treatment as approved early retirement scheme or bona fide redundancy payments.

FACTS

2. The enquiry concerned early retirement and redundancy payments made to employees in South Australia. Under the relevant South Australian legislation, employees generally become entitled to long service leave after completing ten years continuous employment with an employer. A pro-rata payment based on future long service leave entitlements is available to an employee who terminates employment after having completed seven years employment. Other States have similar legislation in force. In some cases, amounts may also be payable under certain industrial awards in respect of pro-rata long service leave entitlements not covered by the relevant State or Territory legislation.

3. In the cases in question, employees not entitled to long service leave - or, under the State legislation or an award, to an amount in respect of pro-rata long service leave entitlements - were paid amounts calculated as if pro-rata entitlements existed. The employer was not under any obligation to make such payments, other than as part of the agreement for the termination of the employees' services.

RULING

4. The term "eligible termination payment" (as defined in sub-section 27A(1) of the Act) includes any payment made in consequence of the termination of any employment of a taxpayer other than certain specified payments. Payments to which section 26AD of the Act applies - i.e., payments in lieu of long service leave entitlements - are specifically excluded from the definition of "eligible termination payment".

5. Section 26AD includes in assessable income any lump sum termination payment made to a taxpayer in lieu of long service leave to which the taxpayer is entitled under a law of the Commonwealth, a State or Territory, an award, etc. By sub-section 26AD(6), the scope of the section extends to a pro-rata payment to which a taxpayer has a similar entitlement. That sub-section, however, envisages that there is some formal arrangement for the making of the payment and a gratuitous payment to a terminating employee, calculated on a basis similar to that for ordinary long service leave entitlements, is not a payment to which section 26AD applies. That is the case whether the payment is a payment to an employee who has not qualified for any long service leave entitlement or is an additional payment calculated by reference to the employee's ordinary long service leave entitlements.

6. Such a gratuitous termination payment, not being a payment to which section 26AD applies, is an eligible termination payment which falls for assessment in terms of Subdivision AA. Where such a payment is an approved early retirement scheme payment, a bona fide redundancy payment or includes an invalidity payment, it will, subject to the other tests of section 27E, 27F or 27G of the Act being met, qualify for concessional taxing treatment.

COMMISSIONER OF TAXATION
27 February 1986

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