IT 41 - Payment received as compensation for termination of service agreement

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RELEASE PAYMENTS
INCOME EARNING STRUCTURE
SERVICE AGREEMENT
COMPENSATION

Legislat. Refs:
25(1)

Case Refs:
Case L60 79 ATC 480

TITLE: PAYMENT RECEIVED AS COMPENSATION FOR TERMINATION OF SERVICE AGREEMENT

FACTS
The question of whether a payment received in two instalments as compensation for termination of a service agreement was assessable or receipts of a capital nature, was referred to the Board of Review.

2. Board of Review No. 2, in a decision reported at 23 CTBR(NS) Case 67: 79 ATC case L60, has concluded that an amount of $17,000 paid to the taxpayer in two instalments in consideration for his releasing a company from its obligations to pay an annual retainer under a service agreement was a receipt of a capital nature.

3. The circumstances were that in late 1969 the taxpayer together with his family company commenced to design machinery for use in exploration and sapphire mining under contract to a second company. A deed formalising the contract was executed on 1 July 1970. Under the terms of the deed the taxpayer was to receive a retainer of $7,500 per annum for a period of five years with an option for a further five years. The services to be rendered to the second company included the design, manufacture, and maintenance of the abovementioned machinery.

4. The Board accepted on the evidence that the designing of mining machinery constituted an entirely new business activity for the taxpayer. It was envisaged that the association between the taxpayer and the second company could continue "for perhaps another 20 years".

5. In May 1971 following a change in controlling interests in the second company the company decided to terminate the services of the taxpayer and his company. Under a tripartite deed of released dated 28 April 1972 between the taxpayer, his family company and the second company, the latter company agreed to pay $17,000 to the taxpayer in two equal instalments in settlement of his claims under the earlier deed. The Board found that this termination of the agreement destroyed the existing income earning structure of the taxpayer in relation to his status as a consulting engineer in the design and manufacture of mining equipment. Accordingly, it concluded that the amounts received were of a capital nature.

6. Reliance was placed by the Board on McLaurin v FC of T (1960-1961) 104 CLR 381 and Allsop v FC of T (1965) 113 CLR 341 but it is not at all certain that those cases, where amounts were paid in satisfaction of legal actions, are necessarily determinative of cases such as the present. The case of Heavy Minerals Pty Ltd v FC of T (1966)) 115 CLR 512 may be more in point.

RULING

7. Bearing in mind the relatively small amount involved here, the decision of the Board on the facts it found has been accepted. It should be noted that the decision is viewed as being limited to its own particular facts and should not be applied generally.

COMMISSIONER OF TAXATION
14 February 1979