CR 2006/22 - Income tax: Approved Early Retirement Scheme - Tarong Energy Corporation Limited

Class Ruling

Income tax: Approved Early Retirement Scheme – Tarong Energy Corporation Limited

Contents Para

This Ruling 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, we must apply the law to you in the way set out in the ruling (or in a way that is more favourable for you if we are satisfied that the ruling is incorrect and disadvantages you, and we are 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.

2. This Ruling approves the particular early retirement scheme and acknowledges the availability of tax concessions for entities receiving payment under the scheme. There are many conditions attached to this Ruling and readers should be careful to ensure that these conditions are met before relying on this Ruling.

Relevant taxation provision(s)

3. The relevant tax provisions dealt with in this Ruling are:

- section 27A of the *Income Tax Assessment Act 1936* (ITAA 1936);
- section 27CB of the ITAA 1936; and
- section 27E of the ITAA 1936.

Class of entities

4. The class of entities to which this Ruling applies is all employees of Tarong Energy Corporation Limited (TEC) who receive a payment under the arrangement described in paragraphs 12 to 30.

Qualifications

5. The Commissioner makes this Ruling based on the precise scheme identified in this Ruling.

6. 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 12 to 30.

7. 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.

9. A copy of this Ruling must be given to all employees eligible to participate in the approved early retirement scheme.

Date of effect

10. This Ruling applies from 5 April 2006 until it is withdrawn (see paragraph 11). However, this Ruling does not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of this Ruling. Furthermore this Ruling applies to the extent that the relevant tax laws are not amended.

Withdrawal

11. This Ruling is withdrawn and ceases to have effect after 29 November 2006. The Ruling continues to apply, in respect of the tax provisions ruled upon, to all entities within the specified class who enter into the specified scheme during the term of the Ruling. Thus, the Ruling continues to apply to those entities, even following its withdrawal, for schemes entered into prior to withdrawal of the Ruling. This is subject to there being no change in the scheme or in the entities' involvement in the scheme.

Scheme

12. The scheme that is the subject of this Ruling is described below. This description is based on the following documents. These documents, or relevant parts of them, as the case may be, form part of and are to be read with this description. The relevant documents or parts of documents incorporated into this description of the scheme are:

- correspondence from representatives of TEC; and
- records of telephone conversations with a representative of TEC.

13. TEC is seeking approval for an early retirement scheme.

14. TEC is an electricity generator operating in the National Electricity Market. TEC was formed in 1997 as a result of a restructure of the Queensland electricity industry and is fully owned by the State of Queensland. TEC has extensive coal fired, hydro and wind generation assets in Queensland and South Australia.

15. TEC's key asset is the Tarong Power Station (TPS) that commenced operations in 1984. Powerworker employees at TPS perform duties such as lubrication, hand and power tool skills, prescribed machinery operation and prescribed occupation activities. A number of Powerworker employees are employed in positions that state their role utilises prescribed machinery and prescribed occupation skills, however most workers possess only a limited number of these tickets.

16. The Production Business Unit has undertaken a review of Powerworker skill requirements at TPS and found that shortages exist in the areas of crane operation, rigging, dogging, scaffolding, cladding and lagging duties. Currently these shortages are being met via overtime performed by suitably skilled TEC employees or through the utilisation of external contract labour.

17. To cover these requirements, it is clear that Powerworker employees will need the full range of prescribed machinery and occupation skills and TPS site-specific skills to enable them to work across the broad range of work tasks required.

18. To facilitate the development of Powerworker employees to meet the range of skills, position descriptions have been developed that identify the skills and the level at which they are required to operate.

19. Training and development for current Powerworker employees will be made available. However, certain Powerworker employees who are not willing to undertake the necessary skills development may express an interest in an early retirement scheme.

20. The class of employees who will be made an offer of early retirement is all TEC employees aged 51 years and over, employed in the Powerworker role at TPS.

21. TEC will have a right of veto over applications to limit the number of employees who retire under the scheme if more employees accept the offer than required. If this veto right is required then the payment will be given to employees in the following order:

- employees with the least number of prescribed occupational certifications held;
- then employees with the least number of prescribed mechanical certifications; and
- then employees who are the eldest.

22. Employees who retire under the scheme will terminate employment and receive payment before 30 November 2006.

23. The payment to be made under the scheme is as follows:

- 3 weeks of annual salary per year of service (capped at 52 weeks); and
- 8 weeks of annual salary as an incentive to accept.

Payments made under the Scheme

24. For a payment made under the above mentioned scheme to qualify as an approved early retirement scheme payment, the conditions set out in paragraphs 25 to 30 must be met. Please note, any payment made under the scheme that does not satisfy these requirements is not covered by this Ruling.

25. The payment must be an eligible termination payment (ETP) made in relation to the employee in consequence of his or her employment being terminated under the approved early retirement scheme.

26. The payment must not be made from an eligible superannuation fund.

27. The payment must not be made in lieu of superannuation benefits.

28. The employee must terminate his or her employment before the earlier of:

- age 65; or
- the date on which his or her employment would have necessarily terminated under the terms of employment because of the taxpayer attaining a certain age or completing a certain period of service.

29. Where 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 what would have been paid to the employee had they been dealing at arm's length.

30. At the termination time, there is no agreement in force between the employee and the employer or the employer and another person, to employ the employee after the date of termination.

Ruling

31. The early retirement scheme offered by TEC is an approved early retirement scheme for the purposes of section 27E of the ITAA 1936.

32. Accordingly, so much of the ETP as exceeds the amount of an ETP that could reasonably be expected to have been made in relation to the taxpayer if the termination of employment had occurred at the termination time otherwise than in accordance with the approved early retirement scheme, is an approved early retirement scheme payment in relation to the taxpayer.

33. In addition, so much of the approved early retirement scheme payment as falls within the threshold calculated in accordance with subsection 27A(19) of the ITAA 1936 is non-assessable and is ignored in working out whether a capital gain has been made via the operation of section 27CB of the ITAA 1936.

Commissioner of Taxation
5 April 2006

Appendix 1 – Explanation

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.

34. Where a scheme satisfies the requirements of section 27E of the ITAA 1936 that scheme will be an 'approved early retirement scheme'.

35. The Commissioner has issued Taxation Ruling TR 94/12 Income tax: approved early retirement scheme and bona fide redundancy payments, which sets out guidelines on the application of section 27E.

36. Paragraph 14 of TR 94/12 states that:

> Three conditions must be satisfied for a scheme to qualify as an approved early retirement scheme. Those conditions are:
>
> (i) the scheme must be offered to all employees within a class identified by the employer (paragraph 27E(1)(a));
>
> (ii) the scheme must be entered into with a view to rationalising or re-organising the operations of the employer with an identified purpose in mind (paragraph 27E(1)(b)); and
>
> (iii) the scheme must be approved by the Commissioner prior to its implementation (paragraph 27E(1)(c)).

These three conditions are discussed below.

The scheme must be offered to all employees within a class identified by the employer

37. In order to satisfy the first condition, the scheme must be offered to all employees within one of the categories specified in subparagraphs 27E(1)(a)(i) to (v).

38. The class of employees to which the scheme is proposed to be offered is set out in paragraph 20.

39. This class of employees does not come within any of subparagraphs 27E(1)(a)(i) to (iv), therefore it must be considered under subparagraph 27E(1)(a)(v), namely, all employees of the employer who constitute a class of employees approved by the Commissioner for the purposes of this paragraph. 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 subparagraph 27E(1)(a)(v).

40. It is noted, however, that TEC retain a limited right of veto as set out in paragraph 21. The limitation of the scheme in this way is acceptable to the Commissioner.

The scheme must be entered into with a view to rationalising or re-organising the operations of the employer with an identified purpose in mind

41. The proposed scheme must be implemented by the employer with a view to rationalising or re-organising the operations of the employer by means of one or more of the objectives set out in subparagraphs 27E(1)(b)(i) to (vi).

42. Paragraphs 14 to 19 describe the nature of the rationalisation or re-organisation of operations. In approving the scheme, although the rationalisation or re-organisation of the employer's operations does not fit within one of the specific methods identified in subparagraphs 27E(1)(b)(i) to (v), the Commissioner has had regard to the changes in the operations and nature of the workforce. It is therefore considered that 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 subparagraph 27E(1)(b)(vi).

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

43. The scheme is proposed to operate for a period from 5 April 2006 to 29 November 2006. Approval was granted prior to implementation therefore the third condition is satisfied.

44. The scheme will be in operation for approximately 8 months which is within the period recommended in TR 94/12.

Other relevant information

45. Under section 27E, so much of the payment received by a taxpayer under the approved early retirement scheme, that exceeds the amount that would ordinarily have been received on voluntary resignation or retirement is an approved early retirement scheme payment.

46. It should be noted that, in order for a payment to qualify as an approved early retirement scheme payment, it must also satisfy the following requirements (as set out in subsections 27E(4) and (5)):

- the payment must be an ETP made in relation to the taxpayer in consequence of the taxpayer's employment being terminated under an approved early retirement scheme;
- the payment must not be from an eligible superannuation fund;
- the payment must not be made in lieu of superannuation benefits;

- if the taxpayer 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 what would have been paid to the taxpayer had they been dealing at arm's length;
- the date of termination was before age 65 or such earlier date on which the taxpayer's employment would necessarily have had to terminate under the terms of employment because of the taxpayer attaining a certain age or completing a certain period of service (whichever occurs first); and
- there was no agreement at the date of termination between the taxpayer and the employer, or the employer and another person to employ the taxpayer after the date of termination.

47. The term 'agreement' is defined in subsection 27A(1) as meaning 'any agreement, arrangement or understanding whether formal or informal, whether express or implied and whether or not enforceable, or intended to be enforceable by legal proceedings'.

48. An approved early retirement scheme payment made on or after 1 July 1994 that falls within the specified limit will be exempt from income tax and called the 'tax-free amount'.

49. For the year ending 30 June 2006, the tax-free amount is limited to $6,491 plus $3,246 for each whole year of completed employment service to which the approved early retirement scheme payment relates. Please note that 6 months, 8 months or even 11 months do not count as a whole year for the purposes of this calculation. The $6,491 and $3,246 limits will be indexed to rise in each subsequent year in line with increases in average weekly ordinary time earnings.

50. The total of the amount received on the termination of employment calculated in accordance with paragraph 23 qualifies as an approved early retirement scheme payment.

51. The total of the payment in the previous paragraph will be measured against the limit calculated in accordance with paragraph 49 to determine the 'tax-free amount'.

52. The tax-free amount will:

- not be an ETP;
- not be able to be rolled-over;
- not include any amount from a superannuation fund or paid in lieu of a superannuation benefit; and
- not count towards the recipient's Reasonable Benefit Limit.

53. Any payment in excess of this limit will be an ordinary ETP and split up into the pre-July 83 and post-June 83 (untaxed element) components. This ETP can be rolled-over.

Appendix 2 – Detailed contents list

54. The following is a detailed contents list for this Ruling:

References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 94/12

Subject references:

- approved early retirement scheme payments
- eligible termination payments
- eligible termination payments components

Legislative references:

- TAA 1953
- ITAA 1936 27A
- ITAA 1936 27A(1)
- ITAA 1936 27A(19)
- ITAA 1936 27CB
- ITAA 1936 27E
- ITAA 1936 27E(1)(a)
- ITAA 1936 27E(1)(a)(i)
- ITAA 1936 27E(1)(a)(ii)
- ITAA 1936 27E(1)(a)(iii)
- ITAA 1936 27E(1)(a)(iv)
- ITAA 1936 27E(1)(a)(v)
- ITAA 1936 27E(1)(b)
- ITAA 1936 27E(1)(b)(i)
- ITAA 1936 27E(1)(b)(ii)
- ITAA 1936 27E(1)(b)(iii)
- ITAA 1936 27E(1)(b)(iv)
- ITAA 1936 27E(1)(b)(v)
- ITAA 1936 27E(1)(b)(vi)
- ITAA 1936 27E(1)(c)
- ITAA 1936 27E(4)
- ITAA 1936 27E(5)
- Copyright Act 1968

ATO references

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