

# ***CR 2006/69 - Income tax: assessable income and tax offsets: payments made by Ensham Workers Entitlement Fund Pty Ltd***



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This document has changed over time. This is a consolidated version of the ruling which was published on *1 July 2006*



## Class Ruling

### Income tax: assessable income and tax offsets: payments made by Ensham Workers Entitlement Fund Pty Ltd

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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, 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

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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 provision(s)**

2. The relevant provisions dealt with in this ruling are:

- section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997);
- section 960-100 of the ITAA 1997;
- section 26AC of the *Income Tax Assessment Act 1936* (ITAA 1936);
- subsection 27A(1) of the ITAA 1936;
- subsection 27B(1) of the ITAA 1936;
- section 27D of the ITAA 1936;
- section 159S of the ITAA 1936;
- section 159SA of the ITAA 1936;

- section 12-35 of Schedule 1 to the *Taxation Administration Act 1953* (TAA);
- section 12-85 of Schedule 1 to the TAA; and
- section 12-90 of Schedule 1 to the TAA.

## Class of entities

3. The class of entities to which this Ruling applies is all employees of Ensham Resources Pty Ltd (Ensham) who receive a payment of employee entitlements from Ensham Workers Entitlement Fund Pty Ltd (the Trustee) as trustee of the Ensham Production and Engineering Employee's Leave Entitlements Trust (the Trust). In this Ruling these entities are referred to as 'employees'.

## 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 13 to 25 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.

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## Date of effect

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8. This Ruling applies from 1 July 2006. However, the 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 the Ruling. Furthermore, the Ruling only applies to the extent that:

- it is not later withdrawn by notice in the *Gazette*; or
- the relevant provisions are not amended.

9. If this Class Ruling is inconsistent with a later public or private ruling, the relevant class of entities may rely on either ruling which applies to them (item 1 of subsection 357-75(1) of Schedule 1 to the TAA).

10. If this Class Ruling is inconsistent with an earlier private ruling, the private ruling is taken not to have been made if, when the Class Ruling is made, the following two conditions are met:

- the income year or other period to which the rulings relate has not begun; and
- the scheme to which the rulings relate has not begun to be carried out.

11. If the above two conditions do not apply, the relevant class of entities may rely on either ruling which applies to them (item 3 of subsection 357-75(1) of Schedule 1 to the TAA).

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## Withdrawal

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12. This Ruling is withdrawn and ceases to have effect after 30 June 2011. However, the Ruling continues to apply after its withdrawal in respect of the relevant provisions ruled upon, to all persons within the specified class who entered into the specific scheme during the term of the Ruling, subject to there being no change in the scheme or in the person's involvement in the scheme.

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## Scheme

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13. The scheme that is the subject of this Ruling is described below. This description is based on the following documents:

- Class Ruling application from Allens Arthur Robinson dated 24 January 2006;
- Ensham Mine Employees Certified Agreement 2004 (Certified Agreement);
- Ensham Production and Engineering Employees' Leave Entitlements Trust Deed (Trust Deed); and

- emails from Allens Arthur Robinson dated 17 February 2006, 20 March 2006, 26 April 2006 and 15 June 2006.

14. Under the terms of the Certified Agreement, Ensham is required to maintain a trust fund for the benefit of employees with the purpose of guaranteeing the ongoing payment of annual leave and personal leave. The Trust was established by Ensham for this purpose.

15. The Trust was approved as a worker entitlement fund on 8 May 2006.

16. The Trust Deed for the Trust governs the conditions under which monies are held and payments made under the Trust in relation to the employee's entitlement. 'Entitlement' is defined in clause 1.1 of the Trust Deed to be the monetary value of Ensham's obligation to an employee in respect of annual leave and personal leave. Employees are entitled to personal leave instead of carers leave or sick leave.

17. Under the Trust Deed the Trustee must keep separate employee accounts for each employee (clause 4.1 of the Trust Deed).

18. Ensham's liabilities for employee entitlements increase or decrease on a monthly basis depending on the extent to which individual employees accrue or drawdown their annual and personal leave entitlements. At the end of each quarter, Ensham will determine the increase or decrease in each employee's entitlement and will advise the Trustee of such. Actual payments to the Trustee will be determined on an aggregate basis depending on the total amount of employee entitlements outstanding at the relevant point in time. The quarterly payment will be directly referable to each individual employee's increase or decrease in entitlements.

19. The Trustee will credit to the employee account the amount of the employee's initial entitlement to annual leave and personal leave, and any increase to that entitlement. The Trustee will also debit to the employee account the amount by which their entitlement has decreased since the end of the previous quarter or by any amount paid to the employee (clause 4.2 of the Trust Deed).

20. Clause 4.3 of the Trust Deed provides that:

No employee shall be entitled whether presently, contingently or otherwise to any amount standing to the credit of their Employee Account and the Employer acknowledges that the Employee Accounts are kept by the Trustee exclusively for the purpose of:

- (a) internal management of the Trust Fund;
- (b) advising Employees of the approximate value of their Entitlements from time to time;
- (c) determining the Employer's vested and indefeasible entitlements to all income earned from the Trust Fund; and
- (d) calculating the Employee's right to share in the Trust Fund upon a winding up of the Trust.

Subject to the above, this deed will confer on the Employees a mere right of action against the Trustee to require the Trustee to hold the benefit of the Trust Fund in accordance with the provisions of this deed and to account to the Employees in accordance with clause 11.

21. Payments to employees for annual leave and personal leave will normally be made directly by Ensham. There will however be direct payments made to the employee by the Trustee if they receive written notice from the employee that their entitlement is due and payable but has not been, or will not be, paid by the employer (clause 6.2 of the Trust Deed).

22. Clause 6.3 of the Trust Deed provides that each recipient of a payment from the Trustee in accordance with clause 6.2, upon receipt of that payment, has an immediate vested indefeasible interest and is presently entitled to the amount of that payment.

23. Under the Certified Agreement an employee, if they accrue more than 12 days personal leave, can elect to convert the net value of any extra credits accrued over and above the 12 day entitlement into superannuation payments.

24. If this election is made, this conversion of the excess credits occurs yearly on the anniversary of the commencement of their employment.

25. If an employee who has elected to convert extra credit to superannuation payments terminates their employment at a time when they have more than 12 days accrued, then at termination, the employee will receive a payment for the 12 days personal leave. The extra credits are paid, in cash, to the employee's superannuation fund.

## **Ruling**

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26. The employee has not derived assessable income for the purposes of section 6-5 of the ITAA 1997 until such time as they receive the payment of their annual leave or personal leave entitlement from the Trustee.

27. A payment of an annual leave entitlement by the Trustee to a continuing employee is a payment of ordinary income and is therefore assessable income of the employee under section 6-5 of the ITAA 1997.

28. A payment of an annual leave entitlement by the Trustee to an employee upon the termination of their employment is assessable income of the employee under subsection 26AC(2) of the ITAA 1936.

29. To the extent that the payment by the Trustee to an employee upon the termination of their employment is a payment of unused annual leave, and meets the requirements of section 159S of the ITAA 1936, the payment will be 'eligible assessable income' for the purposes of section 159SA of the ITAA 1936.

30. A payment of a personal leave entitlement by the Trustee to a continuing employee is a payment of ordinary income and is therefore assessable income for the purposes of section 6-5 of the ITAA 1997.

31. A payment of a personal leave entitlement by the Trustee to an employee upon termination of their employment is assessable income of the employee under subsection 27B(1) of the ITAA 1936.

32. A payment to the employee's superannuation fund, based on excess personal leave credits, for a continuing employee, is assessable income of the employee for the purposes of section 6-5 of the ITAA 1997.

33. A payment to the employee's superannuation fund, based on excess personal leave credits, on termination of employment, is assessable income of the employee under subsection 27B(1) of the ITAA 1936 to the extent that it is not rolled over for the purposes of section 27D of the ITAA 1936.

34. To the extent that payments by the Trustee to an employee and to the employee's superannuation fund, upon the termination of their employment, are payments of unused personal leave, and otherwise meet the requirements of subsection 27A(1) of the ITAA 1936 and are not rolled over for the purposes of section 27D of the ITAA 1936, the payments will be eligible assessable income for the purposes of section 159SA of the ITAA 1936.

## **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.*

35. Subsection 6-5(1) of the ITAA 1997 provides that the assessable income of a taxpayer includes income according to ordinary concepts, which is called ordinary income.

36. Income from employment is generally derived only when received.

37. The employee may accrue an entitlement to annual leave or personal leave. They are not entitled to any payment until they take the leave or terminate their employment.

38. Ensham contributes amounts to the Trust in recognition of its future obligation to provide annual leave and personal leave entitlements to its employees.

39. While the Trust holds those amounts in individual employee accounts, the employees have no present entitlement to any amounts standing to the credit of their employee account.

40. In these circumstances while the employee has an entitlement to a future payment they have not at this time derived that payment and it does not form part of their assessable income.

41. The Trustee will receive contributions from Ensham for annual leave and personal leave and may be required to make payments of entitlements direct to continuing or terminating employees.

### **Annual leave entitlements paid by the Trustee to a continuing employee**

42. A payment of annual leave to a continuing employee by the Trustee is treated in the same way as a payment of annual leave made by Ensham to a continuing employee.

43. The payment of annual leave is a payment of ordinary income to the employee and is part of their assessable income under section 6-5 of the ITAA 1997.

44. Normal payments of annual leave received by a continuing employee do not give rise to any tax concessions.

45. Section 12-35 of Schedule 1 to the TAA provides:

An entity must withhold an amount from salary, wages, commission, bonuses or allowances it pays to an individual as an employee...

46. The payment of annual leave is a payment of assessable income to the employee and as the payment is in respect of the employment of the continuing employee it is not relevant who actually makes the payment.



47. As the Trust is considered to be an entity in accordance with subsection 960-100(2) of the ITAA 1997, the Trustee of the Trust is also obliged under section 12-35 of Schedule 1 of the TAA to withhold an amount from the payment of annual leave to a continuing employee.

## **Annual leave entitlements paid by the Trustee to a terminating employee**

48. A payment of unused annual leave, by the Trustee to a terminating employee, is treated in the same way as an unused leave payment made by Ensham directly to a terminating employee.

49. Section 26AC of the ITAA 1936 deals with lump sum amounts received on retirement or termination of employment in respect of unused annual leave.

50. To be a payment of unused annual leave the lump sum payment must satisfy the factors of subsection 26AC(1) of the ITAA 1936, that the lump sum amount is:

- paid after 15th August 1978;
- paid in consequence of retirement or termination; and
- in respect to unused annual leave.

51. Under subsection 26AC(2) of the ITAA 1936:

where an amount to which this section applies is paid to the taxpayer in a year of income, that amount shall be included in the assessable income of the taxpayer of the year of income.

52. The payment of unused annual leave included in the assessable income under section 26AC of the ITAA 1936 by a terminating employee will be 'eligible assessable income' as defined in section 159S of the ITAA 1936 where:

- the termination payments are in respect of unused annual leave paid on or after 18 August 1993, where termination is due to bona fide redundancy, invalidity or under an approved early retirement scheme; or
- the termination payments in lieu of unused annual leave are in respect of service before 18 August 1993.

53. Item 9 of the table in subsection 159SA(1) of the ITAA 1936 provides for a tax offset such that the rate of tax payable on the eligible assessable income will not exceed 30%. Payments of eligible assessable income by the Trust to terminating employees will be entitled to this tax offset.

54. Section 12-90 of Schedule 1 of the TAA requires that an entity must withhold an amount from a payment it makes to an individual if the payment is included in the individual's assessable income under section 26AC of the ITAA 1936.

**Personal leave entitlements paid by the Trustee to a continuing employee**

55. A payment of personal leave to a continuing employee by the Trustee is treated the same as a payment of personal leave made by Ensham to a continuing employee.

56. The payment of personal leave is a payment of ordinary income to the employee and is part of their assessable income under section 6-5 of the ITAA 1997.

57. Payments of personal leave to a continuing employee do not give rise to any tax concessions.

58. The payment of personal leave is a payment in respect of the employment of the continuing employee and the Trustee will be required to withhold an amount under section 12-35 of Schedule 1 of the TAA.

**Personal leave entitlements paid by the Trustee to a terminating employee**

59. A payment of unused personal leave by the Trustee to a terminating employee is treated the same as an unused personal leave payment made by Ensham to a terminating employee.

60. As this payment for unused personal leave is a payment in consequence of termination, the amount is an eligible termination payment (ETP) (refer to the definition of an ETP under subsection 27A(1) of the ITAA 1936).

61. The employee receiving the ETP will be entitled to a tax offset under one or more of items 4, 5, 6 or 8 of the table in subsection 159SA(1) of the ITAA 1936, that will limit the rate of tax that is payable on the ETP.

62. Section 12-85 of Schedule 1 to the TAA requires that an entity must withhold an amount from an ETP it makes to an individual.

**Personal leave entitlements paid by the Trustee to a superannuation fund for a continuing employee**

63. As described in paragraph 23 of this Ruling an employee may elect to convert excess personal leave entitlements into superannuation payments.

64. Where this election has been made then, on a yearly basis, the excess entitlements will be paid to the employee's superannuation fund.

65. Subsection 6-5(4) of the ITAA 1997 provides that in working out whether an amount of ordinary income has been derived by a taxpayer, the taxpayer is taken to have derived that amount at the time that it is applied or dealt with in any way on their behalf or as they direct.

66. The employee has elected that their excess entitlements be converted into a payment made on their behalf to the superannuation fund. This payment has been 'applied or dealt with' on the employees behalf and as they have directed.

67. The amount of the annual payment made to the superannuation fund is therefore derived by the employee at the time this payment is made and is included in their assessable income under section 6-5 of the ITAA 1997.

**Personal leave entitlements paid by the Trustee to a superannuation fund for a terminating employee**

68. A payment of any unused excess personal leave entitlement to the employee's superannuation fund will be treated as a payment in consequence of termination. This amount will be an ETP. Unless the employee has made an election to roll-over the ETP under section 27D of the ITAA 1936, the ETP will be assessable income of the employee under subsection 27B(1) of the ITAA 1936. The employee receiving the ETP will be entitled to a tax offset under one or more of items 4,5,6 or 8 of the table in subsection 159SA(1) of the ITAA 1936, that will limit the rate of tax that is payable on the ETP.

69. Section 12-85 of Schedule 1 to the TAA requires that an entity must withhold an amount from an ETP it makes to an individual.

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

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

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## References

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*Previous draft:*

Not previously issued as a draft

*Subject references:*

- employee entitlements
- leave entitlements
- terminating employee
- unused recreation leave
- unused personal leave

*Legislative references:*

- ITAA 1936 26AC
  - ITAA 1936 26AC(1)
  - ITAA 1936 26AC(2)
  - ITAA 1936 27A(1)
  - ITAA 1936 27B(1)
  - ITAA 1936 27D
  - ITAA 1936 159S
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  - ITAA 1936 159SA(1)
  - ITAA 1997 6-5
  - ITAA 1997 6-5(1)
  - ITAA 1997 6-5(4)
  - ITAA 1997 960-100
  - ITAA 1997 960-100(2)
  - TAA 1953
  - TAA 1953 Sch 1 12-35
  - TAA 1953 Sch 1 12-85
  - TAA 1953 Sch 1 12-90
  - TAA 1953 Sch 1 357-75(1)
  - Copyright Act 1968
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ATO references

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