


CR 2009/49 - Income tax: payments made by National Entitlement Security Trust to members

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Class Ruling

Income tax: payments made by National Entitlement Security Trust to members

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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.

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What this Ruling is about

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 83-10 of the ITAA 1997;
- section 83-80 of the ITAA 1997;
- section 26AC of the *Income Tax Assessment Act 1936* (ITAA 1936);
- section 26AD of the ITAA 1936;

All legislative references in the Ruling are to the ITAA 1997 unless otherwise indicated.

Class of entities

3. The class of persons to which this Ruling applies is:
- all employee members of the National Entitlement Security Trust (NEST) (collectively referred to as 'employees') who, upon satisfying the requirements to receive employee entitlements under the relevant industrial agreement, receive a payment of employee entitlements directly from the Trustee of NEST; and
 - the legal personal representatives of deceased employees.

Qualifications

4. The Commissioner makes this Ruling based on the precise arrangement 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 10 to 17 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

8. This Ruling applies from 1 July 2006. However, this 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 this Ruling (see paragraphs 75 and 76 of Taxation Ruling TR 2006/10).

Previous Rulings

9. This Ruling replaces CR 2004/49, which was withdrawn from 30 June 2006.

Scheme

10. The following description of the scheme is based on information provided by the applicant. The following documents, or relevant parts of them, as the case may be, form part of and are to be read with the description:

- Application for Class Ruling dated 18 March 2008;
- National Entitlement Security Trust Deed dated 1 June 2002; and
- Emails from applicant dated 29 September 2008 and 11 May 2009.

Description of arrangement

11. Employers are required by their various industrial instruments to make contributions for employee entitlements to NEST. NEST will accept these contributions and hold them until they become payable under the terms of the Trust Deed (Deed).

12. 'Employee entitlements' are defined in clause 32.1 of the Deed as:

any dollar amount payable to a Member under an Industrial Agreement to which that Member has a right and which is identified as such in the Industrial Agreement including the following entitlements:

- (a) annual leave and annual leave loading;
- (b) sick leave;
- (c) long service leave;
- (d) redundancy;
- (e) severance; or
- (f) any other amount from time to time payable by an Employer to a Member accepted by the Trustee.

13. An employer is required to sign a deed of adherence to ensure that the minimum contribution rate as prescribed in each industrial instrument is paid to NEST on a monthly basis. Clause 7.1 of the Deed outlines the minimum contribution requirement:

Employee Entitlement Contributions

Each Employer must pay to the Trustee, or as directed by it, on such dates as agreed with the Trustee an amount equal to the Minimum Contribution for each Member employed or whose services are used by that Employer, in accordance with the terms of the Relevant Industrial Agreement in relation to the Employees of that Employer.

14. In accordance with clause 7.9 of the Deed, all employer contributions to NEST are credited to separate member (employee) accounts identifying the contributions for that member:

Payments and credits/Members Account

All contributions by any Employer will be allocated as directed by it and credited to personal accounts opened in the names of the Members and styled the Members' Account.

15. While Employer contributions are credited to personal accounts of the Members, clause 28.1 of the Deed provides that Members have no entitlement to payment of an amount until the conditions set out in the Deed have been satisfied.

16. The Deed governs the conditions under which monies are held and payments are made under the Trust in relation to the employee's entitlement. Payments may be made by the Trustee of NEST to the employer and/or directly to the employee, as outlined in the NEST administrative provisions:

Employers will pay a claim for Employee Entitlements in the same manner that Employers currently pay these employee entitlements. Employers will however, be entitled to reimbursement from the Trust for an amount calculated in accordance with clause 26 of the Deed.

The Fund Administrator will reimburse the Employer immediately upon receipt and completion of a signed NEST claim form available from the Fund Administrator, in accordance with clause 28. Reimbursements to Employers are paid by direct credit or by cheque. An Employer must exhaust its existing accrued Employer entitlements before claiming from the Fund.

Employees may claim directly from the Fund, in accordance with the Deed if:

- the current Employer becomes insolvent (see clause 26);
- the Employee is claiming Entitlements transported from a previous Employer (see clause 9 or clause 26); and/or
- the Employer's relevant industrial agreement specifically requires Employees to claim directly from the Fund.

Clause 27 of the Deed provides that in the event of the death of an employee, the employee's entitlements will form part of their estate and will be paid to their legal personal representative.

17. No amount of sick leave is paid to an employee on termination of their employment.

Ruling

18. A payment of employee entitlements by the trustee of NEST (Trustee) to an employee will receive the same taxation treatment, including concessional treatment, which would have been applicable had the payment been made directly by the employer to the employee.

19. A payment of annual leave entitlements by the Trustee to a continuing employee is a payment of ordinary income and is assessable income of the employee under section 6-5.

20. A payment of long service leave entitlements by the Trustee to a continuing employee is a payment of ordinary income and is assessable income of the employee under section 6-5.

21. A payment of sick leave by the Trustee to a continuing employee is a payment of ordinary income and is assessable income of the employee under section 6-5.

22. A payment of unused annual leave entitlements by the Trustee to an employee on termination of their employment is assessable income of the employee under section 26AC of the ITAA 1936 and section 83-10 of the ITAA 1997.

23. A payment of unused long service leave entitlements by the Trustee to an employee on termination of their employment is assessable income of the employee under section 26AD of the ITAA 1936 and section 83-80 of the ITAA 1997.

24. A payment of employee entitlements by the Trustee to the legal personal representative of a deceased employee will receive the same taxation treatment, including concessional treatment, which would have been applicable had the payment been made directly by the employer.

25. This Ruling does not address the following:

- the concessional tax treatment of unused annual leave, annual leave loading and long service leave payments by the Trustee to a member on the termination of their employment; and
- employee entitlements for redundancy and severance paid to a member on the termination of their employment.

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.*

26. A payment or other benefit received by a taxpayer is assessable income if it is:

- income in the ordinary sense of the word (ordinary income); or
- an amount or benefit that through the operation of the provisions of the tax law is included in assessable income (statutory income).

27. Ordinary income is not defined in the taxation legislation. It is therefore necessary to apply the principles developed by the courts to the facts of a particular case.

28. In *Scott v. Federal Commissioner of Taxation* (1966) 117 CLR 514; (1966) 10 AITR 367; (1966) 14 ATD 286 Windeyer J stated:

Whether or not a particular receipt is income depends upon its quality in the hands of the recipient.

29. In *GP International Pipecoaters Pty Ltd v. Federal Commissioner of Taxation* (1990) 170 CLR 124; 90 ATC 4413; (1990) 21 ATR 1, the Full High Court stated (at CLR 138; ATR 7; ATC 4420):

To determine whether a receipt is of an income or of a capital nature, various factors may be relevant. Sometimes the character of receipts will be revealed most clearly by their periodicity, regularity or recurrence; sometimes, by the character of a right or thing disposed of in exchange for the receipt; sometimes, by the scope of the transaction, venture or business in or by reason of which money is received and by the recipient's purpose in engaging in the transaction, venture or business.

30. A generally decisive consideration is whether the payment is the product in a real sense of any employment, services or business carried on by the recipient.¹ Ordinary income will include payments received in the capacity as an employee or otherwise in connection with employment activities.

Entitlements paid by the trustee to a continuing employee

31. In the present case, the character of the payment of an employment-related entitlement to a continuing employee is not changed by the fact that the Trustee, rather than the employer, makes the payment. The payment of such an entitlement to the employee by the Trustee attracts the same income tax treatment in the hands of the employee as if the employer had made the payment.

¹ *Squatting Investment Co Ltd v. Federal Commissioner of Taxation* (1953) 86 CLR 570 at 633.

Payment of annual leave and annual leave loading to a continuing employee

32. A payment of annual leave or annual leave loading to a continuing employee is a payment of ordinary income and is part of the employee's assessable income under section 6-5.

33. This is a payment from which an amount of tax must be withheld (refer to subsection 10-5(1) of Schedule 1 to the *Taxation Administration Act 1953* (TAA 1953)). The Trustee who makes this payment to the employee will withhold an amount of tax as required by section 12-35 of Schedule 1 to the TAA 1953.

34. Payments of annual leave and annual leave loading received by a continuing employee do not give rise to any tax concessions.

Payment of long service leave to a continuing employee

35. A payment of long service leave to a continuing employee is a payment of ordinary income and is part of the employee's assessable income under section 6-5.

36. This is a payment from which an amount of tax must be withheld (refer to subsection 10-5(1) of Schedule 1 to the TAA 1953). The Trustee who makes this payment to the employee will withhold an amount of tax as required by section 12-35 of Schedule 1 to the TAA 1953.

37. Payments of long service leave received by a continuing employee do not give rise to any tax concessions.

Payment of sick leave to a continuing employee

38. A payment of sick leave to a continuing employee is a payment of ordinary income and is part of the employee's assessable income under section 6-5.

39. This is a payment from which an amount of tax must be withheld (refer to subsection 10-5(1) of Schedule 1 to the TAA 1953). The Trustee who makes this payment to the employee will withhold an amount of tax as required by section 12-35 of Schedule 1 to the TAA 1953.

40. Payments of sick leave received by a continuing employee do not give rise to any tax concessions.

Entitlements paid by the Trustee to a terminating employee

41. In certain circumstances, an employee will claim their employee entitlements directly from NEST on the termination of their employment. Accordingly, the Trustee may make the following relevant payments to the employee on termination of their employment:

- unused annual leave and annual leave loading; and
- unused long service leave.

42. A payment of employee entitlements by the Trustee to the employee on the termination of their employment is treated in the same way as a payment by the employer to the employee.

Payment of unused annual leave or annual leave loading to a terminating employee

43. A payment for unused annual leave or annual leave loading received prior to 1 July 2007, which satisfies subsection 26AC(1) of the ITAA 1936, is assessable income of the employee in the year in which it is received under subsection 26AC(2) of the ITAA 1936.

44. A payment for unused annual leave and annual leave loading received after 30 June 2007 is assessable income of the employee in the year in which it is received under subsection 83-10(2).

45. As the payments are assessable income of the employee, these are payments from which amounts of tax must be withheld (refer to subsection 10-5(1) of Schedule 1 to the TAA 1953). The Trustee who makes these payments to the employee will withhold amounts of tax as required by section 12-90 of Schedule 1 to the TAA 1953.

Payment of unused long service leave to a terminating employee

46. A payment for unused long service leave received prior to 1 July 2007 is an unused long service leave payment if it satisfies section 26AD of the ITAA 1936. To the extent that the payment is for leave that accrued before 16 August 1978, 5% of the amount is included in the assessable income of the employee. To the extent that the payment is for leave that accrued after 15 August 1978, 100% of the amount is included in the assessable income of the employee.

47. A payment for unused long service leave received after 1 July 2007 is an unused long service leave payment if it satisfies section 83-75. Subsection 83-80(1) provides that to the extent that the payment is for leave that accrued before 16 August 1978, 5% of the amount is included in the assessable income of the employee. To the extent that the payment is for leave that accrued after 15 August 1978, 100% of the payment is included in the assessable income of the employee. This payment is assessable income of the employee in the year it is received under subsection 83-80(1).

48. The payment of unused long service leave is a payment of assessable income to the employee. Therefore, this is a payment from which an amount of tax must be withheld (refer to subsection 10-5(1) of Schedule 1 to the TAA 1953). The Trustee who makes these payments to the employee will withhold amounts of tax as required by section 12-90 of Schedule 1 to the TAA 1953.

49. This Ruling does not examine the concessional treatment of payments on termination of employment. For the purposes of any concessional treatment, the payment by the Trustee is treated in the same way as a payment by the employer to the employee

Entitlements paid by the Trustee on the death of an employee

50. On the death of an employee the Trustee may pay an employee entitlement directly to the employee's legal personal representative.

Payment of unused annual leave and unused long service leave

51. A payment of unused annual or long service leave by the Trustee to an employee's legal personal representative is treated in the same way as a payment of unused annual or long service leave made by the employer to the employee's legal personal representative.

52. Subsection 101A(2) of the ITAA 1936 ensures that if an employee dies, any amount which would have been included in the assessable income of the deceased under sections 26AC and 26AD of the ITAA 1936 or sections 83-10 and 83-80 of the ITAA 1997 had it been received during their lifetime, will not form part of the assessable income of the deceased's estate.

Special rules for death benefits

53. A death benefit termination payment or death benefit eligible termination payment paid by the Trustee is treated in the same way as a payment made by the employer.

54. Section 27AAA of the ITAA 1936 provides concessional treatment for a death benefit eligible termination payment paid prior to 1 July 2007 that is paid on the death of a person to a dependant or the legal representative of the deceased person or to any other person (including non dependants).

55. Sections 82-65, 82-70 and 82-75 provide concessional treatment for a death benefit termination payment paid after 30 June 2007 to dependants, non-dependants and the legal representative of a deceased person.

Appendix 2 – Detailed contents list

56. 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

Previous Rulings/Determinations:

CR 2004/49

Subject references:

- annual leave
- death benefits - dependants
- long service leave
- lump sum payments for unused annual leave
- lump sum payments for unused long service leave
- sick leave
- trusts

Legislative references:

- ITAA 1936 26AC
- ITAA 1936 26AC(1)
- ITAA 1936 26AC(2)
- ITAA 1936 26AD
- ITAA 1936 27AAA
- ITAA 1936 101A
- ITAA 1936 101A(2)
- ITAA 1997 6-5
- ITAA 1997 82-65

- ITAA 1997 82-70
- ITAA 1997 82-75
- ITAA 1997 83-10
- ITAA 1997 83-10(2)
- ITAA 1997 83-75
- ITAA 1997 83-80
- ITAA 1997 83-80(1)
- TAA 1953
- TAA 1953 Sch 1 10-5(1)
- TAA 1953 Sch 1 12-35
- TAA 1953 Sch 1 12-90
- Copyright Act 1968

Case references:

- GP International Pipecoaters Pty Ltd v. Federal Commissioner of Taxation [1990] HCA 25; (1990) 170 CLR 124; 90 ATC 4413; (1990) 21 ATR 1
- Scott v. Federal Commissioner of Taxation (1966) 117 CLR 514; (1966) 10 AITR 367; (1966) 14 ATD 286
- Squatting Investment Co Ltd v. Federal Commissioner of Taxation (1953) 86 CLR 570

ATO references

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