

Fringe benefits tax and income tax: employer contributions to the WA Construction Industry Redundancy (No. 2) Fund

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This Ruling provides you with the following level of protection:

This publication (excluding appendices) 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.

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 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 under-paid tax, penalty or interest in respect of the matters covered by this ruling if it turns out that it does not correctly state the relevant provision that applies to you.

What this Ruling is about

1. This Ruling sets out the Commissioner's opinion on the way in which the relevant taxation provision(s) identified below apply to the defined class of entities, who take part in the scheme to which this Ruling relates.

Relevant taxation provision(s)

2. The taxation provisions dealt with in this Ruling are:

- section 58PA of the *Fringe Benefits Tax Assessment Act 1986* (FBTAA);
- section 8-1 of the *Income Tax Assessment Act 1997* (ITAA 1997); and
- section 6-5 of the ITAA 1997.

Class of entities

3. The class of entities to which this Ruling applies is all employers who make contributions to the WA Construction Industry Redundancy (No. 2) Fund (WACIRF No. 2) for workers who are members (members) of WACIRF No. 2.

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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 10 to 20.

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- this Ruling may be withdrawn or modified.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 April 2006 until it is withdrawn. 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 (see paragraphs 21 and 22 of Taxation Ruling TR 92/20). Furthermore this Ruling applies to the extent that:

- there is no material change in the scheme or in the class of entities involved in the scheme;
- it is not later withdrawn by notice in the *Gazette*; or
- the relevant taxation provisions are not amended.

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Withdrawal

9. This Ruling is withdrawn and ceases to have effect after 31 March 2011. However, the Ruling continues to apply after its withdrawal in respect of the taxation provisions ruled upon, to all entities 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 entities' involvement in the scheme.

Scheme

10. 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 and are part of and are to be read with the description. The relevant documents or parts of documents incorporated into this description of the scheme are:

- Class Ruling application from Jackson McDonald dated 7 November 2005;
- supplementary information provided by Jackson McDonald in a letter dated 17 January 2006;
- WACIRF No. 2 Trust Deed and Regulations (Trust Deed);
- a copy of clause 16.2.7 of the National Building and Construction Industry Award (NBCIA);
- a copy of clause 51(5) of the Building Trades (Construction) Award 1987, Western Australia (BTCA); and
- a copy of clause 34.6 of the Plumbing Industry (QLD and WA) Award 1979 (PIA).

11. WACIRF No. 2 is an Australian resident trust fund governed by a trust deed, which established the fund in Australia. The central management and control of the fund is in Australia.

12. The trustee of WACIRF No. 2 is WA Construction Industry Redundancy Fund Ltd ACN 009 404 273 (the trustee), an Australian resident company.

13. WACIRF No. 2 is an approved worker entitlement fund for fringe benefits tax (FBT) purposes.

14. Employers provide redundancy entitlements for their workers pursuant to various awards and agreements (industrial instruments). Employers can fund worker redundancy entitlements that they are required to make by the payment of contributions to WACIRF No. 2.

15. WACIRF No. 2 accepts contributions from employers to fund each worker's redundancy benefit. WACIRF No. 2 and individual employers either execute an agreement called a Contribution Agreement or lodge a Contribution Return which sets out the amount to be contributed by the employer in respect of each worker calculated by reference to:

- the minimum base contribution rate;
- the minimum base contribution rate plus increments; or
- a redundancy payment rate as provided for in a nominated industrial award or industrial agreement.

16. As outlined in clause 4.2 of the Trust Deed, all contributions made to WACIRF No. 2 by employers will be placed into separate member accounts identifying contributions for that member.

17. On becoming redundant, as defined in the Trust Deed, a member is entitled to be paid a redundancy benefit of the amount held in the member's account.

18. Under clause 2.5A of the Trust Deed, the trustee may accept a transfer of benefits accumulated by a member with another redundancy fund into WACIRF No. 2.

19. Under clause 4.1A of the Trust Deed, the trustee may transfer the amount credited to the members account from WACIRF No. 2 to another 'approved worker entitlement fund'.

20. Under regulation 4.3 (Schedule E) of the trust deed, an employer may receive a refund of contributions credited to the account of a member who is not an employee of the employer.

Ruling

21. Contributions that are made to WACIRF No. 2 by an employer in respect of the employment of their employees are exempt benefits under section 58PA of the FBTA.

22. An employer who makes contributions on behalf of workers to WACIRF No. 2 under the Trust Deed can claim a deduction under section 8-1 of the ITAA 1997 for the amount of the contribution.

23. A refund of contributions that were made by an employer for workers who are not employees of the employer will be assessable income under section 6-5 of the ITAA 1997 at the time the amount is derived by the employer.

Commissioner of Taxation

8 March 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.

Application of section 58PA of the FBTAA

24. When an employer makes a contribution to an approved worker entitlement fund that contribution is an exempt fringe benefit if it meets the requirements of section 58PA of the FBTAA.

25. Section 58PA of the FBTAA states:

If:

- (a) a person makes a contribution to an approved worker entitlement fund; and
- (b) the contribution is made under an industrial instrument; and
- (c) the contribution is either:
 - (i) made for the purposes of ensuring that an obligation under the industrial instrument to make leave payments (including payments in lieu of leave) or payments when an employee ceases employment is met; or
 - (ii) for the reasonable administrative costs of the fund;

the contribution is an exempt benefit.

Contribution to an approved worker entitlement fund

26. Paragraph 58PA(a) of the FBTAA requires the contribution be made to an approved worker entitlement fund. Whether the employer makes the redundancy payments to an approved worker entitlement fund is a question of fact.

27. Section 58PB of the FBTAA deals with the meaning of approved worker entitlement fund. Subsection 58PB(2) of the FBTAA states:

A fund is an **approved worker entitlement fund** if:

- (a) the fund is prescribed for the purposes of this paragraph; and
- (b) a declaration under subsection (3) is not in force in relation to the fund.

28. WACIRF No. 2 has been prescribed as an approved worker entitlement fund for the purposes of paragraph 58PB(2)(a) of the FBTAA with effect from 1 April 2003. There is no declaration under subsection 58PB(3) of the FBTAA in force in relation to this fund.

29. WACIRF No. 2 is an approved worker entitlement fund for the purposes of paragraph 58PA(a) of the FBTAA.

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Contribution made under an industrial instrument

30. Paragraph 58PA(b) of the FBTAA requires the contributions be made under an 'industrial instrument'. An 'industrial instrument' is defined in subsection 136(1) of the FBTAA as 'a law of the Commonwealth or of a State or Territory or an award, order, determination or industrial agreement in force under any such law'.

31. Clause 16.2.7 of the NBCIA provides that, in respect of employees covered by the award, an employer may utilise a fund to satisfy its obligations (to make redundancy/severance payments). Clause 51(5) of the BTCA provides that, in respect of employees covered by the award, an employer may utilise a fund to satisfy its obligations (to make redundancy/severance payments). Clause 34.6 of the PIA provides that, in respect of employees covered by the award, an employer may utilise a fund to satisfy its obligations (to make redundancy/severance payments).

32. The NBCIA, the BTCA and the PIA, are industrial instruments for the purposes of paragraph 58PA(b) of the FBTA.

33. Payments made by employers to the fund are made under an industrial instrument as the awards allow the employer to make the contributions to a fund.

34. Contributions made under the relevant industrial instrument satisfy the requirement of paragraph 58PA(b) of the FBTA.

Contribution made to ensure that leave payment obligation is met

35. Paragraph 58PA(c) of the FBTA requires that the contribution is either for ensuring that an obligation under the industrial instrument for leave or redundancy is met, or for the reasonable administrative expenses of the fund.

36. As the contributions are made under the awards to provide for the payment of redundancy benefits to an employee payable on termination, the requirement of paragraph 58PA(c) of the FBTA will be satisfied.

37. The requirements of section 58PA of the FBTA will be met in relation to the employer contribution in respect of the workers or participating employees of WACIRF No. 2.

Application of section 8-1 of the ITAA 1997

38. Section 8-1 of the ITAA 1997 provides that you can deduct from your assessable income any loss or outgoing to the extent that it is incurred in gaining or producing assessable income and is not:

- capital, private or domestic in nature;
- incurred in gaining or producing exempt income; or
- prevented from being deductible by a provision of the Act.

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Positive limbs

Nexus to gaining and producing assessable income

39. In carrying on business activities an employer is required to fulfil their obligations in respect to the entitlements of their workers. These entitlements may be contained in the governing award, enterprise bargaining agreement or other industrial instrument negotiated between the employer and the employee or the employer and the relevant union on the employee's behalf. If an employer chooses to fund their worker entitlements via a contribution to WACIRF No. 2 either a Contribution Agreement is

executed between the employer and WACIRF No. 2, or the employer lodges a Contribution Return.

40. In addition to the employer's legal obligations under their relevant industrial instrument/s, the employer is also required to meet the obligations contained under the Trust Deed and Fund Regulations. The administrative provisions require the employer to make monthly contributions to WACIRF No. 2 in respect of worker entitlements.

41. It is accepted that there is a nexus between the business activities being carried on by the employer and the employer's obligation to provide for worker entitlements, such that payment of the worker entitlements is incidental and relevant to the production of the assessable income of the business.

Incurring the amount

42. At the point at which an employer makes the contribution to the Trustee of WACIRF No. 2 the amount is placed into member accounts and the amount is no longer available to the employer. This differs from the situation in *Walstern Pty Ltd v. Federal Commissioner of Taxation* [2003] FCA 1428; 2003 ATC 5076; (2003) 54 ATR 423 where there were no members of the trust. The contributions were not expenses incurred by the employer as they remained funds of the employer.

43. The ability for amounts to be reimbursed and returned to the employer under the Trust Deed (a factor which must be possible to satisfy paragraph 58PB(4)(c) of the FBTA) does not effect whether the monthly contributions are incurred by the employer.

44. Even though the Trust Deed enables the employer to seek reimbursement, the contributions to WACIRF No. 2 are definite payments which the employer is required to make to meet the legal obligations of carrying on business activities. As such the contributions are incurred when made (for employers accounting on a cash basis) or when the liability to make the payment each month arises (for employers accounting on an accruals basis).

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45. The employer's monthly contribution/s to WACIRF No. 2 are outgoings incurred in carrying on a business for the purposes of section 8-1 of the ITAA 1997.

Negative limbs

46. Whether the payment of worker entitlements to WACIRF No. 2 is revenue or capital in nature depends on the character of the payment when made by the employer. As stated in *GP International Pipecoaters Pty Ltd v. Federal Commissioner of Taxation* (1990) 90 ATC 4413 at 4419; (1990) 21 ATR 1 at 7:

The character of expenditure is ordinarily determined by reference to the nature of the asset acquired or the liability discharged by the making of the expenditure, for the character of the advantage sought by the making of the expenditure is the chief, if not the critical, factor in determining the character of what is paid: *Sun Newspapers Ltd. v. F.C of T.*(1938) 61 C.L.R. 337 at p. 363.

47. In making the monthly contribution to WACIRF No. 2, the employer meets their immediate legal obligation under the Contribution Agreement or Contribution Return and the Trust Deed.

48. The employer discharges their obligation in respect of their workers each month when the monthly payment is made to WACIRF No. 2 as required by regulation 2.1 of the Trust Deed.

49. The employer is making repetitive monthly contributions to discharge an immediate obligation and the obligation is directly connected to the income earning capacity of the business. Accordingly, the payment of the contribution is revenue in nature.

Refund of contribution

50. A refund of contributions under regulation 4.3 (Schedule E) of the Trust Deed will be made where a worker has ceased to provide labour to the employer because the employer is no longer engaged in works on any building project, maintenance site or other site or under a nominated industrial award/agreement for more than three months (or lesser period determined by the trustee).

51. Where an employer receives a refund of contributions made for workers who are not employees of the employer, the refund must be declared as income. In these cases it is considered that the refund is income received in the ordinary course of business and assessable under section 6-5 of the ITAA 1997 in the income year in which it is derived.

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Appendix 2 – Detailed contents list

52. 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:

CR 2001/1; CR 2004/21; CR 2004/22; CR 2004/27; CR 2004/28; CR 2004/41; CR 2004/111; CR 2005/116; TR 92/1; TR 92/20; TR 97/16

Subject references:

- assessable recoupments
- deductions and expenses
- exempt benefits
- fringe benefits tax
- income
- worker entitlement funds

Legislative references:

- TAA 1953
- ITAA 1997 6-5
- ITAA 1997 8-1
- FBTAA 1986 58PA
- FBTAA 1986 58PA(a)
- FBTAA 1986 58PA(b)
- FBTAA 1986 58PA(c)
- FBTAA 1986 58PB
- FBTAA 1986 58PB(2)
- FBTAA 1986 58PB(2)(a)
- FBTAA 1986 58PB(3)
- FBTAA 1986 58PB(4)(c)
- FBTAA 1986 136(1)
- Copyright Act 1968

Case references:

- GP International Pipecoaters Pty Ltd v. Federal Commissioner of taxation (1990) 90 ATC 4413; (1990) 21 ATR 1
- Sun Newspapers Ltd v. FC of T (1938) 61 CLR 337
- Walstern Pty Ltd v. Federal Commissioner of Taxation [2003] FCA 1428; 2003 ATC 5076; (2003) 54 ATR 423

ATO references

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