FEDERAL INSURANCE CONTRIBUTIONS ACT (FICA) – FRINGE BENEFIT TAX (FBT) LIABILITY

PUBLIC RULING - BR Pub 07/02

Note (not part of ruling): This ruling replaces Public Ruling BR Pub 01/05 published in *Tax Information Bulletin* Vol 13, No 7 (July 2001)). This new ruling is essentially the same as the previous ruling. However, the new ruling has been updated and applies the Income Tax Act 2004 instead of the equivalent provisions in the Income Tax Act 1994. The changes between the provisions of the 1994 and 2004 Acts affecting this ruling do not affect the conclusions previously reached.

This is a public ruling made under section 91D of the Tax Administration Act 1994.

Taxation Laws

All legislative references are to the Income Tax Act 2004 unless otherwise stated.

This Ruling applies in respect of sections CX 12, CX 13 and CX 31.

The Arrangement to which this Ruling applies

The Arrangement is the deduction of contributions from wages payable to employees and the payment of these contributions, together with employer contributions, to the United States Federal Government in accordance with the Federal Insurance Contribution Act ("FICA"), by an "American employer" (as defined in FICA) who is required to do so because the employer employs a citizen or citizens of the United States of America.

How the Taxation Laws apply to the Arrangement

The Taxation Laws apply to the Arrangement as follows:

- Employer contributions paid under FICA do not give rise to a "fringe benefit" under section CX 12 as the contributions are not made for the benefit of employees.

- Employer contributions paid under FICA do not give rise to a "fringe benefit" under section CX 13. As trust funds established for the purpose of paying disability benefits or Medicare and funded by contributions under FICA were not established for the benefit of employees and have not been approved by the Commissioner, they are not "sick, accident or death benefit funds" as defined in section OB 1.

- Employer contributions paid under FICA do not give rise to an "unclassified benefit" in terms of section CX 31 as a benefit is not provided by employers in connection with the employment of employees through the payment of employer contributions under FICA.

- Employee contributions required to be deducted from wages and paid under FICA do not give rise to an "unclassified benefit" as such contributions represent part of the assessable income of employees and are expressly excluded from the definition of "fringe benefit" by section CX 4.

Therefore, payments required under FICA are not subject to fringe benefit tax ("FBT").

The period or income year for which this Ruling applies

This Ruling will apply for the period beginning on 1 July 2004 and ending on 30 June 2009.

This Ruling is signed by me on the 12th day of March 2007.

Martin Smith
Chief Tax Counsel

COMMENTARY ON PUBLIC RULING BR Pub 07/02

This commentary is not a legally binding statement, but is intended to provide assistance in understanding and applying the conclusions reached in Public Ruling BR Pub 07/02 ("the Ruling").

Background

The Federal Insurance Contributions Act (FICA) is the part of the US Internal Revenue Code under which employers and employees are required to make payments for the funding of social security benefits. In some circumstances an employer who employs an employee to provide services in New Zealand is required to comply with obligations under the FICA legislation. FICA applies when an "American employer" pays wages for services performed as an employee by a US citizen outside the US: sections 3101 and 3111 and the definition of "employment" in section 3121 Internal Revenue Code. "American employer" means the US Government or its instruments, residents of the US or companies that are organised under the laws of the US.

If FICA applies, employers must make deductions from wages payable to an employee in respect of Old-Age Survivors and Disability Insurance ("OASDI") and Hospital Insurance (known as "Medicare"), and must pay the deductions to the Internal Revenue Service. In addition, employers are required to make payments for OASDI and Medicare (employer contributions) at the same rate. The current rate in respect of OASDI is 6.2 percent and in respect of Medicare the rate is 1.45 percent. An employer who fails to make the required payments or fails to make the payments on time is liable for a penalty.

Under FICA amounts deducted from wages payable to employees are deemed to have been paid to employees at the time of deduction (Internal Revenue Code 26 US Chapter 21 section 3123). FICA does not provide for recovery of OASDI or Medicare payments imposed on employees from an employee where the employer has failed to make deductions.

Payments collected under FICA are paid into the US Treasury's General Fund and are appropriated to three separate funds: the Federal Hospital Insurance Trust Fund; the Federal Old-Age and Survivors Insurance Trust Fund; and the Federal Disability Insurance Trust Fund. Amounts held in these funds are not held for any particular individual.

A person must be a US citizen or legally resident in the US to be entitled to social security benefits (Public Law 104-193; Personal Responsibility and Work Opportunity Act 1996).

Under the US social security legislation (Public Health and Welfare Code, 42 USC Chapter 7) a person must hold not less than 40 credits to be entitled to a retirement benefit. The amount needed to gain a credit changes from year to year. Currently a credit is gained for every quarter in which an employee earns more than $970 from employment. No more than four credits can be gained in respect of a year. The minimum age to qualify for a retirement benefit depends on when a person was born.

However, a person could qualify for a disability benefit with fewer credits, depending on their age. To be entitled to a disability benefit:

- A person must have a medical condition that meets the definition of "disability" in the social security legislation; and

- Twenty of the 40 credits required to qualify for a disability benefit must have been earned in the 10 years ending in the year in which the person became disabled.

If a person who is covered by social security dies, their surviving spouse or dependent children can receive a survivors benefit. The right to retirement, survivors and disability benefits cannot be assigned or transferred.

The amount of the monthly benefit paid depends on the person's earnings during the person's working life and the age at which the person retires. The amount of the benefit is calculated according to a formula in the legislation.

People aged 65 or older are entitled to receive Medicare benefits if they:

- Receive a social security benefit;

- Have worked long enough to be eligible for a social security benefit;

- Would be entitled to a social security benefit based on their spouse's work record and their spouse is aged at least 62; or

- Have worked long enough in a federal, state or local government job to be insured for Medicare.

People aged under 65 who receive disability benefits or who have permanent kidney failure may qualify for Medicare.

Legislation

"Fringe benefit" is defined in section CX 2(1) as follows:

A **fringe benefit** is a benefit that—

(a) is provided by an employer to an employee in connection with their employment; and

(b) either—

(i) arises in a way described in any of sections CX 6, CX 8, CX 9, or CX 11 to CX 15; or

(ii) is an unclassified benefit; and

(c) is not a benefit excluded from being a fringe benefit by any provision of this subpart.

Section CX 12 provides:

(1) A fringe benefit arises when an employer contributes to a superannuation scheme for the benefit of an employee.

(2) This section does not apply if the contribution is a specified superannuation contribution.

Section CX 13 provides:

A fringe benefit arises when an employer makes a contribution for the benefit of an employee to a sickness, accident, or death benefit fund.

"Unclassified benefit" is defined in section CX 31 as follows:

Unclassified benefit means a fringe benefit that arises if an employer provides an employee with a benefit in connection with their employment that is—

(a) not a benefit referred to in any of sections CX 6 to CX 15; and

(b) not a benefit excluded under this subpart.

Section CX 4 provides:

To the extent to which a benefit that an employer provides to an employee in connection with their employment is assessable income, the benefit is not a fringe benefit.

"Superannuation scheme" is defined in section OB 1 as follows:

superannuation scheme—

(a) means—

(i) a trust or unit trust established by its trust deed mainly for the purposes of providing retirement benefits to beneficiaries who are natural persons or paying benefits to superannuation funds; or

(ii) a company that is not a unit trust, is not resident in New Zealand, and is established mainly for the purpose of providing retirement benefits to members or relatives of members who are natural persons; or

(iii) an arrangement constituted under an Act of the Parliament of New Zealand, other than the Social Security Act 1964, mainly for the purpose of providing retirement benefits to natural persons; or

(iv) an arrangement constituted under the legislation of a country, territory, state, or local authority outside New Zealand mainly for the purpose of providing retirement benefits to natural persons; and

when referring to a superannuation scheme that is a trust, means the trustees of the scheme.

The definition of "arrangement" in section OB 1 reads as follows:

Arrangement means a agreement, contract, plan or understanding (whether enforceable or unenforceable), including all steps and transactions by which it is carried into effect.

The definition of "sickness, accident or death benefit fund" in section OB 1 reads as follows:

sickness, accident, or death benefit fund means a sickness, accident, or death benefit fund that is—

(a) established for the benefit of—

(i) employees; or

(ii) the members of an incorporated society; or

(iii) the surviving spouses and dependants of those employees or members; and

(b) approved by the Commissioner

Application of the legislation

Liability for FBT

Whether an employer is required to pay fringe benefit tax (FBT) in respect of either employer or employee contributions made under FICA depends on whether the employer has provided or granted a "fringe benefit" (section ND 1(1)). There will be a "fringe benefit" where:

- A benefit arises in a way described in any of section CX 6, section CX 8, section CX 9 or sections CX 11 to CX 15 or a benefit of any other type is provided by an employer to an employee in connection with their employment (an "unclassified benefit"); and

- The benefit is not excluded from being a fringe benefit by any provision of subpart CX.

In Australian cases, in the FBT context, the courts have considered that a fringe benefit will not be provided unless there is a link between the benefit and a particular employee: see *Essenbourne Pty Ltd v Commissioner of Taxation* (2002) ATC 5201; *Walstern v Commissioner of Taxation* 2003 ATC 5076; *Cameron Brae Pty Ltd v FCT* 2006 ATC 4433. The Commissioner considers that this principle also applies in the New Zealand context. As with the Australian legislation, the wording of the legislation suggests that it contemplates a benefit provided to a particular employee. The definition of "fringe benefit" in section CX 2(1) refers to "a benefit that is provided by an employer to an employee in connection with their employment". Sections CX 12 and CX 13 also refer to "a contribution for the benefit of an employee". As with the Australian legislation, under the valuation provisions any payment made by the employee is to be taken into account in determining the taxable value of the fringe benefit. The need for a link between the benefit and an employee is consistent with the purpose of the FBT provisions. FBT was intended to apply to non-cash remuneration provided to an employee and although liability for FBT is imposed on the employer, the theoretical basis for the imposition of FBT is that it is payable in respect of amounts that are essentially (or would be) income of an employee.

Contributions to superannuation scheme: section CX 12

Under section CX 12 a fringe benefit arises when an employer makes a contribution to a superannuation scheme (other than a specified superannuation contribution) for the benefit of an employee.

The definition of "superannuation scheme" in section OB 1 includes an arrangement constituted under the legislation of a country, territory, state or local authority outside New Zealand mainly for the purpose of providing retirement benefits to natural persons (paragraph (a)(iv) of the definition).

Superannuation scheme

The definition of "superannuation scheme" specifically includes an arrangement constituted under legislation.

FICA requires employer and employee contributions to fund social security benefits, including retirement benefits. The US social security legislation contains the provisions relating to eligibility for retirement benefits and the payment of retirement benefits. These

two pieces of legislation together establish a system for the funding and payment of social security benefits, including retirement benefits. Therefore, there is an arrangement that is constituted under US legislation (the US social security legislation and FICA).

The Federal Old-Age and Survivors Insurance Trust Fund was established under FICA (Internal Revenue Code Chapter 7 section 401). Under the US social security legislation an amount equal to 100 percent of the amount collected from employees and employers in respect of OASDI is appropriated to that trust fund (42 USC section 401). Monthly retirement benefits and survivors benefits are paid out of that trust fund. (A separate trust fund to be known as "the Federal Disability Insurance Trust Fund" is also established under the social security legislation.) The social security legislation sets out the conditions for entitlement to retirement benefits and provides for the payment of retirement benefits (42 US section 402).

For paragraph (a)(iv) of the definition of "superannuation scheme" to apply, the arrangement must be mainly for the purpose of providing retirement benefits.

Payments under FICA are appropriated to the Federal Old-Age Survivors Insurance Trust Fund and are to be used for the purpose of funding retirement benefits. Survivors' benefits are also paid out of the fund to the widows, widowers and children of people who would have been entitled to receive a retirement benefit (that is, benefits could be paid out of the trust fund to people who have not reached retirement age). However, such people would be entitled to receive a benefit only if a person who qualifies for a retirement benefit has died. The principal object of creating the trust fund is to provide for the payment of retirement benefits.

FICA is part of a legislative scheme for the provision of social security benefits by the US Federal Government, which is the equivalent of provision of benefits under the New Zealand Social Security Act 1964. In *Roe v Social Security Commission* (10 April 1987) unreported, High Court, Wellington, M 270/86, Davison CJ) the plaintiff was the recipient of a social security retirement benefit paid by the US Government. The issue was whether the benefit formed part of a programme providing benefits, pensions or periodical allowances for any of the contingencies for which benefits, pensions or allowances could be paid under the New Zealand Social Security Act. Davison CJ commented:

> The US retirement benefit is clearly on the evidence a benefit paid by the US Government of the same type as a NZ national superannuation benefit. Both are paid by the respective Governments and both are part and parcel of programmes for assistance to age-related beneficiaries. (p. 8)

The Commissioner considers that payments made under FICA and appropriated to the Federal Old-Age and Survivors Insurance Trust Fund are paid under an arrangement constituted under US legislation mainly for the purpose of providing retirement benefits to natural persons. Therefore, there is a superannuation scheme that is constituted under the social security legislation and FICA in terms of paragraph (a)(iv) of the definition of "superannuation scheme". This differs from the view expressed in the Commissioner's previous ruling on this issue (BR Pub 01/05). However, for section CX 12 to apply, payments made by employers under FICA must be contributions for the benefit of an employee.

Whether contributions are for the benefit of employees

Payments employers are required to make under section 3111(a) of FICA are tax. Section 3111(a) imposes on every employer "an excise tax, with respect to having individuals in his employ". An excise tax is "a tax upon an activity" (CCH *Federal Tax Guide Reports* paragraph 21,001), in this case a tax imposed in respect of employment (*Helvering v Davis* 57 SC 904).

However, a payment by an employer could be a contribution although the employer has a statutory obligation to make the payment. In *Case M9* (1990) 12 NZTC 2069 it was held that the predecessor of section CX 12 applied to contributions made by a local authority to the National Provident Fund, although the employer did not have a choice about making the contributions. Judge Bathgate considered that the focus of the FBT legislation was whether the contributions could be regarded as a benefit from the employees' point of view. Judge Bathgate said:

> The objector's claim that the superannuation payments by the objector on behalf of its employees compulsorily paid by it under the National Provident Fund Act, are not benefits because it had no choice as to whether to make the payments is to an extent understandable, from the employer's point of view. A benefit is often regarded as being given voluntarily, rather than compulsorily. A benefit may however be given under compulsion in some circumstances — *Yates v Starkey* [1951] 1 All ER 732. From the employees' point of view, and after all Pt XB of the Income Tax Act is only concerned with benefits received by employees, albeit from employers, the contributions to the superannuation fund can be considered as a benefit. (p. 2073)

In *Yates v Starkey*, referred to by Judge Bathgate, the Court of Appeal held that a person who had been ordered by the court to pay his wife an annual amount in trust for his children had provided funds for the purpose of the settlement of a trust. Jenkins LJ commented:

> I do not agree that the words "has provided" necessarily connote an exercise of free will. It seems to me that the taxpayer here if asked "Who is providing for the maintenance for your children?" could with perfect accuracy have replied "I am doing so under an order of the court". (p. 479)

However, for section CX 12 to apply the contribution must be for the benefit of an employee. In *Case M9*, although the employer was required by the National Provident Fund Act to make contributions, the objective of the contributions was to provide a benefit to employees under the National Provident Fund.

In *NZI Bank Ltd v Euro-National Corporation Ltd* [1992] NZLR 528 Richardson J made the following comments in respect of the interpretation of the phrase "for the benefit of employees":

> It is not sufficient to satisfy para (b) that the shares are to be held on trust for employees. The shares must be held "for the benefit" of employees. "For" in that context means with the object and purpose of benefiting employees and the "benefit" to employees must be discernible and real. As in the case of the exercise of trustees' powers to make advances for a person's benefit, it must confer an advantage which can be enjoyed by employees. It must be of value to employees. An arrangement does not qualify as being "for the benefit of employees" unless employees actually stand to benefit. (p. 544)

Hence, for a contribution to be "for the benefit of an employee" in terms of section CX 12, the contribution must be made for the purpose of benefiting the employee and the contribution must provide something of real value to the employee.

Employer contributions required under FICA are not hold in trust for any employee. The US Social Security system for the payment of retirement benefits is a pay-as-you-go scheme

under which current employer and employee contributions are used to fund the payment of retirement benefits to current recipients of retirement benefits. Neither employer nor employee contributions are allocated to, or held for, individual employees.

Payments that an employer must make under FICA are not attributable to any particular employee. Excise tax is calculated on the total wages paid by the employer. Employees are not entitled to receive a refund of payments made either by employers or employees under FICA. The entitlement of employees to a retirement benefit does not depend on whether the employer has paid the excise tax imposed on the employer under FICA. To qualify for a retirement benefit, a person must be a "fully insured individual" (42 USC 402(a)(1)). To be a "fully insured individual" a person must hold sufficient credits (that is, a minimum of 40 credits). The number of credits earned is based on the amount of the employees' earnings over their working life and not on the payment of employer contributions. Payments made by employers under FICA also do not affect the amount of the benefit payable. The amount of the retirement benefit is based on average earnings over a person's working life, indexed to account for changes in average wages.

Employees cannot transfer or assign their right to any future benefit (42 USC 407). *Flemming v Nestor* 363 US 603 establishes that a person who makes payments under FICA does not as a consequence acquire a right to a benefit analogous to a property right.

The Commissioner considers that payments of excise tax under FICA are not made by employers for the benefit of any particular employee as:

- Employee contributions are not held in trust for any individual employee;
- Employees are not entitled to receive any part of the contributions made by employers;
- Employees do not obtain the right to a retirement benefit as a consequence of the payments made by employers; and
- The payment of employer contributions by employers does not affect the amount of the benefit payable to employees.

Therefore, such payments do not give rise to a fringe benefit in terms of section CX 12.

Contributions to sickness, accident or death benefit fund: section CX 13

Under section CX 13 a fringe benefit arises when an employer makes a contribution for the benefit of an employee to a sickness, an accident or a death benefit fund.

The definition of "sickness, accident, or death benefit fund" refers to a sickness, an accident, or a death fund that is:

- Established for the benefit of employees, the members of an incorporated society, or the surviving spouses and dependants of those employees; and
- Approved by the Commissioner.

Under the US social security legislation separate funds are established for the payment of disability benefits and Medicare (the Federal Disability Insurance Trust Fund and the Hospital Insurance Trust Fund). Self-employed people can also earn credits so that they are entitled to receive disability benefits or Medicare. The funds are not limited to the employees of a particular employer or to employees in general. They were established to fund the payment of government-provided disability benefits and hospital and medical benefits that are available to all people who earn sufficient credits to qualify for benefits and satisfy the other conditions set out in the US legislation. Payments by employers do not directly affect employees' entitlement to disability benefits or Medicare. Whether the employer pays employer contributions does not affect the employees' entitlement to disability benefits or Medicare or the amount of the benefit.

The Commissioner considers that neither the Disability Insurance Fund nor the Hospital Insurance Trust Fund was established for the benefit of employees. The funds were not established for the benefit of a particular employer's employees and were not established for the benefit of employees alone. Employees do not obtain a right to receive Medicare or disability benefits as a consequence of the payments made by their employer.

To be a sickness, an accident or a death fund within the statutory definition, a fund must also be approved by the Commissioner. As the Commissioner has not approved either the Federal Disability Insurance Fund or the Hospital Insurance Fund, the funds cannot be sickness, accident or death benefit funds for the purpose of section CX 13.

Therefore, the Commissioner considers that a benefit does not arise in terms of section CX 13 as a consequence of payments required to be made by employers in respect of the Federal Disability Insurance Trust Fund or the Hospital Insurance Trust Fund under FICA as these funds are not sickness, accident or death funds as defined in section OB 1.

Unclassified benefit: section CX 31

The definition of "unclassified benefit" in section CX 31 refers to a benefit an employer provides to an employee "in connection with their employment" other than the benefits referred to in any of sections CX 6 to CX 15.

"Benefit" is not defined for FBT purposes. Therefore, the ordinary meaning of "benefit" applies. In *CIR v Dick* (2001) 20 NZTC 17,396 Glazebrook J commented as follows on the meaning of "benefit":

> [48] The *New Shorter Oxford Dictionary* (1993 ed) defines benefit (in relevant part) as: a favour, gift, a benefaction, an advantage, a good, pecuniary profit. Likewise the definition of advantage is: a favouring circumstance, something which gives one a better position, benefit. Looking at the dictionary meaning of those words it would appear that something may not be a benefit or advantage if it has been acquired through the provision of services or goods at market value. This, therefore, is in contrast to the definition of income.

The Commissioner considers that in the FBT context a "benefit" is an advantage, a material acquisition that confers an economic benefit on an employee. As outlined in "QB0043 The meaning of 'benefit' for FBT purposes" (published in *Taxation Information Bulletin* Vol 18, No 2 (March 2006)), in considering whether a benefit has been provided to an employee it is not relevant that the employee made a payment for what is provided.

For there to be a "fringe benefit", the benefit must be provided by an employer to an employee in connection with their employment. The meaning of the phrase "in connection with" was considered in *Claremont Petroleum NL v Cummings* (1992) 110 ALR 239. Wilcox J said:

The phrase "in connection" is one of wide import, as I had occasion to observe in a different context in *Our Town FM Pty Ltd v Australian Broadcasting Tribunal* (1987) 16 FCR 465 at 479-80; 77 ALR 577 at 591-592:

> The words "in connection with"…. do not necessarily require a causal relationship between two things: see *Commissioner for Superannuation v Miller* (1985) FCR 153 at 154, 160, 163; 63 ALR 237 at 238, 244, 247. They may be used to describe a relationship with a contemplated future event, see *Koppen v Commissioner for Community Relations* (1986) 11 FCR 360 at 364; 67 ALR 215; *Johnson v Johnson* [1952] P47 at 50-1. In the latter case the United Kingdom Court of Appeal applied a decision of the British Columbia Court of Appeal, *Re Nanaimo Community Hotel Ltd* [1945] 3 DLR 225, in which the question was whether a particular court, which was given "jurisdiction to hear and determine all questions that may arise in connection with any assessment made under this Act", had jurisdiction to deal with a matter which preceded the issue of an assessment. The trial judge held that it did, that the phrase "in connection with" covered matters leading up to, or which might lead up to an assessment. He said:
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> > "One of the very generally accepted meanings of 'connection' is 'relation between things one of which is bound up with or involved in another', or again 'having to do with'. The words include matters occurring prior to as well as subsequent to or consequent upon so long as they are related to the principal thing. The phrase 'having to do with' perhaps gives as good a suggestion of the meaning as could be had."
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> This statement was upheld on appeal. (p 280)

Hardie Boys J made the following comments on the meaning of "in connection with" in *Strachan v Marriott* [1995] 3 NZLR 272:

"In connection with" may signify no more than a relationship between one thing and another. The expression does not necessarily require that it be a causal relationship: *Our Town FM Pty Ltd v Australian Broadcasting Tribunal* (1987) 16 FCR 465, 479 per Wilcox J. But, as Davies J warned in *Hatfield v Health Insurance Commission (*1987) 15 FCR 487, at p 491:

> Expressions such as 'relating to', 'in relation to', 'in connection with' and 'in respect of' are commonly found in legislation but invariably raise problems of statutory interpretation. They are terms which fluctuate in operation from statute to statute . ... The terms may have a very wide operation but they do not usually carry the widest possible ambit, for they are subject to the context in which they are used, to the words with which they are associated, and to the object or purpose of the statutory provision in which they appear. (pp. 279-281)

In *The Queen v Savage* [1983] CTC 393 Dickson J in the Supreme Court of Canada commented:

23 ….Our Act contains the stipulation, not found in the English statutes referred to, "benefits of any kind whatever ... in respect of, in the course of, or by virtue of an office or employment". … Further, our Act speaks of a benefit "in respect of" an office or employment. In *Nowegijick* v *The Queen*, [1983] C.T.C. 20, 83 D.T.C. 5041 this Court said, at 25 [5045], that:

> **The words "in respect of" are, in my opinion, words of the widest possible scope. They import such meanings as "in relation to", "with reference to" or "in connection with".** The phrase "in respect of" probably the widest of any expression intended to convey some connection between two related subject matters.
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> See also *Paterson v. Chadwick*, [1974] 2 All ER 772 (QBD) at 775. [Emphasis added]

Therefore, the phrase "in connection with" is used to describe a relationship between two things, but not necessarily a causal relationship. The phrases "in connection with", "in relation to" and "in respect of" have similar meanings. These expressions are capable of having a very wide meaning. The degree of the relationship required depends on the context in which the expression is used.

In the Australian FBT context, the courts have considered that it cannot be said that any causal relationship between the benefit and the employment is a sufficient relationship for FBT purposes and that a sufficient or material rather than a causal connection or relationship between the benefit and the employment must be established: see *J & G Knowles & Associates Pty Ltd v FCT* 2000 ATC 4151. In that case, the court considered that it was helpful to consider whether the benefit is a product or incident of the employment. The Commissioner considers that this approach would also be appropriate in the New Zealand context, given that FBT was intended to apply to non-cash remuneration provided to employees.

The Commissioner considers that where the employment is a substantial reason for the provision of the benefit, there would be a sufficient relationship between the benefit and the employment (see "QB0043 The meaning of 'benefit' for FBT purposes" (published in *Taxation Information Bulletin* Vol 18, No 2 (March 2006))).

Employer contributions

The Commissioner considers that employer contributions do not give rise to a benefit that is provided by the employer in connection with the employment of any employee. It is not possible to establish a link between a benefit arising from the payment of employer contributions and any particular employee. The reasons are as follows:

- Employees do not obtain a benefit in the form of an entitlement to receive payments made by employers under FICA. Employees have no beneficial entitlement to amounts paid by them or by their employer under FICA.

- An employee's right to receive a social security benefit is conditional on the employee satisfying the eligibility requirements in the social security legislation. When the right to receive payment from a fund is conditional, a benefit would not be provided when payment is made to the fund (*Constable v Commissioner of Taxation* 5 ATD 83). In *Constable* the taxpayer was the member of a provident fund established for the employees of the Shell group of companies. Both employer and employee contributions were paid to the fund. The fund's regulations permitted members to withdraw the amount held on their behalf if an amendment was made to the regulations that curtailed their rights. Such an amendment was made with effect from 30 September 1947. The taxpayer withdrew amounts held to his credit (including the employer's contributions and interest earned on the amount contributed). The High Court of Australia held that these amounts did not constitute an allowance, a gratuity, compensation, a benefit, a bonus or a premium in respect of or for or in relation to the taxpayer's employment or services rendered by him. Dixon CJ and McTiernan, Williams and Fullager JJ in their joint judgment commented:

  > It appears to us that the taxpayer becomes entitled to a payment out of the fund by reason of a contingency (viz an alteration of the regulations curtailing the rights of members) which occurred in the year enabling him to call for the amounts shown by his account. It was a contingent right which became absolute. The happening of the event which made it absolute did not, and could not amount to an allowing, giving or granting to him of any allowance, gratuity, compensation, benefit, bonus or premium. The fund existed as

> one to a share in which he had a contractual, if not a proprietary title. All that occurred in the year of income with respect to the sums in question was that the future and contingent or conditional right became [a] right to present payment and payment was made accordingly.
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> ….
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> It is not of course, a matter which arises for decision in the present case, but to avoid misunderstanding it is we think desirable to say that on the frame of the regulations we find it by no means easy to see how the sums so contributed can be regarded as allowed, granted or given to the employee when they are paid to the Administrators of the Fund. It is only after the Administrators have exercised their discretion that the moneys paid to the special account are reflected in the member's (employee's) account and even then that does not mean that the member becomes presently entitled to the moneys credited to that account. (pp. 95-96)

- A benefit (either in the form of a social security benefit or the right to receive a social security benefit) would not be provided when payments are made by the employer under FICA. Employees must satisfy the statutory criteria (including citizenship or residence requirements, reaching retirement age, disability, earning the minimum number of credits) before a benefit would be paid to the employees. *Fleming v Nestor* 363 US 603 confirms that a right to receive future benefits does not accrue as a consequence of payments made by the employer under FICA.

- The substantial reason for payment or the provision of retirement, disability or Medicare benefits to an employee is that the employee satisfies the statutory criteria for eligibility to receive the benefit. The amount of any benefit paid is not related to the payments made under FICA. The amount depends on a person's earnings history (whether as an employee or a self-employed person). Therefore, there is an insufficient relationship between the payment of a social security benefit and payments made by the employer under FICA.

Employee contributions

The Commissioner considers that the deduction of employee contributions from wages and the payment of such contributions under FICA also do not give rise to a benefit in connection with the employee's employment. As employee contributions form part of the salary or wages paid to employees, employee contributions are assessable income of employees in terms of section CE 1(1)(a). That being the case, such contributions are specifically excluded from the definition of "fringe benefit" by section CX 4. In *Case 20*7 CTBR(NS) 91 it was accepted that deductions made under FICA from the salary paid to an Australian resident who was a visiting professor at a university in the US_ was assessable income of the taxpayer. The issue was whether the amount deducted under FICA was exempt income (on the basis that a liability for income tax in the US had been paid).

Summary

For there to be an FBT liability, the employer must have provided a "fringe benefit" to an employee.

- Employer contributions paid under FICA do not give rise to a "fringe benefit" under section CX 12 as the contributions are not made for the benefit of employees.

- Employer contributions paid under FICA do not give rise to a “fringe benefit” under section CX 13. As trust funds established for the purpose of paying disability benefits or Medicare and funded by payments under FICA were not established for the benefit of employees and have not been approved by the Commissioner, the funds are not “sick, accident or death benefit funds” as defined in section OB 1.

- Employer contributions under FICA do not give rise to an “unclassified benefit” in terms of section CX 31 as a benefit is not provided by employers in connection with the employment of employees through the payment of employer contributions under FICA.

- Employee contributions do not give rise to an “unclassified benefit”. Employee contributions required to be deducted from wages and paid under FICA represent part of employees’ assessable income and are expressly excluded from the definition of “fringe benefit” by section CX 4.

Therefore, payments required under FICA are not subject to FBT.