

24 July 2009

Mr Richard Warburton, AO
Chairman
The Board of Taxation
c/- The Treasury
Langton Crescent
CANBERRA ACT 2600

Via email: taxboard@treasury.gov.au

Dear Mr Warburton,

RE: Post-implementation review into the alienation of personal services income rules

The ACTU welcomes the opportunity to make a brief submission to the Board of Taxation's Post-implementation review into the alienation of personal services income rules.

A decade ago, the ACTU supported the adoption of the recommendations of the Ralph Review of Business Taxation designed to limit the avoidance of income tax that occurred through the alienation of personal service income [Recommendations 7.2 and 7.3]. In making these recommendations, the Ralph Report recognised the inequities arising from the alienation of personal services income in that people in substantially the same position may be paying significantly different levels of taxation. It also recognised the significant risk to tax revenue – through income splitting and accessing of an increased range of alleged business tax deductions – which is posed by continued use of interposed entities to alienate payments in respect of personal services.¹

The ACTU continues to support the policy intent behind the alienation of personal services income rules, now found in Divisions 84-87 of the *Income Tax Assessment Act 1997* (Cth)(the ITAA). Independent contracting arrangements must not be permitted to be used as a mechanism to avoid paying income tax at individual rates and to claim deductions available to businesses. Where work is being performed by an individual in a manner analogous to that of an employee, that person should be treated as an employee for regulatory purposes, including taxation.

¹ Review of Business Taxation (July 1999) p. 287.

The ACTU has concerns, however, that the legislative tests currently set out in Division 87 of the ITAA do not adequately or effectively distinguish those workers who genuinely carry out their own business from those who are working in a dependent or controlled way and should be treated for taxation purposes as employees. The test must be drafted so as to ensure it is the substance of the relationship between the hirer and the provider of services that determines taxation treatment, not its legal form.

We further note that the effectiveness of the rules remains unclear. Existing evidence suggests that the incidence of dependent contractors (that is, persons employed on a commercial contract but whose work arrangements are consistent with them being an employee) continues to be significant, if not increasing.² This is particularly the case in industries such as building and construction.

In addition, what limited evidence we do have on compliance levels suggests that there are significant problems. Of the over 2000 personal services income audits conducted by the ATO in the period 2002 – 2005, for example, an adjustment had to be made in approximately one-third of the cases because people had incorrectly assessed themselves as being engaged in a personal services business.³ These figures are concerning, given that over 99% of the tax claims in this area are self-assessed.⁴ In summary, the ACTU is unaware of any evidence to suggest that the current legislative provisions are having a significant impact on this form of tax evasion and we remain concerned that practices to alienate personal services income continue to be widespread.

Yours sincerely,



Jeff Lawrence
Secretary

² It has been estimated that between 25 and 41 percent of ‘independent contractors’ are dependent contractors: A O’Donnell, ‘Non-Standard Workers in Australia: Counts and Controversies’ (2004) 17 *Australian Journal of Labour Law* 1, 22.

³ Evidence of Mr Mark Konza, Deputy Commissioner of Small Business, Australian Taxation Office to the House of Representatives Standing Committee on Employment Workplace Relations and Workforce Participation’s Inquiry into Independent Contracting and Labour Hire Arrangements, 16 June 2005, p. 3.

⁴ *Ibid*, p. 8.