



Australian Government

Inspector-General of Taxation

Review into the Australian Taxation Office's employer obligations compliance activities

Inspector-General of Taxation

December 2016

Review into the Australian Taxation Office's employer obligations compliance activities

A report to the Minister

Inspector-General of Taxation
December 2016

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2 December 2016

The Hon Kelly O'Dwyer MP
Minister for Revenue and Financial Services
Parliament House
Canberra ACT 2600

Dear Minister

Review into the Australian Taxation Office's employer obligations compliance activities

I am pleased to present you with my report of the above review examining aspects of the Australian Taxation Office's (ATO) employer obligations compliance activities.

I have made two recommendations for the Government's consideration. They are aimed at reducing compliance costs and promoting voluntary compliance through a review of the Fringe Benefits Tax regime and expanding the Taxable Payments Reporting System to the engagement of contractors across all industries with the required reporting ultimately becoming automated.

Nine other recommendations have been made to the ATO. They also address the compliance burden and deal with a number of other important issues such as the classification of workers as contractors or employees, the ATO's capability framework and risk identification processes as well as the implementation of the Single Touch Payroll initiative.

The ATO has agreed in full or in part with seven of the nine recommendations. I am of the view that whilst the implementation of the agreed recommendations will result in significant improvement, the full benefit of the review may not be realised due to disagreement with some recommendations or parts thereof.

I am grateful for the support, contribution and willingness of those who provided their time, expertise and experience in the conduct of this review.

Yours faithfully

A handwritten signature in dark ink, appearing to read 'Ali Noroozi', with a long horizontal stroke extending to the right.

Ali Noroozi
Inspector-General of Taxation

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EXECUTIVE SUMMARY

The Inspector-General of Taxation's (IGT) review into the Australian Taxation Office's (ATO) employer obligations compliance activities was undertaken in response to concerns raised by stakeholders and is based on submissions from a wide range of stakeholders, including employers, workers, superannuation funds and tax practitioners as well as their respective representatives.

Given the Government's focus on reducing the compliance burden, particularly for small businesses, a number of other reviews, considering various aspects of employer obligations, had already been undertaken prior to this review. The ATO had also embarked on a program of improvements. Accordingly, this review seeks to build on existing or developing ATO practices to enhance the tax and superannuation systems as a whole whilst delivering improvements to all relevant parties.

A key focus of this review was the uncertainty associated with the employee/contractor distinction which can lead to misclassification of workers with adverse impacts for all parties. The ATO's online Employer/Contractor Decision Tool is a useful aid and the IGT has recommended further improvements to it such as allowing use by workers as well as businesses to better inform them of their relevant obligations. Whilst the ATO has agreed to this recommendation, it has not agreed to the IGT's recommendation to establish a Voluntary Certification System whereby workers and businesses can seek upfront certainty from the ATO to ensure correct classification of workers at the earliest opportunity and avoid adverse retrospective consequences.

This review has also examined opportunities for reducing compliance costs and improving voluntary compliance. Stakeholders had raised particular concerns with the high costs of complying with the Fringe Benefits Tax (FBT) regime. Accordingly, a recommendation has been made to Government to consider reducing compliance costs in targeted areas in the short-term and conducting a more fundamental review in the longer term. The IGT has also recommended that the Government considers expanding the Taxable Payment Reporting System to the engagement of contractors across all industries and ultimately for the reporting under this system to be automated.

The review has also identified opportunities for the ATO to reduce the FBT and Superannuation Guarantee (SG) compliance burden. The IGT has recommended that the ATO considers developing a capability for the Small Business Superannuation Clearing House to receive electronic and standardised files to remove the need for manual input. Recommendations have also been made for the ATO to publish its areas of FBT compliance focus for each year, provide detailed information on key FBT risks and to increase employers' awareness of its differentiated approach to non-compliance with SG obligations. The ATO has agreed to these recommendations.

Another source of stakeholder concern explored in this review was the risks and costs associated with the implementation of Single Touch Payroll (STP). The IGT has recommended rigorous testing of third party STP software with certification being provided where all requirements are met. The ATO has agreed to this recommendation. Other STP concerns related to those who may not be able to comply with STP because of, for example, technological challenges in regional areas. The STP legislation specifically provides an exemption and allows the Commissioner to provide further exemptions. Accordingly, the IGT has also recommended that appropriate exemptions be made available in the short-term whilst exploring the possibility of providing low or no cost STP software and alternative methods of electronic access in the long-term as the full benefit of STP will only be realised when all employers comply with it. The ATO has not agreed to this recommendation.

Concerns have also been raised in respect of the ATO's approach to employer obligations compliance activities, including the ATO's heavy reliance on reporting by employers and employees to identify non-compliance. A key cause for these concerns is that employers who do not accurately report their obligations may remain undetected and create an uneven playing field. The ATO has acknowledged that there are opportunities to improve its risk identification process. The IGT has, amongst other things, recommended that the ATO analyse the utility of data from third party referrals in order to maximise the use of sources that yield the best results, such as referrals from superannuation funds. The ATO has agreed to this aspect of the recommendation, however, it has not agreed to obtain SuperStream data from superannuation funds for employers who are not required to use STP.

The ATO has also disagreed with a recommendation aimed at enhancing the ATO's existing capability development framework. This recommendation sought improvements to its training packages, assessment of those staff who undertook such training, monitoring quality assessments to identify training needs and processes for documenting how the law applies to the facts of each case.

Overall, the IGT has made 11 recommendations. Two are directed to Government and nine were directed to the ATO. The ATO has agreed in full or in part with seven recommendations and disagreed with two. The IGT is of the view that the implementation of the agreed recommendations should result in significant improvements. However, given disagreement to some recommendations or parts thereof, the full benefit of this review may not be realised as the recommendations are an integrated package building on the improvements that the ATO has developed or is developing in this area.

LIST OF RECOMMENDATIONS

RECOMMENDATION 2.1

The IGT recommends the ATO:

- (a) clarify the protection provided to those who use and rely on the Employee Contractor Decision tool in good faith, promote the tool and allow it to be used by employees and contractors as well as accompanying the result with links to information outlining their respective rights and obligations; and*
- (b) implement and promote a Voluntary Certification System which employers, employees and contractors may use, as soon as possible, to confirm worker status and refer them to information about their respective rights and obligations once their status has been determined.*

RECOMMENDATION 3.1

The IGT recommends that, in relation to Single Touch Payroll, the ATO:

- (a) apply the learnings from the implementation of SuperStream and, in particular, ensure that there is rigorous testing of third party software with certification being provided to those that meet all requirements;*
- (b) seek to reduce employers' reporting requirements by using the information obtained to prefill fields;*
- (c) ensure that there are appropriate exemptions at least in the short-term whilst exploring the possibility of providing:*
 - i) a low or no cost software for qualifying small employers; and*
 - ii) an alternative method of electronic access for employers facing technological challenges, through such means as e-kiosks.*

RECOMMENDATION 3.2

The IGT recommends that the ATO consider developing a capability for the Small Business Superannuation Clearing House to receive:

- (a) electronic files, such as Microsoft Excel and Apple Numbers; and*
- (b) standardised files from commercial payroll software.*

RECOMMENDATION 3.3

The IGT recommends that the Government considers reviewing the Fringe Benefits Tax regime with a view to delivering a reduction in compliance costs in the short to medium term as well as longer term fundamental reform.

RECOMMENDATION 3.4

The IGT recommends that the Government considers expanding the Taxable Payment Reporting System (TPRS) to the engagement of contractors across all industries and automating the required reporting under TPRS.

RECOMMENDATION 4.1

The IGT recommends that the ATO:

- (a) improves its PAYGW and SG risk identification process by analysing the utility of data from third party referrals with a view to maximising the use of sources which yield the best results;*
- (b) improves its SG risk identification process by:*
 - i) encouraging trustees of APRA-regulated superannuation funds to refer more relevant data; and*
 - ii) obtaining SuperStream payment data from superannuation funds for employers not required to use STP to promptly identify those not reporting or paying SG.*

RECOMMENDATION 4.2

The IGT recommends the ATO seeks further means of ensuring superannuation entitlements are paid promptly including the use of deterrents, such as random audits, to curtail the propagation of non-compliance - compliant employers who undergo such audits should be reimbursed for any additional costs.

RECOMMENDATION 4.3

The IGT recommends the ATO publicly announce its areas of FBT compliance focus for future year(s).

RECOMMENDATION 4.4

The IGT recommends the ATO supplement the principles contained in its 'Our approach to information gathering' booklet with practical guidance, such as common scenarios in training materials, to assist compliance staff to apply them in the context of an employer obligation audit or review.

RECOMMENDATION 4.5

The IGT recommends the ATO enhance its capability development framework and compliance support tools with respect to employer obligations and Personal Services Income compliance activities by:

- (a) improving the relevant training packages on the employee/contractor distinction;*
- (b) ensuring that staff are assessed following completion of relevant training packages;*
- (c) monitoring the results of quality assessments over time to identify recurring capability issues with a view to improving training and procedures; and*
- (d) improving the documentation in the 'reasons for decision' templates, by requiring an appropriate assessment of the application of the law to the facts of the case.*

RECOMMENDATION 4.6

The IGT recommends the ATO increase employers' awareness of its differentiated approach to non-compliance with SG obligations and assess the utility of this approach by analysing the results obtained from measuring its effectiveness.

CHAPTER 1—BACKGROUND

CONDUCT OF REVIEW

1.1 The Inspector-General of Taxation's (IGT) review into the Australian Taxation Office's (ATO) employer obligations compliance activities was undertaken in response to concerns raised by stakeholders during public consultation for the IGT's work program. These concerns related to complexity and uncertainty for businesses entering into contracts 'of', or 'for' services, and those providing the services being employees or independent contractors ('contractors') respectively (henceforth, both will be referred to as 'workers'). The then Minister for Small Business, the Hon. Bruce Billson MP, also expressed his support at the time for the investigation of these concerns which reflected the Government's policy focus on reducing the compliance burden particularly for small businesses.¹

1.2 The tax complaints handling function was transferred to the IGT from the Commonwealth Ombudsman on 1 May 2015. Work on this review did not commence in earnest until after this function was developed and operating smoothly. In the intervening period, given the Government's focus on small business,² a number of other agencies undertook work on various aspects of employer obligations and, accordingly, this review builds on their findings.

1.3 The report of this review is produced pursuant to paragraph 7(1)(f) of the *Inspector-General of Taxation Act 2003*.

1.4 The IGT invited and received submissions to this review from employers, workers and tax practitioners, as well as union and superannuation fund representatives. Submissions were also received from professional and industry bodies. The IGT also met with key stakeholders to gain a better understanding of the issues and identify the areas that required improvement. The concerns raised in submissions may be summarised into the following themes:

- the lack of a clear distinction between employees and contractors and the unnecessary associated costs (discussed in Chapter 2);
- the costs of compliance for employers, more generally, including various record keeping or reporting requirements under the Fringe Benefits Tax (FBT) regime, the Taxable Payments Reporting System (TPRS) and Business Activity Statements (BAS) as well as adopting new initiatives such as Single Touch Payroll (STP) and the Small Business Superannuation Clearing House (SBSCH) (discussed in Chapter 3);

1 Bruce Billson communication to the IGT, 19 March 2016, p 1.

2 Bruce Billson, 'Reducing red tape burdens for small business' (Media release, 22 October 2014).

- unnecessary expansion of ATO employer obligations compliance activities, inadequate use of third party data, insufficient compliance activities to create a level playing field, untargeted information requests and lack of technical expertise (discussed in Chapter 4); and
- the punitive nature of the Superannuation Guarantee Charge (SGC) rules (discussed in Chapter 4).

1.5 The IGT has also worked progressively with ATO senior management to distil potential areas for examination and to agree on specific improvements. This work has been informed by IGT review team discussions with ATO staff across a range of business units. The IGT review team also examined various ATO systems, processes and procedures to better understand concerns in this area and analysed ATO statistics which related to ATO performance and its impact on the above issues.

1.6 Before exploring the above concerns specifically, it is helpful to have an appreciation of the Australian workplace relations framework and some of the latest reviews that have been conducted in this area.

WORKPLACE RELATIONS FRAMEWORK

1.7 The relationship between businesses and workers is generally governed by contracts which set out the terms and conditions agreed by both parties. Where the contract establishes an employer/employee relationship, various laws import additional obligations on the parties. For example, such laws may impose obligations which regulate working conditions, restrict working hours, set minimum wages and set mechanisms to resolve disputes.³ A key piece of legislation in this regard is the Commonwealth *Fair Work Act 2009* which is largely mirrored in state-based laws that may still have some application.⁴

1.8 The Fair Work Commission (FWC), the Fair Work Ombudsman (FWO) and Fair Work Building and Construction agency are the key national regulators of workplace relations in Australia.⁵ Ultimately, workplace disputes are dealt with by the Fair Work Federal Division of the Federal Court of Australia and the Federal Circuit Court.⁶

3 Daniel Blackburn, 'The Role, Impact and Future of Labour Law' in International Labour Organization (ILO), 'Labour Law: Its Role, Trends and Potential' (Labour Education 2006/2-3, No. 143-144) p 1.

4 *Australian Constitution* s 109 provides that when a law of a state is inconsistent with a law of the Commonwealth, the latter shall prevail, while the Fair Work Act 2009 s 27 outlines the particular state based law (Anti-Discrimination Acts and Equal Opportunity Acts) that still applies in certain states and territories.

5 The FWO promotes workplace relations. The FWC is the national tribunal which sets minimum wages and conditions, regulates industrial action and resolves workplace disputes amongst other things. Fair Work Building and Construction is a specialist agency which promotes workplace relations in the building industry.

6 Productivity Commission, *Workplace Relations Framework Productivity Commission Inquiry Report*, Volume 1, No. 76 (30 November 2015) p 76 <<http://www.pc.gov.au>>.

1.9 There are also various other institutions, such as state and territory work safety regulators, anti-discrimination bodies and the Australian Competition and Consumer Commission, which have specialist roles.⁷

1.10 Furthermore, the *Fair Entitlement Guarantee Act 2012* established the government-funded Fair Entitlements Guarantee scheme (FEG). Where certain employee pay and leave entitlements are lost as a result of employer insolvency, the FEG pays these entitlements subject to certain limits. The FEG, however, does not provide protection for unpaid superannuation.⁸

1.11 Many aspects of the workplace relations framework are not intended to apply to workers who are engaged by businesses as contractors. For example, most of the protections provided under the *Fair Work Act 2009* do not extend to contractors unless specifically agreed between the parties. Indeed, the sham contracting provisions of the *Fair Work Act 2009* focus on protecting workers by making it illegal for a business to disguise an employment relationship as one of engaging a contractor or to threaten or mislead employees into changing their status to contractors.⁹

1.12 The rights and entitlements of contractors are separately protected by other legislation – primarily the *Independent Contractors Act 2006* and *Independent Contractors Regulations 2007*. For example, an application may be made to the Courts to consider whether a contract is unfair or harsh,¹⁰ and may consider factors such as the bargaining positions of the parties, whether undue influence or unfair tactics were used, and whether the total remuneration is less than that for an employee performing similar work.¹¹

1.13 The misclassification of workers has flow on effects which may lead to businesses and workers not fulfilling their respective legal obligations. This is discussed in the sections below.

EMPLOYEES AND CONTRACTORS

1.14 Under common law, an employee generally enters into a contract to provide labour, a ‘contract of service’, whereas a contractor is engaged through a ‘contract for services’ to achieve a specific result.¹²

7 Ibid.

8 Unpaid superannuation is a ‘tax’ (via the SGC) which is subject to the recovery powers available to the ATO.

9 Department of Industry, Innovation and Science, *Australian Government independent contractor laws*, <<http://www.industry.gov.au>>.

10 *Independent Contractors Act 2006*, s 12.

11 Department of Industry, Innovation, and Science, *Independent contractors – Contracts* <<http://www.industry.gov.au>>.

12 *Commissioner of Payroll Tax (Vic) v. Mary Kay Cosmetics Pty Ltd* (1982) 82 ATC 4444, per Gray J.

1.15 The ATO has published guidance on its interpretation of the common law meaning of employee in Taxation Ruling TR 2005/16. The ruling explains that there is no single factor which is determinative of the relationship. Rather, the totality of the relationship between the parties must be considered to determine whether, on balance, the worker is an employee or a contractor. While there is no exhaustive list of factors, some of the key factors for consideration are:

- the terms and the circumstances of the formation of the contract;
- the degree of control that the payer can exercise over the worker;
- whether the worker operates their own business or within the business of the payer;
- whether the substance of the contract is to achieve a specified result;
- the ability to delegate or subcontract;
- the risk borne; and
- the provision of tools and equipment.¹³

1.16 It should be noted that there are a number of federal and state legislative provisions that contain exclusions or inclusions to the common law definition for the purposes of establishing various employer obligations. For example, the definition is extended to include a person who '*works under a contract that is wholly or principally for the labour of the person*' for Superannuation Guarantee (SG) purposes.¹⁴ Similarly, at a state level the definition differs and is expanded for workers' compensation across most states.¹⁵

1.17 As a result of the above variations, there is no uniform definition that applies federally and in all states for all employer obligations. Thus, to determine their precise obligations as employers, businesses need to determine the status of each worker by considering each definition in the applicable legislation.

REGULATORY OBLIGATIONS FOR ENGAGING WORKERS

1.18 In addition to setting a minimum standard for working conditions, the employment relationship has been used by governments as a basis to identify which party bears the legal responsibility for fulfilling obligations which promote social policies. For example, responsibility for workers' compensation, payroll tax, income tax withholding, and superannuation are all based on the classification of a worker. The key obligations are set out below. In complying with these obligations, employers must also deal with state and federal regulators.

13 ATO, *Income tax: Pay As You Go - withholding from payments to employees*, TR 2005/16 (2005).

14 *Superannuation Guarantee (Administration) Act 1992* (SGAA) s 12.

15 For example, *Workers' Compensation and Rehabilitation Act 2003* (Qld) s 11 extends the definition of employee to include or exclude workers in particular circumstances.

Non-tax obligations

1.19 Under the current workplace relations system explained earlier, employers are required to comply with the National Employment Standards, navigate various awards and agreements set by the FWC, issue payslips and keep appropriate records.

1.20 In addition to the above, state legislation may prescribe requirements for employers to have a level of workers' compensation commensurate to the risks faced in their industry. Workers' compensation is compulsory for employers in every state and territory except New South Wales (NSW), Victoria, and South Australia, where the requirement is subject to relatively low thresholds of wages paid.

1.21 Other legislation which impose further obligations on employers include both federal and state work health and safety legislation which require employers to maintain a suitable, safe working environment and facilities. For example, the Model Work Health and Safety Act¹⁶ places a primary duty of care on a person conducting a business to ensure, so far as is reasonably practicable, the health and safety of workers engaged, including providing the necessary information, training, instruction, and supervision.¹⁷

State tax obligations

1.22 Employers are required to register for state-based payroll taxes when total Australian wages exceeds certain thresholds. These thresholds differ depending on the state in question and are pro-rated where businesses employ workers in multiple states. While the threshold applies to total Australian wages, the tax is levied on the wages for a particular state or territory and can only be taxed in one jurisdiction.

1.23 Wages include any remuneration paid or payable by an employer to an employee for services provided with the payroll threshold applying to the total Australian wages for all grouped businesses.¹⁸

1.24 Unlike workers' compensation discussed above, the payroll tax registration thresholds are large enough to remove the requirement for a significant number of employers. The state with the lowest threshold is Victoria, which requires registration when total Australian wages exceeds \$45,833 a month or \$550,000 over a financial year.¹⁹

16 The Model Work Health and Safety (WHS) Act forms the basis of the WHS Acts being enacted across Australia to harmonise work health and safety law.

17 *Work Health and Safety Act 2010* s 19.

18 Grouped businesses include those that: (1) are defined as corporations that meet the definition of related companies provided in the *Corporations Act 2001* (2) use common employees (3) are commonly controlled; and (4) are subsumed, meaning two or more smaller groups form a larger group via a common member, or members of a group together have a controlling interest in another business.

19 *Payroll Tax Act 2007* (Vic), sch 1.

Federal tax and superannuation obligations

1.25 In addition to their own tax obligations such as income tax, capital gains tax, Goods and Services Tax (GST) and excise tax, employers have tax obligations with respect to their workers such as Pay As You Go Withholding (PAYGW), TPRS, SG, and the FBT.

Pay As You Go

1.26 During the Great Depression, the South Australian government introduced the Pay As You Earn (PAYE) system where employers deducted tax from their employees' pay. This system allowed income tax collection from wage earners in lower income groups which had previously been impracticable. It was also more convenient for taxpayers, created a more even flow of revenue for government and improved compliance as income was taxed at source. During the 1940s, the Federal government had expanded the PAYE system to the other states and territories.²⁰

1.27 The PAYE system was also extended by the Prescribed Payments System and Reportable Payments System which required amounts to be withheld from payments to workers beyond employees in a number of industries.

1.28 The PAYE system continued to operate until a number of systems including PAYE were replaced by the Pay As You Go (PAYG) system on 1 July 2000.²¹

1.29 The PAYG system has two branches – instalments and withholding. It is under PAYGW that employers are required to withhold and remit tax from salary, wages, commissions, bonuses or allowances for employees and amounts of payments to contractors, unless an exception applies. Furthermore, the PAYG system imposes withholding obligations which include:

- labour hire arrangements;
- work or services where it is agreed that withholding will occur;
- a supply where no Australian Business Number (ABN) has been quoted;
- departing Australia superannuation payments;
- payments to foreign residents;
- payments of alienated Personal Services Income (PSI); and
- non-cash benefits.²²

20 Sam Reinhardt and Lee Steel, 'A Brief History of Australia's Tax System' (22nd APEC Finance Ministers' Technical Working Group, Khanh Hoa, Vietnam, 15 June 2006) p 14.

21 The removal of these systems included the Prescribed Payments System and Reportable Payments System.

22 *Taxation Administration Act 1953 (TAA)* sch 1 s 12.

1.30 There is no requirement for payers to withhold where a contractor quotes a correct ABN but where an incorrect or no ABN is quoted, the payer must withhold at the highest marginal rate, comparable to an employee not providing their Tax File Number (TFN). Contractors who provide their ABN to the payer may still enter a voluntary agreement for the payer to withhold amounts from relevant payments. In this regard, where the payer would be entitled to a full GST credit, no GST is charged by the payer to align it to the tax treatment of an employee.

Taxable Payments Reporting System

1.31 The first notion of a reporting framework for workers beyond employees was the Reportable Payments System which applied to certain industries. This system was repealed and replaced by the PAYG system on 1 July 2000 as mentioned above.

1.32 To improve compliance with taxation obligations by contractors, the TPRS²³ was introduced on 1 July 2012, requiring businesses in the building and construction industry to annually report payments to contractors in that industry.²⁴ This report is called the Taxable payments annual report (TPAR) which was previously due on 21 July of each year. Concerns were raised that the closeness of this date to year-end was too onerous for businesses. As a result, from the 2014-15 financial year onwards the due date has been aligned to the quarterly activity statement lodgement date of 28 August.²⁵

Superannuation

1.33 Australia's retirement income system consists of three pillars: the Age Pension, the compulsory SG and voluntary private savings.²⁶

1.34 In 1900, NSW introduced a means tested age pension funded from general revenue. Victoria and Queensland introduced similar schemes shortly thereafter.²⁷

1.35 At Federation in 1901, the *Australian Constitution* gave the Commonwealth explicit power to legislate for the provision of old age and invalid pensions. The *Invalid and Old Age Pensions Act 1908* was subsequently enacted, and the Age Pension was introduced in 1909 to provide basic income support for Australians in retirement.

23 A legislative requirement under the TAA sch 1 s 405-10, and the *Taxation Administration Regulations 1976* reg 64.

24 Building and construction services is defined broadly and includes a number of specific activities if they are performed on, or in relation to, any part of a building, structure, works, surface or sub-surface: *Taxation Administration Regulations 1976* reg 64.

25 ATO, *Taxable payments annual report*, (1 July 2016) <<https://www.ato.gov.au>>; TAA 1953 s 405-10(4).

26 Commonwealth, *Australia's future tax system – Retirement income consultation paper*, (December 2008) p 4.

27 Leslie Nielson and Barbara Harris, Economics Section, Parliament of Australia, 'Chronology of superannuation and retirement income in Australia' (1 June 2010) <<http://www.aph.gov.au>>; Department of the Treasury, 'Towards higher retirement incomes for Australians: a history of the Australian retirement system since Federation' (Economic Roundup Centenary Edition, 2001) p 67.

1.36 To be eligible for the Age Pension an individual must be an Australian resident who is older than the qualifying age, and meet an income and assets test.

1.37 The Age Pension is the largest Commonwealth spend and has risen significantly. In 2000, it cost the Commonwealth \$14 billion,²⁸ which increased to \$20 billion in 2006²⁹ and \$42 billion in 2015.³⁰ The cost is expected to rise at seven per cent each year.³¹

1.38 Between 1923 and 1939, there were two attempts to introduce a universal contributory national superannuation or insurance scheme to address the growing cost of the Age Pension. However, these proposals failed due to concerns, including further increasing the cost of labour, unemployment, the onset of World War II and difficulties in achieving fairness.

1.39 In the 1950s, the requirements for the Age Pension were relaxed and superannuation acted as a supplement to the pension.

1.40 As agreed under the Prices and Incomes Accord negotiated in 1985 (and the negotiation of Accord Mark II), Award superannuation was introduced in 1986. However, superannuation was still largely considered an employment fringe benefit until mandatory superannuation was introduced in 1992.³² The greatest change to superannuation since this time has been the manner in which it is taxed to reduce inequality.

1.41 In January 2015, changes to the SGC were announced to align the penalties under the *Superannuation Guarantee (Administration) Act 1992* (SGAA) with the administrative penalties under the *Taxation Administration Act 1953* (TAA), as well as to amend the non-deductibility of the SGC. However, these changes lapsed on 17 April 2016 when Parliament was prorogued.³³

1.42 Under the SGAA, employers are required to make quarterly superannuation contributions to the fund of choice of all eligible employees unless the employee or payments made to them are excluded. The current minimum superannuation contribution for eligible employees is 9.5 per cent of 'ordinary time earnings'.

1.43 Where employers do not pay the correct level of SG they become liable for the SGC, which, unlike SG contributions, is not tax deductible. SGC is composed of the SG shortfall, interest of 10 per cent per annum and an administration fee of \$20 per employee per quarter.

28 Australian National Audit Office (ANAO), *Assessment of New Claims for the Age Pension by Centrelink* p 13 <<https://www.anao.gov.au>>.

29 Department of Families, Community Services and Indigenous Affairs, *Annual Report*, 2005-06, Table 2.22, <<http://resources.fahcsia.gov.au>>.

30 Department of Human Services (DHS), *Annual Report*, 2014-15, p 22 <<https://www.humanservices.gov.au>>.

31 National Commission of Audit, *Towards Responsible Government*, (February 2014) p 80 <<http://www.ncoa.gov.au>>.

32 Department of the Treasury, *Towards higher retirement incomes for Australians: a history of the Australian retirement system since Federation* (Economic Roundup Centenary Edition, 2001) pp 74-6.

33 Parliament of Australia, *Treasury Legislation Amendment (Repeal Day 2015) Bill 2016*, (17 April 2016) <<http://parlinfo.aph.gov.au>>.

1.44 There is no requirement for contractors to make compulsory superannuation payments on behalf of themselves. Contractors may make personal contributions and claim a full deduction, subject to certain conditions.³⁴

Fringe Benefits Tax

1.45 Fringe benefits³⁵ were previously taxable in Australia in the hands of the recipient. This was the case since the inception of the Federal income tax. Due to the difficulties in determining the value of fringe benefits and for a range of other administrative and related reasons, there was believed to be widespread non-compliance.³⁶

1.46 The level of non-compliance and the growing trend of remunerating employees with non-cash business benefits during the 1980s, led to the explicit taxation of fringe benefits under the *Fringe Benefits Tax Assessment Act 1986* (FBTAA).

1.47 FBT is levied on employers, rather than employees, as it was believed to simplify compliance and administration.³⁷ As a result employers became responsible for reporting benefits. This presented challenges for employers as determining eligibility for various tax offsets and benefits requires consideration at the employee level.

1.48 Under the FBTAA employers are required to pay FBT on all fringe benefits, unless they are exempt benefits. There are 12 categories of fringe benefits, each with their own definition and calculation methodology.³⁸ The FBT year runs from 1 April to 31 March.

1.49 Where an employee receives fringe benefits above \$2,000, the employer must record the grossed-up taxable value of fringe benefits, unless they are excluded fringe benefits, and report it on an employee's individual payment summary which is due on 14 July.³⁹

1.50 Where a worker is not an employee, the non-cash benefits that they received are not subject to the FBT. Instead the benefits are considered part of their non-cash remuneration, the market value of which is included in their assessable income.⁴⁰

34 ATO, *Claiming deductions for personal super contributions* (21 December 2015) <<https://www.ato.gov.au>>.

35 FBT is a tax payable by employers on the value of certain benefits (fringe benefits) that have been provided to their employees or to associates of those employees in relation to their employment. Fringe benefits include indirect, non-cash benefits provided to employees in addition to wages or salary, such as private use of a work vehicle, entertainment, discounted loans or the payment of private health insurance.

36 Australian Government, *Reform of the Australian Tax System: Draft White Paper* (Australian Government Publishing Service, Canberra, 1985) in Sam Reinhardt and Lee Steel, 'A Brief History of Australia's Tax System', above n 20, p 12.

37 Sam Reinhardt and Lee Steel, 'A Brief History of Australia's Tax System', above n 20, p 12.

38 ATO, *1.4 Types of fringe benefits* (18 January 2012) <<https://www.ato.gov.au>>.

39 ATO, *Reportable fringe benefits* (23 January 2015) <<https://www.ato.gov.au>>.

40 TAA Sch 1 s 14-5.

Personal Services Income

1.51 Whilst not an 'employer obligation', the PSI rules aim to address situations where 'contractors' provide labour which would otherwise be characterised as an employer/employee relationship.

1.52 The 1999 Review of Business Taxation (the Ralph Report) noted a significant and accelerating trend for employees to move out of simple employment relationships and become unincorporated contractors or owner-managers of incorporated companies without changing the nature of the employer-employee relationship. Such interposed entities were used to increase claims for work-related tax deductions and income allocation.⁴¹

1.53 In response, the then Government introduced the alienation of PSI legislation⁴² which was effective from 1 July 2000. These rules operate to tax income earned from personal services as if they were earned by employees in appropriate cases.

1.54 The interaction of the employee/contractor distinction and the PSI rules is explained in Taxation Ruling TR 2005/16:

62. Whether or not an individual is subject to the personal services income measures is distinct from and separate to the determination of whether that individual is an employee...

63. However, it is recognised that there is some overlap between the tests used to determine whether a personal services business exists, and the common law tests used to distinguish independent contractors and employees. (For example, a 'results test' is common to both.)⁴³

Reporting and paying employer obligations

Single Touch Payroll

1.55 On 28 December 2014, a proposal was announced to 'cut red tape' for employers by 'simplifying tax and superannuation reporting obligations through STP' from July 2016 subject to consultation with businesses.⁴⁴

1.56 Employers, who will be required to comply with STP, will incur certain set-up costs. They will be required to acquire new software, upgrade their existing accounting software or utilise the service of an intermediary such as an external payroll company to automatically report PAYGW and SG information to the ATO

41 Review of Business Taxation (Ralph Review), *A Tax System Redesigned*, July 1999, p 288.

42 *Income Tax Assessment Act 1997* Part 2-42, as inserted by *New Business Tax System (Alienation of Personal Services Income) Act 2000*.

43 ATO, TR 2005/16, above n 13, pp 14-5.

44 Josh Frydenberg, 'Cutting red tape for employers through Single Touch Payroll' (Media release, 28 December 2014).

every payroll cycle.⁴⁵ Employers will still be required to calculate and report other tax obligations to the ATO via activity statements but they will no longer have to produce annual payment summaries for employees for data reported through STP, provide a payment summary annual report to the ATO or lodge an activity statement for ‘in scope’ PAYGW obligations.⁴⁶ In addition, TFN declarations and superannuation standard choice forms will be provided digitally to simplify the process of bringing on new employees.⁴⁷

1.57 The due dates for payment for PAYGW to the ATO and SG to the respective superannuation funds will not change and will be based on the existing thresholds and legislative deadlines.⁴⁸

1.58 Consultation in early 2015 examined the potential for employers to ‘remit PAYGW and SG amounts at the same time employees are paid their salary and wages’. The ‘support [that] businesses may require to enable such a transformation’ was also considered.⁴⁹

1.59 After initial feedback, it was acknowledged that ‘a start date of July 2016 [would] not be achievable for many businesses’ and that ‘the cash flow implications for business of real time payments’ would present a challenge. As a result, the consultation was to proceed based on ‘real time reporting and real time voluntary payment as an option’. This means that employers will not be required to make the corresponding PAYGW and SG payments in accordance with the payroll cycle.⁵⁰

1.60 During April and May 2016, the Treasury and the ATO consulted with software developers, financial institutions and clearing houses on the design of STP to help inform law design and drafting.⁵¹

1.61 On 31 August 2016, the *Budget Savings (Omnibus) Bill 2016* was introduced to Parliament and proposed to amend the TAA to facilitate the requirement for STP reporting.⁵² It was subsequently enacted into law (STP Legislation) on 16 September 2016.⁵³ The Explanatory Memorandum⁵⁴ to the STP legislation outlines the design of STP and its intended implementation in three phases.

1.62 Phase one involves a pilot and mandatory real time reporting of PAYGW and SG along with voluntary real time payment. The pilot will be conducted from late 2016 with approximately 400 small employers with less than 20 employees⁵⁵ as well as

45 ATO, *Single Touch Payroll Blueprint v1.3* (internal ATO document, July 2015) p 10.

46 The Treasury, Regulation Impact Statement (RIS), *Single Touch Payroll* (October 2015) p 13; ATO, *STP Blueprint*, above n 45, p 10.

47 Josh Frydenberg, ‘Cutting red tape through STP’, above n 44.

48 ATO, *STP Blueprint*, above n 45, p 13.

49 Josh Frydenberg, ‘Cutting red tape through STP’, above n 44.

50 Bruce Bilson, ‘Government moves to get Single Touch Payroll right’ (Media release, 10 June 2015).

51 ATO, *Single Touch Payroll, Design consultation workshops* (May 2016) <<http://softwaredevelopers.ato.gov.au>>.

52 Parliament of Australia, *Budget Savings (Omnibus) Bill 2016*, (31 Aug 2016) <<http://parlinfo.aph.gov.au>>.

53 *Budget Savings (Omnibus) Act 2016*.

54 House of Representatives, Revised Explanatory Memorandum, *Budget Savings (Omnibus) Bill 2016*, p 283.

55 ATO, *Single Touch Payroll – Small Business Pilot Engagement Strategy* (July 2016) p 7.

employers with 20 or more employees who wish to participate.⁵⁶ The pilot is intended to include different industries and sizes including paper and electronic lodgers.⁵⁷

1.63 The main purpose of the pilot is to ascertain the level of 'deregulation benefits' for the 710,000 small employers who have less than 20 employees and 'test support and education tools'.⁵⁸ Following the pilot, the Government will make a decision, by the end of the 2017 calendar year,⁵⁹ as to whether employers with less than 20 employees will be required to comply with STP.⁶⁰

1.64 Another aspect of phase one is that all employers can voluntarily commence STP reporting from 1 July 2017. The legal requirement for the use of STP for employers with 20 or more employees will take effect from 1 July 2018.⁶¹

1.65 Phase two involves sharing the payroll and employment data with other federal government agencies and phase three will extend the collection and sharing of payroll and employment data with the states and territories.⁶²

1.66 Following the introduction of the Bill in Parliament, the ATO issued a consultation paper on the administrative aspects of STP including the circumstances for exemption from STP requirements.⁶³ At the time of writing, this consultation is ongoing.

SuperStream

1.67 SuperStream was introduced as a means to increase efficiency by requiring employers and superannuation funds to transact using a standard electronic format which links data with payments. From 1 July 2016, with limited exemption, all employers will have to comply with SuperStream, however, the ATO provided flexibility in its compliance approach until 28 October 2016 for small employers that were not yet SuperStream ready.⁶⁴

1.68 Compliance with SuperStream is separate from compliance with the SG regime. A decision on whether an employer is liable for SGC does not consider whether payments are SuperStream compliant.

56 ATO, 'Single Touch Payroll Program Phase 1' (Paper presented at the Business Engagement Forum, Sydney, 23 March 2016) p 4.

57 ATO, 'Single Touch Payroll – Business Pilot Project Overview' (internal ATO document) p 3.

58 ATO, *STP design workshops*, above n 51 <<http://softwaredevelopers.ato.gov.au>>.

59 The Treasury, RIS, *STP*, above n 46, p 39.

60 ATO, *STP Pilot Project Overview*, above n 57, pp 2-3.

61 *Budget Savings (Omnibus) Act 2016* sch 23, div 3, item 22.

62 The Treasury, RIS, *STP*, above n 46, p 29.

63 ATO, *Single Touch Payroll: ATO consultation paper* (1 September 2016) <<https://www.ato.gov.au>>.

64 ATO, 'Flexibility for small business to become SuperStream compliant' (Media release, 22 June 2016).

Small Business Superannuation Clearing House

1.69 On 1 July 2010, the Government released the SBSCH as a free digital service to help employers pay SG contributions to their employees' various superannuation funds and reduce time and paperwork associated with making SG contributions.

1.70 The SBSCH is an approved clearing house under the *Superannuation Guarantee (Administration) Regulations 1993*. Quarterly payments made by employers to SBSCH are treated as contributions to a complying superannuation fund.⁶⁵

1.71 Access to the SBSCH was originally limited to small employers with less than 20 employees, but, from 1 July 2015, it has been expanded to employers with an aggregated turnover below \$2 million.⁶⁶

1.72 The SBSCH is one of a number of options available to employers to help them pay SG and which meet the SuperStream requirements. Other options include the use of employer's default superannuation fund portal, commercial clearing houses and payroll bureaus.⁶⁷ The SBSCH takes all the data and payment from the employer and distributes the data and monies to the relevant superannuation funds.

1.73 While the Department of Human Services (DHS) owns the infrastructure of the SBSCH, the administration of the SBSCH moved from the DHS to the ATO after the 2013-14 Federal Budget.⁶⁸

1.74 Statistics provided by the ATO show the user profiles of employers who use the SBSCH:

- At the end of April 2016, there were 176,617 employers registered (with over 1.4 million employees) of which 76 per cent were active users as at February 2016;⁶⁹
- The ATO estimates that there are approximately an additional 120,000 employers that may be potential users of the SBSCH who are yet to begin using a SuperStream compliant solution to make SG contributions;
- SBSCH profiling statistics dated 7 March 2015 show that the two main industries for active employers are 'construction' and 'professional/scientific and technical services'; and
- 62 per cent of active employers had payroll software known to the ATO.⁷⁰

65 *Superannuation Guarantee (Administration) Regulations 1993* s 7AE and SGAA 1992 s 23B, s 79A.

66 ATO, *Using the Small Business Superannuation Clearing House* (11 July 2016) <<https://www.ato.gov.au>>.

67 ATO, *Employer SuperStream FAQs* (22 Jun 2016) <<https://www.ato.gov.au>>.

68 The Commonwealth of Australia, 'Mid-Year Economic and Fiscal Outlook 2013-14' (December 2013) p 192.

69 114,000 of the 150,000 registered users as at February 2016.

70 ATO communication to the IGT, 9 March 2016.

OTHER REPORTS

1.75 As mentioned at the outset of this chapter, other reports have been published which are relevant to aspects of employers' tax and superannuation obligations. The relevant aspects of these reports are outlined below.

Parliamentary Committee Inquiry into Barriers for Small Business Employment

1.76 In March 2016, the House of Representatives Standing Committee on Education and Employment published its report, *Getting small business booming*.⁷¹

1.77 The inquiry acknowledges the current initiatives to support small businesses and identifies additional opportunities to improve the regulatory system and reduce barriers to employment by:

- further cutting red tape;
- defining the difference between an employee and a contractor; and
- reducing the costs involved in taking on an employee, and lessening the states' reliance on payroll tax.

1.78 The report made a number of recommendations. Those relevant to the ATO include the ATO and the FWO setting up a working group to:

- align the definitions of employee and contractor across government agencies;
- develop a single employee or contractor decision tool;
- identify any legislative changes needed; and
- consider proposals advocating for a register of building contractors.

Parliamentary Committee Inquiry into Insolvency in the Australian construction industry

1.79 In December 2015, the Senate Standing Committee on Economics published a report of their inquiry into insolvency in the Australian construction industry.⁷²

1.80 The report noted that businesses in the industry often experience financial distress which increases the likelihood of insolvency. The structure of the industry has created an environment in which non-payment for work carried out is common place

71 Standing Committee on Education and Employment, Parliament of Australia, *Getting business booming, Report on the inquiry into barriers for small business employment* (March 2016).

72 Economics References Committee, Parliament of Australia, *'I just want to be paid' Insolvency in the Australian construction industry* (December 2015).

and businesses lower down in the subcontracting chain have little power relative to those at the top.

1.81 The report also noted the prevalence of deliberate phoenix arrangements, particularly by property developers, which are hard to detect. This makes it difficult for regulators like the ATO to clamp down on these types of activities. High rates of insolvency present challenges, including unpaid employee entitlements (such as SG) and tax debts (such as GST and PAYG).

1.82 The report made a number of recommendations. Those relevant to this review include that the ATO:

- increase cooperation with superannuation funds to enable early detection of non-payment of SG, which may be signs of deeper cash-flow problems, a precursor to insolvency and linked to illegal phoenix activity; and
- actively monitor the tax liabilities of businesses in the construction industry in order to ensure debts owed to the Commonwealth are paid to prevent the accumulation of unrecoverable debts.

Review of Tax Impediments Facing Small Business

1.83 In August 2014, the Board of Taxation (BoT) published a report into their *Review of Tax Impediments Facing Small Business*.⁷³ The review identifies and recommends key reform priorities with the aim of reducing tax impediments facing small business and focusing on simplification and deregulation. The recommendations sought to achieve this by:

- the ATO reviewing its guidance and tools pertaining to various issues including carrying on an enterprise, PSI, the employee/contractor distinction, and transfer pricing;
- simplifying and reducing the frequency of reporting requirements for small business;
- analysing the effectiveness of the TPRS and aligning the reporting date with the 28 August BAS lodgement date;
- increasing the small business entity turnover threshold;
- assessing superannuation obligations against a quarterly threshold;
- redesigning the reporting, non-deductibility and calculation of the SGC, and replacing the penalties and administration charges with the administrative penalties regime provided under the TAA; and
- raising the minor and infrequent threshold for the FBT and investigating the possibility of aligning the FBT year to the income tax year.

⁷³ BoT, *Review of Tax Impediments Facing Small Business* (2013).

Small Business Fix-it Squad

1.84 The Small Business Fix-it Squad (SBFS) is a joint agency initiative which involves small business owners working with federal, state and local government regulators and intermediaries on projects to identify and consider options for improving the broader operating environment for small businesses.⁷⁴

1.85 One SBFS project was *Taking on an employee – making decisions and reducing red tape*. It involved a survey of small business owners⁷⁵ that found there was limited:

- satisfaction with the process of taking on a new employee including the various awards and associated government regulations;
- awareness and usage of products and services available to help businesses; and
- use of electronic payroll systems.⁷⁶

1.86 To address the above findings, the project group recommended:

- a whole-of-government checklist for information about employer requirements – this was released in February 2016 on business.gov.au titled 'Taking on an employee checklist';⁷⁷
- a whole-of-government employee/contractor decision tool and a targeted multi-media awareness strategy, initially by improving the ATO tool, then assessing the next steps; and
- a tool that helps determine the tax and superannuation that applies to entitlements – this was released in February 2016 on the ATO web page titled 'Work out tax to withhold and super to pay'.⁷⁸

Promoting Compliance with Superannuation Guarantee Obligations

1.87 In June 2015, the Australian National Audit Office (ANAO) published a report of its performance audit of the ATO with respect to SG.⁷⁹

1.88 The objective of the audit was to assess the effectiveness of the ATO's activities to promote employer compliance with SG obligations. The audit identified

74 Office of the Australian Small Business Commissioner, *Working together to help small business* (20 October 2014) <www.asbc.gov.au>.

75 Of the 2865 businesses the survey was delivered to, 381 commenced the survey and 320 completed the survey.

76 Corporate Research Centre: Community insights and solutions, *Small Business Fix-It Squad Survey*, ATO (June 2015) p 3.

77 Department of Industry, Innovation and Science, *Taking on an employee checklist* (18 July 2016) [Business.gov.au](http://business.gov.au) <<https://www.business.gov.au>>.

78 ATO, *Work out tax to withhold and super to pay* (30 May 2016) <<https://www.ato.gov.au>>.

79 ANAO, *Promoting Compliance with Superannuation Guarantee Obligations*, Audit report No.39 2014–15 (June 2015).

the administrative complexity of the SG scheme as a driver of non-compliance, particularly with small businesses.

1.89 The audit found that overall the ATO's administration of the SG scheme has been effective, however, a greater understanding of the levels of non-compliance with SG obligations across industry sectors and types of employers is required to more effectively promote employer compliance. The audit found that while the ATO has conducted an evaluation of the effectiveness of its SG compliance strategy at regular intervals, it was not sufficiently robust to enable a reliable assessment.

Regulator Engagement with Small Business

1.90 In September 2013, the Productivity Commission published its research report, entitled: *Regulator Engagement with Small Business*.⁸⁰ The objective of the report was to benchmark regulator approaches to engagement with small business in order to improve the delivery of services whilst reducing unnecessary compliance costs.

1.91 The report made a number of recommendations which are relevant to aspects of this review. These include:

- clear guidance on enforcement priorities particularly where there are short-term resource constraints;
- risk-based approaches be adopted and made known to businesses;
- different treatment be considered for small businesses where it enhances the net benefits to the community;
- the diversity of small businesses should be considered so that information and advice is brief, in user-friendly language and readily available through multiple channels;
- measures be adopted to improve the timeliness of regulatory activities, such as tracking of referrals to other agencies; and
- ensure transparency and accountability in decision making, providing reasons for those decisions.

Administration of the Taxation of Personal Services Income

1.92 On 15 October 2013, the ANAO published a report of its performance audit with respect to the ATO's administration of the PSI rules.⁸¹ The audit assessed the effectiveness of the ATO's administration of the PSI regime including its governance arrangements, systems and processes as well as compliance strategies.

1.93 The ANAO found that PSI comprised a small proportion of the overall activity of the ATO with the program of compliance activities evolving to promote

80 Productivity Commission, *Regulator Engagement with Small Business*, Research Report (September 2013).

81 ANAO, *Administration of the Taxation of Personal Services Income*, Audit Report No.5 2013–14 (October 2013).

voluntary compliance with the rules. However, the report noted that the ATO could better attempt to quantify the net revenue impact of the PSI rules and the population of taxpayers that do not declare PSI. The ANAO recommended that a methodology be developed to estimate the magnitude of the potential revenue at risk, providing a baseline for comparison in the future for the assessment of the effectiveness of the ATO's compliance activities.⁸²

Australia's Future Tax System Review (the Henry review)

1.94 The then Government released the *Final Report* of the Australia's Future Tax System Review on 2 May 2010.⁸³ The review was a comprehensive examination of state and federal taxation and superannuation systems.

1.95 One of its key recommendations was that the Government should assist people to be more aware of the retirement income system so that they are better able to manage their superannuation. Strategies put forward in this regard included:

- SG contributions should be paid at the same time as wages — this was to be introduced over time and staged so businesses could adjust their cash flows;
- employers should report superannuation contributions to their employees when a contribution is made; and
- there should be a method of linking superannuation records to such client identifiers as TFNs to ease the management of individual superannuation affairs.⁸⁴

1.96 Prior to the final report, on 12 May 2009, the Review Panel released its *Retirement Income Strategic Issues Paper*.⁸⁵ The paper recommended against extending SG to the self-employed due to the diverse and varying risks and circumstances of business and entrepreneurship. However, the Review Panel stated that it wanted to consider further the treatment of contractors within the SG system.

1.97 The paper did not recommend embedding the employee/contractor distinction in legislation for superannuation as it would set an arbitrary line and allow people to arrange their affairs to remain outside SG. It also acknowledged that the definition of an employee affects issues outside of the superannuation system.⁸⁶

82 Ibid pp 17-25.

83 Australia's Future Tax System (Ken Henry, chairperson), The Treasury, *Final report: Part 1 – Overview* (AGPS, 2009).

84 Ibid p 86.

85 Australia's Future Tax System (Ken Henry, chairperson) The Treasury, *Retirement income consultation paper* (December 2008).

86 Australia's Future Tax System (Ken Henry, chairperson), The Treasury, *Final report: Part 2 - Detailed Analysis - Volume 1* (AGPS, 2009) pp 130-1.

Review into the ATO's Administration of the Superannuation Guarantee Charge

1.98 In March 2010, the IGT published his report of the review into the ATO's administration of the SGC with particular focus on employees' experiences.⁸⁷ The review found that the SG system works well for the majority of Australians, but that those most at risk are employees who are incorrectly classified as contractors or are the most vulnerable in our society.

1.99 The review made a number of recommendations, including:

- better use of information and data to estimate the level of non-compliance and impact on employees;
- improvement of the payment and information systems to allow the ATO to undertake more real time monitoring and follow-up of high risk employers;
- the ATO to engage with superannuation funds and clearing houses to obtain information to identify potential non-compliance;
- the ATO to further develop its risk identification and expand its proactive SG audit work;
- provision of appropriate and personalised letters in a timely manner to complainants about unpaid SG; and
- revision of ATO policy to impose penalties at a more meaningful level and recognise the need for appropriate remission in circumstances where the non-lodgement of SG statements was due to circumstances outside the employer's control.

Alienation of Personal Services Income Rules: Post-Implementation Review

1.100 On 16 December 2009, the BoT published a report into their post-implementation review into PSI.⁸⁸ The aim of the review was to examine the operation of the rules to determine whether the rules are achieving their desired policy outcome and consider improvements where necessary.⁸⁹

1.101 The BoT found that whilst the PSI rules had some positive impact in improving integrity and equity in the tax system, there was:

- poor compliance with the rules;

⁸⁷ IGT, *Review into the ATO's administration of the Superannuation Guarantee Charge* (March 2010).

⁸⁸ BoT, *Post Implementation Review into the Alienation of Personal Services Income Rules* (2009).

⁸⁹ *Ibid* p 6.

- uncertainty about how the rules interact with the general anti-avoidance rule;⁹⁰
- a lack of clarity around deductions that can be claimed; and
- difficulty in applying the rules, in particular application of the tests for a personal services business and the complexity of the PAYGW obligations on attribution.⁹¹

1.102 Accordingly, the BoT made a series of suggestions to improve compliance such as introducing further reporting obligations, introducing a withholding obligation on payers, imposing a GST registration requirement and clarifying the PSI rules.⁹²

Inquiry into Independent Contracting and Labour Hire Arrangements

1.103 In August 2005, The House of Representatives Standing Committee on Employment, Workplace Relations and Workforce Participation published its report into contracting and labour hire arrangements.⁹³ The terms of reference included the status, range and role of labour hire and contractor engagement, consistency across states and federal jurisdictions and strategies to ensure contract arrangements are legitimate.⁹⁴

1.104 The report noted that while there is difficulty in estimating the prevalence of contractors in the 20 years leading toward 2005, there had been growth in the overall numbers and proportions of contractors in Australia.⁹⁵

1.105 The report made a number of recommendations, including:

- maintaining the common law approach in determining employment status and legitimate contractors;
- adopting components of the alienation of PSI legislation tests when drafting legislation to identify contractors; and
- including certain protections when drafting the legislation for contractors.⁹⁶

1.106 This report led to the introduction of the *Independent Contractors Act 2006*.

90 *Income Tax Assessment Act 1936* pt IVA.

91 BoT, *Post Implementation Review of PSI*, above n 88, p 25.

92 *Ibid* pp 29-39.

93 Standing Committee on Employment, Workplace Relations and Workforce Participation, House of Representatives, *Making it work: Inquiry into independent contracting and labour hire arrangements* (August 2005).

94 *Ibid* p 2.

95 *Ibid* p 7.

96 *Ibid* p xxi.

CHAPTER 2—EMPLOYEE/CONTRACTOR DISTINCTION

SUMMARY OF STAKEHOLDER CONCERNS

Determining worker status

2.1 Many stakeholders raised concerns regarding the uncertainty employers face in determining whether a worker is an employee for specific employer obligations. First, the common law definition of employee is heavily fact-based. It is inherently ambiguous as there are no determining factors with some being more influential in the presence or absence of others.

2.2 Secondly, the common law definition is altered by different rules contained in tax and superannuation legislation. As a result, the uncertainty is heightened and the cost of compliance increased with every working relationship needing to be assessed against each of these rules. For example, courier drivers of Vabu Pty Limited were held to not be employees for SG purposes, in *Vabu Pty Limited v Federal Commissioner of Taxation*,⁹⁷ whilst, in *Hollis v Vabu*,⁹⁸ they were held to be employees for vicarious liability purposes.

2.3 Working arrangements may also change over time which may alter the classification of a worker. A common example provided by stakeholders is where a business becomes more reliant on a particular worker which may be more indicative of an employment relationship.

2.4 The costs involved in seeking professional advice on the application of the various rules may be prohibitive for businesses. Instead, businesses may seek limited or incomplete advice or none at all. For example, some stakeholders reported paying SG based on the extended definition of employee and incorrectly assumed that they were also liable to pay other employee entitlements. In other examples provided by stakeholders, it was observed that some employers may increasingly engage contractors as a way to avoid increasing professional costs as well as being liable for various employee entitlements.

2.5 Stakeholders have also raised concerns that workers may incorrectly assume that being granted an ABN automatically confirms their contractor status, particularly where they may be encouraged to apply for an ABN and be engaged as contractors by their employers.

2.6 Thirdly, where workers are misclassified, intentionally or otherwise, the ATO may after many years, apply retrospective changes to those relationships resulting in significant unplanned liabilities for businesses which may affect their ongoing viability. This may be a particularly harsh outcome for businesses where the workers in question seek to be treated as employees at the end of their engagement despite

⁹⁷ *Vabu Pty Limited v Federal Commissioner of Taxation* (1996) 95 ATC 4898.

⁹⁸ *Hollis v Vabu* (2001) 207 CLR 21.

agreeing to be treated as contractors at the outset and being compensated for managing their own superannuation and PAYG instalments (a type of 'double dipping').

2.7 A retrospective change to workers' status can also have an adverse effect on the workers where tax deductible concessional superannuation contributions become non-deductible as a result of the reclassification. The reclassification could also result in a breach of the contributions cap and liability for excess contributions tax.

2.8 Some stakeholders have also raised concerns with 'unreasonable delays' in obtaining an ABN and insufficient reasons provided for refusal. Whilst such delays and reasons may be indirectly related to whether a worker is a contractor or an employee, the eligibility for an ABN is based on whether an 'enterprise' is being undertaken. This is outside the scope of this review. However, it may be an area for future review if concerns persist.

Guidance on worker status

2.9 Many stakeholders have raised concerns with the ATO's Employee/Contractor Decision tool (ECD tool). The ECD tool is an online aid for businesses to determine whether their worker is an employee or contractor by asking them a series of questions.

2.10 Specific concerns raised with the ECD tool included that it:

- was 'overly simplistic' as it does not reflect all common law factors and does not adequately reflect different business practices or intent;
- may be geared towards finding an employer/employee relationship; and
- may be manipulated to achieve a desired outcome rather than reflecting the actual substance of an arrangement.

2.11 An example provided by stakeholders was that the ECD tool does not accommodate outcome-based contractors who are paid on an hourly basis, such as contracting bookkeepers or BAS agents who work for multiple clients. Such contractors may be considered an employee of each client under the ECD tool which is clearly a misclassification.

2.12 The ECD tool is also believed to be lacking relevant and useful links to information on other employer obligations such as state payroll and workers compensation.

2.13 Some stakeholders have also raised concern with the level of protection afforded to employers when using the ECD tool for determining PAYGW and SG obligations. They believe that there is a lack of protection against penalties where employers use the tool in good faith to determine workers' classification but the ATO later finds those classifications to be incorrect.

2.14 Stakeholders have also raised concerns that the ATO's regimes for the provision of binding advice are only available to employers and not to workers. They

have also questioned the extent to which reliance can be placed on such advice as they are heavily fact-based and the relevant facts may evolve significantly over time.

2.15 Stakeholders have also asserted that the ECD tool is designed for use by employers only and that it is another example of a missed opportunity to inform both workers and employers equally of their respective rights and obligations.

RELEVANT ATO MATERIALS

Guidance on worker status

2.16 The ATO has advised that there were previously two ECD tools – one specifically for the building and construction industry and another for all other industries. Following user testing, on 25 February 2016, the ATO released a new ECD tool which combined the two existing tools into one and included questions on the use of interposed entities and links to guidance on SG, PAYGW and FBT obligations. These updates were in line with the recommendations made by the BoT in 2014.⁹⁹

2.17 The ECD tool instructions state that its questions are ‘based on the outcomes of court cases that considered various indicators to establish whether a person is an employee within the common law meaning of the term’.¹⁰⁰ The areas covered by the questions include:

- the basis of calculating remuneration for workers;
- the worker’s ability to subcontract or delegate tasks;
- who provides equipment, tools and other assets to complete tasks; and
- who bears commercial risks, such as remedying errors.

2.18 The ATO has advised that it has received positive feedback about the new tool such as it was easier to understand. It also received constructive feedback that additional guidance was required particularly in connection with the classification of outcome-based contractors who are paid by the hour.¹⁰¹

2.19 The instructions of the new ECD tool continue to state that it is only to be used ‘by businesses that engage to pay a worker’ and is not ‘designed for labour hire firms or individual workers’. Furthermore, the instructions specifically state that it ‘does not consider other obligations, for example, payroll tax or WorkCover obligations’ but a link to the Department of Industry, Innovation and Science’s website is provided where information on other federal, state and territory employer obligations can be found.¹⁰²

⁹⁹ BoT, *Tax impediments facing small business*, above n 73, pp 20-2.

¹⁰⁰ ATO, *Employee/contractor decision tool* (25 February 2016) <<https://www.ato.gov.au>>.

¹⁰¹ ATO communication to the IGT, 21 March 2016.

¹⁰² ATO, *Employee/contractor decision tool*, above n 100, <<https://www.ato.gov.au>>.

2.20 The new instructions also outline the level of protection offered to employers who rely on the tool:

*Provided your responses accurately reflect the working arrangement, you can rely on the result provided by the tool. It is a record of your genuine attempt to understand your obligations for your worker and would be considered if we review your working arrangement in the future.*¹⁰³

2.21 They do not specifically provide protection against penalties as was the case with the previous instructions.¹⁰⁴

2.22 Once the ECD tool determines the worker status to be that of an employee, links are provided to the main webpages for the various employer obligations where the ATO provides general¹⁰⁵ as well as industry specific¹⁰⁶ information. This information includes case studies,¹⁰⁷ rulings¹⁰⁸ and transcripts of videos on the distinction which demonstrates the distinguishing features of employees from contractors.¹⁰⁹ It should be noted that it does not provide a link to the main Business webpage where the obligations associated with hiring workers are explained and checklists provided.¹¹⁰ It also does not provide links to any information for workers.

2.23 If businesses are still uncertain as to the status of the workers they wish to or have hired, the ECD tool advises them to seek independent advice or request a private ruling from the ATO with a link being provided on how to do this.¹¹¹

2.24 In addition to the ECD tool and materials on its website, the ATO also disseminates information to businesses about their obligations through mail out campaigns.¹¹² An example of such a campaign is the ATO's trial of a new 'online education product'.¹¹³ This trial involves sending a series of emails¹¹⁴ to 1000 small businesses in their first year of operation, at different stages, about their federal and state taxation as well as non-taxation responsibilities.¹¹⁵

2.25 Links to the ECD tool and an explanation of the key differences between employees and contractors¹¹⁶ are also provided as part of the instructions to the online

103 Ibid.

104 ATO webpage – no longer available as the page has been updated.

105 ATO, *Business* <<https://www.ato.gov.au>>.

106 ATO, *Building and construction industry - how to work out if workers are employees or contractors* (13 April 2016) <<https://www.ato.gov.au>>.

107 ATO, *Difference between employees and contractors* (22 February 2016) <<https://www.ato.gov.au>>.

108 ATO, TR 2005/16, above n 13; ATO, *Superannuation guarantee: who is an employee?*, SGR 2005/1 (2005).

109 ATO, *Video transcript – Employee or contractor? Avoid the myths* (25 February 2016) <<https://www.ato.gov.au>>.

110 ATO, *Your workers* (22 February 2016) <<https://www.ato.gov.au>>.

111 ATO, *Employee/contractor decision tool*, above n 100, <<https://www.ato.gov.au>>.

112 ATO letter template, *Are your workers employees or contractors?* (internal ATO document).

113 The information relates to various aspects of tax, superannuation and other government responsibilities on www.business.gov.au, such as access to business advice, record keeping and tax obligation changes.

114 ATO and Department of Industry, Innovation and Science, *Congratulations on starting your new business* (26 February 2016).

115 ATO communication to the IGT, 9 March 2016 p 4.

116 ATO, *Difference between employees and contractors*, above n 107, <<https://www.ato.gov.au>>.

ABN application form.¹¹⁷ It should be noted that the Commissioner of Taxation (Commissioner) is also the Registrar of the Australian Business Register (ABR). The ABR has advised that 99.7 per cent of the ABN applications received in the 2014-15 financial year were submitted using the ABR's online form.¹¹⁸

2.26 The ATO has also advised that the SBFS has made recommendations about how guidance on the employee/contractor distinction should be provided. One of these recommendations is to develop a whole-of-government tool that helps employers determine the status of the worker for federal and state government obligations such as PAYG, SG, WorkCover and Portable Long Service Leave. The recommendation notes that, long term, the considerable data held by the ATO could be used to 'push' employee/contractor classifications to employers, improve legislation to provide one common answer across agencies and link the ECD tool to the ABN registration process to provide early guidance.

2.27 In relation to information on the rights and obligations of workers, the ATO separately provides website materials¹¹⁹ targeted at employees¹²⁰ and contractors.¹²¹ Where workers are unsure about their status, the website material advises the worker to first contact the business before seeking legal advice, contact the FWO, or visit business.gov.au for further information.¹²²

Private Binding Rulings and Administratively Binding Advice

2.28 Businesses may seek binding advice from the ATO at any time about the status of their workers. Such advice is generally in the form of a Private Binding Ruling (PBR) which in this case be requested in the context of PAYGW. The PBR regime does not extend to SG. The ATO can issue an Administratively Binding Advice (ABA) on SG related issues but is not obliged to do so.¹²³

2.29 Both PBRs and ABAs are binding on the Commissioner and offer protection from penalties to the extent that all material facts have been provided in the request and they accurately reflect the working arrangement.

2.30 On average over the last five financial years (2010-11 to 2014-15), the ATO has advised the IGT that it has completed 38 PBR requests regarding the obligation to withhold PAYG.¹²⁴ With respect to ABAs, over the last five financial years (2010-11 to 2014-15), it has received, on average, 51 ABA requests per year and issued 40 ABAs.¹²⁵ Common reasons for the ATO not issuing an ABA include instances where the request

117 Australian Business Register, *Applying for an ABN – ABN entitlement* (19 August 2016) <<http://www.abr.gov.au>>.

118 ATO communication to the IGT, 4 March 2016.

119 ATO, *Working* (4 August 2015) <<https://www.ato.gov.au>>.

120 ATO, *Working as an employee* (9 June 2015) <<https://www.ato.gov.au>>.

121 ATO, *Working as a contractor* (9 June 2015) <<https://www.ato.gov.au>>.

122 ATO, *Working*, above n 119, <<https://www.ato.gov.au>>.

123 ATO, *Provision of advice and guidance by the ATO*, PS LA 2008/3, 28 February 2008, para [190].

124 ATO communication to the IGT, 19 February 2016.

125 ATO communication to the IGT, 7 June 2016.

was withdrawn (60 per cent) or further information was requested but not provided by the employer (20 per cent).¹²⁶

ATO management of the employee/contractor distinction

2.31 Further to providing guidance, binding advice and rulings to employers to assist with the employee/contractor distinction, the ATO has advised that it has implemented compliance strategies during audit to remove the retrospective impact on employers where a worker was unintentionally misclassified as a contractor.

2.32 In this respect, where a failure to withhold PAYGW penalty is raised on the employer in circumstances where a worker has been incorrectly treated as a contractor, the ATO has discretion to remit the penalty.¹²⁷ The ATO's internal procedures provides for such remission where employers can demonstrate that, at the outset, they had made a genuine attempt at correctly classifying their workers and that, moving forward, they would rectify those classifications as per the ATO findings.¹²⁸

2.33 The ATO has also advised that it has a similar strategy, known as the 'go-forward strategy', which applied from 1 July 2014 where workers are incorrectly misclassified for SG purposes. Where the ATO determines that workers have held themselves out to be contractors, demonstrated through the deduction of business expenses and superannuation contributions, employers will not be liable for SGC liabilities relating to prior periods¹²⁹ provided that they comply with their SG obligations for those workers going forward.¹³⁰

INTERNATIONAL COMPARISONS

2.34 Revenue agencies in other jurisdictions encounter similar issues with the employee/contractor distinction and have different approaches to managing the uncertainty associated with the common law definition.

2.35 To assist in the determination of worker status, Her Majesty's Revenue & Customs (HMRC) in the United Kingdom (UK) provides an online 'Employment Status Indicator' tool that can be used by both employers and workers. The outcome of the tool may be used in future disputes about a worker's employment status and can be binding on HMRC.¹³¹ The online Employment Status Manual on the HMRC's website provides lists of relevant factors to consider and provides references to a

¹²⁶ Ibid.

¹²⁷ TAA sch 1 s298-20.

¹²⁸ ATO, *Employer Obligations: s16-30 Failure to withhold penalty method* (internal ATO document, 4 August 2015) p 6.

¹²⁹ ATO, *Employer Obligations (EO): Superannuation guarantee (SG) risk method* (internal ATO document, 16 December 2015) p 17 app A.

¹³⁰ ATO, *Unpaid super* (5 May 2016) <<https://www.ato.gov.au>>.

¹³¹ HMRC, *Business tax – guidance - Employment Status Indicator* (26 November 2014) Gov.uk <<https://www.gov.uk>>.

number of tax court cases.¹³² Written contracts in the UK appear to be a dominant element in a determination for worker classification.¹³³

2.36 The Internal Revenue Service (IRS) in the United States (US) provides guidance on worker classification which focuses primarily on three common law factors - behavioural control, financial control and relationship of the parties.¹³⁴ Under the common law definition of employee, a person is an employee if their employer can control 'what will be done and how it will be done' even if 'freedom of action' is given.¹³⁵

2.37 The US also has a statutory definition of employee for the purposes of Social Security and Medicare taxes, which include certain drivers and salespersons.¹³⁶ Independent contractors are considered self-employed and are subject to Self-Employment Tax, which they calculate themselves and can deduct from their adjusted gross income.¹³⁷ There is a specific category of workers, who are also treated as independent contractors called 'statutory nonemployees'.¹³⁸

2.38 In the US, if there is uncertainty about a worker's status, either the worker or business can lodge an 'SS-8 form' to the IRS who will make an official determination. However this can be a lengthy process with the IRS advising that it can take at least six months to receive a determination.¹³⁹ The requestor is required to complete a form and answer detailed questions about the work relationship between the business and the worker. Once the form is completed, the IRS sends the same form to the other party as the 'determination of employment status affects both parties'.¹⁴⁰ The IRS will then make a determination based on the information provided. If either party disagrees with the IRS determination, they may request reconsideration of the determination if they are able to provide additional information. No administrative appeal rights are currently allowed.¹⁴¹

2.39 Employers may seek a review of certain employment tax determinations (worker status) associated with an audit.¹⁴² They may also utilise the safe harbour rule¹⁴³ that prevents the IRS from retroactively reclassifying 'independent contractors' as employees and subjecting the employer to federal employment taxes, penalties and interest where the employer can demonstrate that they 'in good faith, misclassified their employees as independent contractors'.¹⁴⁴ Employers may also reclassify their

132 HMRC, *ESM0515 Guide to determining status: relevant factors* (7 April 2016) Employment Status Manual, Gov.uk <<https://www.gov.uk>>.

133 HMRC, *ESM0507 Guide to determining status: importance of a written contract* (7 April 2016) Employment Status Manual, Gov.uk <<https://www.gov.uk>>.

134 IRS, *Independent Contractor or Employee* (2012) <<https://www.irs.gov>>; IRS, *Employer's Supplemental Tax Guide* (Cat. No. 21453T, 2016) <<https://www.irs.gov>>.

135 IRS, *Employee (Common-Law Employee)* (4 May 2016) <<https://www.irs.gov>>.

136 IRS, *Statutory Employees* (17 June 2016) <<https://www.irs.gov>>.

137 IRS, *Self-Employment Tax (Social Security and Medicare Taxes)* (20 June 2016) <<https://www.irs.gov>>.

138 IRS, *Statutory Nonemployees* (16 June 2016) <<https://www.irs.gov>>.

139 IRS, *Independent Contractor (Self-Employed) or Employee?* (7 June 2016) <<https://www.irs.gov>>.

140 Taxpayer Advocate Service (US), *2013 Annual report to Congress - Volume One*, MSP #19, (2013) p 199.

141 Ibid p 200.

142 *Internal Revenue Code* (US) s 7436.

143 *Revenue Act 1978* (US) s 530.

144 Taxpayer Advocate Service (US), *2008 Annual report to Congress - Volume One*, LR #5, (2008) p 378.

workers for future tax periods and obtain partial relief from federal employment taxes under the Voluntary Classification Settlement Program.¹⁴⁵

2.40 Where a worker is found to have been misclassified by the employer, the worker may submit a form to the IRS to have their social security and Medicare taxes credited to their social security record.

2.41 In Canada, workers and businesses also have the ability to apply for a ruling of the worker's employment status. Canada has a similar common law definition to Australia with the exception of the province of Quebec, which has a statutory definition of a business contract (contract for services) and thus a different set of factors to consider.¹⁴⁶

2.42 The Canada Revenue Agency (CRA) considers whether there is 'common intent' by the parties or not. If there is no common intent, various factors are considered including:

- the level of control the payer has over the worker's activities;
- whether the worker provides the tools and equipment;
- whether the worker can subcontract work or hire assistants;
- the degree of financial risk the worker takes;
- the worker's opportunity for profit; and
- any other relevant factors, such as written contracts.¹⁴⁷

2.43 If a worker or payer is not sure of the worker's employment status, either party can request a ruling to have the status evaluated. A ruling decides whether a worker is an employee or is a self-employed individual, and whether that worker's employment is pensionable or insurable.¹⁴⁸

IGT OBSERVATIONS

2.44 It is clear from the above discussion that determining the status of a worker can be challenging. The employee/contractor distinction is rooted in a common law definition with no determinative factor. There are number of factors that need to be considered relative to each other, and therefore, making a determination is very much reliant on the facts and the outcome differs from one case to another.

2.45 The above challenge is exacerbated by the fact that many tax and non-tax obligations at both federal and state levels rely on the correct classification of employees and contractors. An incorrect classification of workers may have significant adverse impacts particularly for the businesses that engaged those workers. Any

145 IRS, *Voluntary Classification Settlement Program (VCSP)* (22 June 2016) <<https://www.irs.gov>>.

146 *Civil Code of Québec*.

147 CRA, *RC4110 Employee or Self-employed?* (29 July 2016) p 6-10 <<http://www.cra-arc.gc.ca>>.

148 Ibid pp 5-6.

corrective action may have retrospective effect giving rise to unplanned liabilities going back many years.

2.46 To address the challenges of determining workers' status and the potential of liabilities arising retrospectively, some stakeholders have suggested that the contract between the business and the worker should be respected irrespective of the common law definition. For example, if the relevant contract envisages a contractual relationship between a business and a contractor then it should be regarded as such even if the relationship is more akin to an employer/employee relationship under the common law definition.

2.47 Other stakeholders believe the above approach would be unfair as the business and the worker may have competing interests but not the same bargaining power and/or be equally informed. This may lead to bona fide employees being engaged as contractors thereby foregoing employment benefits to which they may otherwise be entitled.

2.48 Another solution that has been put forward is to legislate a definition of employee that is easier to apply than the common law definition. However, to ensure a fair outcome, such an enacted definition will also require the examination of all the relevant facts and may not be any simpler to apply. Furthermore, an ingrained legislated definition would lack the flexibility of common law which may evolve over time to reflect changing norms.

2.49 Whilst it may not be possible to simplify the employee definition, the IGT believes that businesses and workers could benefit from further assistance in determining the status of workers at an early point in their relationship to minimise any unplanned liabilities arising with respect to prior periods. In addition to ATO's recent initiatives, such as taking steps to reduce the retrospective impact of audits, the IGT believes that the ECD tool could be further improved and a Voluntary Certification System (VCS) could be implemented to provide upfront certainty to both businesses and workers.

ECD and other tools

2.50 As outlined at the beginning of this chapter, stakeholders have raised a number of concerns about the utility of the ECD tool. During the course of this review, the ATO released its new ECD tool in February 2016. It is too early to fully assess the success of the new tool but some stakeholders have commented favourably on it.

2.51 One major concern that has been raised with the new ECD tool is that there is uncertainty as to the level of protection afforded to employers who rely on its outcome. The IGT believes that the ATO should revert back to the wording in the instructions to the old ECD tool, that is, make it clear that no penalties apply to those employers who use and rely on it in good faith.

2.52 There are also issues that the new ECD tool has not addressed, including the inability for workers to use or rely on the ECD tool. The IGT notes, in addition to the

employees who are employed by 905,000 employers,¹⁴⁹ there are approximately one million contractors¹⁵⁰ in Australia. This is a sizeable group who could benefit from the ECD tool and prevent disputes arising at a later time.

2.53 The IGT is of the view that the current ECD tool should be expanded to allow use by workers. The proposed expanded ECD tool should be promoted amongst workers at the earliest possible times to inform them of potential tax and superannuation obligations and aid their decision making process. For example, it should be drawn to workers' attention when they apply for ABNs through the online application process which accounted for 99.7 per cent of all ABN applications in 2014-15. Indeed it could be integrated with the ABN application process as well as the PSI tools to alert contractors of relevant information prior to being hired.

2.54 Consistent with the HMRC's 'Employment Status Indicator tool'¹⁵¹, the outcome of the proposed expansion to the ECD tool could be accompanied by advice about workers' rights and obligations through the use of links to relevant information. For example, where the ECD tool determines the worker status to be one of contractor, it could provide links to the responsibility to remit PAYG instalments, provision of superannuation, or the possibility of being subject to the PSI regime.

2.55 The ECD tool could also be used to encourage businesses and workers to subscribe to specialised ATO communication so that they are provided with relevant updates. For example, employers could be encouraged to visit or subscribe to the 'employers' section of the small business newsroom when the ECD tool provides an outcome that the worker is an employee. Providing targeted information at key interaction points, such as when employers or workers are using the ECD tool or applying for an ABN, is more cost effective than an active communication campaign using television advertisements and mail-outs. Such a process accords with the SBFS's long-term proposal to provide information to workers at the ABN application stage.¹⁵²

2.56 Some stakeholders have also suggested the development of a broad tool that determines worker status across various tax and non-tax employer obligations at federal and state level. Whilst this is beyond the remit of the IGT, it should be noted that the SBFS¹⁵³ and the Standing Committee on Education and Employment have recommended such a whole-of-government single tool.¹⁵⁴ At the time of writing, the Government was yet to provide its response.¹⁵⁵

Voluntary Certification System

2.57 In addition to expanding the ECD tool to provide workers with a basic level of certainty as to the nature of their engagement, the ATO could provide a higher degree of certainty in the form of binding advice to workers through a VCS. A VCS would, in

149 Commissioner of Taxation, *Annual Report 2015-16*, Volume 1 (October 2016) p 12.

150 Australian Bureau of Statistics, *Characteristics of Employment, Australia, August 2014*, Cat. No. 6330.0.

151 HMRC, *Employment Status Indicator*, above n 131, <<https://www.gov.uk>>.

152 ATO, *Small Business Fix-it Squads – concept testing report* (internal ATO document) p 3 product 3.

153 Ibid.

154 Parliament of Australia, *Getting business booming*, above n 71, p xvii rec. 1.

155 ATO communication to the IGT, 2 June 2016.

effect, be an extension of the existing ruling and advice framework but would be based on information provided independently by each party. This would be consistent with the US and Canadian approach where either the worker or business may request a binding determination from the IRS and the CRA respectively.

2.58 Currently, where employers wish to seek binding advice or are uncertain about the classification of their workers after using the ECD tool, they may request the ATO to issue a PBR for any PAYGW obligations or an ABA for any SG obligations. Similar binding advice is not currently available for workers. Towards the end of this review, the ATO advised the IGT that a worker may seek certainty from the ATO in the form of a PBR on the issue of whether the worker is carrying on a business and that a positive ATO determination would mean that the worker is a contractor and not an employee. However, this is not an accurate reflection of a worker's status as it does not consider the business who is engaging the worker nor the relationship between them – the key factor in deciding whether a worker is a contractor or an employee.

2.59 The ATO has also argued that workers and businesses could jointly complete a PBR or ABA application to obtain certainty upfront for both parties but such an approach presents some challenges. The potential power imbalance that may exist between the two parties, may, for example, lead to the workers not raising all their concerns.¹⁵⁶ Whilst this would be unfair on the worker, it is also not ideal for the business if, at a later time, such as after the engagement has concluded, the worker presents different facts and challenges the determination of their status. If the worker's challenge is upheld, retrospective liabilities may arise for the business.

2.60 The proposed VCS would be expected to overcome the inability of workers to obtain relevant binding advice on their status and for both parties to independently submit their facts for consideration. Similar to the proposed expanded ECD tool outlined above, both parties should be encouraged to use it as soon as possible to make them aware of their obligations early in the process and limit their unplanned liabilities relating to prior periods. As noted earlier, the current PBR and ABA requests are minimal – on average, 38 and 51 per year, respectively. Similarly, in order to maximise the benefits of the VCS, it should be promoted to both businesses and workers through such means as the ABN online application process as mentioned above. The VCS would also assist the ATO in their future compliance activities as they are able to use the facts provided as part of the VCS as a baseline from which they can assess changes to working arrangements and the impact it had on worker status.

2.61 The IGT recognises that, as with any binding advice, certification would be a point in time assessment of facts presented and the decision would only be binding to the extent that the relevant facts remain unchanged. Any material changes to the working arrangement over time, intentional or otherwise, would require recertification.

156 GfK Australia Research, *Superannuation Guarantee Research*, ATO (2013). This ATO commissioned research found that employees do not raise concerns with the non-payment of their superannuation entitlements out of fear of losing their job.

Harmonisation of the definition of 'employee'

2.62 As mentioned earlier, the employee/contractor distinction is the basis for determining a number of tax and non-tax employer obligations at state and federal level. Whilst, in all cases, the distinction is based on the common law definition of employee, it is altered by the governing legislation in most instances such that businesses have the burden and associated costs of determining worker status multiple times for each category of workers.

2.63 Some stakeholders have suggested that a simple solution would be to have one definition for all obligations. However, the current definitions reflect the different policy intents of each of the relevant legislative regimes. For example, the definition of employee for SG is broader compared to that of PAYGW to reduce reliance on the Age Pension. It would require significant work and cooperation to achieve a single definition which meets the legislative intent of all these regimes.

2.64 Harmonisation of the definitions across all tax and non-tax employer obligations at federal and state levels may be more achievable than a single definition. Many stakeholders have for some time called for such harmonisation,¹⁵⁷ however, it is a considerable undertaking and one that is beyond the remit of the IGT. It should be noted that some steps towards harmonisation are being taken¹⁵⁸ such as the recent recommendation of the House of Representatives Standing Committee on Education and Employment for the ATO and the FWO to set up a working group for identification of the legislative change required to align the definitions of 'employee' across federal government agencies.¹⁵⁹

RECOMMENDATION 2.1

The IGT recommends the ATO:

- (a) *clarify the protection provided to those who use and rely on the Employee Contractor Decision tool in good faith, promote the tool and allow it to be used by employees and contractors as well as accompanying the result with links to information outlining their respective rights and obligations; and*
- (b) *implement and promote a Voluntary Certification System which employers, employees and contractors may use, as soon as possible, to confirm worker status and refer them to information about their respective rights and obligations once their status has been determined.*

157 Combined Small Business Alliance of Western Australia Inc., Submission 6 to the Standing Committee on Employment, Workplace Relations and Workforce Participation, House of Representatives, *Making it work: Inquiry into independent contracting and labour hire arrangements* (August 2005) p 2 citing Small Business Regulation Task Force, *Time for Business* (November 1996) p 5.

158 ATO, 'Small Business Fix-it Squads – concept testing report', above n 152, p 3; Council of Australian Governments, *Business Regulation and Competition Working Group Report Card on progress of deregulation priorities* (19 August 2011) <<https://www.coag.gov.au>>.

159 Parliament of Australia, *Getting business booming*, above n 71, p xvii rec. 1.

ATO response

Agree with recommendation 2.1(a).

Disagree with recommendation 2.1(b).

We agree to clarify the protection provided to those who use and rely on the Employee Contractor Decision (ECD) tool, to the extent this is supported from a further analysis of users' needs which we will conduct.

We already actively promote the ECD tool and ran a funded advertising campaign earlier this year to promote the tool and myths about worker status. We will continue with our planned promotional activities.

We will explore the use of the ECD tool by workers. We will undertake the necessary design and consultation work with employees/contractors to assess the relative merits and priority of this suggestion, and schedule for implementation in accordance with the findings of that work.

We are not convinced that the proposed Voluntary Certification System offers advantages over the existing advice system, especially if we can enable the ECD tool to be used by workers. For example, the current private advice service provided by the ATO supports:

- the provision of advice to workers on their status and
- whether or not an individual is carrying on an enterprise.

While binding advice cannot be given to a worker about whether they should be subject to PAYGW or superannuation guarantee (because these obligations are not borne by the worker) we can and do give general advice in these situations.

A voluntary certification system would not overcome the issues identified in the review. A voluntary certification system would still require the parties to set out the facts and details of their arrangement in order for a decision to be made, as with the current private ruling system. A voluntary certification system would also only be able to make a decision based on the facts of the arrangement at the time as does the current advice system.

CHAPTER 3—EMPLOYER OBLIGATIONS COMPLIANCE COSTS

BACKGROUND

3.1 Commentators generally recognise that modern tax systems, particularly because of their self-assessment nature, impose significant costs on taxpayers in complying with their tax obligations. These costs may be particularly high for small businesses relative to their turnover, income or the number of employees.¹⁶⁰

3.2 Small businesses form the largest group of business in Australia. A Department of Treasury report shows that those with annual turnover less than \$2 million account for the largest share of tax compliance costs, at \$18.7 billion in 2011, compared with all other market segments. These costs mainly related to those associated with record keeping and external fees.¹⁶¹

3.3 The Treasury report also estimated the compliance costs in relation to SG and PAYGW to be \$2.6 billion and \$1.1 billion respectively for all market segments. The compliance cost for the FBT was relatively small, however, both the Treasury and the BoT were of the view that the model used had delivered too low an estimate and that such costs may have been captured elsewhere such as in the total cost for external professional fees¹⁶² which were separately estimated to be \$14 billion with respect to all taxes.¹⁶³ Similarly, the costs in relation to PAYGW may also be higher – the ATO has estimated it to be approximately \$2.5 billion in 2011.¹⁶⁴

SUMMARY OF STAKEHOLDER CONCERNS

3.4 Stakeholders have raised concerns that a number of employer obligations impose significant compliance costs particularly for small businesses. These costs include those related to record keeping and reporting obligations.

3.5 Stakeholders have acknowledged that a number of initiatives have been introduced with the goal of reducing compliance cost for businesses. However they have raised concerns that this goal may not be fully achieved with respect to some of these initiatives. For example, they believe STP will not be sufficiently tested before going live and barriers to its adoption, particularly by small business, have not been adequately considered. Another example is the requirement by SBSCH to manually enter SG data.

160 For example: Lignier, Philip and Evans, Chris, 'The Rise and Rise of Tax Compliance Costs for the Small Business Sector in Australia' (2012) 27 *Australian Tax Forum* 615, cited in The Treasury, RIS, *STP*, above n 46, p 4.

161 The Treasury, *Stocktake of Regulation: Final Report* (2015) p 20.

162 Ibid p 26.

163 Ibid p 21.

164 The Treasury, RIS, *STP*, above n 46, p 4.

3.6 Some stakeholders have also raised concerns in relation to the extent of GST reporting required in BAS and the different lodgement dates for BAS and TPRS forms. The IGT notes that these lodgement dates have now been aligned to 28 August from the 2014-15 financial year. More generally, GST is not being considered in this review as it is not connected with employment, however, should these concerns persist they may form part of a more targeted review.

SINGLE TOUCH PAYROLL

3.7 As described in Chapter 1, the aim of STP is to cut red tape for employers by simplifying tax and superannuation reporting through software which will automatically report payroll information to the ATO.

3.8 Stakeholders have raised concerns that STP may not significantly reduce compliance costs for employers due to a number of issues, including:

- the ATO has not worked adequately with third party software developers to mitigate design and implementation risks such as minimising compatibility or interaction issues of their software with ATO systems;
- no provisions have been made for late reporting by employers due to STP system issues;
- there may be additional compliance costs if the existing PAYGW related reporting obligations are not removed;
- implementation costs may be an adoption barrier, particularly for small employers, despite the proposed funding mentioned in Chapter 1; and
- no provisions or alternatives have been made for employers who do not have access to a reliable internet connection or are unable to use technology.

Relevant ATO materials

Design and implementation

3.9 The ATO has produced a blueprint outlining the STP design. In relation to STP software development, it states that the ATO will facilitate discussions with software developers, employers and intermediaries to determine standards and minimum requirements.¹⁶⁵

3.10 The ATO has also prepared a Regulation Impact Statement (RIS) for Parliament which outlines the design, savings and potential impact of STP. To mitigate concerns about the ATO's level of engagement with software developers, the RIS states

¹⁶⁵ ATO, *STP Blueprint*, above n 45, p 7.

that the ATO will draw upon established networks in the design and implementation of STP.¹⁶⁶

3.11 The ATO has advised that it expects that development of STP software will follow its usual process¹⁶⁷ where the ATO publishes a set of specifications in accordance to which software developers produce the final product.¹⁶⁸ Following a self-certification process,¹⁶⁹ the name and version of the final product is published on the ATO's software developers' webpage.¹⁷⁰ The ATO has also advised that while it does not endorse¹⁷¹ or conduct testing of the final product to ensure that the specifications are met,¹⁷² it does allow developers to test it with a small set of data once it goes live.¹⁷³

3.12 In addition to the above standard process, the ATO has provided management representation that it has a test strategy to manage the implementation of STP software but is unable to provide documentation, at the time of writing, as it is 'still under development and is contingent on the final design'.¹⁷⁴

3.13 The STP legislation also allows employers to correct mistakes without penalty within two weeks after the end of the financial year to which the report relates.¹⁷⁵ Furthermore, a failure to notify the ATO of the amounts required by STP will not attract a penalty until 1 July 2019¹⁷⁶ or any later date as determined by the Commissioner.¹⁷⁷ In this later respect, the ATO is seeking feedback from the community on an appropriate date and whether other materiality thresholds should apply, for example, the maximum values for correction of such errors.¹⁷⁸

3.14 Under the STP legislation, employers who comply with STP will not be required to meet a number of reporting obligations, including the need to provide annual reports and annual and part-year payment summaries.¹⁷⁹ As part of relieving employers from the requirement to provide payment summaries, the ATO has advised the IGT that it plans to provide payment summaries to employees who are not able to register to myGov.¹⁸⁰ The ATO has not indicated when this service would be operational.

166 The Treasury, RIS, *STP*, above n 46, p 46.

167 ATO communication to the IGT, 5 April 2016.

168 Standard Business Reporting, *What can I expect?* (19 April 2016) <<http://www.sbr.gov.au>>; ATO communication to the IGT, 5 August 2016.

169 ATO communication to the IGT, 24 March 2016 and 6 June 2016, citing Standard Business Reporting, *What can I expect?*, above n 168, <<http://www.sbr.gov.au>>.

170 ATO, *View product register* <<http://softwaredevelopers.ato.gov.au>>.

171 ATO, *Disclaimer*, <<http://softwaredevelopers.ato.gov.au>>.

172 ATO communication to the IGT, 24 March 2016.

173 ATO communication to the IGT, 24 June 2016.

174 ATO communication to the IGT, 5 August 2016.

175 TAA, sch 1 s 389-20.

176 TAA s 8K(2A), sch 1 s 389-25.

177 TAA, sch 1 s 389-25.

178 ATO, *STP design workshops*, above n 51 <<http://softwaredevelopers.ato.gov.au>> p 4; ATO, *STP consultation paper*, above n 63, <<https://www.ato.gov.au>>.

179 TAA sch 1 s 389-20.

180 ATO, *Single Touch Payroll solution summary version 1.0* (internal ATO document, 10 June 2016) p 14.

3.15 The ATO has also advised the IGT that it will use STP data to prefill the W2 label (amounts withheld for salary/wages) on BAS from 1 July 2017 but will allow employers to verify the amount prior to submission.¹⁸¹

3.16 It should also be noted that the RIS states employer reporting may be further reduced, in the long term, when STP is able to facilitate the sharing of real time payroll data with federal, state and territory government agencies.¹⁸²

Adoption of STP

3.17 As mentioned earlier in Chapter 1, employers will incur STP implementation costs such as acquiring new software, upgrading existing software or engaging the services of an intermediary. The extent of implementation costs will vary between employers with those already using digital systems for PAYGW being 'potentially well aligned' with the STP.¹⁸³ However, small employers, particularly those without digital systems, will have proportionately larger implementation costs.¹⁸⁴

3.18 The ATO has estimated the total implementation cost for employers to be \$300 million¹⁸⁵ over a two to three year period. This estimate is based on mandated adoption by all large employers and voluntary adoption by 30 per cent of small employers.¹⁸⁶ If the Government decides to include small employers into STP, the total implementation cost for all employers will increase to approximately \$670 million over a two to three year period.¹⁸⁷

3.19 It is estimated that there will be \$135 million in annual savings and \$900 million in net compliance cost savings over 10 years based on mandatory adoption of STP by all large employers and 30 per cent voluntary adoption by small employers. Mandatory adoption by all employers is estimated to provide annual savings and net compliance cost savings of \$295 million and \$2 billion respectively. These savings are expected to be generated by 'record keeping improvements' from the streamlining and automation of the withholding process with further savings from the new TFN declaration and superannuation standard choice forms.¹⁸⁸

3.20 In the event that there is an insufficient availability of affordable software for employers, the ATO had identified that the effective implementation of STP could be at risk and, as a contingency, the ATO would 'look to fund the development of a low or no cost solution' to mitigate this risk.¹⁸⁹

181 ATO, *Single Touch Payroll Solution Summary – payroll processing* (internal ATO document, 28 September 2016) p 9; *Single Touch Payroll Core – Scope and Delivery Plan* (internal ATO document, 9 September 2016)

182 The Treasury, RIS, *STP*, above n 46, pp 3, 13, 29.

183 Ibid p 21.

184 Ibid p 26.

185 Ibid p 23.

186 Ibid p 19.

187 Ibid pp 23-4.

188 Ibid pp 23-6.

189 Ibid p 46.

3.21 Other employers, who may have difficulties complying with STP, include those in remote locations or those who otherwise face challenges accessing the internet. At the time of writing, it seems that the only way in which the ATO intends to address these challenges is by exempting such employers from STP requirements.

3.22 The STP legislation allows the Commissioner to exempt a class of employers or particular employers from STP requirements.¹⁹⁰ An ATO consultation paper indicates that the Commissioner will consult on the circumstances under which an employer may be exempt including situations where employment is on a seasonal basis.¹⁹¹

IGT observations

3.23 In addition to wealth generation and employment, employers play an important role in collecting and paying taxes on behalf of their employees. The ATO has reported that almost half of the \$419.26 billion taxation revenue in 2013-14 was collected by approximately 846,500 employers.¹⁹² This comes at a cost for employers. For example, as mentioned above, the SG compliance costs for employers across all market segments has been estimated to be \$2.6 billion,¹⁹³ collectively they issue 1.9 million annual paper payment summaries to employees and complete approximately 1.6 million PAYGW-only activity statements each year.¹⁹⁴

3.24 Unnecessary regulatory costs do not contribute to economic output and can actually be a form of disincentive to employers, which can in turn affect potential employment opportunities for employees. Accordingly, it is important that such costs be carefully considered and minimised to the extent possible.

Design and implementation of STP

3.25 One initiative aimed at reducing employers' compliance burden is STP. It is intended to provide substantial benefits, however, there are risks associated with its implementation and management. The ATO has sought to mitigate these risks through a staged implementation approach including an initial voluntary adoption by any employer with STP-enabled software as well as a pilot to assess suitability for small employers.

3.26 STP is still in the 'co-design' phase and implementation strategies are being formulated. In designing and implementing STP, it is crucial that the ATO applies the key principles of change management, such as clearly articulating the change and the 'future state', consulting with relevant stakeholders early and conducting testing on the software and its interaction with other systems. The IGT notes that the staged implementation approach being used by the ATO accords with the key principles of change management.

190 TAA 1953 sch 1 s 389-10.

191 ATO, *STP consultation paper*, above n 63, <<https://www.ato.gov.au>>.

192 ATO, *Compliance in focus 2013-14* (July 2013) p 8; Commissioner of Taxation, *Annual Report 2013-14* p iii-v.

193 The Treasury, *Stocktake of Regulation*, above n 161, p 21.

194 The Treasury, RIS, *STP*, above n 46, p 7.

3.27 Stakeholders have raised concerns that there is significant risk that the software, being developed by third parties, may not allow employers to fully discharge their legislated obligations particularly due to compatibility with ATO systems. The ATO is seeking to minimise this risk by providing minimum specifications for the software and engaging the same developers that it used in the SuperStream initiative.¹⁹⁵ Engaging with the relevant software providers for STP early in the design process will help to ensure 'buy-in' and provide adequate lead time for them to make the necessary changes to their products and conduct adequate testing.

3.28 Whilst the particular details on the design and testing of STP, including the pilot, is not settled, it is commonly accepted that large scale changes to information technology systems should include end-to-end testing (for example, from employer systems to ATO systems) of data in test and production environments. This should include testing the system under a number of scenarios including load and stress testing of ATO internal systems to ensure readiness to accept the expected volume of messages. Such testing is particularly important because STP will not operate in isolation of other ATO systems and may eventually be integrated with reporting systems of other agencies, for example, the DHS in relation to child support.

3.29 The ATO's management has advised that the details regarding the testing process are not available as the design is not yet final, including whether testing will occur in a controlled testing environment.

3.30 The IGT is of the view that while the ATO is in the development stage, the testing methodology needs to be incorporated in the software developers' design. The product needs to be rigorously tested in both test and production or 'go live' environments with ATO systems prior to STP becoming mandatory.

3.31 As part of the testing process, the ATO should clearly communicate to software developers that before they are permitted to use the test environments, they should meet an 'entry criteria'. This criterion requires base-level software being developed which has already been subjected to a certain level of testing. In addition, they should also be informed of the 'exit criteria', that is, the performance level that the product must meet before progressing to a 'go live' environment.

3.32 The above testing process was facilitated by the ATO in the development of SuperStream. It is designed to identify any defects for early rectification and is particularly important where a number of parties are involved in a complex system with integrated reporting and potential funds transfer. Software developers and employers will also welcome such an approach. It will provide a degree of assurance that the third party software product operates and interacts with ATO systems as intended in a controlled setting before 'go live' occurs in a pilot which will then be followed by normal operations. This increased level of confidence in the product should encourage the voluntary uptake of STP.

3.33 Those software developers that successfully complete the entire testing process with ATO systems should receive appropriate certification from the ATO. Such certification would be the 'gold standard' for assuring employers and other user

¹⁹⁵ The Treasury, RIS, *STP*, above n 46, p 46.

groups that the software is robust, reliable and allows them to fulfil their statutory obligations more efficiently.

3.34 The above testing process and the gold standard certification for the third party software was an important part of the success of the SuperStream which affected a similar population. In this instance, the ATO created a ‘SuperStream certified product register’ which only contained software developers who could demonstrate that their product met the required specifications and minimum standards. The ATO even sought to go further by ensuring that developers received direct feedback via a ratings process to ensure users were fully informed of the software’s functionality. Such transparency and support is to be commended.

3.35 The ATO may be faced with a considerable workload if the number of software providers requiring certification is much larger than was the case with SuperStream. However, without ATO certification, a significant risk remains that ‘self-certified’ software may not meet the required standard. Given the large-scale nature of STP and the longer term benefits anticipated, the IGT believes certification by the ATO has to be a key aspect of STP implementation.

3.36 Even where comprehensive testing and certification may have occurred, as with any new system, unexpected problems may arise, particularly in the early stages of release. These problems may impact on an employer’s ability to comply with the STP requirements and expose them to the risk of penalties. The STP legislation addresses such risks by allowing the ATO to take a concessional approach to penalties in the first 12 months of operation.¹⁹⁶ The IGT notes that this is one of the issues being considered by the ATO in its consultation with the community on how STP will be administered.¹⁹⁷

3.37 The IGT believes that, in addition to assuring employers of the reliability of the software and taking a concessional approach to penalties during the early stages of implementation, it is important that the ATO should promote the benefits of STP to employers. Following the commencement of this review, the ATO has now developed a plan to pre-fill the relevant labels on BAS and is looking to provide payment summaries to employees.¹⁹⁸

3.38 The IGT is also of the view the ATO should seek further opportunities to utilise STP data to pre-fill amounts for employers which are required to be reported elsewhere, including amounts reported to other government agencies.¹⁹⁹ The reduction of these reporting requirements will be vital to the voluntary uptake of the STP and its ultimate success.

¹⁹⁶ *Budget Savings (Omnibus) Act 2016* sch 23, div 3, item 22.

¹⁹⁷ ATO, *STP consultation paper*, above n 63, <<https://www.ato.gov.au>>.

¹⁹⁸ ATO, *STP solution summary*, above n 180, p 14; ATO, *STP Solution Summary – payroll processing*, above n 181, p 9; ATO, *STP Core – Scope and Delivery Plan*, above n 181.

¹⁹⁹ The Treasury, *RIS, STP*, above n 46, p 13; ATO, *STP Blueprint*, above n 45, p 10.

Adoption of STP

3.39 Stakeholders indicated that there are a number of barriers to employers adopting STP. The substantial upfront cost of purchasing or upgrading their software is one such barrier. Employers may also face technological barriers where they do not operate in a digital environment or do not have a reliable internet connection. These barriers are not limited to the adoption of STP but apply more broadly to the ATO's move to digital services.

3.40 In cases where employers face particular challenges in complying with STP, the IGT notes that the STP legislation allows the Commissioner to exempt particular employers or classes of employers from meeting those requirements. Therefore, the Commissioner is able to exempt qualifying employers where, for example, they face technological challenges. With regard to the upfront cost of purchasing STP software, the Government announced a \$100 tax offset to assist small employers.²⁰⁰

3.41 As stated earlier, the legislation provides an exemption from the adoption of STP to employers with less than 20 employees. Stakeholders have identified that further exemptions are necessary and that these should be provided by the Commissioner exercising the discretion afforded to him by the legislation. The IGT is of the view that appropriate exemptions should be provided particularly in the transition period and that the appropriate channel for identifying such exemptions is the ATO's current consultation on administering the STP legislation.

3.42 Whilst appropriate exemption would be of considerable relief for affected employers, the RIS does state that the benefits and efficiencies anticipated from the successful implementation of STP can only be realised through 'full participation by all businesses'.²⁰¹ Therefore, the IGT believes that whilst exemptions are necessary in the short term, the ATO should explore alternative ways whereby exempt employers can adopt STP in the long term so that they too can reap the expected benefits as well as the tax system as a whole.

3.43 One alternative would be to offer a low or no cost option to mitigate the current upfront costs which are a barrier for a considerable number of employers including 56 per cent of small employers who do not currently have electronic payroll software.²⁰²

3.44 As mentioned earlier, the ATO has stated that it would consider funding the development of low or no cost STP software as a contingency if it does not become commercially available.²⁰³ The IGT also notes that the New Zealand Inland Revenue is currently implementing an initiative similar to STP and is working with software developers to investigate the production of a low or no cost solution.²⁰⁴

200 Kelly O'Dwyer, 'Streamlining business reporting with a single touch payroll' (Media release, 21 December 2015).

201 House of Representatives, Revised Explanatory Memorandum, *Budget Savings (Omnibus) Bill 2016*, p 283.

202 ATO Corporate Research Centre, *Small Business Fix-It Squad Survey*, above n 76, p 3.

203 The Treasury, RIS, *STP*, above n 46, p 46.

204 Todd McClay, Minister of Revenue (NZ), *Making Tax Simpler – Better digital services: a government discussion document* (March 2015) p 32.

3.45 The IGT believes that the ATO should also explore the provision of a low or no cost solution as a means of encouraging voluntary uptake of STP by small employers, for example, by expanding the use of the SBSCH as a platform for employers to meet STP requirements.

3.46 The IGT also believes that the ATO should provide insight and raise awareness of employers that the upfront implementation costs would be outweighed by the long-term savings particularly for those in a position to meet such costs.

3.47 Another alternative way of adopting STP, particularly for those with technological challenges or lack of a reliable internet connection, is for the ATO to provide the digital connection. In this respect, the IGT notes that, in New Zealand, consideration is being given to providing digital access to government services through the use of physical 'e-kiosks' for taxpayers without internet access.²⁰⁵ The IGT believes that the ATO could explore similar options in Australia such as e-kiosks at Australia Post outlets.

RECOMMENDATION 3.1

The IGT recommends that, in relation to Single Touch Payroll, the ATO:

- (a) *apply the learnings from the implementation of SuperStream and, in particular, ensure that there is rigorous testing of third party software with certification being provided to those that meet all requirements;*
- (b) *seek to reduce employers' reporting requirements by using the information obtained to prefill fields;*
- (c) *ensure that there are appropriate exemptions at least in the short-term whilst exploring the possibility of providing:*
 - i) *a low or no cost software for qualifying small employers; and*
 - ii) *an alternative method of electronic access for employers facing technological challenges, through such means as e-kiosks.*

ATO response

Agree with recommendation 3.1(a).

Agree with recommendation 3.1(b).

Disagree with recommendation 3.1(c) (i).

Disagree with recommendation 3.1(c) (ii).

The recommendation implicitly acknowledges the successful work that has been undertaken by the ATO in implementing Superstream. We have been keen to ensure that the lessons learned through the Superstream implementation are taken into account in implementing Single Touch Payroll and for this reason have joined the

²⁰⁵ Ibid p 25.

Superstream and Single Touch Payroll projects under single leadership. Our intent is to continue to ensure the Superstream lessons are taken into account as appropriate, as well as the lessons from other software related implementations such as the new practitioner lodgement service, acknowledging that each implementation has its unique features and challenges.

We agree with the recommendation encouraging us to continue to bring those lessons to bear as appropriate as we continue the design and implementation work, although we would argue that we have already been doing this. We are already in discussions with industry on developing a 'fit for purpose' accreditation model for Single Touch Payroll enabled software.

In terms of reducing employers' reporting requirements, this is already a key part of the design of Single Touch Payroll.

In relation to ensuring appropriate exemptions and low or no cost software for small employers, we note that small businesses currently have no obligation to report under Single Touch Payroll. Part of the current pilot for exploring the potential benefits of small businesses using STP is to also explore what mechanisms could best support their usage. In light of this work and the further consideration required to be given by government about STP and small businesses, we think it is premature to agree to these aspects of your recommendations.

SMALL BUSINESS SUPERANNUATION CLEARING HOUSE

3.48 Stakeholders have raised concerns that the SBSCH does not significantly reduce an employer's compliance cost as it does not integrate with commercial software and requires employers to separately input data outside of their natural business systems.

3.49 Other concerns were raised in relation to commercial agreements between employers and their superannuation fund or clearing house. These agreements may require more frequent SG reporting and payment than what is mandated by legislation. They may also require provision of additional data when non-SuperStream methods are used. These concerns relate to business-to-business commercial agreements and are beyond the scope of this review as they do not relate to administrative aspects of the law or actions of the ATO.

Relevant ATO materials

3.50 The ATO has advised that the SBSCH is a:

...basic no-frills service that does not offer many of the features associated with commercial providers. Feedback from employer associations with commercial providers and the superannuation industry supports the position of the SBSCH as providing an important 'safety net' role. Specifically, it assists new-to-business employers and supports employers with limited software or payroll processing capabilities.²⁰⁶

206 ATO, Concept Brief, *SBSCH Transfer to the ATO* (internal ATO document, 24 June 2016) p 8.

3.51 While the SBSCH is an online service, it does not have the capability to interface with payroll or other software nor does it have the capability to accept files generated by such software.²⁰⁷

3.52 The administration of the SBSCH was transferred to the ATO as part of the 2013-14 Federal Budget and the SBSCH infrastructure is currently owned by the DHS.²⁰⁸ In February 2016, the ATO and the DHS agreed in principle to move the SBSCH infrastructure to the ATO.²⁰⁹ Preliminary briefings on the concept indicate a timeframe for commencement of transfer in August 2016 and completion by March 2018.²¹⁰

3.53 The ATO has advised that transferring the SBSCH to the ATO will provide opportunities to make changes to the service such as extending its use and access through different channels (such as via mobile apps), over the counter services, and pre-filling ATO-held data into the SBSCH.²¹¹ However, any commitment to implement such improvement depends upon the successful transfer of the SBSCH into the ATO's systems environment as well as the anticipated costs, benefits and impacts including the impact on relevant commercial software providers.

3.54 The ATO has confirmed that employers who use the SBSCH are required to manually input details of the employee at the registration stage and update the relevant fields at every payment period for the different components (that is, SG, additional employer contributions, salary sacrifice, and voluntary employee contributions) and where there are changes in employee details.²¹²

3.55 Statistics provided by the ATO regarding the user profiles of employers who use the SBSCH²¹³ show that:

- at the end of April 2016, there were 176,617 employers registered with the SBSCH with over 1.4 million employees;²¹⁴
- as at February 2016, the proportion of active users was 76 per cent;²¹⁵ and
- 62 per cent of active employers had payroll software known to the ATO.²¹⁶

IGT observations

3.56 One of the ways to reduce the administrative cost for employers is to minimise the need to manually transfer data from one system to another. Electronic

207 Ibid p 8.

208 The Commonwealth of Australia, 'MYEFO 2013-14', above n 68, p 192.

209 ATO, *SBSCH Transfer to the ATO*, above n 206, p 4.

210 Ibid p 6.

211 Ibid pp 8-9.

212 ATO communication to the IGT, 20 May 2016.

213 ATO communication to the IGT, 9 March 2016.

214 ATO communication to the IGT, 10 June 2016.

215 114,000 of the 150,000 registered users as at February 2016.

216 ATO communication to the IGT, 9 March 2016.

payroll software assists employers in this regard. For example, employers can use commercially available software to comply with the SuperStream requirement without the need to manually transfer data.

3.57 The current design of the SBSCH requires manual data input into the SBSCH portal. The costs in using the SBSCH is likely to be of greater concern to those employers with a larger number of employees as they would need to perform SG calculations for each employee, either in their electronic payroll systems or on paper, before transposing the amounts into the SBSCH interface.

3.58 In preparation for the transfer of the SBSCH infrastructure from DHS, the IGT believes that the ATO should consider ways in which the SBSCH can be improved to reduce the compliance burden on employers. The IGT recognises any changes that the ATO may identify at this stage would have to be finalised and implemented after the infrastructure has been transferred.

3.59 One improvement, perhaps the simplest, that the ATO could consider is developing an interface which would allow employers to upload pro forma electronic files, such as Microsoft Excel or Apple Numbers, into the SBSCH. Such an upgrade could potentially assist 51,007 small employers²¹⁷ who do not currently use payroll software. It is unclear how many of this group use Microsoft Excel or Apple Numbers as opposed to paper record keeping systems. However, it is likely that a significant number of them do and in any event, purchasing such applications would be more cost effective and easier to use than purchasing an entire payroll system.

3.60 A further step to reduce compliance cost for another group of employers is to upgrade the SBSCH such that it can accept standardised file extracts from commercial payroll software. This could assist a further 83,211 employers²¹⁸ who use payroll software as well as the SBSCH. The reasons for use of both systems are not entirely clear. There may be many explanations, such as that their payroll software is not SuperStream compliant or they may have bespoke systems and an integrated system upgrade is anticipated in the future. They may also use the SBSCH where commercial clearing houses require advance payment for monies to clear and data to be checked prior to sending it to the relevant superannuation funds.²¹⁹

3.61 The IGT notes that allowing the SBSCH to accept electronic files or standardised files from payroll software may, on one view, be considered as potentially competing with those commercial clearing houses and may go beyond its initial aim of providing a safety net for employers. However, the IGT is of the view that providing an interface to SBSCH of the kind outlined above would provide significant benefits by reducing the need for over 134,000 employers to make manual entries quarterly for every employee. It could also encourage the proportion of 51,007 employers who are not currently using electronic files for managing SG to adopt

217 Estimated number of active employers with no payroll software – 176,617 registered users, of which 76 per cent are active and 38 per cent have no known payroll software ($176,617 \times 0.76 \times 0.38$).

218 Estimated number of active employers with known payroll software – 176,617 registered users, of which 76 per cent are active and 62 per cent have known payroll software ($176,617 \times 0.76 \times 0.62$).

219 *Superannuation Guarantee (Administration) Regulations 1993* s 7AE and SGAA 1992 s 23B, s 79A.

a basic electronic record keeping system — thereby further improving voluntary compliance.

RECOMMENDATION 3.2

The IGT recommends that the ATO consider developing a capability for the Small Business Superannuation Clearing House to receive:

- (a) *electronic files, such as Microsoft Excel and Apple Numbers; and*
- (b) *standardised files from commercial payroll software.*

ATO response

Agree with recommendation 3.2.

The Small Business Superannuation Clearing House (SBSCH) is currently run on IT systems maintained by the DHS. It is proposed that the SBSCH be redeveloped into ATO operated IT systems, although details of that redevelopment are yet to be settled. When the redevelopment occurs (perhaps in 2018-19) we will consider potential improvements.

FRINGE BENEFITS TAX

3.62 A range of stakeholders have raised concerns regarding the cost of complying with FBT requirements, particularly when compared to the amount of FBT revenue raised. Stakeholders have also observed that such costs are disproportionately high for small employers. Particular stakeholder concerns about the cost and difficulty associated with complying with FBT requirements include:

- administrative difficulties for employers around reporting non-cash benefits provided by third parties, salary packaging and record keeping requirements such as logbooks for cars;
- valuation and apportionment methodologies impose unnecessarily high compliance costs on small employers; and
- current software does not automatically calculate expense payment benefits at the employee level for the purposes of disclosing reportable fringe benefits on PAYG payment summaries.

3.63 Some stakeholders have observed that since the ATO's National Tax Liaison Group FBT subcommittee was disbanded, employers and practitioners no longer have a forum to informally seek the ATO's views on FBT matters. Whilst this issue is out of scope of the current review, the IGT has noted broader concerns with the ATO's public consultation arrangements and has flagged it as an area of potential review in the future.²²⁰

220 IGT, *Our Work Program* (10 April 2014) <<https://www.igt.gov.au>>.

Relevant ATO materials

3.64 The ATO's annual reports provide data on the net cash collections for the FBT and total income tax for the five financial years from 2010-11 to 2014-15. This information is reproduced in Table 3.1 below.

Table 3.1: FBT and total income tax net collections

	2010-11 \$m	2011-12 \$m	2012-13 \$m	2013-14 \$m	2014-15 \$m
Fringe benefits tax	3,303	3,731	3,922	4,077	4,347
Total income tax	199,657	227,737	236,623	242,585	256,896
Proportion of FBT collections to total income tax collections	1.65%	1.64%	1.66%	1.68%	1.69%

Source: ATO.

3.65 Table 3.1 shows that net cash collections for the FBT has increased over the last five financial years, from approximately \$3.3 billion in 2010-11 to \$4.35 billion in 2014-15.²²¹ This represents an increase in FBT collections of approximately 32 per cent over five years. However, FBT collections as a proportion of total income tax collections remain relatively steady at approximately 1.66 per cent over the same period.

3.66 The ATO's *Taxation Statistics 2013-14* provides an indication of the time taken to complete the FBT returns. It is based on the employers' estimate of time taken to complete the return. However, it is up to employers as to whether they provide such an estimate.²²² This data indicates that it takes on average, approximately 12 hours to complete an FBT return.²²³ Similar data was not available for other years.

3.67 The ATO has advised that stakeholder submissions to this review regarding the compliance burden of FBT are consistent with other feedback it has received in previous Government reviews.²²⁴ In this respect, the ATO management view is that legislative change would be required to address most of the concerns.²²⁵ However, it has advised that it has been exploring what can be achieved administratively through its FBT and Remuneration Safe Harbour Working Group (SHWG) to reduce compliance costs.²²⁶

3.68 The ATO has also advised that it is considering two areas identified by the SHWG which may benefit from additional guidance,²²⁷ being practical examples on:

- the level of infrequent/minor use that is acceptable for 'exempt' vehicles; and

221 Commissioner of Taxation, *Annual Report 2014-15* p 36 table 2.6.

222 The ATO's *Taxation statistics 2013-14* suggests that 21 per cent of FBT forms had completed the voluntary 'time taken' field.

223 ATO, *Taxation statistics 2013-14* (18 March 2016) Cost of Compliance, Table 3 <<https://www.ato.gov.au>>.

224 ATO communication to the IGT, 10 March 2016; see also BoT, *Tax impediments facing small business*, above n 73, p 53.

225 ATO communication to the IGT, 10 March 2016.

226 ATO, *Consultation* (2 August 2016) <<https://www.ato.gov.au>>.

227 ATO, *FBT and Remuneration Safe Harbour Working Group – safe harbour topic register* (internal ATO document, 13 August 2015); ATO communication to the IGT, 15 April 2016.

- the application of the minor benefit rule for the provision of food and drink as well as recreational entertainment.²²⁸

3.69 In addition to the above, the ATO has released a Practical Compliance Guideline which is intended to provide employers with a fleet of vehicles a simplified method of determining the taxable value of car fringe benefits.²²⁹

International comparisons

3.70 In the UK, remuneration received by the employee as ‘benefits in kind’ is treated as taxable earnings and only amounts drawn in cash from the benefits plan are subject to withholding.²³⁰

3.71 The US²³¹ and Canada²³² have similar FBT regimes with the benefits being taxable and generally included in the employee’s income.

3.72 New Zealand’s treatment of FBT, like Australia, levies the tax on employers. However the rate of FBT is chosen by the employer based on the ease of calculation, compliance costs, tax savings and whether the benefits are attributed to particular employees.²³³

IGT observations

3.73 As a general principle, simplicity of ascertaining liabilities and compliance with obligations is a key to good tax design. It also promotes voluntary compliance. Uncertainty and high compliance costs seem to have the opposite effect.

3.74 As noted in Chapter 1, the FBT was an integrity measure introduced to address tax avoidance and evasion practices by non-reporting of non-cash benefits to employees. As fringe benefits are generally not expected to comprise the bulk of an employee’s remuneration package, the proportion of taxes collected through the FBT would not be expected to be significantly high. This is reflected in the figures contained in Table 3.1 that the FBT accounts for approximately 1.66 per cent of all income tax collected.

3.75 Notwithstanding the relatively smaller amount of FBT collections, the compliance costs for large employers are relatively high. For example, a recent cost of compliance survey conducted by the Corporate Tax Association found that compliance with the FBT requirements represents the fourth largest component of large employers’ tax compliance costs after income tax, GST and transfer pricing. The average cost for

228 ATO communication to the IGT, 10 March 2016.

229 ATO, *Fleet Cars: simplified approach for calculating car fringe benefits*, Practical Compliance Guide 2016/10 (2016).

230 HMRC, *EIM01143 Employment income: flexible benefit plans* (2 March 2016) Employment Income Manual, Gov.uk <<https://www.gov.uk>>.

231 IRS, *Publication 15-B - Main Content* <<https://www.irs.gov>>.

232 CRA, *Employers' Guide – Taxable Benefits and Allowances* (25 November 2015) Ch 1 <<http://www.cra-arc.gc.ca>>.

233 Inland Revenue, *Fringe benefit tax rates* (11 February 2016) <<http://www.ird.govt.nz>>.

these employers was approximately \$233,000 per annum.²³⁴ Furthermore, the Treasury Stocktake of Regulation report, discussed earlier in this chapter, suggests that costs with respect to the FBT were underestimated and may largely be reflected in costs attributable to external fees which totalled \$14 billion in 2011. The report also noted that FBT affects a small population which makes aggregate figures less useful in indicating the compliance burden for affected employers.

3.76 The available ATO data suggests that the average time for employers to complete an FBT return was 12 hours, while for income returns it was 5.5 hours.²³⁵ It should be noted that these average times do not include time spent on record keeping or ascertaining whether a liability arises at all. It is likely that the costs associated with these latter activities are proportionately higher for FBT.

3.77 To address the complexity of the FBT regime and resulting compliance costs, there are a number of potential options which have different consequences.

3.78 Some of the complexity of the FBT regime may be due to the fact that the provider of the benefit is being taxed rather than the receiver. One option would be to tax fringe benefits as part of salary and wages, that is, tax would be payable by employees but withheld at source by employers. This would be consistent with the approach in the UK²³⁶, the US²³⁷ and Canada²³⁸ where employees are liable for tax on fringe benefits and not employers. However, this option was considered at the time of introduction of the FBT regime but was not favoured by all stakeholders.²³⁹ It also involves a major overhaul of the current system and may not be achievable in the short term.

3.79 Another option would be to maintain the current FBT regime but reduce some of the complexity and costs of complying with it. For example, currently the FBT regime requires employers to consider the 12 different categories of benefits, each with its own calculations, exemptions, and valuations. Consideration could be given to replacing these multiple categories with a single, 'whole-of-benefit' test. Wide-ranging consultation processes would be required to ensure that complexity is reduced and ease of compliance is achieved without affecting the tax base. Whilst this option is not as far-reaching as the first, it is still a significant reform requiring some time to make the best policy decisions and subsequently implementing it.

3.80 A more achievable option in the short term, which may be carried out whilst progressing the second option, would be to reduce the compliance cost by limiting the application of FBT to certain employer groups or to certain fringe benefits. For instance, small businesses with a turnover below a certain low threshold could be exempt from FBT or FBT may be limited to the most common benefits such as car and entertainment. While such exemptions or limitations may ease the compliance burden, carving out particular groups or benefits may result in unintended behaviour. For

234 Corporate Tax Association communication to the IGT, 24 March 2016.

235 ATO, *Taxation statistics 2013–14*, above n 223, Cost of Compliance - table 1 <<https://www.data.gov.au>>.

236 HMRC, *Flexible benefit plans*, above n 230, <<https://www.gov.uk>>.

237 IRS, *Publication 15-B*, above n 231, <<https://www.irs.gov>>.

238 CRA, *Taxable Benefits and Allowances*, above n 232, Ch 1 <<http://www.cra-arc.gc.ca>>.

239 Commonwealth, *Cabinet Memorandum 2875 - Draft White Paper on reform of the Australian tax system*, Decision 5629 (1985) paras [8.7]-[8.21]

example, limiting FBT to commonly provided benefits may result in an increase in the provision of those benefits to which FBT would no longer apply. Therefore, there is a risk of undermining FBT as an integrity measure.

3.81 Other more targeted options to limit the application of FBT include the BoT's recommendations to increase the minor benefits exemption from \$300 to at least \$500.²⁴⁰ Stakeholders, as well as the IGT, support this recommendation as it is a practical way of reducing some compliance costs, for example no calculations would be needed with respect to these benefits. However, it is acknowledged that some compliance costs remain in interpreting terms such as 'minor, infrequent and irregular'.

3.82 It should be noted that the above \$300 threshold has not been increased since 2007²⁴¹ and the suggested increase is timely. Further to the BoT's recommendation, the IGT is of the view that this threshold should be annually indexed to ensure that it keeps pace with economic conditions.

3.83 The BoT also recommended investigation of the possibility of aligning the FBT year to the income tax year.²⁴² The IGT notes that the current FBT reporting date allows time for employees to provide information to their employers to determine the reportable FBT amounts for PAYG payment summaries. If the FBT year was aligned with the income tax year, it would substantially reduce this period down to 14 days which may be insufficient for employers to process the relevant information. The employers' other workload during this time of the year should also be considered. Therefore, further consultation may be necessary to determine the best outcome.

3.84 In considering the above reform options, it should be noted that any reconsideration of the FBT regime needs to examine whether the employer or the employee should be liable for the tax on fringe benefits and which of them should bear the compliance costs. Its role as an integrity measure needs to also be considered. Whilst it may not raise a significant amount of tax compared to the cost of complying with it, its deterrent factor cannot be ignored. A broad review²⁴³ of the FBT regime is required with options to deliver improvement in the short to medium term. It is recognised that some short-term measures may be administratively achievable without legislative change being necessary. These options are explored in the next chapter.

RECOMMENDATION 3.3

The IGT recommends that the Government considers reviewing the Fringe Benefits Tax regime with a view to delivering a reduction in compliance costs in the short to medium term as well as longer term fundamental reform.

240 BoT, *Tax impediments facing small business*, above n 73, pp 54-5.

241 *Tax Laws Amendment (2006 Measure No. 5) Bill 2006*.

242 BoT, *Tax impediments facing small business*, above n 73, pp 54-5.

243 It should be noted that the relevant issues were largely raised in the Government's Tax White Paper. See The Treasury, *Re:think Tax discussion paper* (March 2015) p 56.

ATO response

Matter for Government.

TAXABLE PAYMENTS REPORTING SYSTEM

3.85 Stakeholders have acknowledged the value of the TPRS as an effective tool for promoting voluntary compliance and support its expansion to cover other industries beyond just building and construction. However, the cost of compliance was also raised as a concern. Businesses either have to manually complete TPARs or, to lodge them electronically, they have to acquire the necessary software which may be costly and have compatibility issues with their current systems.

Relevant ATO materials

3.86 The ATO website describes the methods by which employers may lodge their TPAR. These include electronic methods via the ATO Business Portal or Standard Business Reporting (SBR) enabled software as well as by paper lodgement.²⁴⁴

3.87 For employers who wish to lodge their TPAR through SBR enabled software, there are currently 11 SBR enabled software products with TPAR functionality listed on the SBR website.²⁴⁵

3.88 The ATO has advised that of the 91,437 TPARs lodged during the 2014-15 financial year:

- 64 per cent (59,136 lodgements) were lodged via paper – representing businesses with an average of nine contractors;
- 29 per cent (26,779 lodgements) were lodged electronically via the ATO portals and SBR enabled software – representing businesses with an average of 34 contractors; and
- 6 per cent (5,522 lodgements) were processed manually by the ATO as they were received in the incorrect format – representing businesses with an average of five contractors.²⁴⁶

3.89 The ATO has also advised that the paper TPAR form only allows reporting for a maximum of nine contractors and businesses. Accordingly, those who have more than nine contractors and wish to lodge in paper form, have to lodge multiple TPARs.

IGT observations

3.90 As mentioned in Chapter 1, the TPRS was introduced to promote voluntary compliance and to create a level playing field amongst contractors in the building and

244 ATO, *Taxable payments annual report*, above n 25 <<https://www.ato.gov.au>>; and ATO communication to the IGT, 8 July 2016.

245 Standard Business Reporting, *Products by form* – ATO <<http://www.sbr.gov.au>>.

246 ATO communication to the IGT, 8 July 2016.

construction industry.²⁴⁷ TPRS data plays a broader role in the economy and regulatory regimes as it is shared with the FWO and state and territory revenue offices (SRO) as well as being used to identify certain risks, such as phoenix activities.

3.91 The IGT is of the view that there is merit in expanding TPRS to apply to the engagement of all contractors, to foster voluntary compliance with taxation and non-taxation obligations across all industries. Such an initiative would be supported by taxpayers provided any associated compliance costs are kept to a minimum. As noted above, there are already some concerns in this regard.

3.92 Attempts have already been made to reduce the compliance cost associated with the current TPRS by 11 software products being available to facilitate their electronic lodgement. This compares well with 27 software products being available for the electronic lodgement of PAYG payment summary which impacts all employers. However, there are still a high percentage of paper lodgements. A reason for this may be that, the cost associated with acquiring the required software, relative to the number payments made to contractors, is too high. This is supported by ATO statistics that indicated businesses with a greater number of contractors tend to lodge their TPAR via electronic means. Another reason may be compatibility issues with businesses' existing systems.

3.93 The above compliance challenges may be overcome if the relevant information could be automatically provided to the ATO, without the need to lodge TPARs, similar to the automation that is to occur in STP. Such reduction in compliance costs would also facilitate the expansion of TPRS to all engagement of contractors in all industries.

3.94 The key principles of change management in implementing STP, discussed earlier, would also apply to the automation of reporting for TPRS. Similar analysis as in the initial development of STP will be required to determine whether inclusion of TPAR in automated reporting will reduce compliance costs for businesses who are already lodging electronically through SBR enabled software. A number of other issues also need to be considered such as whether a low or no cost solution is required for businesses that are not currently utilising electronic reporting systems.

3.95 There are some key differences between STP implementation and automation of reporting for TPRS. These arise from the fact that STP relates to payment of salary and wages whilst TPRS concerns payment to contractors. Therefore, the relevant amounts for TPRS appear in 'accounts payable' and not in payroll systems and there is less reporting because contract payments are not made as frequently as payment of salary and wages.

3.96 In summary, the expansion of TPRS to all industries and the automation of the required reporting would further promote voluntary compliance whilst minimising overall compliance costs. However, it would be prudent to delay the consideration of such a measure until STP has been fully implemented as augmented by the recommendations of this report.

²⁴⁷ ATO, *Taxable payments reporting – effectiveness measurement* (23 June 2016) <<https://www.ato.gov.au>>.

RECOMMENDATION 3.4

The IGT recommends that the Government considers expanding the Taxable Payment Reporting System (TPRS) to the engagement of contractors across all industries and automating the required reporting under TPRS.

ATO response

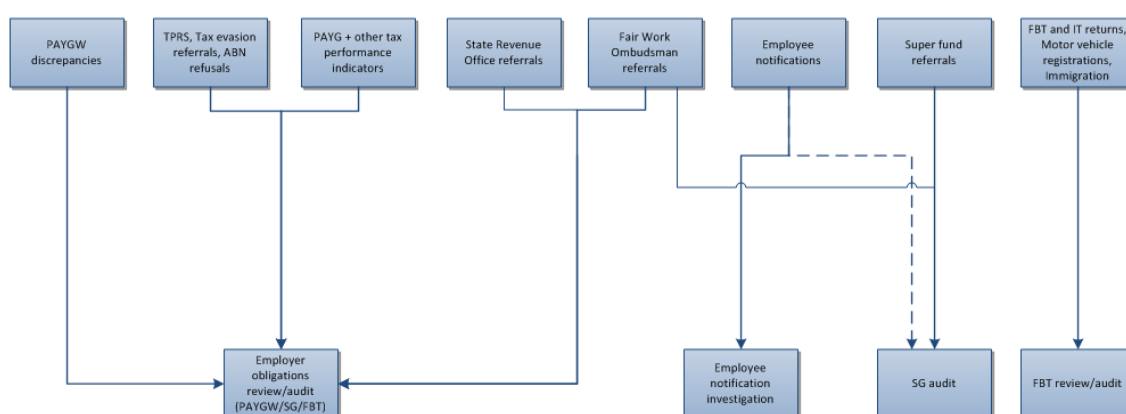
Matter for Government.

CHAPTER 4—EMPLOYER OBLIGATIONS COMPLIANCE ACTIVITIES

BACKGROUND

4.1 The ATO takes a risk-based approach to compliance activities and allocates resources to cases posing the highest risk to government revenue.²⁴⁸ The ATO's risk identification process, with respect to employer tax and superannuation obligations, varies depending on the risks being investigated. It may be targeted to a particular obligation or may involve investigating multiple obligations at once. A diagrammatic representation of how sources of intelligence inform primary risks and trigger different types of compliance activities is produced in Figure 4.1 below.

Figure 4.1: Employer obligations intelligence sources, risks, and compliance activities



Source: IGT based on ATO correspondence.

4.2 The above diagram depicts how the ATO identifies employer obligations risks through a number of sources including third party data, notifications by employees and tax evasion referrals.

Pay As You Go Withholding

4.3 In relation to identifying potential non-compliance with PAYGW obligations, the ATO has advised that it compares amounts reported by employers on their activity statements with amounts on employers' PAYGW annual reports as well as the credits claimed by employees in their individual income tax returns.²⁴⁹

4.4 In order to identify instances where employers have failed to withhold, such as by paying cash wages or incorrectly treating workers as contractors, the ATO utilises a variety of information to assess the risk and select candidates for review. Such information may include income tax performance indicators such as PAYGW as well as benchmark expenses including wages, payment to contractors and superannuation

²⁴⁸ ATO, *Reinventing the ATO, Program blueprint* (March 2015) p 3.

²⁴⁹ ATO, *Employers Failure to Notify or Withhold PAYGW* (internal ATO document, 25 March 2015) p 11.

payments.²⁵⁰ Furthermore, the ATO may receive referrals from external agencies, such as SROs.²⁵¹

4.5 Once PAYGW risks are identified, ATO compliance activities aim to determine the PAYGW amount for each period and ensure that this amount was debited to the employer's account.

4.6 If employers have failed to notify or withhold the appropriate PAYGW liability, the ATO may raise the liabilities based on information available²⁵² or estimates.²⁵³ The ATO may also impose failure to lodge,²⁵⁴ failure to withhold²⁵⁵ and administrative penalties.²⁵⁶

Superannuation Guarantee

4.7 The ATO identifies potential non-compliance with employers' SG obligations through:

- Employee Notifications (ENs) from workers who believe that they are employees and have not been paid the correct amount of SG;²⁵⁷
- data matching, behavioural analysis, which considers employers' compliance histories, and certain high risk industries;²⁵⁸ and
- third party referrals.²⁵⁹

4.8 Where the ATO has identified non-compliance with SG obligations, it may raise an SGC liability. Employers may also be subject to an additional penalty which can be up to 200 per cent of the SGC amount.²⁶⁰

Fringe Benefits Tax

4.9 The ATO utilises data obtained from employer lodged activity statements, FBT returns and income tax returns as the main basis for identifying potential non-compliance with FBT obligations. Intelligence and data is also obtained from

250 ATO, *Risk Treatment Plan Employers Failure to Withhold PAYGW – SBIT* (internal ATO document, 11 September 2014) p 17.

251 Ibid p 17.

252 ATO, *Employer Obligations – Liability Shortfall (LSFO) Method* (internal ATO document, 4 December 2015).

253 TAA sch 1 div 268.

254 Ibid sch 1 s 286-75.

255 Ibid sch 1 s 16-30.

256 Ibid sch 1 s 284-75.

257 ATO, *Report unpaid superannuation contribution from my employer tool* (7 October 2016) <<https://www.ato.gov.au>>.

258 ATO, *Risk Summary – Superannuation Guarantee* (internal ATO document, November 2015).

259 ATO, *Superannuation enquiries* (2 February 2016) <<https://www.ato.gov.au>>; ATO, *Report fraud, scams, tax evasion or a tax planning scheme* (8 June 2016) <<https://www.ato.gov.au>>.

260 SGAA 1992 pt 7.

third parties including motor vehicle registration data, immigration data and Australian Charities and Not-for-profits Commission data.²⁶¹

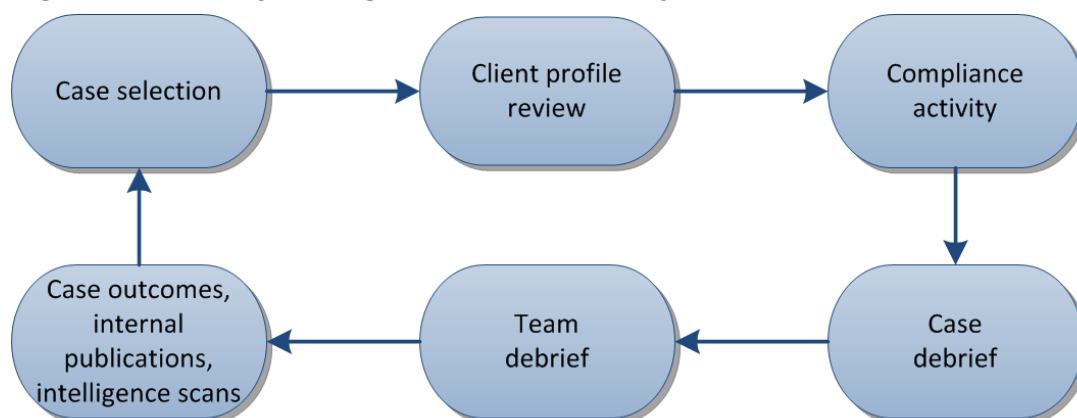
4.10 Employers that provide benefits in kind are required to register for FBT and lodge FBT returns if they have a FBT liability in a particular year.²⁶² Where the ATO identifies discrepancies in FBT returns lodged by employers, the ATO will request amendments to the returns and the lodgement of amended payment summaries to reflect the correct amounts.²⁶³ Employers may also be liable for an administrative penalty where they have understated their FBT liability.²⁶⁴

4.11 Where employers have not lodged their FBT return, the ATO may issue a default FBT assessment.²⁶⁵ The ATO may also impose a failure-to-lodge penalty.²⁶⁶

Broad employer obligations compliance cycle

4.12 Where PAYGW risks are identified, the ATO has advised that it will also investigate other employer obligations such as superannuation and possibly FBT. There are a number of compliance methods which may be employed depending on the circumstances of each case. These methods are part of a broader employer obligations compliance cycle which is diagrammatically represented below in figure 4.2.

Figure 4.2: Employer obligations compliance cycle



Source: IGT based on ATO correspondence.

4.13 In the above diagram, case selection is the process of selecting employers with an identified risk for review or audit. The decision to select an employer for review or audit is based on application of risk ratings and business rules such as a de minimus threshold below which risks are not investigated.

²⁶¹ ATO, *Risk Treatment Plan – Fringe Benefits Tax (FBT)* (internal ATO document, 29 June 2015) p 8.

²⁶² Taxpayers become registered for FBT by completing a registration form, lodgement of an FBT return or as a result of a default FBT assessment.

²⁶³ ATO, *Employer Obligations (EO) Fringe Benefits Tax (FBT) audit method* (internal ATO document, 28 October 2015).

²⁶⁴ TAA sch 1 s 284-75(1).

²⁶⁵ The default assessment is raised under s 73 of the FBTA and considers the guidance provided by PS LA 2007/24 *Making default assessments: section 167 of the Income Tax Assessment Act 1936 and other similar provisions*.

²⁶⁶ TAA sch 1 s 286-75.

4.14 Once a case is selected, pre-compliance profiling is undertaken to determine whether the employer should be excluded from compliance activity. Where the employer is not excluded, the existence of the earlier identified or new risks will inform the choice of compliance activity which is described in the following section.²⁶⁷

4.15 After the completion of each compliance activity, staff are required to complete a case debrief. The debrief captures quantitative and qualitative data which may include reasons for non-compliance such as natural disasters.

4.16 There are also team debriefs which are a qualitative form of intelligence undertaken every two months by each team. The case and team debriefs, combined with case outcomes, filter into internal publications and intelligence scans which are then used to raise awareness of emerging trends and assist in targeting future compliance activities.²⁶⁸

Broad employer obligations compliance methods

4.17 As mentioned earlier, the ATO has different types of compliance activities which are used to investigate the various compliance risks. These are described below.

Reviews

4.18 Since 18 February 2015, the ATO has been conducting streamlined field reviews where an employer has not recently been audited, the potential debts are not excessive and the employer is considered to be at least partially engaged and therefore more likely to meet their compliance obligations.²⁶⁹

4.19 From 2 September 2015, the ATO has also been using streamlined desk reviews. The selection criteria for this type of review are the same as the above field reviews. Desk reviews are generally used when the geographical location of an employer makes field reviews difficult.²⁷⁰

4.20 Both desk and field reviews seek to verify PAYGW and SG compliance, but not FBT and may result in penalties and interest charges on employers for non-compliance. The streamlined field review also considers employers' record keeping practices, payroll information, preparation and lodgement of activity statements as well as the administration of PAYGW and SG.²⁷¹

4.21 The ATO also uses the above two types of reviews to provide education to employers, assist them in complying with their taxation obligations and where necessary, negotiate the collection of any outstanding liabilities.²⁷²

²⁶⁷ For example, cases may be excluded from selection at this stage due to identifying that PAYGW was reported at the incorrect label in the BAS, or because the employer is now insolvent.

²⁶⁸ ATO communication to IGT, 14 June 2016.

²⁶⁹ ATO, *Employer Obligations (EO) – Streamlined field review method* (internal ATO document, 14 January 2016).

²⁷⁰ ATO, *Employer Obligations (EO) – Streamlined desk review method* (internal ATO document, 2 December 2015).

²⁷¹ ATO, *Streamlined field review method*, above n 269.

²⁷² ATO, *Streamlined field review method*, above n 269.

4.22 The ATO has advised that, where there is a high risk that employers in a particular industry are paying cash wages and are not complying with PAYGW and SG obligations, they may use another type of review called ‘Walk in’. It involves an unannounced visit to the employer’s premises where the ATO gathers intelligence, requires completion of a questionnaire and makes ‘real time’ observations to identify risks. Employers are provided with an opportunity to make a voluntary disclosure, are educated on their obligations and informed that further compliance activity may be undertaken.²⁷³

4.23 Where employers do not comply with their obligations during the course of any of the above types of review or significant risks are identified, the review would be escalated to an audit for further investigation.²⁷⁴

Audits

4.24 The ATO may undertake a desk audit where it has identified PAYGW discrepancies. Desk audits are also used in situations where the geographical location of an employer makes field audits difficult. During desk audits, the ATO will seek to gather information in relation to identified discrepancies and correct those discrepancies. Desk audits are not considered appropriate where FBT, contracting arrangements or large employer risks are being examined.²⁷⁵

4.25 The ATO uses field audits where risks and issues have been identified but employers’ circumstances do not meet the streamlined field review criteria, discussed above, or when the ATO considers the employer is not cooperating with a streamlined field review. The field audit also seeks to investigate certain FBT risks.²⁷⁶

4.26 The field audit is conducted on the employer’s premises and involves an interview with the employer, their staff, contractors and representatives. A questionnaire focusing on the identified risks is also to be completed onsite. For example, the questionnaire may focus on any contracting arrangements and the nature of the relationship between the parties.²⁷⁷

4.27 The field audit also involves discussion and analysis of the employer’s records and their record keeping practices for payroll, PAYGW and SG.²⁷⁸

4.28 Where non-compliance is identified, the relevant treatments discussed earlier such as PAYGW estimates and penalties will be applied.²⁷⁹ The ATO uses intelligence gathered from the audit to refer other identified risks to the relevant business lines or external agencies, such as SROs, for further action if necessary.

²⁷³ ATO, *Employer Obligations Walk in risk method* (internal ATO document, 2 June 2015).

²⁷⁴ Ibid.

²⁷⁵ ATO, *Employer Obligations (EO): Desk audit method* (internal ATO document, 21 January 2016).

²⁷⁶ ATO, *Employer Obligations (EO) field audit method* (internal ATO document, 13 January 2016).

²⁷⁷ Ibid.

²⁷⁸ Ibid.

²⁷⁹ Ibid.

Compliance with Contracting Arrangements

4.29 Compliance with Contracting Arrangements (CCA) audits are used to specifically address the risk of an employer failing to withhold PAYG amounts which is usually due to incorrect classification of workers.²⁸⁰

4.30 As part of CCA audits, the ATO obtains contractor payment data for the purposes of income matching, identifying and addressing ABN registration issues as well as to assist in determining the status of the worker, that is, whether they are contractors or employees. This may also involve the use of the ECD Tool.²⁸¹

TPRS Audits

4.31 For employers involved in the building and construction industry, the ATO may conduct specialised field audits to investigate TPRS issues, such as non-lodgement of the TPAR and identified discrepancies.²⁸²

Targeted compliance methods

4.32 The ATO also investigates specific risks associated with SG and FBT. Such investigations may be triggered through risk assessment or by way of a referral following another compliance activity such as the reviews and audits mentioned above.

4.33 Of particular relevance to the concerns raised by stakeholders are the targeted SG audit strategies, namely, the High Risk Employer (HRE) and High Risk Industry (HRI) strategies and the extent to which they sufficiently address non-compliance with SG.

High risk employers and industries

4.34 The HRE and HRI strategies are designed to proactively select industries and employers presenting the highest risk of SG non-compliance for audit.

4.35 The HRE risk assessment considers a number of factors when assessing the risk of employers for audit. It includes a comparison of salary and wage amounts reported by employees to superannuation payment amounts reported by superannuation funds. This comparison is followed by determining the number of employees for whom SG is fully paid as against the total number of employees.²⁸³

280 ATO, *Employer Obligations (EO): Compliance with contracting arrangements (CCA) audit method* (internal ATO document, 27 November 2015).

281 Ibid.

282 Ibid.

283 ATO communication to the IGT, 26 April 2016.

4.36 The HRI strategy targets employers in sub-industries that are considered to have a higher risk of non-compliance with their SG obligations. The sub-industries are selected for targeted audit activity by analysing the outcomes of EN investigations per sub-industry. The ATO then selects a group of sub-industries for targeted education and communication followed by targeted audits in appropriate cases.²⁸⁴

4.37 The two strategies work together as follows:

- Step one - Identify employers presenting a high risk of SG non-compliance and select those with the highest risk rating.
- Step two - Identify high risk industries.
- Step three - Select employers from within each high risk industry that would not otherwise be selected under Step one based on their risk rating.

4.38 As the intention of the HRI strategy is to promote voluntary compliance with SG, the effectiveness of the HRI is measured by comparing the number of SG statements voluntarily lodged in an industry before and after the strategy. This measurement occurs three months after the completion of the strategy to allow for the subsequent quarterly due date to lapse.²⁸⁵

4.39 An internal ATO document indicates that the HRI strategy has demonstrated varying level of effectiveness across different industries. For example, in the most recent group selected for the HRI strategy, which commenced in November 2014 and concluded June 2016, there was a 34.3 per cent increase in voluntary statements lodged for the 'pub, taverns and bars' sub-industry whilst there was a 39.3 per cent decrease in voluntary statements lodged in the 'building and industrial cleaning' sub-industry compared to the level prior to the HRI strategy.²⁸⁶

SUMMARY OF STAKEHOLDER CONCERNS

4.40 Stakeholders have raised a number of concerns with respect to the ATO's end-to-end approach to employer obligations compliance activities. These concerns include that the ATO:

- is heavily reliant on reporting by employees of potential non-compliance of employers and does not sufficiently use third party data at an early stage to improve its risk assessment and case selection processes;
- unnecessarily expands the scope of employer obligations compliance activities to include other obligations which increases the compliance cost for employers and delivers little additional revenue;

284 ATO, *Superannuation Subcommittee submission paper - Selection of SG High Risk Industries for Group Seven* (internal ATO document, 13 August 2015).

285 ATO communication to the IGT, 10 June 2016.

286 ATO, *Selection of SG High Risk Industries for Group Seven*, above n 284 p 2.

- does not adequately enforce FBT compliance other than in relation to cars;
- makes broad information requests which do not provide sufficient context to assist employers' in understanding what information to provide, identify suitable alternative documents, consider the resource impacts on employers, or provide employers sufficient time to respond to requests;
- does not have the technical ability or commercial understanding to consistently determine status of workers and deal with FBT and PSI issues resulting in delays in the resolution of issues due to poor decision-making with inadequate reasons being provided for those decisions; and
- is unduly harsh in its SG compliance activities although it is acknowledged that it may partly be due to the punitive nature of the relevant legislation.

4.41 Some stakeholders have also raised concerns with the ATO's approach to phoenix activities and Director Penalty Notices (DPN). The IGT recently considered these issues and made recommendations with respect to phoenix activities and DPNs in his *Debt Collection* review.²⁸⁷

4.42 Stakeholders held mixed views regarding the difficulties associated with applying the PSI rules. Some stakeholders believe that the PSI rules are too complex while others felt that the rules provide a bright line test for the employee/contractor distinction. In this regard, various aspects of the PSI regime and stakeholder concerns have been recently investigated by the BoT, the Department of Treasury and the ANAO. The key aspects of these reviews were summarised in Chapter 1. Accordingly, this report only considers issues raised that have not already been covered by these reports.

4.43 It is appropriate to delay the consideration of issues raised with respect to phoenix activities, DPNs and PSI rules until recommendations of the above reviews have been implemented and sufficient time has elapsed so that an assessment can be made of the new environment. If these issues persist, they may be detected through the IGT complaint handling service.

ATO USE OF THIRD PARTY REFERRALS IN RISK IDENTIFICATION AND CASE SELECTION

4.44 Stakeholders have raised concerns with the degree to which the ATO currently relies on direct reporting by employers and employees to identify non-compliance with employer obligations. Such reliance is said to create an uneven playing field for employers as there are some that do not accurately report their obligations and may remain undetected.

²⁸⁷ IGT, *Debt Collection* (2015).

4.45 Many stakeholders believe that the ATO should take a more proactive compliance approach by better using third party data to identify risks that may go otherwise undetected. Such third party data may include state payroll information whilst an examination of previous employment relationships or other contractual arrangements may also unearth useful information.

4.46 A small number of stakeholders have raised concerns that the use of third party data without taxpayer knowledge may constitute a breach of privacy. However, the majority of stakeholders are of the view that the third party data should be used and the employer in question be afforded an opportunity to give context or correct the data.

4.47 Stakeholders believe that the above proactive approach is particularly important with respect to SG as many affected employees may not become aware of the non-compliance for a significant period of time after the breach and, in any event, they may be reluctant to inform the ATO of the breach during their period of employment for fear of losing their job. They may also be unaware as to the avenues open to them for redress and, in particular, may be unaware of the ATO's role in this regard.

4.48 To reinforce the importance of a proactive approach, stakeholders have asserted that where non-compliance remains undetected and the employer becomes bankrupt or is liquidated, the amount of unpaid SG cannot be recovered. Unpaid SG is not protected under the FEG. The IGT has previously recommended to the then Government to consider expanding the former *General Employee Entitlements and Redundancy Scheme* (now FEG) to cover unpaid SGC liabilities where a company has been placed in liquidation and the ATO has not been able to recover against the directors personally.²⁸⁸

4.49 It should also be noted that where the ATO decides not to further investigate an employee's claim for non-payment of SG, there are no avenues of appeal for that ATO decision.

Relevant ATO materials

4.50 The ATO has advised that it utilises a variety of information sources in its risk identification and case selection of employer obligations compliance activities, including data and payments directly made to the ATO as well as data from third parties.

288 IGT, *Review into the ATO's administration of the Superannuation Guarantee Charge* (March 2010) pp 92-3.

4.51 The ATO makes use of internal data by:

- matching PAYGW discrepancies with annual amounts reported to the ATO through individual income tax returns;
- comparing employees' salary and wages with estimated employer superannuation contributions; and
- matching the outcome of previous audit work with industry codes.

4.52 To assist with its risk identification and case selection, the ATO also receives third party data, including those from:

- the FWO;
- the various SROs;
- superannuation funds via the lodgement of Member Contribution Statements (MCS) and referrals of potential SG non-compliance; and
- employees who have lodged ENs to the ATO for the potential non-payment of SG.

4.53 The type and use of third party information received by the ATO from the above sources as they relate to employer obligations is described below.

Fair Work Ombudsman referrals to the ATO

4.54 The ATO has advised that it has Memorandums of Understanding (MOU) with the FWO to facilitate the sharing of information.²⁸⁹ At the time of writing, a new MOU was in the process of being drafted.

4.55 The new draft MOU largely reflects the existing MOU in that the ATO receives information from the FWO in relation to their investigations, which may indicate certain:

- employers that have not paid SG;
- employers incorrectly treating employees as contractors; and
- entities and individuals suspected of participating in fraudulent phoenix and cash economy activities.²⁹⁰

4.56 The new draft MOU provides for quarterly meetings between the ATO and FWO to discuss operational compliance activities, such as opportunities for joint activities and high profile issues.²⁹¹

289 ATO communication to the IGT, 8 March 2016.

290 ATO, *Draft Memorandum of Understanding – Data exchange – Schedule* (internal ATO document) p 11.

291 Ibid p 6.

4.57 The ATO has provided statistics on the number of referrals made by the FWO over the five financial years to 30 June 2015 which is shown in Table 4.1 below.²⁹²

Table 4.1: Aggregate FWO referral to the ATO from 1 July 2011 to 30 June 2015

FWO referrals to SG	3500
FWO referrals to Phoenix Taskforce	1
FWO referrals to Employer Obligations	0

Source: ATO.

4.58 The above table shows that a great majority of FWO referrals are made to the ATO with respect to potential SG non-compliance. Only one referral was made concerning potential phoenix activity and none were made to the Employer Obligations business area.

4.59 The ATO has advised that all FWO referrals concerning potential SG non-compliance are placed into the pool of potential HREs and subjected to that risk assessment process, which is described in the background to this chapter. The ATO has advised that it is unable to provide records on whether FWO referrals resulted in compliance activity.²⁹³

State and Territory Revenue Office Referrals

4.60 The ATO has advised that it has MOUs with all of the SROs which allow the exchange of information. The ATO uses this information to identify tax compliance risks including those relating to employer obligations. The exchange of information may either be formal which may occur periodically pursuant to the MOU. It may also be proactive in that one agency may forward information to the other where the former believes the latter would find the information useful. Information may also be requested on an ad hoc basis from one agency to another.²⁹⁴

4.61 The formal exchange mechanism is predominately used by the ATO to identify non-compliance with GST rather than non-compliance with employer obligations.²⁹⁵

4.62 A pilot was conducted for the proactive exchange of information with SRO which resulted in 795 referrals to the ATO.²⁹⁶ However, the ATO ultimately concluded that, whilst the referrals provided valuable information, the number of referrals which resulted in an outcome was relatively low such that the cost of the program outweighed its benefits.²⁹⁷

²⁹² ATO communication to the IGT, 10 May 2016.

²⁹³ ATO communication to the IGT, 26 April 2016.

²⁹⁴ ATO, *Procedural Guide: Exchange of unsolicited information* (internal ATO document, December 2015) p 6.

²⁹⁵ ATO communication to the IGT, 8 July 2016 citing ATO, Memorandum of Understanding, *Subsidiary arrangement – Data exchange* (internal ATO document, 31 March 2014) pp 18, 20.

²⁹⁶ ATO, *Procedural Guide: Exchange of unsolicited information*, above n 294, p 6.

²⁹⁷ ATO, *ATRO Employment Taxes Working Group – meeting minutes* (internal ATO document, 21 October 2014) pp 5-6.

4.63 The ad hoc requests for information between the ATO and SROs²⁹⁸ focus on shared risks. Information shared through ad hoc requests may include the results of SRO audits that identified contractors who are employees for payroll tax purposes.

4.64 Table 4.2 below shows statistics provided by the ATO on the number of referrals received from ad hoc requests, the number that proceeded to audit, the number and aggregate value of audits with an outcome as well as the number of nil outcomes (for completeness) for the last three financial years.

Table 4.2: SRO referrals, ATO audits and outcomes from 1 July 2013 to 30 June 2016

Financial year	Number of cases from ad hoc requests	Number selected for audit	Number with outcome	\$	Number with nil outcome
2013-14	97	23	14	2,106,607	9
2014-15	84	66	31	3,204,050	35
2015-16	6	1	0	0	1
Total	187	90	45	5,310,657	45

Source: ATO.

4.65 The above table shows a decreasing amount of cases received by the ATO in response to ad hoc requests. In 2013-14, 23.7 per cent of cases were selected for audit. In 2014-15, despite receiving fewer cases than the previous year, a greater proportion (78.6 per cent) was selected for audit. Liabilities were raised in 60.9 per cent and 47 per cent of audits for the 2013-14 and 2014-15 financial years respectively.

Superannuation fund – Member Contributions Statements and referrals

4.66 The ATO has advised that all superannuation funds regulated by the Australian Prudential Regulation Authority (APRA) must submit MCSs to the ATO by 31 October each year. Amongst other things, the MCS reports all the contributions received by the superannuation fund for each member during the financial year.²⁹⁹ In this respect, the ATO has advised that the MCS data it receives may be up to 18 months old by the time it is received and available for use in its risk assessment processes.³⁰⁰

4.67 In addition to data in the MCS, the ATO receives proactive referrals from superannuation funds in relation to potential unpaid SG.³⁰¹ During the period from 1 July 2013 to 29 February 2016, the ATO assessed a total of 130 of such referrals.³⁰²

4.68 During the review, the ATO has advised that it upgraded the mechanism by which superannuation funds could lodge a proactive referral with the ATO. Prior to 1 November 2015, proactive referrals were received by the ATO via email. As a result of the upgrade, superannuation funds can lodge their referrals via a new online Fund Notification Form. Whilst it was primarily designed for superannuation funds to

298 ATO, *Memorandum of Understanding - Subsidiary arrangement – Data exchange* (internal ATO document, 31 March 2014) p 5.

299 ATO, *APRA-regulated funds* (8 September 2015) <<https://www.ato.gov.au>>.

300 ATO communication to the IGT, 10 June 2016.

301 ATO, *Proactive SG Compliance Strategy* (internal ATO document, April 2008) p 6.

302 ATO communication to the IGT, 9 March 2016.

report employers' non-compliance with SuperStream requirements, it also allows them to report employers who have not paid an SG contribution.³⁰³

4.69 Unlike referrals from the FWO described earlier, the ATO has advised that superannuation fund referrals are risk assessed separately and not placed into the same pool as HREs. This is because data from superannuation funds is likely to be more recent than FWO referrals as superannuation funds receive quarterly contributions and would know how long it has been since an employer last made a contribution.³⁰⁴

4.70 Where superannuation funds notify the ATO that employers have not paid certain contributions, the ATO would profile the employer to determine the level of risk and refer such matters to the superannuation active compliance teams, now called 'Engagement and Assurance' teams, to determine whether an audit should be conducted.³⁰⁵

4.71 Table 4.3 below sets out the number of proactive superannuation fund referrals and the proportion selected for audit during the 2013-14 to 2015-16 financial years. The number of referrals actioned in the 2015-16 financial year include 57 referrals from the 2010-11 financial year which were misplaced due to a 'routing error' but were found and actioned in early 2016. These referrals are displayed separately in the table for completeness.

Table 4.3: Numbers of proactive superannuation fund referrals, by ATO action and financial year

Financial year	Referrals received	ATO action				Outcome		No Outcome	In Progress
		No further action	%	Selected for audit	%		\$		
2010-11	57	48	84.2	9	15.8	3	101,184	3	3
2013-14	33	13	39.4	20	60.6	10	-	10	
2014-15	33	20	60.6	13	39.4	7	303,145	6	
2015-16	7	5	71.4	2	28.6	1	148,611	1	
Total	130	86	66.2	44	33.8	21	552,940	20	3

Source: ATO.

4.72 The data provided by the ATO in the above table shows that the number of proactive referrals from superannuation funds has decreased significantly in 2015-16. Furthermore, over the period from 2010-11 to 2015-16, approximately one third of all referrals (44) were selected for audit and no further action was taken in relation to the remaining two-thirds (86). An outcome was obtained in 50 per cent (21) of the cases selected for audit with an overall 'strike rate' of 16 per cent.

303 ATO communication to the IGT, 7 April 2016.

304 ATO communication to the IGT, 10 June 2016.

305 ATO communication to the IGT, 9 March 2016.

4.73 For the 2013-14 financial year, over 60 per cent of cases were selected for audit. After factoring in the routing error for 2010-11 which had a low strike rate of 5 per cent, the figures indicate a gradual decline in the number of referrals received from superannuation funds.

4.74 The ATO has advised that there are a number of reasons why 'no further action' may be taken in relation to referrals from superannuation funds. These reasons are outlined in Table 4.4 below including the number of referrals to which they apply.

Table 4.4: Reasons why the ATO did not investigate referrals from superannuation funds

Reasons for 'No further action'	2013-14	2014-15	2015-16	Total (%)
Employer had already been audited for the period	6	5	11	22 (25.6%)
Employer subject to an audit by another ATO unit	0	1	0	1 (1.2%)
An EN investigation is currently in progress	2	6	3	11 (12.8%)
Employer is insolvent	1	1	10	12 (14%)
Employer is deemed to be low risk	0	6	15	21 (24.4%)
Insufficient information to identify relevant entity	4	1	14	19 (22.1%)
Total 'No further action'	13	20	53	86

Source: ATO.

4.75 Table 4.4 indicates that the number of superannuation fund referrals not being subject to any audit action has increased over the 2013-14 to 2015-16 financial years. The main reasons appear to be that employers had already been audited by the ATO or there was insufficient information to identify the employer. There has also been a growth in referrals not being investigated because the employer is insolvent or deemed to be low risk. It is unclear whether the late investigation of 2010-11 cases in the 2015-16 financial year may have contributed to the relatively high number of cases with 'no further action' due to insolvency.

4.76 While the number of proactive referrals from superannuation funds may not be large, the proportion of cases in which audit action is taken is significant. For example, Table 4.3 and Table 4.4 together show that in 2013-14, of the 33 referrals received, 85 per cent were either:

- referred for audit (20);
- closed because a previous audit addressed the period (6); or
- closed because an investigation was in progress (2).

4.77 In 2014-15, the proportion of proactive referrals from superannuation funds was slightly lower at 73 per cent.

Employee Notifications

4.78 The ATO has advised that employees, who believe that their employer is not paying their SG, may lodge an enquiry about their unpaid superannuation using an

online form - 'Employee SG calculator'.³⁰⁶ Employees are required to provide information about themselves, the employer and periods where SG has not been paid.³⁰⁷ The ATO will then advise the employee whether an investigation will take place.

4.79 Table 4.5 shows the number of ENs received and the number of employer audits that were finalised in the five financial years up to and including the 2014-15 financial year. On average, over the five years, the 'strike rate' is 58 per cent per year.³⁰⁸

Table 4.5: Number of Employee Notifications, by ATO action and financial year

	Employee Notifications received	Finalised employer audits resulting from ENs	Finalised audits resulting in raising of liabilities			Finalised audits with no liabilities raised
			No.	%	\$m	
2010-11	18017	17943	11378	63%	329	6565
2011-12	19440	19752	11442	59%	306	8310
2012-13	18564	16976	11413	61%	331	5563
2013-14	21274	18107	11539	54%	417	6568
2014-15	21009	17444	11333	54%	474	6111
Total	98304	90222	57105	58%	1857	33117

Source: ATO.

4.80 The above table shows that the number of ENs received varies over the 2010-11 to 2014-15 period (the lowest number of ENs received was in the 2010-11 year at 18,017 and the highest was 21,274 in 2013-14). The proportion of these audits that resulted in liabilities being raised varies between 54 per cent, in the 2013-14 and 2014-15 years, and 63 per cent in the 2010-11 year.

ATO's move to a proactive approach for SG and PAYGW

4.81 The ATO has advised that, for the period 1 July 2015 to February 2016, the number of full time staff allocated to investigate ENs was approximately seven times more than the number of staff allocated to conduct proactive audits.³⁰⁹ In terms of cases over a longer period, in the five financial years leading to 30 June 2015, the ATO completed 84,058 EN audits³¹⁰ compared with 3,512 proactive SG audits.³¹¹

4.82 The ATO has advised that it has a number of strategies to reduce its reliance on ENs and free up resources for proactive work.³¹² One such strategy involves the superannuation area working with other areas of the ATO to consider SG during broad employer obligations compliance activities.³¹³ The ATO has conducted 32,442 broad

³⁰⁶ ATO, *Unpaid super from your employer* (10 May 2016) <<https://www.ato.gov.au>>.

³⁰⁷ ATO, *Unpaid super*, above n 130, <<https://www.ato.gov.au>>.

³⁰⁸ ATO, *Annual Reports 2010-11, 2011-12, 2012-13, 2013-14, 2014-15, 2015-16* and ATO communication to the IGT, 26 October 2016.

³⁰⁹ ATO communication to the IGT, 9 March 2016.

³¹⁰ ATO communication to the IGT, 15 March 2016.

³¹¹ ATO communication to the IGT, 9 March 2016.

³¹² ATO, *Proactive SG Compliance Strategy*, above n 301, p 4.

³¹³ ATO communication to the IGT, 7 April 2016.

employer obligations reviews and audits in the five financial years to 30 June 2015, with 19,382 cases resulting in SGC liabilities raised, totalling \$531,935,510.³¹⁴

4.83 The ATO has also advised the IGT that it has reduced the number of full audit cases stemming from ENs through its new tailored approach which allows generally compliant employers to 'catch up' on the contributions. This tailored approach is discussed later in this chapter.

4.84 The ATO has also publicly committed in 2015 to estimate the SG gap³¹⁵ which would further inform its future compliance strategies. The SG gap is the difference between the estimated amount of SG theoretically payable assuming full compliance by all employers and the amount actually paid to superannuation funds for a defined period. The ATO had expected to announce the estimate of the SG gap in 2015-16, however, it found that 'methodological improvements and further data were required' and is now expected to provide an update to the House of Representatives Standing Committee on Tax and Revenue in late 2016, together with an overall timetable for completion.³¹⁶

4.85 It should be noted that the ATO also plans to use the 'real time' nature of STP data to proactively address PAYGW³¹⁷ and SG³¹⁸ risks. The Explanatory Memorandum to the STP legislation states that:

More timely information will allow the Commissioner to engage with employers earlier to address cases of non-compliance. This could potentially prevent more punitive outcomes for such employers which would apply under the SG charge regime where non-compliance is identified further down the track.³¹⁹

4.86 Under STP, employers will be required to notify the Commissioner of certain SG related information such as the ordinary time earnings or salary or wages, SG contributions paid to a superannuation fund and any contributions that reduces SGC liability.³²⁰ Towards the end of this review, the ATO advised the IGT that it will obtain this information from two sources. Amounts of ordinary time earnings and salary and wages will be automatically extracted from the employer's payroll software. In relation to SG contributions paid, the ATO plans to obtain the SuperStream data sent by employers to superannuation funds. These two sources together will satisfy employers' SG reporting requirements under STP.³²¹

314 ATO communication to the IGT, 3 June 2016.

315 House of Representatives Standing Committee on Tax and Revenue, '2014 Annual Report of the Australian Taxation Office', Second Report (November 2015), para [2.121].

316 Standing Committee on Tax and Revenue, 2014 Annual Report of the ATO, Second Report, above n 315, para [2.62]; House of Representatives Standing Committee on Tax and Revenue, '2015 Annual Report of the Australian Taxation Office', First Report, paras [2.85], [3.35].

317 ATO, 'SuperStream & Single Touch Payroll - Working together to improve the client experience' (Paper presented at Business Engagement Forum, Sydney, 23 March 2016) p 2.

318 ATO, *STP design workshops*, above n 51 <<http://softwaredevelopers.ato.gov.au>>.

319 House of Representatives, Revised Explanatory Memorandum, *Budget Savings (Omnibus) Bill 2016*, p 265.

320 TAA Sch 1 s389-5(1) item 3.

321 ATO, 'Single Touch Payroll Design walkthrough' (Paper presented at Single Touch Payroll Engagement Forum, 19 October 2016) pp 14-16.

IGT observations

4.87 The IGT has consistently supported the use and refinement of ATO risk assessment tools³²² to appropriately target ATO resources for identifying non-compliance and taking proportionate action. Such an approach should reduce unnecessary costs for both the ATO and taxpayers particularly those that are compliant.

4.88 A key part of the risk assessment process is the effective use of relevant third party referrals including those obtained from other government agencies as well as bodies, such as superannuation funds. There are challenges in this regard such as the timeliness of the provision of reliable information. For example, typically, SROs inform the ATO that a particular employer has incorrectly classified an employee as a contractor, for payroll tax purposes, following the completion of their audits. The information is reliable at this stage but there is a significant passage of time from risk identification by the SRO through to notification to the ATO, the conduct of an investigation and subsequent action. By such time it may be too late for the ATO to recover any SG amounts from an employer, particularly where they have become insolvent.

4.89 The situation outlined above indicates the importance of periodically assessing whether benefits of using certain data from third party referrals are so limited as to be outweighed by its costs. Strike rates are a good indication. They involve analysing the use of particular third party referrals to determine the percentage of cases where their use has led to corrective action being taken following an audit. Included in this percentage should be instances where the referral identifies risks that have already been addressed. For example, based on the IGT's processing of ATO material, it appears that whilst there are a relatively small number of referrals from superannuation funds, the strike rate is high because the majority of such referrals have identified risks that have already been addressed or have resulted in an audit with subsequent corrective action. The ATO's current analysis of data and calculation of the strike rate only considers instances where the ATO takes action as a result of the referral.

4.90 Analysing the utility of third party referrals all the way to case outcome also provides an opportunity for the ATO to identify what is working well in the referral process as well as areas for improvement. For example, the number and reasons for why 'no further action' was taken on a referral can assist with refining the referral process. Tables 4.3 and 4.4 together show that 19 out of the 130 unsolicited referrals received from superannuation funds were treated as 'no further action' as there was insufficient information provided to identify the relevant entity. Accordingly, further inquiry could determine the type of missing information that prevented the referral from being actioned and subsequent adjustment made to the online Fund Notification Form to ensure the future capture of such information.

4.91 The ATO currently does some analysis of data from ENs, superannuation fund referrals, and ad hoc referrals from SROs but not referrals from the FWO. The IGT

322 IGT, *Review into aspects of the Australian Taxation Office's use of compliance risk assessment tools* (October 2013).

is of the view that the ATO should improve its analysis as described above and extend it to all sources of third party data including FWO referrals.

4.92 The more extensive analysis of third party data, suggested above, should validate the effectiveness of the source and, where possible the ATO should seek to maximise its use of those sources. For example, given the high strike rate when data from superannuation fund referrals is used, the ATO should seek to encourage superannuation funds to make more referrals. Whilst there may be some reluctance by some superannuation fund trustees to do so due to their contractual relationships with employers, they are ultimately charged with a responsibility to act in the best interest of their members who depend on SG contributions to help fund their retirement income.

4.93 One of the ways to encourage referrals from superannuation fund trustees is to increase their awareness of the ATO's Fund Notification Form. The IGT believes that the ATO may collaborate with trusted third parties, such as APRA or superannuation industry bodies, and issue joint letters to the trustees to highlight the importance of maintaining the integrity of the system through referrals and assure them that their confidentiality would be strictly observed. The ATO should also point out to the trustees that they would not be informed of any action taken as a result of the referral due to the corresponding confidentiality owed to the employers.

4.94 Another potentially valuable data source, in the future, is STP which may provide 'real time' data with respect to PAYGW and SG. This would be particularly beneficial for SG compliance because employers, generally, pay SG directly to superannuation funds, and presently the ATO does not have visibility over the timing and amount of SG payments. Only SGC payments are made to the ATO as described in Chapter 1.

4.95 As stated in Chapters 1 and 3, STP will not provide a complete data set for some time. Large employers will not be required to comply until 1 July 2018 and small employers will not be required to adopt STP unless the legislation is amended. Until all employers are required to remit data and payments to the ATO under STP, the ATO will experience limitations in detecting potential non-compliance in relation to a large proportion of employers. Furthermore, even if STP becomes mandatory for all employers, some time will be required before meaningful trend analysis can be conducted.

4.96 Furthermore, as STP data does not confirm amounts received by superannuation funds, the ATO may face similar limitations under the current system as it will need to await payment information before it can fully verify compliance. This challenge can be easily overcome in relation to PAYGW as the ATO will receive the monthly or quarterly remittance of PAYGW amounts and can conduct reconciliation of the data reported.

4.97 This above challenge cannot be as easily overcome in relation to SG as the ATO does not receive SG contributions in the normal course of events. One solution may be to obtain confirmation of SG payment from superannuation funds in the form of MCS. However, as MCS are compiled and provided annually there can be significant delays, up to 18 months, before the ATO is in a position to conduct

reconciliation and become aware of unpaid SG. Another option would be for the ATO to obtain SuperStream payment data. Although such data could be obtained through employers' STP compliant software and clearing houses, these sources would not confirm that the correct amount of SG has been paid on time. If such data was obtained from the superannuation funds, it would confirm whether payments were received by the funds and whether those payments were made on time.

4.98 Obtaining SuperStream data directly from superannuation funds would also provide the ATO with greater visibility with respect to the level of SG compliance than obtaining it through STP as fewer employers are required to comply with STP than with SuperStream. The ATO can use the SuperStream data, obtained from superannuation funds, in conjunction with PAYGW data to estimate potential SG shortfalls. However, some allowance should be made to account for minor errors in calculating PAYGW which are later corrected by the employer.

4.99 Some stakeholders have raised privacy concerns about the ATO's use of third party data. It should be noted that the ATO is required to abide by the *Privacy Act 1988*, the Privacy Commissioner's Privacy Principles (APPs) as well as his *Guidelines on Data Matching in Commonwealth Administration* which relates to agencies' access and use of data for programs.³²³ The ATO has also provided management representation that this data is only used for risk identification and would not be used for other purposes including amending assessments.³²⁴

RECOMMENDATION 4.1

The IGT recommends that the ATO:

- (a) *improves its PAYGW and SG risk identification process by analysing the utility of data from third party referrals with a view to maximising the use of sources which yield the best results;*
- (b) *improves its SG risk identification process by:*
 - i) *encouraging trustees of APRA-regulated superannuation funds to refer more relevant data; and*
 - ii) *obtaining SuperStream payment data from superannuation funds for employers not required to use STP to promptly identify those not reporting or paying SG.*

ATO response

Agree with recommendation 4.1(a).

Agree with recommendation 4.1(b) (i).

Disagree with recommendation 4.1(b) (ii).

323 Office of the Australian Information Commissioner, *Guidelines on Data Matching in Australian Government Administration* (June 2014) <www.oaic.gov.au>.

324 ATO communication to the IGT, 3 August 2016.

We will explore options, including through APRA, to promote awareness of and channels for APRA regulated funds to report SG compliance matters. This was also addressed in a recent ANAO recommendation.

We recognise that if Single Touch Payroll is not extended to employers with fewer than 20 employees that there will still be limitations in identifying SG risks posed by these employers. However, until a decision is made by the Government about whether to extend Single Touch Payroll to cover these employers, and the design of STP implementation is finalised, we think it is premature to pursue an alternative option to obtaining the SuperStream data.

COMPLIANCE ACTIVITIES

4.100 Stakeholders have raised concerns about the effectiveness of audits in addressing risks associated with employer obligations, especially in the area of SG as left untreated, it would have wide ranging impacts on employees, employers and government more broadly.

4.101 In contrast, other stakeholders have raised concerns with the scope of employer obligations compliance activities. They believe such activities are frequently expanded beyond the initial identified risk. For example, stakeholders have commented that an employer may be selected for audit due to a discrepancy identified with PAYGW which is then expanded to investigate unpaid SG amounts and FBT over multiple periods. Stakeholders believe that such expansion often achieves immaterial adjustments and imposes unnecessary compliance cost on employers.

Relevant ATO materials

4.102 As described in the background to this chapter, the ATO utilises a number of broad and targeted review and audit methods to identify and address PAYGW, SG and FBT risks. In the five years up to and including the 2014-15 financial year, the ATO has conducted 125,825 such compliance activities.

4.103 Unpaid SG is investigated in almost all of the above compliance activities. Approximately 70 per cent of all SG compliance activities were audits conducted in response to ENs. There was an outcome, that is, at least a portion of unpaid SG was recovered, in 70 per cent of all EN related audits.

4.104 The remaining compliance activities consisted of broader employer obligations audits and reviews (27 per cent), proactive audits undertaken by superannuation areas (3 per cent) and audits as a result of superannuation fund referrals (0.03%).³²⁵

4.105 The ATO has advised that risk identification and case selection for broad employer obligations compliance activities is predominately identified through PAYGW discrepancies.³²⁶ Case selection is further refined through pre-compliance profiling.³²⁷ The ATO has advised that, in the five financial years up to and including

³²⁵ ATO communication to the IGT, 3 June 2016.

³²⁶ ATO, *Employers Failure to Notify or Withhold PAYGW*, above n 249, p 11.

³²⁷ ATO, *Risk Treatment Plan Employers Failure to Withhold PAYGW*, above n 250, p 17.

the 2014-15 financial year, such profiling has excluded approximately 40 per cent of cases initially identified.³²⁸

4.106 As part of the profiling, the ATO will consider whether other risks such as SG or FBT should be investigated using the field audit method (FBT risks are not investigated using desks audits or the streamlined review methods).³²⁹ The ATO has advised that approximately 75 per cent of broad employer obligations audits may expand to all risks (field audits), while the remaining 25 per cent are desk audits involving PAYGW and SG only.³³⁰

4.107 Table 4.6 below sets out the number of broad employer obligations compliance activities conducted in the five financial years leading to 30 June 2015, the overall outcome and the outcome for each employer obligation.

Table 4.6: Broad employer obligations compliance activities completed from 1 July 2010 to 30 June 2015, by number, outcome, and revenue raised

Employer obligations	Number	Per cent	Revenue raised
No. of Cases	32,442	100	
No. of outcomes	26,532	82	
- PAYGW	23,415	72	\$ 1,574,300,365
- SG	19,382	60	\$ 531,935,510
- FBT	793	2	\$ 15,885,508

Source: ATO.

4.108 The ATO has conducted 32,442 broader employer obligations compliance activities and has raised liabilities in 26,532 cases with an overall strike rate of 82 per cent. The outcomes for PAYGW (72 per cent) and SG (60 per cent) were considerably higher than the outcomes for FBT (2 per cent).³³¹

4.109 The ATO has also advised that since the introduction of streamlined reviews, the time for field investigation has been reduced from 114 to 35 days in some cases. The ATO has advised that debts raised under the streamlined review method are more likely to be collected than under its previous approach.³³²

IGT observations

4.110 As compliance activities can be a resource intensive and costly exercise for the ATO and employers, it is important that where they do occur, they are effective in identifying and addressing risks.

³²⁸ ATO communication to the IGT, 13 July 2016.

³²⁹ For example, where the employer is not registered for FBT and a motor vehicle registration search shows no evidence of car fringe benefits as per ATO procedures - *Employer Obligations (EO) - How to complete the EO audit confirmation letter: Period of review (POR) and Schedules* (internal ATO document 24 August 2015).

³³⁰ ATO communication to the IGT, 14 June 2016.

³³¹ ATO communication to the IGT, 19 February 2016.

³³² ATO, *Small Business / Individual Taxpayers - Employer Obligations, How we are changing the client experience* (internal ATO document) p 3.

4.111 As mentioned earlier in this chapter, one of the risks that employer obligations compliance activities seek to address is unpaid SG. Information provided by the ATO indicates that 70 per cent of the investigations into unpaid SG are in response to ENs. This raises a concern that the origins of the bulk of the compliance activities may not sufficiently address the proportion of employees who are more vulnerable to non-compliance and do not lodge ENs for fear of losing their jobs, including those from non-English speaking backgrounds or in casual or part time employment.³³³

4.112 Unpaid SG, if left undetected and untreated, can have wide ranging and adverse impacts. Firstly, the affected employees miss out on superannuation entitlements which impacts their standard of living in retirement and increases their reliance on the Age Pension. Correspondingly the Government would be exposed to higher Age Pension outlays which would be funded by future generations.³³⁴

4.113 Secondly, compliant employers are adversely affected in that an uneven playing field is created where non-compliant employers obtain an unfair advantage if they remain undetected. Such non-compliance may propagate a domino effect. For example, if there are a number of businesses in the same geographic area offering the same services and one of them is not paying the correct amount of SG for their employees, the other business may be forced to follow suit in order to remain competitive.

4.114 The IGT recognises that, when implemented, STP will improve the SG risk identification, however, it will not be sufficient of itself as currently a significant portion of employers are not required to adopt STP.

4.115 As a result, it is crucial that the ATO considers other proactive approaches in addressing SG risks at the earliest possible stage. One option would be to conduct some random audits as considered in a broader context in the IGT's review of the ATO's risk assessment tools.³³⁵ The ATO has previously rejected such an option.³³⁶

4.116 Whilst carrying out random audits may expose some compliant employers to unnecessary compliance cost, these costs and inconveniences may be minimised by the manner in which the ATO might conduct the audits. The IGT noted in a previous review that such costs may also be mitigated by the ATO reimbursing compliant taxpayers for any additional compliance cost incurred.³³⁷ Furthermore, such costs and inconveniences should be weighed against the potential disadvantage that the very same compliant employers face if their competitors do not pay SG and remain undetected. It should be noted that, in the long term, random audits may also lead to better targeting of non-compliant taxpayers. As the ATO's current risk assessment processes rely largely on reported data, these audits may be the only way that the most non-compliant employers can be detected. Certain common characteristics of

333 IGT, *Review into the ATO's administration of the Superannuation Guarantee Charge* (March 2010) p 6.

334 Ibid.

335 IGT, *Review into aspects of the Australian Taxation Office's use of compliance risk assessment tools* (October 2013) pp 126, 145-7.

336 IGT, *Review into the ATO's administration of the Superannuation Guarantee Charge* (March 2010) p 8.

337 IGT, *Review into aspects of the Australian Taxation Office's use of compliance risk assessment tools* (October 2013) p 146.

non-compliant taxpayers may also be exposed and they could be used to improve the ATO's current risk assessment tools.

4.117 The IGT continues to receive complaints from employees whose superannuation entitlements have not been paid and who are unlikely to be able to recover such unpaid amounts due to, for example, the employer becoming insolvent by the time any recovery action can be initiated. Both the Government and the ATO are aware of these challenges and since the IGT carried out its review of SGC,³³⁸ they have taken a number of positive steps to address it.³³⁹ However, further measures including the use of deterrents, such as random audits, may need to be considered. Better detection and resulting improvement in SG compliance would ultimately reduce employees' reliance on the Age Pension.

4.118 Turning to the issue of compliance activities being expanded beyond the identified risk giving rise to them, it is reasonable to expect that expansion should be proportionate to the likelihood of additional risks. In this regard, the ATO has provided some justification, in particular with respect to expanding PAYGW audits to also cover SG.

4.119 The ATO's outcomes for PAYGW, SG and FBT compliance activities indicate that there is a correlation between raising PAYGW and SG liabilities with respect to the same employer with 'strike rates' being 72 and 60 per cent respectively. Thus PAYGW discrepancies are a reasonably effective indicator of SG non-compliance. This is not surprising given that the definition of employee for SG purposes is, in essence, the expanded definition of that used for PAYGW.

4.120 The ATO correlation data on audit outcomes also indicates that a relatively small number of broad employer obligations compliance activities resulted in FBT liabilities (2 per cent). This may be partly due to the investigations in these field audits being limited to profiling where no information is requested from the employer. In such circumstances, from the employer's perspective, FBT has not been 'investigated'. It is not clear whether the absence of any correlation is due to no liabilities being raised after thorough investigations, or alternatively, the FBT aspects of the audits not being progressed beyond profiling.

RECOMMENDATION 4.2

The IGT recommends the ATO seeks further means of ensuring superannuation entitlements are paid promptly including the use of deterrents, such as random audits, to curtail the propagation of non-compliance - compliant employers who undergo such audits should be reimbursed for any additional costs.

³³⁸ IGT, *Review into the ATO's administration of the Superannuation Guarantee Charge* (March 2010).

³³⁹ For example, targeting compliance activities for HRE and HRI.

ATO response

Disagree with recommendation 4.2.

We do not support random audits as a cost effective approach to compliance. As the report acknowledges, we have an active and diverse set of strategies in respect of SG compliance that delivers significant benefits for employees who have not otherwise received their entitlements.

Random audits are an untargeted approach that imposes unnecessary costs and time burdens on compliant taxpayers. Investment in random audits would be at the expense of more effective and beneficial approaches.

STP will provide a new source of data that will further assist our targeted approaches.

The ATO is already investigating the use of educational reminders and prompts to deter non-compliance as part of our SG compliance strategies.

FRINGE BENEFITS TAX

4.121 As mentioned in Chapter 3, the breadth of the existing FBT regime imposes a high level of compliance cost on employers, making it difficult to achieve full compliance, whilst not raising a significant amount of revenue compared to income tax. The challenge is not limited to small employers alone. Large employers are required to determine FBT liability for large numbers of employees and given its complexity, accurately capturing every fringe benefit provided to each of them may not always be achievable.

4.122 Based on the above, there is a view that there is a significant level of unintentional or unavoidable FBT non-compliance which by its very nature is undetected. Certain stakeholders believe the ATO's level of compliance activity in this area may be due to the fact that the ATO is cognisant of the challenges employers face in their efforts to fully comply.

Relevant ATO materials

4.123 The ATO has provided data on the number and type of compliance activities undertaken which have considered FBT risks. This is set out in Table 4.7 below.

Table 4.7: FBT liabilities raised from compliance activities

Primary risk		2010-11	2011-12	2012-13	2013-14	2014-15
Audits	Amount	\$12,282,261	\$23,273,243	\$16,860,277	\$27,564,282	\$56,623,753
	No.	292	384	367	704	787
- FBT		28	64	24	255	372
- GST		173	139	140	214	219
- Income tax		8	12	16	49	17
- Luxury Car Tax		-	-	1	-	-
- PAYG W		83	169	186	186	179

Table 4.7 continued

Primary risk		2010-11	2011-12	2012-13	2013-14	2014-15
Reviews	Amount	\$5,694,641	\$4,039,851	\$6,717,526	\$12,559,037	\$8,127,261
	No.	134	191	1,257	1,070	578
- FBT		111	170	1,222	1,028	529
- GST		17	9	9	9	10
- Income tax		6	12	26	32	35
- Luxury Car Tax		-	-	-	1	4
Compliance agreement	Amount	\$0	\$2,391,497	\$0	\$0	\$0
	No.	3	2	1	-	-
- FBT		3	2	1	-	-
Investigate and prosecute	Amount	\$0	\$0	\$0	\$0	\$0
	No.	-	-	-	-	1
- FBT		-	-	-	-	1
Grand Total	Amount	\$17,976,901	\$29,704,592	\$23,577,803	\$40,123,319	\$64,751,014
	No.	429	577	1,625	1,774	1,366

Source: ATO.

4.124 The above table shows that there has been a general increase in the number of targeted FBT audits over the last five financial years up to and including the 2014-15 year. The ATO has advised that in addition to targeted FBT audits and reviews, FBT may also be investigated as part of other types of audits, such as GST and income tax, depending on outcomes of its risk assessment processes. In the five financial years up to and including the 2014-15 year, the ATO has raised additional FBT liabilities of \$176,133,629.³⁴⁰

4.125 The ATO has advised the IGT that key FBT compliance risks, generally, relate to car fringe benefits and outstanding FBT lodgements. Auditors in Employer Obligations teams are advised to close the FBT aspect of the audit where car fringe benefits are not provided by the employer, unless there is strong evidence of other FBT non-compliance.³⁴¹ If the auditor identifies that car fringe benefits have been provided by the employer, the auditor will also obtain the relevant documentation to calculate the taxable value of other benefits such as health insurance premiums, a mobile phone or home computer.³⁴²

4.126 The ATO publishes the number of FBT compliance activities conducted in the appendices to its annual report³⁴³ and provides an indication of its areas of focus on its website.³⁴⁴ Although the ATO may provide a detailed list of focus areas for its compliance activities as well as a list of common mistakes in its presentations at

³⁴⁰ ATO communication to the IGT, 19 February 2016 and 10 March 2016.

³⁴¹ ATO, *Employer Obligations Fringe benefits tax (FBT) audit method* (internal ATO document, 28 October 2015) p 1.

³⁴² Ibid p 5.

³⁴³ Commissioner of Taxation, *Annual Report 2014-15* (October 2015) p 100.

³⁴⁴ ATO, *What attracts our attention* (25 May 2016) <<https://www.ato.gov.au>>.

external forums, such lists are not always published or otherwise freely accessible by the public.³⁴⁵

IGT observations

4.127 As mentioned in the previous chapter, the key to addressing stakeholders' concerns is to focus on appropriately limiting the scope of the FBT regime to ease the compliance burden and the ATO enforcing compliance with the resulting regime more strictly. Such an approach would also create a more level playing field as more employers would be better placed to comply.

4.128 In the previous chapter, a recommendation has been made to the Government to review the FBT regime with the above goal in mind. However, the IGT believes that the ATO could take some remedial action in the meantime. One option would be for the ATO to publically announce its area of FBT compliance focus for coming years as it used to do more broadly in its Compliance Program.³⁴⁶ Such action is consistent with a recommendation by the Productivity Commissioner that regulators should provide clear guidance on enforcement priorities, especially where resource constraints cannot be addressed in the short term.³⁴⁷

4.129 For example, currently, key FBT risks that the ATO seeks to address include the provision of cars and entertainment to employees. More detailed information on these risks, for example the correct use of depreciation values and rates, could be made public on the ATO website for coming years to raise awareness, focus employer attentions on target areas and further improve voluntary compliance. Such an approach would also result in a reduction in the overall compliance burden and create a more level playing field.

RECOMMENDATION 4.3

The IGT recommends the ATO publicly announce its areas of FBT compliance focus for future year(s).

ATO response

Agree with recommendation 4.3.

We will include, on our 'Building Confidence' site, material which expressly outlines our FBT compliance focus and priorities for the FBT year.

Further, as part of our commitment to transparency we will continue to provide information on the approaches we are taking and the issues and risks we typically encounter in FBT on our 'What attracts our attention' site, with targeted guidance (including FBT specific webinars), and through industry forums and other public engagement events which reach a range of employers.

³⁴⁵ ATO, Meeting your annual FBT obligations (presentation February 2016) unpublished.

³⁴⁶ ATO, *Compliance in focus 2013-14* (July 2013).

³⁴⁷ Productivity Commission, *Regulator Engagement with Small Business*, above n 80, p 20.

INFORMATION REQUESTS AND TIMEFRAMES IN COMPLIANCE ACTIVITIES

4.130 Many stakeholders have raised concerns that the ATO's information requests, during employer obligations compliance activities, are too broad, do not consider the resource impacts on them and the time provided for an appropriate response is insufficient. The situation is further exacerbated by the paucity of reasoning or context being provided such that they are not in a position to, for example, provide alternative documents where the requested documents are not readily accessible.

4.131 A number of examples were provided as part of submissions to this review and in specific complaints lodged with the IGT. The majority of the concerns related to the costs and impacts of information requests.

4.132 In a more extreme example, the employer was asked to provide information for every employee over a three year period in relation to SG. The auditor had requested the employer to submit the information via fax and informed the employer that only a one-week extension could be granted under 'federal law'.

4.133 In another example, an audit involved multiple companies in the same group, for multiple years with respect to all employer obligation tax risks. The ATO information request did not consider the complexity of the employer's payroll system or the resources required to extract the necessary information. The audit resulted in an amended assessment and was only resolved at the objections stage when a face-to-face meeting was held with the ATO.

4.134 In addition to the adverse impact on their resources, stakeholders believe that the above practices prolong the length of compliance activities and potentially give rise to disputes that could have been avoided.

Relevant ATO materials

4.135 The ATO has advised that its principles with respect to information gathering are set out in its publication entitled: *Our approach to information gathering*. It states that taxpayers can expect the ATO to provide an opportunity to discuss the scope, appropriateness and relevance of the information requested and work with taxpayers to identify alternative documents where they have difficulties in providing the documents that were requested.³⁴⁸

4.136 The publication also sets out the timeframes for requesting information, and states that:

- the period of time is generally 28 days, and while extensions are not normal practice, they may be granted in some circumstances;
- consideration is given to the nature, extent, and urgency of the information requested; and

³⁴⁸ ATO, *Our approach to information gathering* (22 December 2015) <<http://www.ato.gov.au>>.

- consideration is given to a taxpayer's locality, the availability of information, processes necessary to retrieve, and cost of compliance.³⁴⁹

4.137 The ATO has also advised that its active case management guidelines for employer obligations reinforce the above flexible timeframes.³⁵⁰ There is an exception with regard to seeking lodgement of overdue statements.³⁵¹ In such cases, staff may consider negotiating a staggered lodgement plan where there are several overdue lodgements spanning more than one financial year.³⁵²

4.138 The ATO may narrow the scope of an audit without requesting information from the employer based on business profiling which takes place during the planning phase of the audit as set out in the background section to this chapter. For example, where profiling confirms no motor vehicles exist for FBT purposes, such information may not be requested from the employer by the ATO auditors.

4.139 The ATO has advised that the application of the audit approach, including information requests, is guided by the procedures relating to the specific methods and discussions amongst the staff, their team and technical leaders.³⁵³

4.140 The ATO has provided representation that there is no specific direction given to staff on the degree of information required to test a particular risk and that discretion is provided in determining the information the auditor believes is required to investigate that risk.

4.141 The ATO provides instructions to staff³⁵⁴ and requires them to tailor information requests based on profiling.³⁵⁵ The ATO's methods and procedures state that audit confirmation letters which request information must be approved by team or technical leaders prior to being issued unless they are issued without modification. In such cases, there may be approvals sought from peers.³⁵⁶

IGT observations

4.142 As mentioned earlier in this chapter, seeking to comply including assisting the ATO with its compliance activities imposes a significant burden on employers. Therefore, it is important that information requests do not impose any additional cost that can be avoided through appropriate discussions which may lead to better identifying the required information.

349 Ibid.

350 ATO, *Employer obligations (EO) – Active case management guidelines* (internal ATO document, 1 June 2016).

351 For example, ATO, *Employer Obligations (EO): Desk audit method*, above n 275, task 3.1.10.

352 ATO, *Risk Treatment Plan Employers Failure to Notify PAYGW – SBIT* (internal ATO document, 11 September 2014) step 2.

353 ATO communication to the IGT, 27 July 2016.

354 ATO, *How to complete the EO audit confirmation letter*, above n 329.

355 For example, ATO *Employer Obligations: Compliance with contracting arrangements audit method*, above n 280, task 3.1.

356 ATO, *Employer Obligations (EO) field audit method*, above n 276, task 3.4.

4.143 In a number of previous reviews, the IGT has considered the ATO's information gathering processes across various ATO business lines.³⁵⁷ These reviews prompted the ATO to develop the *Our approach to information gathering* publication which generally reflects the above principles. This publication indicates that at a corporate level, ATO management have set appropriate principles in relation to how staff are expected to manage information requests.

4.144 The above principles, however, do not appear to be supported by sufficient practical guidance as to how they should apply in a review or audit context. For example, the relevant staff are not advised on the use of business profiling for estimating the amount of time the employer might require to respond to an information request. Accordingly, the IGT believes that the ATO could provide more practical guidance, such as common scenarios in training materials, to compliance staff on tailoring an information request, being cognisant of its impact on the employer and considering alternative sources of information in appropriate circumstances.

RECOMMENDATION 4.4

The IGT recommends the ATO supplement the principles contained in its 'Our approach to information gathering' booklet with practical guidance, such as common scenarios in training materials, to assist compliance staff to apply them in the context of an employer obligations audit or review.

ATO response

Agree with recommendation 4.4.

We agree with this recommendation and will incorporate the examples provided by the IGT as practical scenarios into existing training material to provide further guidance to staff when undertaking an employer obligation audit or review.

TECHNICAL EXPERTISE AND DISCIPLINE

4.145 Stakeholders have raised concerns that the relevant ATO officers do not have the technical ability or commercial understanding to consistently determine the status of workers and deal with FBT and PSI issues. Examples include auditors relying solely on the ECD tool or checklists to determine audit outcomes, with inadequate reasoning being provided for decisions. The lack of sufficient reasoning provided by ATO officers in these situations has led to employers questioning how the law was applied and what use was made of the information they had provided at the ATO's request.

4.146 Some stakeholders also raised particular concerns regarding ENs. They believe that the ATO does not adequately communicate the outcome of EN investigations or its decision to decline to investigate ENs. The IGT has previously investigated such concerns in 2010 and made a recommendation to the ATO on improving communication to employees through appropriate and personalised letters

³⁵⁷ IGT, *Review into the ATO's compliance approaches to small and medium enterprises with annual turnovers between \$100 million and \$250 million and high wealth individuals* (December 2011); IGT, *Report into the Australian Taxation Office's large business risk review and audit policies, procedures and practices* (May 2011).

in relation to collection and non-collection of SGC.³⁵⁸ The IGT has also completed a follow up review into the ATO's implementation of agreed recommendations in 2014 and considered that the ATO had implemented this recommendation.³⁵⁹

Relevant ATO materials

4.147 The ATO has provided senior management representation that it manages its workforce through its workforce planning infrastructure which has the following features:

- Effective structural design to ensure jobs are designed in a way to provide meaningful and correct work at the right level with built-in stretch opportunities to build capability for the future
- Built-in technical leader roles (in addition to the team leader) that provide the technical leadership and mentoring to less experienced staff
- Routine succession risk analysis is undertaken to assess the likelihood and impact of employees leaving ahead of time to identify opportunities for skills and knowledge transfer prior to departure
- Single-source skill and knowledge dependencies are minimised through structural and job design by broadening [staff] skill base through exposure to various work which results in spreading capability across a range of officers to minimise succession risk.³⁶⁰

4.148 The ATO has also provided management representations that it develops and manages capability through the following measures:

- Employees are mapped to Employer Obligation Audit jobs through their position numbers
- These jobs have defined capability and knowledge requirements
- Employees in these positions are assessed against these capabilities and knowledge requirements
- This information is aggregated at the corporate level on an ongoing basis to ensure:
 - That the ATO has the required number of capable employees to perform [employer obligations] Audit jobs to deliver business outcomes
 - That employees themselves have attained the capabilities and knowledge to perform these jobs

358 IGT, *Review into the ATO's administration of the Superannuation Guarantee Charge* (2010) p 61.

359 IGT, *Follow up review into the ATO's implementation of agreed recommendations in the five reports released between August 2009 and November 2010* (July 2014) p 78.

360 ATO communication to the IGT, 7 July 2016.

- That capability gaps are identified early and a plan can be developed between the manager and the employee to develop these requirements
- The performance process (COMPASS) is used as the vehicle for the discussion, the plan going forward and also the ongoing monitoring of progress into the future. In Employer Obligations, team leaders actively manage quality assurance and staff capability needs. The Team leaders use Sero, Small Business line quality and coaching tool, as an indicator of capability and quality issues of their staff. Sero provides leaders and staff with a consolidated view of capability at all levels. The system has automated sampling, reports and captures data from a number of sources to provide an operational view to building capability, that is, new staff/work types, focused products and performance improvement.
- From an [employer obligations] perspective, [the ATO] also monitor complaints and use this as an indicator of any capability issues. To date [the ATO] have very low complaint levels. [The ATO] also receive positive feedback in relation to [its] staff and their ability to help clients and provide quality advice.³⁶¹

4.149 As part of the COMPASS performance process, ATO management have also advised that staff are expected to take ownership of their performance, check-in regularly with their manager and seek feedback from others.³⁶²

4.150 The ATO has also provided documents outlining the training for its staff who are engaged in employer obligations compliance activities. It consists of induction programs and further training to develop their capability for undertaking compliance activities.³⁶³ There are technical resources for PAYG, SG, and FBT. Of these resources, only the SG training material addresses the definition of employee³⁶⁴ which provides links to the ECD tool and the relevant SG rulings³⁶⁵ for further information. In relation to PSI, the relevant learning package addresses the common law definition of employee³⁶⁶ and also provides reference to the relevant PSI tax rulings for further information.³⁶⁷

4.151 The above learning packages require reading the relevant information followed by answering a number of questions. The packages are effectively of a self-taught and self-assessed nature.

³⁶¹ Ibid.

³⁶² Ibid.

³⁶³ ATO communication to the IGT, June 2016; ATO, *EO Training needs analysis and learning pathway* (internal ATO document).

³⁶⁴ ATO, *Introduction to super guarantee* (internal ATO document) pp 19-27.

³⁶⁵ ATO, *Superannuation guarantee: who is an employee?*, SGR 2005/1, 23 February 2005.

³⁶⁶ ATO, *Alienation of Personal Services Income – Introduction* (internal ATO document) pp 76-7.

³⁶⁷ ATO, TR 2005/16, above n 13.

4.152 In addition to the above training, the ATO management representation indicates that, upon joining a team, new staff are paired with more experienced staff and receive mentoring from the team's technical leader.³⁶⁸

4.153 The ATO staff are also provided with procedures on how to conduct employer obligations audits including the ability to seek technical advice and approval from technical leaders within and outside the employer obligations area. For example, in relation to FBT, compliance officers can escalate an issue to their technical leader who can seek further assistance by sending an email to the mailbox of the Employer Obligations Product Team.³⁶⁹ The ATO has provided management representation that further assistance is available from its Private Groups and High Wealth Individuals business area, where the ATO predominately houses its FBT capability, as well as Tax Counsel Network for FBT matters which are particularly complex, novel or involve setting a new ATO view.³⁷⁰

4.154 At the conclusion of each employer obligations audit, the ATO's audit procedures require staff to complete case debriefs which collate intelligence about employers, business structure and compliance issues and the audit outcome.³⁷¹ Intelligence from case debriefs is incorporated into the Employer Obligations business area newsletter to share corporate knowledge amongst compliance staff.³⁷²

4.155 As mentioned above, the ATO also has a quality and coaching framework in the employer obligations business area, referred to as 'Sero'. It involves the assessment of a sample of recently completed compliance activities by quality assessors against a matrix of criteria tailored to employer obligations. Where assessors find that a criterion has not been met, they must provide their reasons.³⁷³ These assessments, including the reasons, are provided to the relevant case officers and their team leaders. Case officers are required to acknowledge the assessment and feedback³⁷⁴ and undertake corrective action, such as following a coaching plan.³⁷⁵

4.156 Aggregate level reports of the Sero assessments are generated monthly and used to identify trends and address emerging or ongoing issues.³⁷⁶ To provide assurance on the capability of the assessors themselves, a sample of Sero assessments is also peer reviewed.³⁷⁷

4.157 The ATO has advised that it may focus all Sero assessments in a particular month to a particular risk in order to gain a deeper understanding of that risk. With regard to employee/contractor issues, this occurred in October 2015 and January 2016 by focusing on the CCA audits.³⁷⁸ The ATO has provided the Sero reports for these

368 ATO communication to the IGT, 14 June 2016.

369 ATO, *Employer Obligations (EO): fringe benefits tax audit method* (internal ATO document, 22 January 2016) p 1.

370 ATO communication to the IGT, 7 July 2016.

371 ATO, *Case debrief - Employer obligations/CCA and large withholder field audit* (internal ATO document).

372 ATO communication to the IGT, 3 March 2016.

373 ATO, *IND Sero system, User Procedures for Team Leaders* (internal ATO document, 4 December 2015) p 6.

374 Ibid p 8.

375 ATO, *Sero roles and support tools reference card* (internal ATO document).

376 Ibid.

377 ATO, *IND Sero system, User Procedures for Team Leaders*, above n 373, pp 13-7.

378 ATO, *SMB Quality and Coaching Update: October 2015* (internal ATO document); ATO, *SMB Quality and Coaching Update: January 2016* (internal ATO document).

months. The results, produced in Table 4.8 below, indicate that the standards were met in approximately 96 per cent of compliance activities.

Table 4.8: Sero monthly reports, employer obligations, compliance activities which met standard

Criteria	October 2015 (%)	January 2016 (%)
Overall	96	96
Correct decision made	98	100
Professional client	99	98

Source: ATO.

4.158 The ATO has advised that it received 73 complaints during the four financial years up to and including the 2015-16 financial year in relation to employer obligations compliance activities. Five of these complaints make reference to decisions involving the employee/contractor distinction.³⁷⁹ However, specific details of the complaints were not provided.

4.159 Insight into the ATO's handling of the employee/contractor distinction, in the audit context, can be gleaned from CCA audit procedures which are described in the background section of this chapter. Where auditors identify potential misclassification of workers, the CCA audit procedures direct them to consider the responses provided to the ECD tool and the additional questions using the relevant facts and evidence obtained during audit.³⁸⁰ The auditor's findings and analysis are recorded in a template³⁸¹ and sent to the technical leader for approval.³⁸² The template requires auditors to present the relevant facts, employers' contentions, evidence relied upon as well as all the answers to the questions outlined in the ECD tool.³⁸³

4.160 The employee/contractor distinction as it applies to the PSI rules is investigated separately through the PSI audit method.³⁸⁴ The ATO has advised that, as PSI is examined as part of broader income tax audits, they are only able to provide quality assurance results on income tax audits as a whole and are unable to provide specific reports on PSI decisions. However, the ATO has also advised that during the four financial years up to and including the 2015-16 financial year, it did not receive any complaints about its application of the PSI rules, but did receive five complaints mainly relating to the lodgement of PSI returns.³⁸⁵

4.161 ATO officers apply Taxation Ruling TR 2001/8³⁸⁶ in PSI audits. In determining whether income earned is excluded from the assessable income of the individual, the individual must meet one of four tests, including the 'results' test. Paragraph 110 of TR 2001/8³⁸⁷ states that the 'results' test is based on the traditional criteria for distinguishing contractors from employees and outlines the 11 relevant common law

379 ATO communication to the IGT, 8 August 2016.

380 ATO, *Employer Obligations: Compliance with contracting arrangements audit method*, above n 280, step 6.4.

381 ATO, *Reasons for decision template, Workers identified as <employees><contractors>* (internal ATO document).

382 ATO, *Employer Obligations: Compliance with contracting arrangements audit method*, above n 280, step 6.5.

383 ATO, *Reasons for decision template, Workers identified as <employees><contractors>*, above n 381.

384 ATO, *Case Context Document: Personal Services Income* (internal ATO document, 3 February 2014).

385 ATO communication to the IGT, 5 August 2016.

386 ATO, *Income tax: what is a personal services business*, TR 2001/8.

387 *Ibid* para [110].

factors. It also states that there are no determinative factors and that the 'totality of the relationship' should be considered.³⁸⁸

4.162 Further, TR 2001/8 makes reference to the Explanatory Memorandum, of the PSI legislation, which states that 'the individual must actually be paid on the basis of achieving a result, rather than for example, for hours worked'.³⁸⁹ Where there is a contract, the ruling states that the 'true essence' of the contract should be considered and that the 'manner in which payment is structured will not of itself exclude genuine result based contracts'. For example, there are results based contracts where the contract price is based on an estimate of the time and labour.³⁹⁰

4.163 The PSI audit procedures require the auditor to obtain and review the contracts to determine whether the income from the contract is PSI and whether the taxpayer passes the 'results' test.³⁹¹ The template, for recording the reasons for any decision, requires auditors to set out the issues, including the application of the 'results' test to the taxpayer's circumstances against the three legislative criteria, specifically, whether the:

- PSI is income for producing a result;
- taxpayer supplies plant and equipment or the tools of trade to perform the work from which the result is produced; and
- taxpayer would be liable for the cost of rectifying any defect in the work performed.

4.164 The template advises auditors that the essence of the contract should be to achieve a result and refer to the method of payment as a major relevant factor.³⁹² The letter, which sets out the reasons for the decision, is approved before it is sent to the taxpayer.³⁹³

4.165 During this review, ATO management advised the IGT that it had commenced trialling a new 'streamlined' PSI audit in July 2016. This approach involves ATO staff having telephone conversations with taxpayers to identify and obtain relevant documents and alert taxpayers to any changes needed for ensuring future compliance with the PSI rules. At the time of finalising this report, the ATO advised the IGT that it had completed 40 such streamlined audits. However, the procedures and results for these audits were not available.³⁹⁴

388 Ibid para [111]-[112].

389 Ibid para [116].

390 Ibid para [121].

391 ATO, *Case Context Document: Personal Services Income*, above n 384.

392 ATO, *Reasons for Decision template, Personal Services Business Decision* (internal ATO document).

393 ATO, *Case Context Document: Personal Services Income – hourly or daily rate paid* (internal ATO document, 29 August 2014).

394 ATO communication to the IGT, 27 July 2016 and 28 October 2016.

IGT observations

4.166 As compliance activities may result in significant adjustment in taxpayers' liabilities, it is important that the evidence used and reasons for arriving at key decisions are clearly explained to taxpayers. ATO staff need to receive adequate training and support to ensure that they discharge such duties equitably, accurately, expeditiously, confidently and with due care to the taxpayers' circumstances.

4.167 Overall, it appears that the ATO's workforce planning does include sound processes for capability development, including appropriate training packages. There also seems to be adequate procedures and templates to guide compliance officers in providing reasoning for their decisions. IGT has identified some further improvements which should enhance the ATO's existing practices.

4.168 Capability development, including the importance of identifying the key skills required for specific roles and training to develop those skills, have been considered in previous IGT reviews.³⁹⁵ In this regard, ATO management has indicated that its workforce planning, training and coaching in the employer obligations business line predominately relies on a mixture of job design, learning packages and mentoring by more experienced team members.

4.169 Whilst learning packages are provided to staff, much of the packages are voluntary and self-directed without assessment. It would be beneficial if staff are assessed upon completion of training packages that are considered essential to the conduct of employer obligations compliance activities. At a minimum, the assessment may be done electronically in the form of multiple choice questions. Such an approach would provide assurance or identify knowledge gaps for both the team leaders and the compliance officers themselves. Ultimately, it should result in an improved taxpayer experience as well.

4.170 Turning to more tailored training, the employee/contractor distinction is only referred to as an ancillary concept in SG and PSI training packages and is not mentioned in PAYGW or FBT materials. Being central to the assessment of all employer obligations, the IGT believes that improvements to relevant training packages on the employee/contractor distinction, including links to detailed information about the risks, would be beneficial.

4.171 It is also important to monitor compliance activities for identifying capability gaps and take action to address them. Sero, as a process, seems to achieve this reasonably efficiently at the case level through feedback to case officers and team leaders. However, it is unclear how capability issues identified are recorded and tracked over time. Accordingly, the IGT believes that trends should be monitored to ensure that broader capability risks are addressed as early as possible. For example, Sero assessments for CCA audits could be reviewed over time to determine whether there are recurring issues relating to the evidentiary support for decisions and how these issues may be addressed through training or improvements to procedures.

³⁹⁵ IGT, *Review into the ATO's compliance approaches to small and medium enterprises with annual turnovers between \$100 million and \$250 million and high wealth individuals* (December 2011).

4.172 Providing support tools to staff during compliance activities is also essential. Such support tools may be in the form of a compliance approach or in the form of templates. As mentioned earlier, the ATO's 2016 trial telephony approach to making PSI determinations and the utilisation of conversations with taxpayers should assist in reducing the compliance cost for compliant taxpayers. However, as it is a recent initiative and the procedures are yet to be documented, more time is required before an assessment can be made of the effectiveness of this approach.

4.173 Currently, templates are provided to compliance officers to assist them in making decisions and documenting the reasons behind those decisions. The template relating to the employee/contractor distinction is based on the multiple choice style answers of the ECD tool. In the audit context, a more appropriate assessment, which includes the application of the law to the relevant facts, is necessary particularly in determining worker status which is heavily fact-based.

4.174 The template for recording decisions relating to PSI instructs compliance officers to apply the three legislative criteria of the results test but does not set out the various common law factors that require consideration.³⁹⁶

4.175 The IGT is of the view that templates could be generally improved by the use of 'macros' within templates. Using macros, compliance officers would select the relevant legislative and common law principles and the macro would populate the document with the necessary details on the interpretation of those factors by the courts.

RECOMMENDATION 4.5

The IGT recommends the ATO enhance its capability development framework and compliance support tools with respect to employer obligations and Personal Services Income compliance activities by:

- (a) improving the relevant training packages on the employee/contractor distinction;*
- (b) ensuring that staff are assessed following completion of relevant training packages;*
- (c) monitoring the results of quality assessments over time to identify recurring capability issues with a view to improving training and procedures; and*
- (d) improving the documentation in the 'reasons for decision' templates, by requiring an appropriate assessment of the application of the law to the facts of the case.*

ATO response

Disagree with recommendation 4.5.

We appreciate the IGT's acknowledgement in the report (and in discussions) of the sound approaches already in place to support workforce and capability development

³⁹⁶ ATO, TR 2001/8, above n 386, para [110].

and to assure quality outcomes. These approaches are generating good quality outcomes in the vast majority of cases as the IGT's report highlights.

Training in the employee/contractor distinction is part of training available to ATO staff. Our staff are well trained and supported to use their judgement when documenting reasons for decision and utilise a facts and evidence worksheet for complex cases. Not all staff in employer obligations areas action cases related to the classification status of workers. Therefore, training and capability building in these issues is focused on those staff who will be actioning this type of work.

Although there is no formal assessment at the completion of these training packages, technical advisers and team leaders review the work of their staff and any ongoing learning and development needs are managed through the ATO's personal development system (COMPASS). We do not believe there would be additional value from having a formal assessment process in place.

In terms of monitoring the results of quality to identify recurring capability, the business areas that are responsible for employer obligations and PSI work currently use the SERO coaching system to review cases and identify individual capability needs. In addition to this, the ATO has an enterprise wide approach to individual learning and development. Under the COMPASS system team leaders have regular conversations with each team member about their development and learning needs.

The ATO has made some significant changes in its approach to identified PSI risks that are resulting in far fewer of these cases being escalated to audit. Where a case does escalate to an audit or review process the reasons for decisions do require an application of the law to the facts of the case.

CONSEQUENCES OF NON-COMPLIANCE WITH SUPERANNUATION GUARANTEE OBLIGATIONS

4.176 Many stakeholders have raised concerns that non-compliance with SG obligations results in disproportionate consequences for employers. Specific concerns were raised by stakeholders that the relevant legislation requires employers to:

- lodge an SG statement as soon as the payment of SG is late regardless of an employer's compliance history or if the late payment was only a few days late; and
- pay SGC which is not tax deductible.

4.177 Stakeholders were of the view that the above consequences, whilst acting as a deterrent, discourage employers from self-reporting their late SG payments to the ATO.

Relevant ATO materials

4.178 Where employers miss a SG payment, or make late or insufficient SG payments for a quarter, they will have an SG shortfall and the legislation requires the lodgement of an SG statement³⁹⁷ and the payment of SGC.³⁹⁸

³⁹⁷ SGAA s 33.

4.179 The SGC is imposed on the SG shortfall and arises quarterly to the extent that the latter remains unpaid. It comprises of an employer's SG shortfalls, an administrative fee for each employee and nominal interest. While SG contributions are deductible in the financial year that they are made, payments of SGC are not tax-deductible.³⁹⁹ Where employers become liable for the SGC due to a late payment, they have the option to:

- use the late payment to reduce the amount of SGC, in which case the payment is not tax-deductible; or
- use the late payment as a pre-payment for future SG, in which case it is tax deductible, but the non-deductible SGC balance is not reduced.⁴⁰⁰

4.180 There are circumstances where raising an SGC assessment may result in the employer paying a disproportionate amount of interest.⁴⁰¹ This is because nominal interest is calculated from the first day of the quarter to the date the assessment is raised, not the date the payment was made.⁴⁰² It may also result in a disproportionate administrative component of the SGC⁴⁰³ where large employers have very small shortfalls for a large number of employees.⁴⁰⁴

4.181 The ATO has advised that, previously, its approach was to pursue all cases of potential SG non-compliance, especially where employees had lodged ENs with the ATO.⁴⁰⁵ From 1 July 2014, it commenced tailoring its approach to pursuing lodgement of SG statements through the use of the Commissioner's powers of 'general administration under section 43 of the SGAA and the proper use and management of public resources of the *Public Governance, Performance and Accountability Act 2013*'. The ATO strategy document states that exercising the Commissioner's discretion means that it can target the 'highest risk taxpayers', maximise outcomes and ensure 'return on investment'.⁴⁰⁶

4.182 This differentiated treatment strategy was implemented in two phases. The first phase took place from 1 July 2014 and is based on compliance history, not to pursue employers who had been impacted by natural disaster or those who would incur disproportionate nominal interest or administrative components. In addition, as discussed in Chapter 2, the strategy also provides a discretion to apply a 'go-forward' approach to employers who have unintentionally misclassified their workers such that SG statements for prior periods are not being required.⁴⁰⁷

398 Ibid s 46.

399 ATO, *Claiming a tax deduction* (1 June 2015) <<http://www.ato.gov.au>>.

400 ATO, *Missed and late payments* (17 June 2015) <www.ato.gov.au>.

401 ATO, *Superannuation Guarantee Compliance Strategy and Treatments - SG Compliance Program 1 July 2014* (internal ATO document, May 2015) p 14.

402 ATO intranet, *Superannuation Compliance Treatment One and Two Procedure* (internal ATO document).

403 ATO, *Superannuation Guarantee Compliance Strategy and Treatments*, above n 401, p 16.

404 ATO communication to the IGT, 15 April 2016.

405 ATO, *Superannuation Guarantee Compliance Strategy and Treatments*, above n 401, p 4.

406 Ibid.

407 Ibid.

4.183 Where the ATO exercises the above discretion, it would do so on the basis that the employer had paid the required SG contributions in full within three months of the relevant cut-off date, or in the case of a natural disaster, as soon as practicable.⁴⁰⁸ The ATO has advised that it also encourages the employer to pay 10 per cent interest per annum for the number of days that the payment was late. This is significantly less than the overall legislative requirement as discussed earlier.⁴⁰⁹

4.184 From 1 July 2015, the ATO commenced the second phase of its differentiated treatment strategy where it adopts a tailored approach to SG compliance. Under this tailored approach, the ATO considers the compliance history of all employers when deciding whether to pursue lodgement of SG statements. Employers are categorised into four classes based on their compliance behaviours. Those who are 'largely' or 'mainly' compliant may pay SG and interest directly to superannuation funds rather than lodge SG statements and pay SGC to the ATO. Employers categorised as 'poor compliers' or 'seriously poor compliers' will be subject to firmer compliance action, including being subject to audit, required to lodge SG statements, issued default assessments or Director Penalty Notices (DPN) or have legal action taken against them.⁴¹⁰

4.185 The ATO has advised that between 1 July 2015 and 31 January 2016, its adoption of the above tailored approach resulted in 121 instances where employers, who were the subject of an EN, had made payment of SG and interest on behalf of their employees directly to a superannuation fund, totalling \$311,967. These employers were not required to lodge SG statements.⁴¹¹

4.186 The ATO has released an infographic⁴¹² about employers' obligations to pay SG and a 90 second video which communicates key messages about an employer's option to use the SBSCH to meet their SG obligations.⁴¹³ The above differentiated approach to non-compliance is also conveyed, but only on its website⁴¹⁴ which explains that the ATO 'may not check the current compliance of those employers who are viewed as low risk (as a result of having a good compliance history) and who have appropriately compensated their employees'.⁴¹⁵

4.187 Towards the end of this review, ATO management has advised the IGT that it is in the process of designing the implementation review of its tailored approach, including qualitative and quantitative measures of effectiveness.⁴¹⁶

408 Ibid, pp 14-5.

409 ATO, *Superannuation Compliance Treatment One and Two Procedure*, above n 402.

410 ATO, *Superannuation Guarantee Compliance Strategy and Treatments*, above n 401, pp 20-5.

411 ATO communication to the IGT, 24 June 2016.

412 ATO, *Super obligation employer's checklist* (19 October 2016) <<https://ato.gov.au>>.

413 ATO, *Small Business Superannuation Clearing House* (22 September 2016) <<https://ato.gov.au>>.

414 ATO, *Communication strategy and action plan for Superannuation Guarantee 2015-16* (internal ATO document, 30 November 2015) p 2.

415 ATO, *Super for employers - Our compliance approach* (28 October 2015) <www.ato.gov.au>.

416 ATO communication to the IGT, 27 October 2016.

IGT observations

4.188 In his 2010 *Review into the ATO's administration of the Superannuation Guarantee Charge*,⁴¹⁷ the IGT had identified the need to strike a balance between the deterrent aspects of SGC in discouraging non-compliance and appropriate consideration of the employer's circumstances in imposing it. The Commissioner's recent policy in exercising his general powers of administration and his decision to effectively manage his resources under the *Public Governance, Performance and Accountability Act 2013*,⁴¹⁸ as stated above, appears consistent with the approach recommended by the IGT.

4.189 The ATO's new administrative approach has been fully operational since 1 July 2015. It is important that employers are made aware of it and that its effectiveness in promoting voluntary compliance be assessed after the passage of an appropriate amount of time. Whilst ATO management has advised the IGT that it is currently designing the review of the implementation of this new approach, it is unclear, based on the documents provided, when and how it will be assessed.

4.190 The IGT is generally supportive of the ATO's new approach and believes more can be done to raise employers' awareness of it. For example, it should be highlighted in ATO publications and webinars in addition to its website content.

RECOMMENDATION 4.6

The IGT recommends the ATO increase employers' awareness of its differentiated approach to non-compliance with SG obligations and assess the utility of this approach by analysing the results obtained from measuring its effectiveness.

ATO response

Agree with recommendation 4.6.

We agree with the recommendation. We are currently drafting a Practical Compliance Guideline to outline how we consider an employer's circumstances and how that influences our engagement. This will provide a basis for increasing employers' awareness of our differentiated approach to non-compliance with SG obligations.

We have built a framework and measures of success for evaluating the effectiveness of our new approaches for SG, and will be moving to complete an initial evaluation now that we have had a year of operation of the new approach.

⁴¹⁷ IGT, *Review into the ATO's administration of the Superannuation Guarantee Charge* (March 2010) p 77.

⁴¹⁸ ATO, *Superannuation Guarantee Compliance Strategy and Treatments*, above n 401, p 4.

APPENDIX 1—TERMS OF REFERENCE AND SUBMISSION GUIDELINES

BACKGROUND

To maintain a strong economy and achieve Government objectives, including provision of services to its citizens, revenue needs to be raised through taxation of businesses and individuals. In addition to complying with their own taxation obligations, businesses, and not-for-profit organisations, have to play a vital role in collecting taxes from their employees as well as ensuring that employee entitlements such as superannuation payments are made.

Furthermore, employers have to comply with a multitude of other taxation and legal obligations both at the Federal and state levels. As a result, it is important to provide them with as much support as possible with these obligations so that their primary focus continues to be their core commercial goals. The health of the Australian economy is, to a large extent, dependent on their efficiency and profitability.

This review is aimed at assisting employers to comply with their obligations under the superannuation, Pay As You Go (PAYG) withholding and Fringe Benefits Tax (FBT) regimes.⁴¹⁹ Opportunities will be sought to ease their compliance burden whilst ensuring that the relevant taxes and superannuation entitlements are paid promptly. In this respect, the Australian Taxation Office (ATO) has been undertaking a number of initiatives, such as 'Single Touch Payroll', to reduce employers' reporting requirements.⁴²⁰

Approximately 97% of businesses are identified as small businesses with a turnover of \$2 million or less.⁴²¹ Accordingly, the review will need to consider the challenges faced by small businesses, particularly in meeting the above obligations. It should be noted that the Government has already implemented a joint agency initiative called the Small Business Fix-it Squad which involves small business owners working with Federal, state and local government regulators to identify and consider options for improving the broader operating environment for these businesses.⁴²²

The ATO reports that around half of the taxation revenue collected, which totalled \$419.26 billion in 2013-14, flows through approximately 846,500 employers.⁴²³ This revenue amount includes PAYG withholding and Superannuation Guarantee Charge (SGC). In 2014-15, employers remitted Superannuation Guarantee (SG) of more than \$79.19 billion to employees' superannuation funds.⁴²⁴ SG is an important element of the broader taxation and superannuation system where non-compliance adversely impacts retirement savings resulting in increased reliance on the aged pension as well as an uneven commercial playing field.

419 ATO, *Pay as you go (PAYG) withholding* (1 September 2014) <www.ato.gov.au>; ATO, *Fringe Benefits Tax* (12 September 2014) <www.ato.gov.au>; ATO, *Super* (1 September 2014) <www.ato.gov.au>.

420 Josh Frydenberg, 'Cutting red tape through STP', above n 44.

421 ATO, *Taxation statistics 2012-13* (4 May 2015) <www.ato.gov.au>.

422 Office of the Australian Small Business Commissioner, *Working together to help small business*, above n 74, <www.asbc.gov.au>.

423 ATO, *Compliance in focus 2013-14* (July 2013) p 8 <www.ato.gov.au>; Commissioner of Taxation, *Annual Report* (2013-14) p iii-v.

424 Australian Prudential Regulation Authority, *Quarterly Superannuation Performance* (20 August 2015) p 10.

The ATO also utilises employer reporting and taxable payments to certain contractors,⁴²⁵ to verify employee/contractor compliance with their own obligations. In addition, the ATO uses such information in the prefilling of income tax returns. Other Government agencies benefit directly or indirectly from this employer reporting as well, for example, managing social security and child support obligations.

During the Inspector-General of Taxation's (IGT) work program consultations, a broad range of stakeholders raised particular concerns regarding the ATO's approach to employer compliance with taxation and superannuation obligations. These concerns included:

- Difficulty and uncertainty in determining employee or contractor status. For example, unexpected multi-year liabilities may arise for employers as a result of an audit or otherwise genuine employees may be left without an avenue to pursue their unpaid entitlements. Similar status challenges may have led to the increase from 13,696 in 2008-09 to 50,358 in 2013-14 (with a peak of 59,885 in 2012-13) in the number of Australian Business Number (ABN) applications being rejected by the ATO.⁴²⁶
- SG non-compliance due to difficulties in ATO detection and enforcement as well as limited ability of employees to take direct action for unpaid SG. There is also a lack of ATO feedback to employees who report potential employer non-compliance. In the last five financial years, the ATO has raised a total of \$2.97 billion in unpaid SG liabilities and collected a total of \$1.59 billion.⁴²⁷ Further liabilities may remain undetected as the ATO relies more on employee notifications than proactive risk-based audits.⁴²⁸
- Unnecessary compliance costs for employers arising from ATO conduct during compliance activities. These include onerous information requests to employers, Director Penalty Notices (DPN) being issued in inappropriate circumstances, unwillingness to discuss issues and practical solutions.
- Aspects of the penalty regimes, particularly with respect to SGC, not adequately promoting voluntary compliance or self-reporting of non-compliance. However, it should be noted that the Government has recently concluded consultation on proposed legislation to simplify and reduce the harshness that may result from imposition of interest and penalties with respect to SGC.⁴²⁹

There are certain arrangements, known as 'phoenix', which involve companies being deliberately placed into administration or liquidation, leaving taxes and employee entitlements unpaid. This review will also examine the effectiveness of ATO actions to address these phoenix activities. It should be noted that the Government has established an Inter-Agency Phoenix Forum to share intelligence and implement cross-agency strategies to reduce and deter phoenix activity.⁴³⁰

⁴²⁵ ATO, *Taxable payments reporting – building and construction industry* (26 August 2015) <www.ato.gov.au>.

⁴²⁶ Commissioner of Taxation, *Annual Report* (2008-09) p 50; Australian Business Register, *Report of the Australian Business Registrar* 2012-13 (November 2013) p 80; Australian Business Register, *Report of the Australian Business Registrar* 2013-14 (November 2014) p 74.

⁴²⁷ Commissioner of Taxation, *Annual Report* (2013-14) p 68; Commissioner of Taxation, *Annual Report* (2011-12) p 89; Commissioner of Taxation, *Annual Report* (2009-10) p 105.

⁴²⁸ IGT, *Review into the ATO's administration of the Superannuation Guarantee Charge* (March 2010) pp 48-54.

⁴²⁹ Treasury, *Exposure Draft to Superannuation Guarantee Legislation Amendment (Simplification) Bill* 2015 No. , 2015 (21 August 2015) <www.treasury.gov.au>.

⁴³⁰ *Taxation Administration Regulations* 1976 reg 48.

The IGT will conduct this review pursuant to subsection 8(1) of the *Inspector-General of Taxation Act 2003* (IGT Act) and welcomes your input. The following terms of reference and guidelines are provided to assist with the preparation of your submission.

TERMS OF REFERENCE

The IGT review into the ATO's employer obligations compliance activities will focus on:

Easing the compliance burden for employers

1. *The distinction between 'employee' and 'contractor' for Federal taxation and superannuation purposes, its coherence with business practices, state taxation and other legal requirements as well as the interactions with ABN and GST registrations.*
2. *Simplification of reporting, withholding and payment obligations for employers as well as certain contractors.*
3. *The effectiveness of the ATO's use of existing third party data to reduce the compliance burden for employers.*
4. *Guidance and tools for employers to discharge their employee-related taxation and superannuation obligations, including the level of protection afforded to those relying upon the information provided.*
5. *Information and support for employees to understand their rights, entitlements and avenues for redress where they become aware of potential non-compliance by their employers.*

ATO conduct of compliance activities

1. *The effectiveness of the ATO's risk assessment and verification processes to detect and address non-compliance of employer obligations in a timely manner.*
2. *The ATO's consideration of relevant employee entitlements protection and business viability impacts when undertaking compliance actions.*
3. *The effectiveness of the ATO's actions to address phoenix activities.*
4. *The ATO's conduct during employer obligations compliance activities, including the:*
 - a. *proportionality and use of information gathering powers;*
 - b. *access and use of available third party information to verify compliance;*
 - c. *appropriateness of auditor communications;*
 - d. *pathways for escalating and resolving issues before such activities are finalised;*
 - e. *sustainability of audit and penalty decisions;*
 - f. *costs for employers and employees; and*

- g. *the feedback given to employees who notify the ATO of potential employer non-compliance.*
5. *The ATO's administration of alienation of personal services income provisions and its interaction with other compliance activities including those relating to employer obligations.*
6. *The extent to which aspects of the administrative penalty regimes encourage or hinder voluntary compliance and self-reporting of non-compliance by employers.*

The IGT may also examine other relevant concerns raised or potential improvements identified during the course of this review.

SUBMISSION GUIDELINES

We envisage that your submission will set out your experiences and views on the ATO's management of employer obligations compliance activities.

It is important to provide detailed accounts of your experiences with the ATO. A timeline outlining your major interactions with the ATO, including key correspondence, formal notices and related outcomes would be helpful. Your submission should address the terms of reference above.

In addition to your views on potential improvements, we are also seeking examples of ATO approaches that have contributed to positive experiences or outcomes.

The following questions may assist you in your response.

EASING THE COMPLIANCE BURDEN FOR EMPLOYERS

- Q1. What is your experience with the employee/contractor distinction for taxation and superannuation purposes? Does it reflect your business practices and how does it compare with state taxation and other legal requirements? Can the employee/contractor distinction be improved for all parties? If so, how?
- Q2. As an employer, what are the business pressures that impact on your decision to engage an individual as a contractor or an employee? Provide an account of your experience.
- Q3. As an individual, what are the business and personal pressures that impact on your decision to be engaged as a contractor or employee? Provide an account of your experience.
- Q4. Have you had any experience in dealing with the ATO regarding the employee/contractor distinction, including for ABN and GST registration purposes? Were they able to sufficiently clarify areas of uncertainty? Were any third parties impacted by the ATO's determination?

EASING THE COMPLIANCE BURDEN FOR EMPLOYERS (CONTINUED)

- Q5. Do you believe the documentary evidence required to substantiate employee/contractor status is reasonable and easily produced? Explain your views.
- Q6. Do you believe that the ATO's publicly available guidance and tools for determining worker status (for example, the employee/contractor decision tool) are clear and provide a sufficient level of protection?
- Q7. Are there ways in which guidance and tools for employers can be improved more generally to assist them in discharging their employee and contractor related taxation and superannuation obligations? Explain your views.
- Q8. Are there ways in which the employer's reporting and payment obligations with respect to their employees and contractors can be simplified without jeopardising the payment of taxes and superannuation entitlements? Explain your recommendations and provide reasoning.
- Q9. Did the ATO use third party data in its risk assessment? If so, did the use of this data reduce your compliance burden?
- Q10. Are there are other improvements that can be made to ease your compliance burden in relation to your PAYG withholding, FBT and SG obligations?

ATO conduct of compliance activities

- Q11. Have you had experience with the ATO's compliance activities relating to PAYG withholding, FBT and SG including penalty matters such as unpaid PAYG and SG penalties? If so, provide a detailed account of your experience, including:
- a. A timeline of key events and a description of the actions taken by the ATO.
 - b. The effectiveness of the ATO communication throughout the compliance activity including reasons for why you were selected.
 - c. The use of available third party data to verify compliance.
 - d. Your views on whether ATO actions, including information requests, were appropriate and commensurate with the circumstances, the risks to the revenue and unpaid employee entitlements. What were the impacts of such actions on you?
 - e. Where the ATO identified an error, did it take into account appropriate mitigation factors, such as your compliance history for remission of penalty and interest?
 - f. Where there was a disagreement, did the ATO initiate and engage in alternative dispute resolution with you? What were your views on the process and the outcome?
 - g. Comment on the reasonableness of any assistance that the ATO made available to you, such as payment arrangements, interest remission, guidance and support.

EASING THE COMPLIANCE BURDEN FOR EMPLOYERS (CONTINUED)

ATO conduct of compliance activities (continued)

- Q12. If you disagreed with the ATO's decision following an employer obligations compliance activity, what was your experience? Which avenues of review or appeal (if any) did you pursue? Provide a detailed account of your experience including:
- whether the ATO clearly explained to you the escalation/review pathways;
 - whether the ATO attempted to narrow the issues in dispute and facilitate resolution in order to minimise cost for all parties; and
 - the outcome of the disagreement.
 - If you were issued with a DPN for SG or unpaid PAYG, what was your experience with the ATO? Explain your views, in particular:
 - whether you had adequate opportunity to engage with the ATO to discuss concerns prior to the issue of the DPN;
 - whether the ATO adequately explained to you the DPN and the reasons for issuing the notice;
 - whether the DPN was issued for correct reporting periods and amounts;
 - if you sought independent advice, whether it led you to a particular action, such as entering into voluntary administration; and
 - if there was a dispute regarding the DPN, how it was resolved.
- Q13. Was alienation of personal services income part of the scope of ATO employer obligations compliance activities in which you were involved? If so, explain your experience and the impact. Are any improvements required including the need for more guidance and tools as to their application and the ATO's administration of these provisions?
- Q14. At a broader level, how effective is the ATO's approach to detecting, prioritising and enforcing compliance with the PAYG withholding, FBT and SG obligations? Explain your views and provide any supporting examples.
- Q15. How effective are the ATO strategies for improving employer compliance with their obligations over time? In particular, what improvements can be made to its detection and enforcement of these obligations? Explain your suggestions.
- Q16. How could the ATO give greater consideration to the protection of relevant employee entitlements and impact on business viability when undertaking a compliance action?
- Q17. How should unpaid SG amounts be managed? How would your idea be funded? A legislative scheme exists for unpaid wages and leave entitlements when an employer goes into liquidation or bankruptcy. Should SG entitlements be included in this scheme? Explain your views.

EASING THE COMPLIANCE BURDEN FOR EMPLOYERS (CONTINUED)

ATO conduct of compliance activities (continued)

- Q19. How could the ATO give greater consideration to the protection of relevant employee entitlements and impact on business viability when undertaking a compliance action?
- Q20. How should unpaid SG amounts be managed? How would your idea be funded? A legislative scheme exists for unpaid wages and leave entitlements when an employer goes into liquidation or bankruptcy. Should SG entitlements be included in this scheme? Explain your views.
- Q21. What are the impacts on employers and employees over time as a result of ATO compliance actions? What were the effects on the business for employers and, for employees, how would their retirement savings be impacted over the longer term? Explain your views.
- Q22. How effective are the ATO's actions to detect and address 'phoenix' activities and recover relevant employee entitlements? Where you believe improvements are necessary, provide reasons and explain the improvements that you recommend.
- Q23. Are there aspects of the administrative penalty regimes that may be improved to promote voluntary compliance and self-reporting of non-compliance by employers? Explain your suggestions and reasoning.
- Q24. If you are an individual who reported potential non-compliance of an employer to the ATO, what was your experience? How easy was it to lodge your report? Do you believe the ATO response was appropriate?
- Q25. Are there ways the ATO could improve its interaction with individuals reporting potential non-compliance of their employer, including initial notifications and follow up thereafter?
- Q26. Have you had any positive experiences in dealing with the ATO in relation to employer obligations compliance activities? Provide examples.

Other

- Q27. Are there any other areas on which you would like to make a submission? For example, you may wish to cite international experiences or comparisons which you believe would lead to improvements.

LODGEMENT

The closing date for submissions is 11 December 2015. Submissions can be sent by:

Post to: Inspector-General of Taxation
 GPO Box 551
 SYDNEY NSW 2001

Email to: eoreview@igt.gov.au

CONFIDENTIALITY

Submissions provided to the IGT are in strict confidence (unless you specify otherwise). This means that the identity of the taxpayer, the identity of the adviser and any information contained in such submissions will not be made available to any other person, including the ATO. Section 37 of the IGT Act safeguards the confidentiality and secrecy of such information provided to the IGT – for example, the IGT cannot disclose the information as a result of a court order generally. Furthermore, if such information is the subject of client legal privilege (or legal professional privilege), disclosing that information to the IGT will **not** result in a waiver of that privilege.

APPENDIX 2—LABOUR LAWS IN AUSTRALIA

A2.1 The table below provides a brief overview of the development of labour laws in New South Wales.

Table A.2.1: Timeline of industrial relations in NSW

Year	Development
1828	<i>Master & Servants Act 1828</i> (England) permitted employers to prosecute any employee who refuses to work, or who loses or damages the employer's possessions. Maximum penalty 6 months prison.
1856	Eight hour day, stonemasons became the first NSW workers to win an 8 hour working day.
1860s	Rise of unionism. NSW's first trade unions commenced forming and recruiting members.
1871	Trades & Labour Council of NSW formed on 25 May 1871.
1881	<i>Trade Union Act 1881</i> recognised NSW trade unions for the first time as being distinct corporate organisations.
1892	NSW Labour Bureau established and was the first NSW Government agency to deal with employment-related issues, predominantly focused on providing job opportunities and accommodation for the unemployed. In 1895 the Bureau was absorbed into the NSW Department of Public Instruction.
1896	<i>Factories and Shops Act 1896</i> was the first comprehensive regulation of working conditions in factories, shops and other industrial establishments. The legislation restricted the working hours of women and children.
1899	<i>Early Closing Act 1899</i> restricted the length of working hours for all employees.
1900	<i>Truck Act 1900</i> required the payment of wages in money, and prohibited employers from influencing how employees spent wages.
1901	<i>Industrial Arbitration Act 1901</i> , first 'modern' industrial relations statute came into force in December 1901. A separate arbitration court was established, with binding arbitration powers. <i>Apprentices Act 1901</i> created the basis for the administration of all apprenticeships in NSW and reduced the hours of apprentices to a maximum of 48 per week. <i>Shearers' Accommodation Act 1901</i> set standards for the accommodation of shearers and others engaged in pastoral occupations.
1907	Basic wage set for male employees only. The Federal Harvester Case established a basic wage for male workers on the basis of their 'breadwinner' status. In the 1912 Fruitpickers Case the Federal Commission rejected an argument that male and female basic wage be equal. These decisions were followed by all Australian industrial relations tribunals.
1908	<i>Industrial Disputes Act 1908</i> replaced the 1901 Industrial Arbitration Act and introduced "Wages Boards" that could determine pay and conditions applying across all industries.
1911	The Attorney General continued to administer industrial relations legislation until 1911, when the Minister for Labour and Industry took up this responsibility.
1912	The Department of Labour & Industry was created, marking the first time employment relations were regulated by a separate government department in NSW. <i>Industrial Arbitration Act 1912</i> replaced the 1908 <i>Industrial Disputes Act</i> . The <i>Industrial Disputes Act 1912</i> saw the introduction of the wages boards, which regulated pay and conditions for workers.
1916	<i>Eight Hours Act 1916</i> created a standard 48 hour working week.
1919	Basic female wage was established. The basic female wage was 54% of the male basic wage.
1926	<i>Forty-four Hours Week Act 1926</i> reduced the standard working week to 44 hours. <i>Workmen's Compensation Act 1926</i> introduced NSW's first 'modern' compensation scheme for workers injured at work. <i>Rural Workers' Accommodation Act 1926</i> replaced, modernised and extended the coverage of the <i>Shearers' Accommodation Act 1901</i> .
1938	Shop registration was introduced. The licensing of shops and the regulation of shop trading hours was introduced under the <i>Factories and Shops Act 1901</i> .

Year	Development
1940	<i>Industrial Arbitration Act 1940</i> replaced the 1912 Act. This legislation further modernised the framework for NSW industrial relations.
1944	<i>Annual Holidays Act 1944</i> introduced a standard entitlement to 2 weeks holiday leave for each completed year of service. In 1958, this entitlement increased to three weeks leave per annum.
1947	Forty hour working week introduced. Amendments to the <i>Industrial Arbitration Act 1940</i> reduced the standard working week to 40 hours.
1955	<i>Long Service Leave Act 1955</i> introduced a standard entitlement to 13 weeks long service leave after 20 years of service.
1958	Equal pay. NSW became one of the first Australian States to legislate for equal pay for male and female workers.
1959	Unfair contracts regulated. Amendments to the <i>Industrial Arbitration Act 1940</i> enabled the NSW Industrial Relations Commission to alter or void any contracts involving work performed in any industry. These provisions then covered most forms of individual contracts for the performance of work, including franchise arrangements.
1963	Long service leave improved and extended. Standard entitlements increased to 3 months leave after 15 years service. New legislation was introduced extending long service leave entitlements to the metalliferous mining industry.
1973	State Equal Pay Decision. The NSW Industrial Relations Commission handed down its equal pay decision.
1974	Annual holiday entitlements increased. Following a test case decision by the NSW Industrial Relations Commission, the <i>Industrial Arbitration Act 1940</i> was amended to introduce a standard entitlement of 4 weeks leave for each year of service.
1975	Employment agents regulated. Amendments to the <i>Industrial Arbitration Act 1940</i> introduced a scheme for the licensing of private employment agents. A portable long service payments scheme for workers in the building and construction industry in New South Wales was also established and administered by the former Builders Licensing Board - now part of the Department of Fair Trading.
1977	<i>Anti Discrimination Act 1977</i> . Discrimination in employment on the grounds of sex, race and marital status was made unlawful. Grounds for unlawful discrimination were subsequently expanded to include age, disability, sexual harassment and family responsibilities as well as race, homosexual, HIV and transgender vilification.
1979	Transport industry workers covered. Amendments to the <i>Industrial Arbitration Act 1940</i> enabled the NSW Commission to regulate contracts of carriage (couriers) and contracts of bailment (taxi-drivers). The Department of Labour and Industry was abolished and a new Department of Industrial Relations and Technology was formed.
1980	Re-named the Department of Industrial Relations. <i>Industrial Arbitration Act</i> amended to provide a standard 12 months unpaid maternity leave. Later expanded to include paternity and adoption leave and, in 2000, to allow leave to be taken by regular and systematic casual employees.
1981	<i>Apprentices Act 1981</i> replaced the <i>Apprentices Act 1901</i> with a modern system for the regulation of apprenticeships in NSW.
1982	<i>Employment Protection Act 1982</i> created minimum redundancy entitlements for NSW workers under awards.
1983	<i>Occupational Health and Safety Act 1983</i> . New occupational health and safety (OH&S) regime introduced, placing greater OH&S obligations on employers and employees and focussed upon injury prevention strategies, employee involvement in OH&S matters and new penalties for breaches of the legislation.
1985	Long service leave entitlements increased to two months leave after 10 years of service.
1986	As a result of an amalgamation with the Ministry of Employment in 1986, the Department became known as the Department of Industrial Relations and Employment.

Year	Development
1987	<i>Workers' Compensation Act 1987</i> . Fundamental reforms to the workers' compensation system were introduced to reduce costs to employers. Amendments to the <i>Industrial Arbitration Act 1940</i> introduced new protections against dismissal for employees whilst receiving workers' compensation benefits.
1988	<i>Essential Services Act 1988</i> protected the NSW community from disruption to essential services.
1989	<i>Industrial & Commercial Training Act 1989</i> replaced the <i>Apprentices Act 1981</i> and introduced an integrated administration system for apprenticeships and traineeships. <i>Entertainment Industry Act 1989</i> replaced various arrangements under the <i>Industrial Arbitration Act 1940</i> with a new scheme to partially self-regulate the licensing of NSW theatrical agents and employers under the auspices of the NSW Entertainment Industry Council. John Fahey, the Minister for Industrial Relations and Employment in the Greiner Government, prepared an Information Paper announcing an overhaul of NSW's Industrial Relations system. The occupational health and safety functions were transferred out of the Department to join with the state Compensation Board and form the Workcover Authority of NSW.
1990	Re-named to become the Department of Industrial Relations, Employment, Training and Further Education, to reflect a focus on vocational education and training.
1991	Unfair dismissal laws reformed by amendments to the <i>Industrial Arbitration Act 1940</i> introduced to allow individual access and compensation for NSW workers who were unfairly dismissed.
1992	<i>Industrial Relations Act 1991</i> introduced enterprise bargaining, voluntary unionism and increased penalties for industrial action.
1994	NSW anti-discrimination legislation was amended to make awards and agreements subject to anti-discrimination legislation.
1995	Employment, Training and Further Education functions were transferred out to the Department of Training and Education Coordination and the name changed back to the Department of Industrial Relations.
1996	<i>Industrial Relations Act 1996</i> replaced the <i>Industrial Relations Act 1991</i> .
1997	Regulations made excluding certain classes of employees from unfair dismissal jurisdiction.
1998	Report of the Pay Equity Inquiry confirms that work in certain female dominated industries was undervalued.
2000	NSW Industrial Relations Commission adopts the Equal Remuneration Principle as a wage fixing principle. <i>Industrial Relations Amendment Act 2000</i> makes wide ranging amendments to the Act including: <ul style="list-style-type: none"> • Right of Federal award employees to make unfair dismissal claims to NSW Industrial Relations Commission; • Parental leave rights for casual employees; and • Establishing in victimisation proceedings a rebuttable presumption that any detrimental action taken against any employee was victimisation.
2001	Amendments to the <i>Industrial Relations Act 1996</i> limits applications under unfair contracts provisions. First pay equity decision increases rates of pay in public sector librarians' award on basis that there had been a history of undervaluation of work in a traditionally female dominated industry.
2002	<i>Ethical Clothing Trades Act</i> sets up Ethical Clothing Trades Council to advise on compliance with work related obligations to outworkers in the clothing industry. The <i>Industrial Relations Act 1996</i> was amended to provide for recovery of moneys unpaid or underpaid to outworkers. Report on review of the first five years of the <i>Industrial Relations Act 1996</i> tabled in Parliament. <i>Industrial Relations Act 1996</i> amended to regulate the conduct of industrial agents, who are neither legal practitioners nor officers or members of industrial organisations.

Year	Development
2003	<i>Industrial Relations Act 1996</i> amended to extend the adoption leave provisions of the Act (12 months unpaid leave) to parents who adopt children under 18 years of age. Department of Industrial Relations abolished and the new Office of Industrial Relations (OIR) was created under the Department of Commerce.
2005	<p>1 July 2005: The Ethical Clothing Trades Extended Responsibility Scheme comes into effect. The mandatory code protects outworkers and requires clothing retailers to source clothes from manufacturers who abide by NSW award conditions when using outworkers.</p> <p>7 October 2005: The <i>Workplace Surveillance Act 2005</i> prohibits spying on employees using technologies including video cameras, email and tracking devices.</p> <p>19 December 2005: The NSW Industrial Relations Commission handed down its General Order in the Family Provisions Case 2005. This case varied all NSW awards to include:</p> <ul style="list-style-type: none"> Extended use of sick leave for caring responsibilities when a family or household member is sick. Casuals can access unpaid leave to meet their caring responsibilities. Increase simultaneous unpaid parental leave to eight weeks Extending unpaid parental leave from 52 weeks to 104 weeks Permitting an employee to return from parental leave on a part-time basis until the child reaches school age.
2006	<p>28 February 2006: In the Secure Employment Test Case, the NSW Industrial Relations Commission establishes a right for casuals to convert to permanent employment after a period of six months of employment.</p> <p>March 2006: The <i>Public Sector Employment Legislation Amendment Act 2006</i> protects more than 186,000 NSW public sector staff employees of the Crown from the impact of the previous Federal government's Work Choices legislation.</p> <p>10 March 2006: The <i>Industrial Relations Amendment Act 2006</i> extended powers of the NSW Industrial Relations Commission to hear disputes referred to it pursuant to common law agreements between employers and employees.</p> <p>27 March 2006: The previous Federal government's <i>Workplace Relations Amendment (Work Choices) Act 2006</i> commences. Rights and responsibilities for employers who are 'constitutional corporations' employing staff in NSW are now under Federal jurisdiction.</p> <p>NSW industrial relations laws continue to apply to unincorporated businesses, such as sole traders, partnerships or trusts, and corporations that do not engage in significant financial or trading activities (eg not-for-profit organisations).</p> <p>14 November 2006: High Court of Australia hands down its decision on a challenge by all state and Territory Governments, upholding the constitutional validity of the previous Federal government's Work Choices laws.</p> <p>23 November 2006: The Legislative Council Standing Committee on Social Issues hands down its final report, finding that Work Choices should be repealed. Failing that, the Committee called on the NSW Government to take action to 'ameliorate' its effects.</p> <p>1 December 2006: <i>Industrial Relations (Child Employment) Act 2006</i> commences to protect the employment and conditions of young people aged under 18 employed by constitutional corporations. NSW Industrial Relations Commission commences proceedings to set principles for establishing whether such a child has suffered a net detriment as compared to the state award that would apply to the child's work.</p>
2007	<p>7 June 2007: Legislation introduced to state Parliament to ensure workplace entitlements for Sydney workers are protected during the APEC holiday. Industrial and Other Legislation Amendment (APEC Public Holiday) Bill 2007</p> <p>24 November 2007: Federal election is won by the Labor government, who announces that it intends to implement its Forward With Fairness industrial relations policy, with transitional legislation expected early 2008.</p>

Year	Development
2008	<p>13 February 2008: The <i>Workplace Relations Amendment (Transition to Forward with Fairness) Bill 2008</i> was introduced into Parliament. The Bill included amendments [to] the <i>Workplace Relations Act 1996</i> to make a number of changes to the framework for workplace agreements, and to enable the process of award modernisation to commence.</p> <p>25 November 2008: Deputy Prime Minister and Workplace Relations Minister Julia Gillard introduced the Fair Work Bill into the Commonwealth Parliament.</p>
2009	<p>1 July 2009: The Commonwealth Government's <i>Fair Work Act 2009</i> commences, repealing the <i>Workplace Relations Act 1996</i>. Components of the new Fair Work Act and Fair Work Regulations apply to all corporations and businesses in the national workplace relations system.</p> <p>Changes that commenced on 1 July 2009 include:</p> <ul style="list-style-type: none"> • New unfair dismissal laws • New national agencies, Fair Work Australia and the Fair Work Ombudsman, which replace the Australian Industrial Relations Commission, the Workplace Authority and the Workplace Ombudsman • New enterprise agreement options • Good-faith bargaining requirements • Transfer of business laws • New union right of entry laws <p>December 2009: The NSW Government announces that NSW will join the national industrial relations system from 1 January 2010, meaning that the Commonwealth's <i>Fair Work Act 2009</i> will cover every private sector employer and employee in NSW.</p> <p>The NSW referral bill was passed in NSW Parliament on 1 December 2009 and The Commonwealth Parliament voted to pass the state Referrals bill on 2 December 2009.</p>
2010	<p>1 January 2010: Final parts of Fair Work Act commence. This includes the new modern award system and the ten new National Employment Standards (NES).</p> <p>1 July 2010: In many modern awards, pay rates and some loading / penalty rates will start to be phased in. Changes to pre-existing rates may be phased in over 5 annual instalments. Fair Work Australia's first national minimum wage order to be completed.</p>
2012	<p>1 July 2012: The Public Sector Employment and Management (Mental Health Commission and Other Matters) Order 2012 No 270 transferred the industrial relations powers in the <i>Public Sector Employment and Management Act 2002</i> from the Director General of the Department of Premier and Cabinet to the Director General of the Department of Finance and Services. The transfer excluded powers relating to special temporary employees.</p>

Source: NSW Industrial Relations, Timeline of Industrial Relations (31 August 2011)

<http://www.industrialrelations.nsw.gov.au/oirwww/About_NSW_IR/Timeline_of_Industrial_Relations.page>.

A2.2 The table below provides a brief overview of the development of superannuation and retirement income in Australia.

Table A.2.2: Timeline of superannuation and retirement income in Australia

Year/Date	Measure
1900	<p>New South Wales introduced a means tested age pension of 26 a year, funded out of general revenue.</p> <p>Victoria and Queensland followed suit.</p>
1901	The Constitution gave the Commonwealth explicit power to legislate for provision of old age and invalid pensions.
10 June 1908	<i>Invalid and Old Age Pensions Act 1908</i> passed by the Deakin Government. Rate 26 per year (10/- a week). Eligibility limited according to character, race, age, residency and means. Paid to eligible men and women at 65. Commenced 15 April 1909.

Year/Date	Measure
1910	Pension age for eligible women reduced to 60.
1912	1908 Act amended to completely remove the family home from the means test.
1915	<i>Income Tax Assessment Act 1915</i> provided for tax deductibility of employer contributions made on behalf of employees, and for the exemption of superannuation fund earnings from taxation.
1923	Bruce Government established a Royal Commission to examine the possibility of having a comprehensive national insurance scheme for retirement, sickness or disability.
1928	<i>National Insurance Bill</i> introduced. It lapsed in 1929 when the Government was defeated.
1938	<i>National Health and Pensions Bill</i> passed, but its introduction was delayed, then abandoned because of World War 2.
1945	Chifley Government introduced an additional levy on personal income tax which, along with a payroll tax from employers, was credited to the National Welfare Fund. There was, however, no direct link between contributions and benefits and the pension. The National Welfare Fund, whilst set up as a means of establishing a base from which a national superannuation fund could be operated, was in practice merely an accounting device until its abolition in 1985.
1961	Superannuation funds exempt from tax if they held required amounts of Commonwealth Bonds. Commonwealth control of superannuation funds by use of taxation power firmly established.
1965	High Court upholds Commonwealth's ability to control superannuation fund investment by use of taxation power.
By late 1960s	Means assessed on basis of income plus a proportion of countable assets except for the family home (which has always been assets-test-exempt.) About 70% of people qualifying on grounds of age received the pension.
1972	Only 32% of workers covered by superannuation.
1973	Whitlam Labor Government established the <i>National Superannuation Committee of Inquiry</i> . Chairman Keith Hancock.
1973	Means test for pensioners 75 years of age and over abolished.
1974	Australian Bureau of Statistics conducted the first national survey of superannuation coverage. 32% of the workforce was covered by superannuation 36% male; 15% females. 24% of people in the private sector had super cover compared with 58% in the public sector.
1975	Means test removed for persons aged 70 to 74 inclusive.
1975	Pensions linked to 25% of average weekly earnings, to be indexed annually.
1976	Pensions became subject to automatic increases twice yearly. Age pension assets test abolished.
1976	The Hancock Inquiry recommended a partially contributory, universal pension system with an earnings-related supplement. A minority recommendation suggested a non-contributory flat rate universal pension, a means tested supplement, and encouragement of voluntary savings through expanding occupational superannuation.
20 June 1977	Fraser government decides not to establish a contributory national superannuation scheme.
1978	Pension increases to be adjusted only once a year (in November). Future increases in the Age Pension for those aged 70 or over made subject to an income test.
1979	Fraser Government rejected the recommendations of the Hancock Inquiry. Pension increases subject to twice yearly increases, in May and November.
May 1983	Base pension for those aged 70 and over subject to an incomes test.

Year/Date	Measure
1983	The <i>Statement of Accord (Prices and Incomes Accord)</i> between the ALP and the ACTU was endorsed in February, shortly before the Federal election. Claims for wage increases were to be restricted to movements in the CPI.
1983	Hawke Labor Government expressed support for the principles of employee superannuation. The May Economic Statement began the process of reform of the taxation of superannuation. For lump sums at age 55 or later, the first \$50,000 would be taxed at 15%; the remainder at 30%. Lump sums taken below age 55 would be taxed at 30%. These thresholds indexed to AWOTE.
1984	CBUSS - Superannuation for the building industry created, from an idea shared by building union leaders and ACTU officials. Regarded as a world first. (funds owned and controlled by a board comprising equal numbers of employer and employee or union representatives.) A number of other similar funds established in the following years- These funds are called Industry Funds.
1984	Age pension assets test reintroduced. Family home excluded.
1985	Renegotiation of the Accord identified superannuation as a key issue.
1986	Labor joined with the ACTU in seeking a universal 3% superannuation contribution by employers to be paid into an industry fund, in lieu of a wage rise.
1986	Accord Mk II between the Government and the unions stipulated that compensation to employees should be 6% (to keep pace with inflation). This was to be 3% employer superannuation contribution, a 2% wage rise, and tax cuts. Agreement endorsed by the Conciliation and Arbitration Commission February 1986.
1986	Employer groups, including the Confederation of Australian Industry, challenged the Commission's decision in the High Court, claiming that superannuation was not an industrial matter within s.51 (xxxv) of the Constitution.
15 May 1986	High Court ruled in favour of the Conciliation and Arbitration Commission.
June 1986	National Wage Case established guidelines to require new industry superannuation schemes to conform to Commonwealth operational standards.
1987	Insurance and Superannuation Commission (ISC) was established as an industry regulator.
1987	Superannuation funds total assets \$41.1bn. [1]
21 December 1987	The Government introduced the <i>Occupational Superannuation Standards Act 1987</i> (OSSA). Operating standards were prescribed for the vesting of benefits from employer and employee contribution; preservation of benefits until age 55; more member involvement in the control of superannuation funds; security of members benefits. [2]
May 1988	Hawke Government statement <i>Reform of the Taxation of Superannuation</i> contained measures to bring forward payment of superannuation taxation liabilities by introducing a tax on contributions and reducing tax on benefits. Reasonable Benefits Limits introduced.
June 1988	51.3% employed persons covered by Superannuation
1989	The Government's 1989 retirement income policy statement established a policy in Australia based on the "twin pillars" of the age pension and private superannuation, specifically rejecting the option of a National Superannuation Scheme.
December 1989	Superannuation funds total assets \$119bn
December 1990	Superannuation fund assets \$123bn, 64% of all employees had superannuation coverage.
1991	In the Budget, Treasurer John Kerin announced that from 1 July 1992, under a new system to be known as the Superannuation Guarantee (SG), employers would be required to make superannuation contributions on behalf of their employees.

Year/Date	Measure
March 1992	Superannuation Assets estimated to be \$148bn.
June 1992	Senate Select Committee on Superannuation presents its first report. This Senate Committee, in various forms, reviewed and issued reports on various superannuation issues up to the end of the 40 th Parliament (2004). Many of these reports led to significant changes in the superannuation system.
1992	Labor Government implemented the Superannuation Guarantee (SG), which extended retirement savings to 72 % of workers. Employers were required to make prescribed contributions on behalf of their employees to a complying superannuation fund. Super contributions were to be progressively increased between 1992-2002, from 3% to 9%.
1993	Labor Government overhauls regulation of superannuation with introduction of the <i>Superannuation Industry (Supervision) Act 1993</i> (SIS Act). The OSSA continues in force but many of its provisions are repealed and transferred to the SIS Act.
1993	World Bank endorses Australia's three pillar system for the provision of retirement income as world's best practice.
June 1993	Superannuation assets reaches \$169bn
June 1993	FitzGerald report advocates increasing household savings via superannuation, but recommends that national savings be increased by increasing public sector savings. Superannuation's role in increasing national savings no longer seen as important. This is a significant change in the policy rationale for superannuation system.
November 1993	80% of employed persons either made superannuation contributions or had them made on their behalf.
1994	Pension age for eligible women to be raised to 65, in a phased process.
June 1994	Superannuation assets \$183bn
1995	In the 1995 budget speech Treasurer Ralph Willis outlined plans to pay previously announced tax cuts into employee's superannuation funds. Government to make matching contributions. The principal of matching government superannuation co-contributions established.
1995	Shadow Treasurer Peter Costello called for employee choice and for funds to compete for business
March 1995	Superannuation Assets \$187bn.
June 1995	80.5 % employed persons covered by superannuation
June 1996	Superannuation assets \$245.3bn, 37.9% of GDP
20 August 1996	Superannuation Surcharge introduced by Treasurer Peter Costello in the Howard Government's first budget.
1997	Wallis Financial System Inquiry, established by Treasurer Costello in May 1996, advocated superannuation choice and other changes to the superannuation system.
1997	Age pension to be formally maintained at 25% AWOTE. Retirement savings accounts (RSA) established. Superannuation surcharge implemented. Maximum age for SG contributions increased from 65 to 70.
1997	Limited access to superannuation possible on compassionate grounds.
June 1997	Superannuation assets \$321.0bn, 47.7% of GDP, 81% were covered by superannuation.
9 December 1997	Limited access to superannuation possible if member is in severe financial hardship. This is defined as being in receipt of commonwealth income support for a continuous period of 26 weeks or a cumulative period of 39 weeks.

Year/Date	Measure
1998	Age pension means test for retirement income streams revised. Pension Bonus scheme introduced. A person could accrue a pension bonus payment by deferring claiming the pension while still working.
1998	Reforms to business taxation, including proposals to reduce the CGT rate for super funds to 10%
1998	Australian Prudential Regulation Authority established on 1 July 1998 . APRA is the lead superannuation regulator. The Australian Securities and Investments Commission also took a significant role in the regulation of superannuation. The Australian Taxation Office continued to carry out some regulatory functions and administer the superannuation taxation legislation. The Insurance and Superannuation Commission ceases to operate on the same date. These changes were in response to the recommendations of the Wallis Inquiry.
June 1998	Superannuation assets \$360.3bn, 51.2% of GDP
1999	In 1999, the SIS Act was amended to establish a new category of small superannuation fund, the Self Managed Superannuation Fund to be regulated by the Australian Taxation Office.
June 1999	Superannuation assets \$411.4bn, 55.6% of GDP
8 October 1999	Australian Taxation Office took administrative responsibility for Self Managed Superannuation Funds (SMSF).
June 2000	Superannuation assets \$484.2bn, 63.0% of GDP, 87% of employed persons (both part and full time workers) covered by superannuation.
2001	Financial Services Reform Act is designed to be a single licensing and disclosure approach for all financial services, including superannuation. Commenced in March 2002.
June 2001	Superannuation assets \$519.0bn, 66.2% of GDP
2002	Maximum age for superannuation contributions increased from 70 to 75 (for people working at least 10 hours a week).
June 2002	Superannuation assets \$518.1bn, 63.7% of GDP
1 July 2002	Temporary residents permanently departing Australia may withdraw their accumulated superannuation benefits before their preservation age. This does not apply to New Zealand residents.
28 December 2002	Superannuation assets able to be divided between the parties in a marriage breakdown
2003	Superannuation surcharge reduced from 15% to 12.5%. Government co-contribution for low/middle income earners introduced.
June 2003	Superannuation assets \$546.8bn, 65.2% of GDP, 90% of employed persons have employer provided superannuation.
1 July 2003	Superannuation co-contributions policy takes effect in respect of personal (or undeducted) contributions made after this date.
25 February 2004	On 25 February 2004, the Treasurer released <i>A more flexible and adaptable retirement income system</i> as part of Australia's Demographic Challenges announcement. Amongst other things this report proposed to allow access to a person's superannuation, in the form of an income stream, before they had left the work force (that is, transition to retirement pensions) and to scrap the work test for those under age 65.
2004	<i>Superannuation Safety Amendment Act 2004</i> enacted changes to regulation of superannuation. All superannuation trustees of large eligible funds have to be licensed from 1 July 2004. Trustees of SMSFs do not have to be licensed.
2004	Superannuation regulations changed to allow the portability of money between different superannuation accounts.

Year/Date	Measure
2004	Employee choice of fund passed Senate in June, to come into operation from 1 July 2005. Superannuation surcharge reduced from 12.5% to 10%.
2004	Tax free payment of superannuation benefits can be made to the surviving partner on an interdependent relationship. An interdependent relationship can encompass same sex couples, or a relationship where one person is financial dependent on another person. For example, where a son or daughter is financially supporting a parent.
June 2004	Superannuation assets \$643.0bn, 73.6% of GDP
1 July 2004	Work test governing contributions made under age 65 ceased to operate. Work test remains for contributions made above age 65.
10 May 2005	Treasurer Costello announced in the Budget the abolition of the Superannuation Surcharge. Changes take effect from 1 July 2005
June 2005	Superannuation assets \$762.9bn, 85.1% of GDP, 90% of employed persons have employer provided superannuation.
1 July 2005	Transition to Retirement Pensions available. A member may commence to receive a transition to retirement pension without having to leave the workforce or retire. Choice of Superannuation Fund takes effect.
1 Jan 2006	Contributions Splitting took effect. A Member's SG and other contributions may be split with their spouse.
9 May 2006	In the Budget, Treasurer Costello announced plans to simplify superannuation. Simpler Super includes: <ul style="list-style-type: none"> - exemption from tax on end benefits for Australians aged 60 or over from 1 July 2007; - no tax on a lump sum; - no tax on a superannuation pension; - reasonable benefit limits to be abolished; and - transferring super between funds made easier. Implementation date is 1 July 2007.
June 2006	Superannuation assets \$912.0bn, 98.8% of GDP, 90% of all employed persons covered by superannuation.
June 2007	Superannuation assets \$1153.3bn (that is, 1 trillion), 119% of GDP.
1 July 2007	Most Simplified Superannuation amendments take effect. Bulk of operating superannuation tax law now in the <i>Income Tax Assessment Act 1997</i> . Prudential and operational aspects now largely in the SIS Act. Residual parts of superannuation law remain in <i>Income Tax Assessment Act 1936</i> .
11 September 2007 Measure applies to lump sums paid on or after 1 July 2007	Tax free benefits able to be paid to those with a terminal illness.
20 September 2007	Social Security assets test threshold raised from \$531,000 to \$839,500 (couple); from \$343,750 to \$529,250 (single); it is estimated that more than 300,000 extra people will be eligible for the age pension.
31 December 2007	Employee's ability to recover unpaid superannuation amounts from employers that have ceased operating enhanced.
3 March 2008	Minister for Superannuation and Corporate Law Sherry announced the establishment of a Superannuation Advisory Group to advise on matters relevant to current or prospective superannuation legislation and on Government policy proposals which have significant impact for the superannuation industry.

Year/Date	Measure
5 May 2008	Minister Sherry announces consultation on a measure introduced by the Coalition Government which required future superannuation contributions and existing balances for temporary residents to be transferred to the ATO. If these were unclaimed after 5 years, the amounts would be confiscated. Extra revenue of up to \$1 billion a year is predicted.
13 May 2008	Labor's first Budget contains details of a review of taxation Australia's future tax system, to be chaired by Dr Ken Henry. Terms of reference include the government's commitment to preserve tax-free superannuation payments for the over 60s.
19 May 2008	Minister Sherry announced that universal forecasting of superannuation end-benefits could be introduced to enable better understanding of retirement savings.
28 May 2008	Attorney-General Robert McClelland introduced the first of a range of amendments to remove same-sex discrimination from Acts governing Commonwealth superannuation schemes. This ensures that same-sex couples are not denied the payment of death benefits from superannuation schemes or the tax concessions on death benefits currently made available to opposite-sex couples.
June 2008	ASIC begins to provide advice on long term superannuation returns
17 Jun 2008	The <i>Same-Sex Relationships (Equal Treatment in Commonwealth Laws Superannuation) Bill 2008</i> is sent to a committee inquiry without an end date
25 June 2008	Legislation providing further relief for employers who make a late superannuation guarantee contribution receives Royal Assent
26 June 2008	Minister Sherry announced a review of pension indexation arrangements for Australian Government superannuation schemes (civilian and military). The review commences in July and is expected to conclude by the end of 2008.
December 2008	Review of Australian government pension indexation (Mathews Review) completed. Report not released to the public.
18 December 2008	Act requiring temporary resident's superannuation benefits to be paid to the ATO, if not claimed within 6 months of departing Australia, commences operation.
4 December 2008	Royal Assent to the <i>Same-Sex Relationships (Equal Treatment in Commonwealth Laws—Superannuation) Bill 2008</i> (No. 107 of 2008) passes through Parliament.
1 April 2009	Act raising tax rates of Temporary Residents superannuation benefits when paid takes effect.
28 April 2009	Minister Sherry announces Review into the governance, efficiency, structure and operation of Australia's superannuation system.
4 May 2009	Release of the Report on Strategic issues for the Retirement Income System – as part of the Australia's future tax system inquiry (Henry Review). Amongst other things recommends that superannuation guarantee contribution rate remain at 9 per cent of ordinary time earnings and retains the \$450 per month minimum wage threshold for superannuation guarantee purposes.
29 May 2009	Minister Sherry announces the terms of reference and makeup of Review into the governance, efficiency, structure and operation of Australia's superannuation system.
1 July 2009	Rate at which government superannuation co-contribution is paid reduced temporarily between 1 July 2009 and 30 June 2014. Rate returns to \$1.50 for every \$1 contribution (subject to income test threshold) on 1 July 2014.
1 July 2009	Limit on concessional contributions (formally known as tax deductible contributions) reduced from \$50 000 p.a. to \$25 000 p.a. for 2009–10 and later years. This limit is indexed to changes in AWOTE (if those changes are sufficiently large enough). Transitional measures remain in place for those over 50 years of age to 2011–2012. Annual limits on non-concessional contributions (that is, after tax contributions) are now 6 times the limit on concessional contributions for those under 50 years of age (that is, 6 times \$25 000 or \$150 000 p.a. for the 2009–10 year).
1 July 2009	Income for government superannuation co-contribution purposes now includes a person's reportable employer superannuation contributions. That is the amount that the employer puts into superannuation on the employee's behalf that exceeds the superannuation guarantee requirements.

Year/Date	Measure
1 July 2009	Expanded definition of 'ordinary time earnings' for superannuation guarantee purposes takes effect. 'Ordinary time earnings' now include over award payments, shift loadings, allowances and piece rates paid in relation to a person's ordinary hours of work. It does not include overtime payments.
9 July 2009	Superannuation funds now able to offer limited financial advice to their members.
21 August 2009	Release of the Mathews Report recommends that government superannuation pensions continue to be adjusted by increases in the Consumer Price Index (CPI). Government fully supports this recommendation.
20 September 2009	<p>The rate of the age pension was raised by \$30 per week for single people. Existing pension supplements were consolidated into one pension supplement and increased by \$2.49 per week for single people and \$10.14 per week for couples.</p> <p>The 25% of MTAWA adequacy benchmark was adjusted to 27.7% for single people and 41.76% for couples. A new prices measure called the Pensioner and Beneficiary Living Cost Index (PBLCI) was added to the pension indexation process. Where the increase in the PBLCI is greater than that for the CPI it will be used instead of the CPI in the indexation process.</p> <p>The pension income test taper rate was increased from 40% to 50%. A work bonus was introduced that exempted half of any income from employment up to \$500 per fortnight from consideration under the income test.</p> <p>The Pension Bonus Scheme was abolished</p>
14 December 2009	Release of phase one preliminary report of the Review into the governance, efficiency, structure and operation of Australia's superannuation system (that is, the Cooper Review) on superannuation fund governance
January 2010	Formal inclusion of specific superannuation funds (usually industry funds) in industrial awards. This change does not restrict an employee's right to have contributions made to a superannuation fund of their choice
20 April 2010	Release of Cooper Review Phase two preliminary report – 'Mysuper, optimising Australian superannuation'.
29 April 2010	Release of Cooper Review Phase three preliminary report – 'Self managed super solutions'.
2 May 2010	Government response to Australia's future tax system review (that is, the Henry Review) released. Superannuation Guarantee rate proposed to be raised to 12% between 2013–14 and 2019–20, Superannuation Guarantee age limit to be increased to 75 in from 1 July 2013, an annual superannuation contribution of up to \$500 provided for those receiving and adjusted taxable income of up to \$37 000 p.a. and the concessional contribution cap for those over age 50, with less than \$500 000 in total superannuation benefits to be permanently raised from \$25 000 to \$50 000 p.a. Proposed measures repeated in budget papers released on 11 May 2010 (see below).
11 May 2010	Government proposed changes to Co-contributions scheme. Income thresholds applying for 2009–10 to continue for a further two years, Government co-contribution rate to be set permanently at \$1 for every \$1 of personal contributions made by those receiving an adjusted annual income less than \$31 920 p.a.
July 2017	The qualifying age for the age pension will increase by six months every two years until it reaches 67 years of age on 1 January 2024

Source: Leslie Nielson and Barbara Harris, Economics Section, Parliament of Australia, 'Chronology of superannuation and retirement income in Australia' (1 June 2010) <<http://www.aph.gov.au>>.

APPENDIX 3—ATO RESPONSE



Australian Government
Australian Taxation Office

Second Commissioner of Taxation

Mr Ali Noroozi
Inspector-General of Taxation
GPO Box 551
SYDNEY ACT 2001

Dear Ali

Review into the ATO's employer obligations compliance activities

Thank you for the opportunity to comment on your final draft of your report on the review into employer obligations compliance activities.

We appreciate your acknowledgement in the report of the sound approaches we have in place to support our workforce and their capability development and to assure good quality outcomes from the work they do. This is helpful in countering claims reported in the media recently of systemic deficiencies in our work in this area, and I think a very positive outcome from the work your office does.

We agree in full or in part with 7 of the recommendations, disagree with 2 of the recommendations, and note that 2 of the recommendations are for Government to consider. Our detailed response to all your recommendations is attached at *Annexure 1*.

I would like to acknowledge the efforts of all involved in undertaking this review. If you require further information on our response, please contact Emma Haines on (08) 8218 9330.

Yours sincerely

A handwritten signature in dark ink, appearing to read 'Neil Olesen'.

Neil Olesen
Second Commissioner
Australian Taxation Office
24 November 2016

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[To minimise space, the annexure to the ATO's response has not been reproduced here, but has been inserted into the text of this report underneath each of the recommendations to which that text relates.]

SHORTENED FORMS

ATO	Australian Taxation Office
ABA	Administratively Binding Advice
ABN	Australian Business Number
ANAO	Australian National Audit Office
BAS	Business Activity Statement
BoT	Board of Taxation
CRA	Canada Revenue Agency
DHS	Department of Human Service
ECD tool	Employee/Contractor Decision tool
EN	Employee Notification
FBT	Fringe Benefits Tax
FBTAA	<i>Fringe Benefits Tax Assessment Act 1986</i>
FEG	Fair Entitlements Guarantee scheme
FWC	Fair Work Commission
FWO	Fair Work Ombudsman
GST	Goods and Services Tax
HMRC	Her Majesty's Revenue & Customs
HRE	High Risk Employer
HRI	High Risk Industry
IGT	Inspector-General of Taxation
IRS	Internal Revenue Service
NSW	New South Wales
PAYE	Pay As You Earn
PAYG	Pay As You Go
PAYGW	Pay As You Go Withholding
PBR	Private Binding Ruling
PSI	Personal Services Income
RIS	Regulation Impact Statement
SBFS	Small Business Fix-it Squad
SBSCH	Small Business Superannuation Clearing House

SG	Superannuation Guarantee
SGAA	<i>Superannuation Guarantee (Administration) Act 1992</i>
SGC	Superannuation Guarantee Charge
SHWG	FBT and Remuneration Safe Harbour Working Group
SRO	State and Territory Revenue Offices
STP	Single Touch Payroll
TAA	<i>Taxation Administration Act 1953</i>
TFN	Tax File Number
TPAR	Taxable Payments Annual Report
TPRS	Taxable Payments Reporting System
UK	United Kingdom
US	United States
VCS	Voluntary Certification System