



THE LAW SOCIETY
OF NEW SOUTH WALES

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6 July 2018

Payroll Tax Review
NSW Treasury
GPO Box 5469
Sydney NSW 2001

By email: payrolltax.review@treasury.nsw.gov.au

Dear Sir/Madam,

Review of Payroll Tax Administration

The Law Society of NSW appreciates the opportunity to comment in relation to the current Review of Payroll Tax Administration. The Law Society members of the Revenue NSW / Law Society Liaison Committee and the Law Society's Business Law Committee have contributed to this submission.

The Law Society responds to the questions raised in the Consultation Guide below.

1. How can payroll tax administration processes in NSW be streamlined noting that thresholds and rates are outside the scope of this review?

We note that Single Touch Payroll reporting commenced on 1 July 2018. If this proves to be efficient for employers and the Australian Taxation Office ("ATO"), NSW might investigate how this data can be shared and harnessed for payroll tax purposes, without requiring employers to duplicate reporting processes.

2. What is the single change to the way payroll tax is administered in NSW which would be of greatest benefit?

From our perspective, early engagement in the audit and objection process would be beneficial in terms of efficiency and negotiating successful outcomes for taxpayers.

One area in which early engagement could be beneficial is in relation to the administration of the grouping provisions. Where an audit results in a finding that employers are grouped, the audit team could engage with the employer at that time to ascertain whether it is reasonable to exercise the discretion to exclude members from the group pursuant to s 79 of the *Payroll Tax Act 2007* ("Act"). The legislation does not appear to require a formal application for exclusion in order for the Chief Commissioner to determine that a person is not a member of a group.

Early engagement could provide efficiencies by having the same team, familiar with the payroll tax group from the audit process, assessing the information gathered on audit and requesting any further information needed to exercise the discretion to exclude the relevant member from the group. The current practice involves s 79

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applications being received by the exclusions team, which has no background or information in relation to the group and who must often familiarise themselves with the data already collected by the audit team. Adopting this approach would provide continuity for Revenue NSW and allow a single point of contact for the taxpayer or its adviser. However, any liaising or sharing of resources between audit and exclusion teams, or personnel undertaking dual roles, must not compromise the independence of the decisions made in relation to audit and exclusion, and should be sensitive to the confidential nature of information received.

3. Is there a simple, short term change that should be considered to make an immediate improvement to tax administration?

In the short term, we have two suggestions for consideration, which would be of particular assistance to small businesses.

We suggest that where applicable, certain exemptions could apply up to a specified payroll threshold. That is, where the threshold applied, the employer could rely on the exemption without the need to retain records to satisfy the evidentiary requirements.

We also recommend that consideration be given to an exemption from the relevant contractor provisions in s 32 of the Act in respect of certain groups, such as financial planners, as a class where the relevant contractor is only included because of the regulatory regime in which they operate.

It may be illustrative to look at a case study relating to the financial planning industry where the relevant contractor provisions have caused major concerns because of the regulatory regime in which financial planners operate. We note that this issue was also highlighted in the Law Society's 2012 submission to Treasury on the more general review of the Act.

Case Study

Financial planners run independent businesses which they operate under a licensing regime imposed by the *Corporations Act 2001* (Cth) ("Corporations Act"). In seeking to apply Division 7 of the Act, the following points are noted:

1) *Modernisation of contractor provisions*

To be a relevant contract there must be a payment for services rendered under a contract. However, the way the industry operates particularly now under the Future of Financial Advice ("FOFA") regime is that planners provide services to their clients (consumers) and it is those clients that make payments to the planners. The licensing regime under which the planners operate requires the licensee to administratively collect the fee from the client and then pass it on to the planner, after deduction of costs. However, there are no services being provided by the planner to the licensee for which it receives payment. If anything, there are services being provided by the licensee to the planner (e.g. education, para-planning etc). There is therefore arguably no relevant contract that can come within the provisions. However, the nature of the arrangements causes confusion due to the overlay of the Corporations Act obligations and the poor drafting of the definition of a relevant contract which makes it difficult for small businesses, in this case financial planners, to understand how the provisions apply.

Modern business practice means that the use of external resources in the form of independent contractors is likely to increase as head count and

economic issues cause organisations to downsize and seek increasing access to such external resources. The definition of relevant contract therefore requires significant modernisation and clarification to better reflect current business practices as currently it works on a “catch all” and then “exclude by exception” regime.

2) *Clarification of exclusions*

There are exclusions for businesses from the relevant contract provisions where there are two or more persons employed in or who provide services for the contractor's business (the “two or more persons exemption”)¹. For example, if a sole trader employs another person in his or her business the sole trader should be exempt. In 2005, the Supreme Court of NSW examined a similar provision in the Act in the context of licensed brokers and confirmed not only the application of the two or more persons exclusion but also construed the exemption as having a wide application: *Bridges Financial Services Pty Ltd v Chief Commissioner of State Revenue* [2005] NSWSC 788. However modern business practice and economic conditions mean that small businesses may employ staff part time or on a casual basis or seasonally depending on work load. The exclusion makes little reference to these situations and so again requires modernisation to reflect these scenarios. In addition, in order to prove the exemption, the business must keep extensive records of who was employed, including details of each period of employment, which imposes a huge regulatory burden upon small businesses.

In summary, the application of Division 7 is causing a significant administrative burden to small business without any net revenue gain to the State. The complexity of the provisions and the burden of proof due to self-assessment means that there is not only uncertainty but also disproportionate costs in trying to comply. In addition, the legal costs in seeking a merits or judicial review usually far outweigh the amounts of tax involved.

In the case of financial planners, there was an exemption in place in the 1971 Act for the very reason that financial planners were considered independent businesses. However, the relevant contract provisions caused unnecessary uncertainty. The removal of the exemption in 2007 was a function of payroll tax harmonisation and supposedly cutting red tape. It has instead highlighted the uncertainty of how the provisions apply to that industry.

The issues faced by the financial planning industry are mirrored across many other industries where regulation has meant particular business practices are used but where there is no intention to avoid tax and other business obligations.

4. Are there practices that NSW should adapt from other jurisdictions, and what would their impact be if taken up in NSW?

We consider it would be beneficial to both Revenue NSW and the taxpayer for the objections team to meet with the taxpayer's advisors prior to finalising the objection decision. In our experience, the ATO generally approaches taxation administration with greater opportunity for early engagement, which can streamline the process, provide efficiencies and facilitate a better outcome for taxpayers.

¹ Section 32(2)(c) of the *Payroll Tax Act 2007*

5. Are there additional guidance/materials/tools that could be provided by Revenue NSW to improve an employer's user experience?

In our experience, two issues that employers appear to have difficulties with are using the correct grouping percentage threshold and applying the threshold. Revenue NSW has a number of resources on its website covering these areas but perhaps these could be further enhanced.

Employers and their advisers are also not always aware of the review process and timeframes to lodge an application for review. In our experience the payroll tax objections team is unlikely to exercise its discretion and allow an out of time objection unless exceptional circumstances apply. However, the exclusion team is able to review applications even where the assessment is out of time. Further public information and resources in relation to the review process and timeline, including external reviews, such as at the NSW Civil and Administrative Tribunal, would be beneficial to employers and their advisers.

6. What is the administrative burden (time, cost) on your business associated with:

a. the initial payroll tax registration process?

The registration process is straight-forward and easily accessible, with clear Revenue NSW instructions in terms of information required. Most taxpayers will, however, be required to retain a tax adviser prior to completing the online registration for the 'grouping' question in order to correctly assess members of the group.

b. monthly and annual returns and payments? How might this burden be reduced?

No comments.

c. record keeping and evidentiary requirements for employers when claiming exemptions under the relevant contracts provisions? How might this burden be reduced?

As noted above, employers often have difficulty determining the extent and type of records needed to satisfy Revenue NSW of an entitlement to an exemption or that payroll tax does not apply. In our experience, there are three issues that commonly arise.

First, proving that a supply of services is not a relevant contract pursuant to s 32(2) of the Act is difficult. We understand that this represents the majority of the payroll tax objections at present. The published cases also reflect this trend.

Second, difficulties are experienced in proving that a business is sufficiently independent of other businesses in a payroll tax group so as to be excluded from that group under s 79. Many advisers and employers are not aware of the ability to de-group (or that holding and subsidiary companies cannot be de-grouped). Revenue NSW's Application for Exclusion from Grouping form² includes a list of factors for employers to complete to show that their business operates independently and separately from another business. However, often when this

² https://www.revenue.nsw.gov.au/sites/default/files/file_manager/opt018.pdf

form is completed, the necessary evidence to support a successful exclusion application is not included. For example, the omission of statutory declarations to show that a director does not have ultimate control of the business and that management and control was conducted by other parties.

Third, comprehending the breadth of application of the grouping provision and the inherent uncertainty surrounding whether the Chief Commissioner will exercise the discretion to exclude employers from a group is problematic. In our experience, an application for exclusion from grouping is more successful with two or three businesses. However, with a complex group with over 50 entities, the subsuming provisions are far-reaching and the Commissioner is less likely to exercise discretion.

d. the audit process undertaken by Revenue NSW?

Depending on the audit team, the prevailing sentiment amongst our members is that Revenue NSW adopts a fairly bureaucratic approach to both undertaking their audits and imposing penalties. The feedback from taxpayers is that payroll tax audits will generally result in high compliance costs to the business and will cause displacement of day-to-day operations.

We have been advised of situations where taxpayers are forced to obtain legal representation to avoid the potential imposition of increased penalties foreshadowed in correspondence by the audit team. Further, there is a view that audit teams are quick to assess on minimal analysis, forcing the taxpayer to apply resources to object.

There also appears to be the potential to expand the use of the Commissioner's discretion pursuant to Division 2 of the Act in relation to excluding members from the payroll tax group where the circumstances would suggest it commercially sensible to do so.

As advisers, we have also seen taxpayers significantly impacted by Revenue NSW's sharing of audit findings with other members of the payroll tax group being investigated. The information pertaining to one business in the group does, in many cases, contain confidential business information that Revenue NSW has openly shared with other group members in their audit findings (and vice versa), causing distress to the taxpayers involved.

How might this burden be reduced?

We suggest that the compliance burden would be greatly decreased through better communication on the expected focus of the audit prior to any face-to-face meeting with the taxpayer. We also recommend careful consideration of confidentiality by Revenue NSW prior to release of confidential business information upon releasing the audit report to members of the payroll tax group. Such taxpayer protections would not necessarily impede the powers of the Commissioner to undertake an audit or investigation but would protect the financial position of taxpayers attempting to comply with Revenue NSW requirements.

7. Are there any areas where further harmonisation or co-ordination with other jurisdictions would be beneficial?

We support continued harmonisation and co-ordination with other jurisdictions. However, we note that even where legislation has been harmonised with other jurisdictions, there are differences in the application of the legislation which compromise the benefits and efficiencies that can be gained from harmonisation.

Where there is harmony between the payroll tax provisions and administration among different jurisdictions, we suggest consideration be given to co-ordination of online interactive educational webinars on payroll tax by Revenue NSW and revenue offices of other jurisdictions. For example, Revenue NSW could become involved in joint presentations with revenue offices of other states and territories, of online interactive educational webinars on payroll tax.

Co-ordination of online interactive educational webinars on payroll tax could be beneficial to NSW and other jurisdictions by facilitating inter-jurisdictional sharing of educational resources and information for more efficient Australia-wide administration of state and territory payroll taxes. This approach could also save costs by avoiding duplication and assist in optimising attendance numbers. We suggest it would also provide an efficient means of more broadly alerting revenue offices to questions and concerns of taxpayers and assist in compliance.

8. How might the performance of the NSW payroll tax administration process be measured to keep track of the efficiency and effectiveness of the system, and to benchmark with other tax administration systems?

It is difficult to answer this question without knowing how performance is currently measured. We anticipate that data is already collected as to the amount of additional revenue received due to the audit process. Under an efficient and effective overall process, additional revenue obtained through the audit process should be minimal.

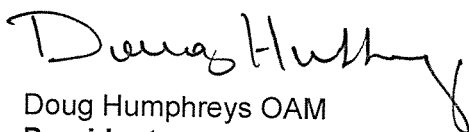
We would note that there appears to be a sentiment that tax administration is measured by Treasury purely by the amount of revenue raised – rather than qualitative factors such as how thorough the audit team was. Further internal reviews of decisions often appear revenue focused rather than being truly independent.

A more transparent approach to audits and the review process would arguably be beneficial – perhaps introducing qualitative factors which includes feedback from taxpayers (“clients”) regarding how the audit was run, whether the staff were knowledgeable about their application of the law, whether it was run efficiently etc.

We note that such reviews of the audit process are done regularly in the case of ATO audits of taxpayers and would we suggest, provide valuable feedback as to how to improve efficiency, transparency and fairness going forward.

Any questions in relation to this submission should be directed to Gabrielle Lea, Policy Lawyer on 9926 0375 or email: gabrielle.lea@lawsociety.com.au.

Yours faithfully,


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President