

The Board of Taxation
c/- The Treasury
Langton Crescent
CANBERRA ACT 2600

Dear Chairman

Re: Post-implementation review into the Alienation of Personal Services Income Rules ('APSI')

Thank you for the opportunity to make a submission in respect of the above-mentioned review.

There are two aspects of the APSI rules that we would like to comment on. The first deals with the rules themselves as to how they treat certain taxpayers. The second deals with where the rules sit in relation to larger area of personal services income ('PSI').

1. The APSI rules as a self contained measure

The APSI rules have been in operation for over nine years now (since 1 July 2000) and as a general observation, we believe the rules are targeting well those taxpayers whom the rules were designed to impact upon.

We note that several cases have come before the Administrative Appeal Tribunal (e.g., *Scimitar Systems Pty Ltd* [2004] AATA 720, *Dibarr Pty Ltd* [2004] AATA 1030, *Nguyen & Anor* [2005] AATA 15, *Metaskills Pty Ltd* [2005] AATA 647, *Skiba* [2007] AATA 1705 and *Taneja* [2009] AATA 87 as well as the Federal Court (e.g., *IRG Technical Services Pty Ltd & Anor* [2007] FCA 1867 and *Fowler* [2008] FCA 528).

Most of these cases were decided in favour of the Commissioner. This suggests that the taxpayers identified by the Commissioner as being caught by the rules are the same taxpayers the Government intended to be caught.

Prior to the enactment of the APSI rules, the Commissioner needed to rely on Part IVA to challenge the arrangements now caught under Part 2-42. Having relatively clear and delineated provisions to deal with these arrangements has allowed the Commissioner and taxation practitioners/advisers to offer a greater degree of certainty to clients who may or may not be effected by the rules. Ultimately, this has improved the compliance and administration of this somewhat difficult area of the tax law.

2. The APSI rules in Part 2-42 and PSI overall

As stated above, prior to the APSI rules being enacted the Commissioner needed to rely on Part IVA to challenge taxpayers who were obtaining a tax benefit from splitting or alienating PSI. When Part 2-42 was introduced it was clear (and not controversial) that only a particular type of taxpayer was intended to be caught, ie., one who did not pass any of the tests to establish they are a PSB. This by default meant all those taxpayers that were not caught but were deriving PSI remained exposed to challenge under Part IVA.

This potential residual application of Part IVA is made clear in a note to S.86-10, as follows:

" Note: The general anti-avoidance provisions of Part IVA of the Income Tax Assessment Act 1936 may still apply to cases of alienation of personal services income that fall outside this Division."

This point is also made clear in the Explanatory Memorandum to the New Business Tax System (Alienation of Personal Services Income) Bill 2000. Refer to paragraph 1.16 and diagram 1.1.

Despite these references to Part IVA, the whole area of PSI has become a 'problem'. As to the current legal position of when Part IVA will apply to the splitting of PSI, the Commissioner has formed the "Alienation and Part IVA working group". The NTAA is currently represented on this group. The need for the group has arisen out of the fact it is very difficult to determine which arrangements fall foul of part IVA and which do not.

Without attempting to pre-empt the findings of the working group we wish to put forward the following propositions for your consideration as part of the review:

- (a) One of the reasons for the introduction of Part 2-42, as stated in the EM, is that "applying Part IVA has to be on a case by case basis which is labour intensive and an inefficient use of ATO resources" (refer paragraph 1.12). The same can be said for those taxpayers with residual exposure to Part IVA.
- (b) Whilst Part 2-42 is well targeted in its own right, it is perceived that this was somewhat of an attempt by the Government of the day to clean up the 'real problem' with PSI. As such, despite the potential residual application of Part IVA to PSBs, there is arguably a clear gap between the Commissioner's view of what factual scenario would be caught under Part IVA and the view held by the tax practitioner community. Given the number of factors that must be considered in applying Part IVA and its general nature, its application can be seen as subjective. That is, it does not target PSI specifically.
- (c) The NTAA proposes a clear 'carve-out' from the application of Part IVA represented by those taxpayers who are PSBs to whom Part IVA would not or should not apply. Such recognition should preferably be embedded into the tax legislation.
- (d) The concept of PSI which is central to Part 2-42 and to PSBs may need to be reviewed given the ever changing way in which taxpayers work and the contractual arrangements they work under. Whilst it may be a matter of policy, manifest anomalies may arise for taxpayers who, as PSBs, utilise equipment and staff and have a significant client base and perhaps even goodwill yet, because they technically derive PSI they remain exposed to Part IVA. The NTAA is not convinced whether it is right to default to treating all PSBs in a way not dissimilar to part 2-42 as opposed to businesses with similar structures who are not deriving PSI.

Please feel free to contact me (03 9209 9917 or nick.connell@corsem.com.au) should you wish to discuss any aspect of this.

Yours faithfully

Nick Connell
on behalf of the NTAA