SGR 2004/D1 - Superannuation guarantee: who is an employee?

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Draft Superannuation Guarantee Ruling

Superannuation guarantee: who is an employee?

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Preamble

This document is a draft for industry and professional comment. As such, it represents the preliminary, though considered views of the Australian Taxation Office. This draft may not be relied on by taxpayers and practitioners.

What this Ruling is about

1. This Ruling explains when an individual is considered to be an 'employee' under section 12 of the *Superannuation Guarantee (Administration) Act 1992* (SGAA). The expressions 'employee' and 'employer' in the SGAA have both their ordinary meaning and an extended meaning.

2. The Ruling discusses the various indicators the courts have considered in establishing whether a person engaged by another individual or entity is an employee within the common law meaning of the term.

3. The Ruling clarifies the circumstances in which persons are employees under the extended definition and also considers the circumstances in which an individual who may otherwise be an employee is specifically exempted from the scope of the SGAA.[1]

4. It also provides the Australian Taxation Office (ATO) view on the implications of the alienation of personal services income (PSI) measures contained in Part 2-42 of the *Income Tax Assessment Act 1997* (ITAA 1997) for deciding whether an individual is an employee within the meaning of the SGAA. The Ruling further considers whether an individual who holds an Australian Business Number (ABN) can be an employee for the purposes of the SGAA. The ruling also discusses arrangements or relationships which do not give rise to an employer/employee relationship.

5. Unless otherwise stated, all legislative references in this Ruling are to the SGAA.

[1] This explanation does not extend to a discussion of the application of sections 27, 28 and 29 of the SGAA. These sections exclude salary or wages paid to certain employees in certain circumstances for the purposes of calculating the superannuation guarantee charge.

Date of effect

6. It is proposed that when the final Ruling is issued, it will apply from the date of its issue.

Previous Rulings

7. This Ruling replaces SGR 93/1. SGR 93/1 is withdrawn from the date of issue of this Ruling.

Ruling

8. Under subsection 12(1) of the SGAA, if a person is an employee at common law, that person is an employee under the SGAA.[2]

9. Whether a person is an employee of another is a question of fact to be determined having regard to the key indicators expressed in judicial decisions which have considered the issue of whether a person is a common law employee. Defining the contractual relationship is often a process of examining a number of factors and evaluating those factors within the context of the relationship between the parties. No one indicator of itself is determinative of that relationship. The totality of the relationship between the parties must be considered.

10. The classification of a person as an employee for the purposes of the SGAA is not solely dependent upon the existence of a common law employment relationship. While the definition includes most persons who at common law would be regarded as employees, it also extends to certain persons who would not be regarded as employees at common law such as Members of Parliament.

11. Where an individual performs work for another party through an entity such as a company or trust, there is no employer-employee relationship between the individual and other party for the purposes of the SGAA, either at common law or under the extended definition of employee. This is because the company or trust (not the individual) has entered into an agreement rather than the individual. However, the individual may be the employee of the intermediary company or trust, depending on the terms of the arrangement.

12. If a partnership has contracted to provide services, then the person who actually does the work is not the employee of the other party to the contract. This is so even if the worker is a partner and even if the contract requires the partner to do the work. However, if partners contract outside the partnership in their own personal

[2] This principle is subject to the minor exceptions in subsections 12(9A) and (11) of the SGAA.

capacity to provide their labour to fulfil a contractual obligation, they can be an employee of the other party to the contract.

13. A partner in a partnership is not an employee of the partnership.

14. A person who holds an ABN may still be an employee for the purposes of the SGAA.

15. The question of whether or not a person is an employee for SGAA purposes is not determined by reference to whether the person is a full-time, part time or casual worker.

16. The application or otherwise of the PSI measures in Part 2-42 of the ITAA 1997 is not determinative of whether an individual is an employee within the meaning of section 12 of the SGAA.

17. An arrangement between parties that is structured in a way that does not give rise to a payment for services rendered but rather a payment for something entirely different, such as a lease or a bailment does not give rise to an employer/employee relationship for the purposes of the SGAA.

Explanation

18. Under the SGAA, employers are required to make superannuation contributions into a complying superannuation fund or Retirement Savings Account for the benefit of their eligible employees in accordance with minimum prescribed levels. If an employer does not make the required superannuation contributions, they will be subject to the Superannuation Guarantee Charge (SGC). If an individual is not an employee as defined in the SGAA or is an employee but is otherwise exempted from the application of the SGAA by a specific provision, an employer will not have a potential liability for the SGC.

19. The SGAA defines 'employee' in section 12. The definition is both a clarifying and extending provision. Subsection 12(1) defines the term 'employee' as having its ordinary meaning – that is, its meaning under common law. If a worker is held to be an employee at common law, then they will be an employee under the SGAA (unless one of the limited exceptions in subsections 12(9A) and (11) applies).

20. Apart from stating that 'employee' has its ordinary meaning, the SGAA does not list the indicators that may be considered in determining whether a worker is an employee at common law. In most cases, it will be self-evident whether an employer/employee or a principal/independent contractor relationship exists. However, it is sometimes difficult to discern the true character of the relationship from the facts of the case as the intentions of the parties may be unclear or ambiguous, such as where the terms of the contract are disputed by the parties or are otherwise in apparent conflict. Because of these difficulties, the ordinary meaning of employee has been the subject of a significant amount of judicial consideration. These cases

have discussed a number of indicators that may be applied in determining whether an individual is a common law employee.

21. If it is considered that the relationship at common law is one of principal and independent contractor or the determination of the status of the worker is unclear, the extended definition of 'employee' in the SGAA must be considered. The SGAA also has two provisions which exclude certain workers from being employees for SGAA purposes, even if they otherwise would be employees.

Who is an employee within the ordinary meaning of that term?

Background

22. The relationship between an employer and employee is a contractual one. It is often referred to as a *contract of service*. Such a relationship is typically contrasted with the principal/independent contractor relationship that is referred to as a *contract for services*. An independent contractor typically contracts to achieve a result whereas an employee contracts to provide their labour (typically to enable the employer to achieve a result).

23. The Courts have considered the common law contractual relationship between parties in a variety of legislative contexts, including income tax, industrial relations, payroll tax, vicarious liability, workers compensation and superannuation guarantee. As a result, a substantial and well-established body of case law has developed on the issue. There are often many relevant facts and circumstances, some pointing to a contract of service, others pointing to a contract for services.[3] Whatever the facts of each particular case may be, there is no single feature which is determinative of the contractual relationship; the totality of the relationship between the parties must be considered to determine whether, on balance, the worker is an employee or independent contractor.[4]

24. Consideration should be given to the various indicators identified in judicial decisions which have considered the employee/independent contractor distinction bearing in mind that no list of factors is to be regarded as exhaustive and the weight to be given to particular facts will vary according to the circumstances.[5] Where a consideration of the indicia points one way so as to yield a

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

[4] *Stevens v. Brodribb Sawmilling Company Pty Ltd* (1986) 160 CLR 16; (1986) 63 ALR 513 (*Stevens v. Brodribb*) at CLR 29; ALR 521, per Mason J. The principle that the 'totality of the relationship between the parties' be considered to determine the nature of the contractual relationship at common law was adopted with approval by the majority of the High Court in *Hollis v. Vabu* (2001) 207 CLR 21 (*Hollis v. Vabu*).

[5] *Abdalla v. Viewdaze Pty Ltd t/as Malta Travel* [2003] 53 ATR 30 (*Abdalla v. Viewdaze*). The Full Bench of the Industrial Relations Commission provided a summary of the state of the law governing the determination of whether an individual is an employee or independent contractor following *Hollis v. Vabu*.

clear result, the determination should be in accordance with that result.[6]

Key indicators of whether an individual is an employee or independent contractor

25. The features discussed below have been regarded by the Courts as key indicators of whether an individual is an employee or independent contractor at common law.

Terms and the circumstances of the formation of the contract

26. In determining the nature of the contractual relationship, the terms of the contract, whether express or implied, in light of the circumstances surrounding the making of the contract are an important consideration.[7]

27. A clause in a contract that purports to characterise the relationship between the parties as that of principal and independent contractor and not that of employer and employee must be considered with all the other terms of the contract. Such a clause cannot receive effect according to its terms if it contradicts the effect of the agreement as a whole[8] – that is, the parties cannot deem the relationship between themselves to be something that is not.[9] The parties to an agreement cannot alter the true substance of the relationship by simply giving it a different label.[10] As Gray J stated in *Re Porter: re Transport Union of Australia*:[11]

> Although the parties are free, as a matter of law, to choose the nature of the contract which they will make between themselves, their own characterisation of that contract will not be conclusive. A court will always look at all of the terms of the contract, to determine its true essence, and will not be bound by the express choice of the parties as to the label to be attached to it. As Mr Black put it in the present case, the parties cannot create something which has every feature of a rooster, but call it a duck and insist that everybody else recognise it as a duck.

However, the parties may use such a clause to overcome any ambiguity as to the true nature of the relationship.[12]

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[6] Ibid.
[7] See *Stevens v. Brodribb* (1986) 160 CLR 16 at 37, per Wilson and Dawson JJ.
[8] *Australian Mutual Provident Society v. Chaplin and Anor* (1978) 18 ALR 385 at 389.
[9] *Hollis v. Vabu* (2001) 207 CLR 21 at 45.
[10] *Massey v. Crown Life Insurance Co* [1978] 1 WLR 676; [1978] 2 All ER 576.
[11] (1989) 34 IR 179 at 184.
[12] *Australian Mutual Provident Society v. Chaplin and Anor* (1978) 18 ALR 385 at 389-390.

28. For example, an employer may seek to change the status of an employee to that of independent contractor by both parties signing a contract of engagement that includes a clause to the effect that the worker is an independent contractor rather than an employee. That clause is ineffective if it is inconsistent with the apparent true nature of the relationship inferred from the contract as a whole. If the terms of the subsisting relationship are not changed, it is likely that the worker's status would remain that of an employee.

29. The circumstances surrounding the formation of the contract may assist in determining the true character of the contract.[13] Thus, if a contract comes into existence because the contractor advertises their services to the public in the ordinary course of carrying on a business or as a result of a successful tender application, the existence of a principal/independent contractor relationship is more likely. Conversely, if the contract is formed in response to a job vacancy advertisement or through the services of a placement agency, the existence of an employer/employee relationship is more likely.[14]

Control

30. The classic 'test' for determining the nature of the relationship between a person who engages another to perform work and the person so engaged is the degree of control which the former can exercise over the latter.[15] A common law employee is told not only what work is to be done, but how and where it is to be done. With the increasing usage of skilled labour and consequential reduction in supervisory functions, the importance of control lies not so much in its actual exercise, although clearly that is relevant, as in the right of the employer to exercise it.[16] As stated by Dixon J in *Humberstone v. Northern Timber Mills*:[17]

> The question is not whether in practice the work was in fact done subject to a direction and control exercised by an actual supervision or whether an actual supervision was possible but whether ultimate

[13] For example, *Reardon Smith Line Ltd v. Yngvar Hansen-Tangen* (1976) 1WLR 989 at 997 per Lord Wilberforce; and *Codelfa Construction Pty Ltd v. State Rail Authority of New South Wales* (1982) 149 CLR 337 at 347-352; (1982) 41 ALR 367 at 371-375; (1982) 56 ALJR 459 at 461-463 per Mason J.

[14] *Roy Morgan Research Centre Pty Ltd v. Commissioner of State Revenue (Vic)* 96 ATC 4767 at 4772-4773; (1996) 33 ATR 361 at 366-367 per Byrne J. This decision was affirmed by the Court of Appeal (97 ATC 5070; (1997) 37 ATR 528) and an application for special leave to the High Court was refused.

[15] *Stevens v. Brodribb* (1986) 160 CLR 16 at 24, per Mason J and CLR 35, per Wilson and Dawson JJ.

[16] *Stevens v. Brodribb* (1986) 160 CLR 16 at 24, per Mason J and CLR 36, per Wilson and Dawson JJ. In *Stevens v. Brodribb*, the High Court was adjusting the notion of 'control' to modern industrial conditions and, in doing so, continued the developments in *Zuijs v. Wirth Brothers Pty Ltd* (1955) 93 CLR 561 and *Humberstone v. Northern Timber Mills* (1949) 79 CLR 389. The control test as articulated in *Stevens v. Brodribb* was cited and adopted with approval by the majority of the High Court in *Hollis v. Vabu*.

[17] (1949) 79 CLR 389 at 404.

> authority over the man in the performance of his work resided in the employer so that he was subject to the latter's orders and directions.

31. The mere fact that a contract may specify in detail how the contracted services are to be performed does not necessarily imply an employment relationship. In fact, a high degree of direction and control is not uncommon in contracts for services. The payer has a right to specify how the contracted services are to be performed, but such control must be expressed in the terms of the contract; otherwise the contractor is free to exercise their discretion (subject to any terms implied by law). This is because the contractor is working for themselves.

32. Under a contract of service, on the other hand, the employer has an implied right, within the limits imposed by industrial relations laws, to direct and control the work of an employee. This is because the employee is working in the employer's business and the owner of a business has the right (within the confines of applicable law) to manage that business as the owner sees fit.

33. Therefore, while control is important, it is not the sole indicator of whether or not a relationship is one of employment.[18] The approach of the Courts has been to regard it as one of a number of indicia which must be considered in determination of that question.

34. However, even though the modern approach to defining the contractual relationship is to have regard to the totality of the relationship between the parties, control is still the most important factor to be considered. This was recognised by Wilson and Dawson JJ in *Stevens v. Brodribb* ((1986) 160 CLR 16 at 36), where they state:

> In many, if not most cases, it is still appropriate to apply the control test in the first instance because it remains the surest guide to whether a person is contracting independently or serving as an employee.

35. In *Hollis v. Vabu*, the fact that the couriers engaged by Vabu had little control over the manner of performing their work (the corollary being that Vabu had considerable scope for the actual exercise of control over the performance of the couriers activities) was an important factor leading to the conclusion that the bicycle courier in question was a common law employee of Vabu. Gleeson CJ, Gaudron, Gummow, Kirby and Hayne JJ observed that:

> Vabu's whole business consisted of the delivery of documents and parcels by means of couriers. Vabu retained control of the allocation and direction of the various deliveries…Their work was allocated by Vabu's fleet controller. They were to deliver goods in the manner in which Vabu directed. In this way, Vabu's business involved the marshalling and direction of the labour of the couriers, whose efforts comprised the very essence of the public manifestation of Vabu's business. [19]

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[18] For example, *Stevens v. Brodribb* (1986) 160 CLR 16 at 24, per Mason J.
[19] *Hollis v Vabu* (2001) 207 CLR 21 at 44-45.

Does the worker operate on his or her own account or in the business of the payer?

36. In *Hollis v. Vabu*, the majority of the High Court quoted the following statement by Windeyer J in *Marshall v. Whittaker's Building Supply Co*:

> … the distinction between an employee and independent contractor is 'rooted fundamentally in the difference between a person who serves his employer in his, the employer's business, and a person who carries on a trade or business of his own.'[20]

This distinction is also referred to as the integration or organisation test.[21]

37. In *Hollis v. Vabu*, the High Court considered this distinction when determining whether a bicycle courier was a common law employee of Vabu. The majority found that the bicycle courier was an employee and stated:

> Viewed as a practical matter, the bicycle couriers were not running their own business or enterprise, nor did they have independence in the conduct of their operations.[22]

38. While the majority did, in reaching its decision, consider lawful authority to command (that is control) and other relevant aspects of the relationship between the parties, it at the same time was concerned with the fundamental question of whether the worker was operating their own business or was operating within Vabu's business. Therefore, whenever applying the indicators of employment listed in this ruling it is also necessary to keep in mind the distinction between a worker operating on his or her own account and a worker operating in the business of the payer.

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[20] *Hollis v Vabu* (2001) 207 CLR 21 at 39, per Gleeson CJ, Gaudron, Gummow, Kirby and Hayne JJ.

[21] The notion of an 'integration' test arose in *Montreal v. Montreal Locomotive Works* 20 (1947) 1 DLR 161 at 169 and was affirmed by Lord Denning in *Stevenson Jordan and Harrison Ltd v. MacDonald and Evans* [1952] 1 TLR 101 at 111 and reaffirmed in *Bank Voor Handel En Scheepvaart NV v. Slatford* [1953] 1 QB 248 at 295.

[22] *Hollis v. Vabu* at (2001) 207 CLR 21 at 41.

'Results' contracts

39. Where the substance of a contract is to achieve a specified result, there is a strong (but not conclusive) indication that the contract is one for services. In *World Book (Australia) Pty Ltd v. FC of T*[23] Sheller JA said:

> Undertaking the production of a given result has been considered to be a mark, if not the mark, of an independent contractor...[24]

40. The phrase 'the production of a given result' means the performance of a service by one party for another where the first-mentioned party is free to employ their own means (such as third party labour, plant and equipment) to achieve the contractually specified outcome. Satisfactory completion of the specified services is the 'result' for which the parties have bargained. The consideration is often a fixed sum on completion of the particular job as opposed to an amount paid by reference to hours worked. If remuneration is payable when, and only when, the contractual conditions have been fulfilled, the remuneration is for producing a given result.[25]

41. In contracts to produce a result, payment is often made for a negotiated contract price, as opposed to an hourly rate. For example, in *Stevens v. Brodribb*, payment was determined by reference to the volume of timber delivered, and in *Queensland Stations* where it was a fixed sum per head of cattle delivered.

42. While the notion of 'payment for a result' is expected in a contract for services, it is not necessarily inconsistent with a contract of service, for example, in contracts for commission only sales.[26] Accordingly, the other terms of the contract must still be considered to determine the true character of the relationship between the parties.

Whether the work can be delegated or subcontracted

43. The power to delegate (in the sense of the capacity to engage others to do the work) is a factor in deciding whether a worker is an employee or independent contractor.[27] If a person is contractually required to personally perform the work, this is an indication that the person is an employee.

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[23] 92 ATC 4327.

[24] *World Book (Australia) Pty Ltd v. FC of T* 92 ATC 4327 at 4334. Sheller JA referred to the High Court decision in *Queensland Stations Pty Ltd v. FC of T* (1945) 70 CLR 539; (1945) 19 ALJ 253; (1945) 8 ATD 30; (1945) ALR 273 (1945) (*Queensland Stations*) as authority for that proposition. He also used the facts of that case as an example of a contract to produce a result. Note that, given the emphasis that the courts have placed on the control test (discussed above), the production of a given result is probably not *the* mark of an independent contractor but merely *a* mark.

[25] *Neale v. Atlas Products (Vic) Proprietary Limited* (1955) 94 CLR 419 at 424-425.

[26] *Federal Commissioner of Taxation v. Barrett and Ors* 73 ATC 4147; (1973) 4 ATR 122.

[27] See for example, *Australian Mutual Provident Society v. Chaplin and Anor* (1978) 18 ALR 385 at 391 and *Stevens v. Brodribb* at (1986) 160 CLR 16 at 26, per Mason J and at CLR 38, per Wilson and Dawson JJ.

44. If a person is contractually entitled to delegate the work to others, then this is an indication that the person is an independent contractor. Under a contract for services, the emphasis is on the performance of the agreed services (achievement of the 'result'). Unless the contract expressly requires the service provider to personally perform the contracted services, the contractor is free to arrange for his or her employees to perform all or some of the work or may subcontract all or some of the work to another service provider.

45. A common law employee may frequently 'delegate' tasks to other employees, particularly where the employee is performing a supervisory or managerial role. However, this 'delegation' exercised by an employee is fundamentally different to the delegation exercised by a contractor outlined above. When an employee asks a colleague to take an additional shift or responsibility, the employee is not responsible for paying that replacement worker, rather the workers have merely organised a substitution or shared the work load. This is not delegation consistent with that exercised by a contractor.

Risk

46. Where the worker bears little or no risk of the costs arising out of injury or defect in carrying out their work, they are more likely to be an employee.[28] On the other hand, an independent contractor bears the commercial risk and responsibility for any poor workmanship or injury sustained in the performance of work. An independent contractor often carries their own insurance and indemnity policies.

Whether the worker performs work for others

47. A factor suggesting that an individual is an employee is the right of the principal to the exclusive services of the person engaged.[29] On the other hand, if the individual also works for others (or has a genuine and practical entitlement to do so) then this suggests that the worker is an independent contractor.[30]

Provision of tools and equipment and payment of business expenses

48. It has been held that the provision of assets, equipment and tools by an individual and the incurring of expenses and other overheads is an indicator that the individual is an independent contractor.[31]

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[28] In *Hollis v. Vabu*, Vabu undertook the provision of insurance for the couriers and deducted the amounts from their wages.
[29] *Stevens v. Brodribb* at (1986) 160 CLR 16 at 36, per Wilson and Dawson JJ.
[30] *Abdalla v. Viewdaze* [2003] 53 ATR 30, at paragraph 34.
[31] See, for example, *Stevens v. Brodribb* and *Vabu Pty Ltd* v. *FC of T* 96 ATC 4898; (1996) 33 ATR 537 (*Vabu Pty Ltd v. FC of T*).

49. In *Stevens v. Brodribb*, the High Court observed that working on one's own account (as an independent contractor) often involves:

> the provision by him of his own place of work or of his equipment, the creation by him of goodwill or saleable assets in the course of his work, the payment by him from his remuneration of business expenses of any significant proportion…[32]

50. Similarly, in *Queensland Stations* the droving contractor was required to find and pay for all the men, plant, horses and rations necessary and sufficient for the task. Their own means were employed to accomplish a result.[33]

51. However, the provision of necessary tools and equipment is not necessarily inconsistent with an employment relationship. As highlighted in *Hollis v. Vabu*, the provision and maintenance of tools and equipment and payment of business expenses should be significant for the individual to be considered an independent contractor. The majority of the High Court stated that:

> In classifying the bicycle contractors as independent contractors, the Court of Appeal fell into error in making too much of the circumstances that the bicycle couriers owned their own bicycles, bore the expenses of running them and supplied many of their own accessories…A different conclusion might, for example, be appropriate where the investment in capital was more significant, and greater skill and training were required to operate it.[34]

52. Further, an employee, unlike an independent contractor, is often reimbursed (or receives an allowance) for expenses incurred in the course of employment, including for the use of their own assets such as a car.

Other indicators

53. In addition to the above, other indicia of the nature of the contractual relationship have been variously stated and have been added to from time to time.[35] Those suggesting an employer-employee relationship include the right to suspend or dismiss the person engaged,[36] provision of benefits such as annual, sick and long service leave[37] and the provision of other benefits prescribed under an award for employees.

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[32] (1986) 160 CLR 16 at 37, per Wilson and Dawson JJ.
[33] Per Rich J at CLR 548.
[34] (2001) 207 CLR 21 at 41. The High Court was referring to the NSW Court of Appeal taxation decision in *Vabu v. FC of T* where it was held that the couriers engaged by Vabu (including those who provided motor vehicles and motor cycles) were independent contractors. The majority decision in *Hollis v. Vabu* overturned that decision insofar as bicycle couriers were concerned.
[35] *Stevens v. Brodribb* (1986) 160 CLR 16 at 36, per Wilson and Dawson JJ.
[36] Ibid.
[37] *Stevens v. Brodribb* (1986) 160 CLR 16 at 24, per Mason J.

54. The requirement that a worker wear a company uniform is an indicator of an employment relationship existing between the contracting parties. In *Hollis v. Vabu*, the fact that the couriers were presented to the public and to those using the courier service as emanations of Vabu (the couriers were wearing uniforms bearing Vabu's logo) was an important factor supporting the majority's decision that the bicycle couriers were employees.[38]

55. If it is determined that an individual is an employee within the ordinary or common law meaning of the term, they will be an employee for the purposes of the SGAA (unless one of the exceptions in subsections 12(9A) and (11) applies).

The statutorily expanded definition of employee under subsections 12(2) to (11) of the SGAA

56. Although the term 'employee' has its ordinary meaning in the SGAA, subsections 12(2) to 12(11) list a number of further persons who are also treated as employees. These subsections deem persons who come within these subsections to be employees for the purposes of the SGAA, even if they are not common law employees and are clearly distinguishable from common law employees.

Members of executive bodies of bodies corporate

57. Under subsection 12(2) of the SGAA, a person who is entitled to payment for the performance of duties as a member of the executive body (whether described as the board of directors or otherwise) of a body corporate[39] is, in relation to those duties, an employee of the body corporate.

58. In the majority of circumstances, such a person will be called a 'director'. The SGAA will apply even if the person is not referred to as a director but falls within the terms of subsection 12(2).

Contracts for the labour of the person

59. Subsection 12(3) of the SGAA provides that if a person works under a contract that is wholly or principally for the labour of the person, the person is an employee of the other party of the contract. Whenever a contract is formed with an individual to perform work, the first test is always to determine if a contract of service exists and only if the answer to that question is negative, is the 'wholly or principally' for labour issue considered.

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[38] *Hollis v. Vabu* (2001) 207 CLR 21 at 42, per Gleeson CJ, Gaudron, Gummow, Kirby and Hayne JJ.

[39] 'Body corporate' is a general term to describe an artificial entity having a separate legal existence.

60. The words 'wholly or principally' are used to limit or restrict the types of contracts that will be covered by subsection 12(3). To the extent that a contract is partly for labour and partly for something else (for example, the supply of goods, materials or hire of plant or machinery), it will qualify only if it is 'principally' for labour.

61. In the context of subsection 12(3), the word 'principally' assumes its commonly understood meaning, that is, 'chiefly' or 'mainly'.

62. 'Labour' includes mental and artistic effort as well as physical toil.[40]

63. Subsection 12(3) was enacted to extend the scope of the SGAA beyond traditional employment relationships to take into account some independent contractors who principally provide their own labour to meet obligations under a contract. However, the operation of subsection 12(3) has been restricted by the interpretation which the courts placed on the equivalent expression in paragraph (a) of the definition of 'salary or wages' in subsection 221A(1) of the *Income Tax Assessment Act 1936* (ITAA 1936) ('paragraph (a)').[41]

64. Both subsection 12(3) of the SGAA and paragraph (a) contain the identical phrase '…under a contract that is wholly or principally for the labour of the person…'.

65. In the High Court decision in *Neale*, it was decided that, for a payment to fall within paragraph (a) of the 'salary or wages' definition, it was necessary that the contract require the person to whom the payment was made to perform the work personally and that if the contract left it open for the person to engage someone else to perform it, it was not a payment to which paragraph (a) applied. Rather, it was a contract to produce a given result.

66. An amendment inserting paragraph 221A(2)(b) into the ITAA 1936 was made in 1983 to correct the perceived deficiency in paragraph (a) identified in Neale.[42] However, in *World Book*, the NSW Court of Appeal found that paragraph 221A(2)(b) did not entirely succeed in altering the law. World Book is not directly relevant to section 12 of the SGAA in any event because section 12 has no equivalent of paragraph 221A(2)(b). However, in discussing the interpretation of the crucial expression 'wholly or principally for the labour of the person', Sheller JA said:

> In my opinion by retaining the description of contract wholly or principally for the labour of a person the legislature has maintained a distinction between a contract for labour and a contract, to use the

[40] *Deputy Commissioner of Taxation v. Bolwell* (1967) 1 ATR 862 at 873.
[41] *Neale v. Atlas Products (Vic) Pty Ltd* (1955) 94 CLR 419 (*Neale*); *Case V158* 88 ATC 1030; *World Book (Australia) Pty Ltd v. FC of T* 92 ATC 4327 (*World Book*) and *Filsell v. Top Notch Fashions Pty Ltd* 94 ATC 4656.
[42] Paragraph 221A(2)(b) was intended to apply where the person who was paid actually performed, or could reasonably be expected to perform, the whole or principal part of the labour under the contract. That is, a right of delegation that was not, or was not reasonably expected to be, acted upon other than in minor respects would be insufficient to take the contract outside the scope of the expression.

> expression of the High Court in *Neale* at ATD 461; CLR 425 'whereby the contractor has undertaken to produce a given result and [the amount to be paid] becomes payable when, and only when, the contractual conditions have been fulfilled'.
>
> …But a contract which is undertaken by the contractor to produce a given result is not, in my opinion, a contract wholly or principally for the labour of the person for reason that the labour is undertaken not for the principal but for the contracting party himself to produce the result he has contracted to produce. [43]

67. It is clear from *Neale and World Book* that a person who has 'a right to delegate work' does not work under a contract wholly or principally for his or her labour and that a contract for labour must be distinguished from 'a contract to produce a given result.'

68. As subsection 12(3) of the SGAA uses the expression 'wholly or principally for labour', the Tax Office considers that the meaning given to the phrase by the authorities cited in the context of paragraph (a) of the definition of 'salary or wages' in subsection 221A(1) of the ITAA 1936 applies to the application of subsection 12(3).

69. Despite the restriction that has been placed on the meaning of the phrase 'wholly or principally for the labour of the person', the *obiter dicta* in the judgments in *Neale and World Book* left open the possibility of the application of paragraph (a) (and by extension subsection 12(3) of the SGAA) to independent contractors.

70. In *Neale*, the High Court made the following comment:

> It may be, however, that in cases where an independent contractor is required by the terms of his contract to perform the contractual work himself the addition to the general definition may have some application, but it is unnecessary, in the circumstances of this case, to express any concluded view concerning contracts of such a special class.'[44]

71. In *World Book*, Sheller JA in the NSW Court of Appeal concluded:

> It may be that there are contracts for services which are wholly or principally for the labour of a person and which are not undertaken by the contractor to produce a given result. To the rewards of such contracts the definition may apply.[45]

72. Where a particular individual engaged under a contract is an independent contractor at common law and the terms of the contract in light of the subsequent conduct of the parties indicates that:

- the contractor is remunerated (either wholly or principally) for their personal labour and skills;
- the contractor must perform the contractual work personally (there is no right of delegation); and

[43] *World Book* 92 ATC 4327 at 4334.
[44] (1955) 94 CLR 419 at 425.
[45] 92 ATC 4327 at 4334; (1992) 23 ATR 412 at 419-420.

- the contractor is paid by reference to hours worked, rather than for the amount or quality of work performed (payment is not for a result),

the contract is considered to be wholly or principally for the labour of the contractor and he or she will be an employee under subsection 12(3).

73. Further, certain labour hire arrangements as described below whereby labour hire firms supply or provide the services and labour of workers to client organisations are considered by the Tax Office to come within the scope of subsection 12(3).

74. Where a contract of service does not exist (that is, the worker engaged is an independent contractor), the contract between the labour hire firm and the worker is characterised as one wholly or principally for labour. It is considered that the contract between the labour hire firm and worker is not properly characterised as a contract for a result. In a labour hire arrangement, the contract in substance requires the worker to provide some services for the benefit of a third party. The worker does not undertake to produce a given result; rather, the worker undertakes to perform some work for a client of the labour hire firm.[46] The worker is thus an employee under subsection 12(3) of the SGAA. The nature of labour hire arrangements are discussed in greater detail in Superannuation Guarantee Ruling SGR 93/2.[47]

75. The AAT decision in *Brinkley v. FC of T*[48] also provides an example of the application of subsection 12(3) of the SGAA. The AAT, sitting as the Small Taxation Claims Tribunal, had to determine whether an employment relationship existed between a boat owner and fishing boat skipper for the purposes of the SGAA. It held that the fishing boat skipper was an employee at common law (because the boat owner had the capacity to control the skipper and the others who worked on the boat) and therefore an employee under subsection 12(1). If there was any doubt as to whether an employment relationship existed at common law, the AAT considered that subsection 12(3) put the matter beyond doubt by expressly including contracts for labour (although the AAT did not expressly refer to the principles established by *Neale and World Book*). As stated by Member McCabe:

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[46] The view that the contracts in labour hire arrangements are not 'results' contracts is supported by cases including *Construction Industry Training Board v. Labour Force Ltd* [1970] 3 All ER 220; *Building Workers' Industrial Union of Australia and Others v. Odco Pty Ltd* (1991) 29 FCR 104 and *Drake Personnel Ltd & Ors v. Commissioner of State Revenue* (2000) ATC 4500. In these cases, the workers supplied by the labour hire firm to the end users of labour were paid an agreed rate per hour for the hours worked and there was no evidence, either express or implied, which suggested that the workers could delegate their contractual work.

[47] SGR 93/2 – Independent agencies: service firms, labour hire firms and employment agencies.

[48] 2002 ATC 2053.

> the nature of the relationship…here was in substance a contract for the supply of labour. Mr Brinkley [boat owner] was not acquiring a package of services and /or goods. He was simply contracting Taggart to work for him as a skipper.[49]

Members of Commonwealth and State Parliament, members of ACT Legislative Assembly and members of NT Legislative Assembly

76. Members of the Commonwealth House of Representatives and of the Senate, members of State Legislative Assemblies and Legislative Councils, members of the Northern Territory and Australian Capital Territory Legislative Assemblies are not common law employees because they have no identifiable employer.[50] None of the usual indicators of an employer/employee relationship, such as an express or implied contract of employment, ability to direct activities or exercise control over the employee, apply to members.

77. However, the members in question are specifically incorporated into the definition of employee in the SGAA by virtue of subsections 12(4) to 12(7).

Artists, musicians, sports persons etc

78. Subsection 12(8) of the SGAA defines 'employee' to include:

> (a) a person who is paid to perform or present, or to participate in the performance or presentation of, any music, play, dance, entertainment, sport, display or promotional activity or any similar activity involving the exercise of intellectual, artistic, musical, physical or other personal skills is an employee of the person liable to make the payment.

79. One clear limitation on these words is that the active participation of the artist or sportsperson is required. If not, it could not be said that the person is 'paid to perform or present' the activity. A painter, for instance, does not perform or present a painting exhibition. They merely produce the works used in the exhibition. Therefore, even though the products of their work can form part of, for example, a display, people such as painters and photographers do not usually come within the scope of paragraph 12(8)(a).

80. That the word 'similar' is used also shows clearly that 'activity' is limited to things of a like kind. We consider that the activities covered by paragraph 12(8)(a) are those which derive their artistic or sporting content from the performance or presentation because that is the common thread running through the listed activities.

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[49] *Brinkley v. FCT* 2002 ATC 2053 at 2057.

[50] See, for example, *State Chamber of Commerce and Industry & Ors v. The Commonwealth of Australia* (1987) 163 CLR 329. See also Taxation Ruling TR 1999/10 Income Tax and fringe benefits tax: Members of Parliament – allowances, reimbursements, donations and gifts, benefits, deductions and recoupments, at paragraph 36.

Paragraphs 12(8)(b) and 12(8)(c)

81. The requirement of paragraph 12(8)(a) that the employees it covers must be active participants will, in some cases, be of little significance because the persons defined to be employees are extended further in paragraphs 12(8)(b) and 12(8)(c). These provide:

> (b) a person who is paid to provide services in connection with an activity referred to in paragraph (a) is an employee of the person liable to make the payment; and
>
> (c) a person who is paid to perform services in, or in connection with, the making of any film, tape or disc or of any television or radio broadcast is an employee of the person liable to make the payment.

82. These paragraphs are not limited in the way that subsection 12(3) is limited to contracts wholly or principally for a person's labour. However, it is necessary that the particular person is actually paid to provide services rather than for some other purpose. For example, a person engaged to write a script is performing services but one who sells existing scripts is not – they are merely selling property.

83. Paragraphs 12(8)(b) and 12(8)(c) of the SGAA do not require the person to actively participate in a performance, presentation, broadcast or other activity described within paragraph 12(8)(a) to be defined as an employee; rather the paragraphs specify that the person will be an employee if they provide a service in connection with the activity. For example, a technician engaged to control the sound quality for a concert is not an active participant in any performance. Even though the technician is not within paragraph 12(8)(a), they are still an employee because they are paid for services in connection with a musical performance.

A person who holds, or performs the duties of, an appointment, office or position under the Constitution or under a law of the Commonwealth, of a State or of a Territory

84. A person who holds, or performs the duties of, an appointment, office or position under the Constitution or under a law of the Commonwealth, of a State or of a Territory is an employee by virtue of paragraph 12(9)(a) of the SGAA. Similarly, a person who is otherwise in the service of the Commonwealth, the State or of a Territory, including service as a member of the Defence Force or as a member of the police force is an employee of the Commonwealth, State or the Territory, as the case requires: paragraph 12(9)(b).

85. The wording in subsection 12(9) of the SGAA is very similar to the wording contained in paragraphs 12-45(1)(b), (c), and (d) of Schedule 1 to the *Taxation Administration Act 1953* (TAA 1953). Taxation Ruling TR 2002/21[51] provides comprehensive guidance on the interpretation of the wording contained in those paragraphs. A similar interpretation applies for the purposes of interpreting subsection 12(9) of the SGAA.

Local government councillors and members of an eligible local governing body

86. Under section 12 as originally enacted, a person who held an office as a member of a local government council was regarded as an employee of the council and the payments they received (allowances and sitting or member fees) were regarded as 'salary or wages' for SGAA purposes. However, amendments were made to the SGAA by *Taxation Laws Amendment Act (No 2) 1995* to exclude local government councillors and the payments they receive in the course of their duties from the definition of 'employee' and 'salary or wages' contained in the SGAA. Accordingly, subject to subsection 12(10) of the SGAA, a person who holds office as a member of a local government council is not an employee of the council.

87. Under subsection 12(10), a person who is a member of an 'eligible local governing body' (as that term is defined in section 221A of the ITAA 1936) is an employee for the purposes of the SGAA. An eligible local governing body is a local governing body that made a resolution which, in effect, brought the remuneration of its members into the old PAYE system. The effect of subsection 12(10) is to also bring those members into the Superannuation Guarantee system.

Work of a domestic or private nature

88. Subsection 12(11) of the SGAA provides that a person who is paid to do work wholly or principally of a domestic or private nature for not more than 30 hours per week is not an employee in relation to that work. A person who is paid to do work of this nature for more than 30 hours per week may or may not be an employee depending on whether they fall within the other provisions of section 12, as discussed above.

89. The terms 'private' and 'domestic' are not defined in the SGAA so it is necessary to refer to the ordinary meaning of the words.

90. The *Macquarie Dictionary* (third edition) defines 'domestic' to mean 'of or relating to the home, the household or household affairs' and 'private' to mean 'belonging to oneself', 'being one's own', 'individual or personal'.

[51] Taxation Ruling TR 2002/21, Income Tax: Pay As You Go (PAYG) Withholding from salary, wages, commissions, bonuses, or allowances paid to office holders.

91. In (1955) 5 CTBR (NS) *Case* 50, the Board of Review defined 'private or domestic' expenditure (under subsection 51(1) of the ITAA 1936) as:

> ... losses or outgoings of a private nature we take to mean here losses or outgoings relating solely to the person incurring them ... e.g., travelling expenses incurred by a person to and from his place of employment.... Losses or outgoings of a domestic nature we take to mean here losses or outgoings which relate solely to the house, home or family organisation, of the person incurring them....

92. Although this case was about losses or outgoings of a private nature we think it also illustrates the similar concept of work of a domestic or private nature. In our view, work of a domestic or private nature ordinarily means work relating personally to the individual making payment for the work or to the person's home, household affairs or family organisation.

93. For example, people employed by someone to clean their home, to mind their children, to effect repairs or maintenance of their home, or to tend their home garden would be engaged in domestic or private work. If they worked for that person for not more than 30 hours a week, they would not be that person's employee under the SGAA.

Partnerships

94. At common law, a partnership (except an incorporated limited partnership),[52] is not a legal entity separate and distinct from its members.[53] However, subsection 72(1) of the SGAA deems a partnership to be a separate legal entity for the purposes of that Act. Despite the separate legal status conferred on a partnership under the SGAA, a partner cannot be an employee of the partnership and a partner at the same time.[54]

95. Furthermore, an agreement that a partner may draw a 'salary' against the partnership does not create an employer/employee relationship but rather operates as an agreement to vary the sharing of partnership profits between the parties.[55]

96. An individual other than a partner engaged by the partnership to perform work for the partnership may be an employee of the partnership, depending on the circumstances of the contractual arrangement.

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[52] Incorporated limited partnerships are a body corporate with a separate legal personality from the partners, for example, see section 84 of the *Partnerships Act 1958* (Vic).
[53] *Rose v. Federal Commissioner of Taxation* (1951) 84 CLR 118.
[54] *Stubbs v. Lakos* (1994) 56 IR 110.
[55] *Ellis v. Joseph Ellis & Co* [1905] 1 KB 324.

Personal services income measures

97. Part 2-42 of the ITAA 1997 contains the alienation measures that set out the income tax treatment of the ordinary or statutory income of an individual or personal services entity that is an individual's personal services income. Income will constitute personal services income if the income is mainly a reward for an individual's personal efforts or skills.[56] The purpose of the measures is to prevent individuals from reducing their tax by alienating their personal services income through the use of an interposed company, partnership, trust or individual, or by claiming a greater range of deductions than those individuals who provided personal services as employees.[57]

98. The alienation measures will not apply where the income is derived in the course of conducting a personal services business.[58] The object of Division 87 of the ITAA 1997 is to define personal services businesses to ensure the alienation measures do not apply to legitimate independent contractors. A number of tests are set out for determining if the income is from the conduct of a personal services business.

99. It is recognised that there is some overlap between the tests used to determine whether a personal services business exists, particularly between the 'results test'[59] and the common law tests used to distinguish independent contractors and employees. However, section 84-10 of the ITAA 1997 ensures that the application of the alienation measures to an individual does not make the individual an employee for the purposes of the SGAA.[60] Whether or not an individual is subject to the PSI measures is distinct from and separate to the determination of whether that individual is an employee within the meaning of section 12 of the SGAA.

Neither employee nor independent contractor – lease or bailment

100. There are circumstances in which the relationship between a person who engages another to perform work and the person engaged does not give rise to a payment for services rendered or provision of labour but rather a payment for something entirely different, such as a lease or 'bailment'. In these circumstances, a person enters into a lease or bailment for the use of property owned

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[56] Section 84-5 of the ITAA 1997.
[57] A number of taxation rulings discuss the personal services income measures. They include TR 2001/7 – Income Tax: the meaning of personal services income; TR 2001/8 – Income Tax: what is a personal services business; TR 2003/6 – Income Tax: Attribution of personal services income; TR 2003/10 – Income Tax: deductions that relate to personal services income.
[58] Division 87 of the ITAA 1997.
[59] Which is set out in section 87-18 of the ITAA 1997.
[60] Section 84-10 of the ITAA 1997 states that the application of Part 2-42 to an individual does not imply, for the purposes of any Australian law or any instrument made under an Australian law, that the individual is an employee.

by another person, and the payments are made from the lessee or bailee to the lessor or bailor. Consequently, the lessee or bailee, rather than being a provider of services to the owner of the asset, acquires a right to exploit that asset for their own benefit in return for a 'rental' payment to the owner.

101. A common form of bailment relationship is that of owner and taxi driver. In the taxi industry, some taxi drivers who operate under a bailment arrangement make a payment to the owner allowing them to use the taxi to drive. These payments may take the form of lease payments or a percentage of shift takings. In *FC of T v. De Luxe Red and Yellow Cabs Co-operative (Trading) Society Ltd & Ors*,[61] the Full Federal Court held that a taxi licence owner and taxi drivers were not in a relationship of employer and employee within the meaning of those terms in section 12 of the SGAA. The relationship was rather one of 'bailment', even though the licence owner had a degree of control over the drivers' work.

The interaction of ABN with the SGAA

102. Section 8 of the *Australian Business Number Act 1999* (ABNA) provides in part that an entity is entitled to an ABN if they carry on an enterprise in Australia. Section 38 of the ABNA provides in part that an enterprise includes activities done in the form of a business but does not include activities done by a person as an employee.[62]

103. The fact that an individual has an ABN does not prevent that individual from also being engaged as an employee in another role or position. Someone who carries on a business or trade in their own right other than as an employee might also at certain times perform work for another as an employee. For instance, a mechanic may have an ABN because the activities he undertakes as a mechanic in sole practice amount to an enterprise. He may also be an employee because he is employed on weekends by the local hotel as a barman. Ultimately, in the common law context, each individual contract entered into by an individual must be examined to determine whether, on balance, the individual is engaged as an employee or independent contractor.

104. Moreover, an individual with an ABN may undertake a contractual engagement as an independent contractor and still be an employee for SGAA purposes. This is because, as discussed, the scope of the SGAA is extended beyond common law employees.[63] For example, a sole trader who has an ABN may be an employee under subsection 12(3) of the SGAA if they have been contracted wholly or principally for their labour.

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[61] 98 ATC 4466; (1998) 82 FCR 507.
[62] This is subject to certain exceptions stated in paragraph 38(2)(a) of the ABNA.
[63] Employee is not otherwise defined in the ABNA so it takes its common law meaning.

Your comments

105. We invite you to comment on this draft Superannuation Guarantee Ruling. Please forward your comments to the contact officer by the due date.

Due date: **8 October 2004**

Contact officer: **Peter Bou-Samra**

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Detailed contents list

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25 August 2004

Previous draft:

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Related Rulings/Determinations:

TR 92/20; TR 1999/10;
TR 2000/14; TR 2001/7;
TR 2001/8; TR 2002/21;
TR 2003/6; TR 2003/10;
SGR 93/2

Previous Rulings/Determinations:

SGR 93/1

Subject references:

- ABN
- alienation of personal services income
- bailment
- contractors
- employer v. independent contractor
- partnerships
- PAYG
- remuneration to councillors of an eligible local governing body

Legislative references:

- SGAA 1992 12
- SGAA 1992 12(1)
- SGAA 1992 12(2)
- SGAA 1992 12(3)
- SGAA 1992 12(3)(a)
- SGAA 1992 12(4)
- SGAA 1992 12(5)
- SGAA 1992 12(6)
- SGAA 1992 12(7)
- SGAA 1992 12(8)
- SGAA 1992 12(8)(a)
- SGAA 1992 12(8)(b)
- SGAA 1992 12(8)(c)
- SGAA 1992 12(9)
- SGAA 1992 12(9A)
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- SGAA 1992 12(11)
- SGAA 1992 72(1)
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