TR 2012/D4 - Income tax: the identification of 'employer' for the purposes of the short-term visit exception under the Income from Employment Article, or its equivalent, of Australia's tax treaties

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Draft Taxation Ruling

Income tax: the identification of 'employer' for the purposes of the short-term visit exception under the Income from Employment Article, or its equivalent, of Australia's tax treaties

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What this Ruling is about

1. This draft Ruling explains:

- the meaning of the term 'employer' in the general exclusion provision provided under the Income from Employment Article, or its equivalent,[1] of Australia's tax treaties ('short-term visit exception'); and
- the approach to be taken in determining who the employer is for the purposes of the short-term visit exception.

2. This draft Ruling applies to entities that engage non-resident individuals to render services in Australia and to those non-resident individuals.

[1] The heading of equivalent Articles in other tax treaties vary. Consistent with the heading of Article 15 of the OECD Model until it changed in 2000, many such Articles are headed 'Dependent Personal Services', for example, Article 14 of the Canadian convention. Others may have no heading at all, for example, Article 14 of the German agreement and Article 12 of the Singapore agreement.

3. This draft Ruling does not deal with income from employment dealt with by other Articles in Australia's tax treaties. This may include any of those articles in one of Australia's tax treaties dealing with directors' fees, pensions, government service[2] and entertainers and sportspersons.[3]

Previous Ruling

4. This draft Ruling replaces Taxation Ruling TR 2003/11 *Income tax: the interpretation of the general exclusion provision of the Dependent Personal Services Article, or its equivalent, of Australia's Double Tax Agreements*. To the extent that the Australian Taxation Office (ATO) views in that Ruling still apply, they have been incorporated into this draft Ruling.

Ruling

The meaning of the term 'employer'

5. The term 'employer' for the purposes of the short-term visit exception in provisions of Australia's tax treaties equivalent to Article 15(2) of the OECD Model Tax Convention on Income and on Capital ('the OECD Model') is undefined. Unless a particular tax treaty requires the term to have a different meaning, the term takes its meaning from Australian domestic law and the context, object and purpose of the short-term visit exception.

6. The employer for the purposes of the short-term visit exception is the enterprise to which a non-resident individual renders his or her services in what would be considered an employment relationship.

Determining the employer

7. In determining who the employer is for the purposes of the short term visit exception, the Commissioner will in each case have regard to:

- the principles and factors at paragraphs 12 to 17 arising from Australian domestic law; and
- the context, object and purpose of the short-term visit exception, especially subparagraphs b) and c).[4]

[2] Paragraph 1 of the Income from Employment Articles in Australia's tax treaties provides that this Article is subject to the operation of Articles in a treaty dealing with these aspects.
[3] Paragraph 1of the Entertainers and Sportspersons Article in Australia's tax treaties contains an express exception to the short term visit exception.
[4] In relation to the object and purpose of these subparagraphs, see below at paragraph 62.

8. Application of the underlying principles and factors at paragraphs 12 to 17 is, of itself and in most instances, unlikely to result in the short-term visit exception being applied so as not to be in accordance with its object and purpose.

The existence of a contract

9. The relationship between an employer and employee is a contractual one often referred to as a contract of service. Whether such a contractual relationship exists is a question of law and depends on the proper characterisation of the arrangements made between the various parties.

10. In ascertaining the proper characterisation, the totality of the relationship between the parties must be considered.

Nature of contractual relationship

11. In characterising the relationship between the parties, it is not only the express terms of the contract but also the substance or reality of the contractual relations (in other words, the actual behaviour of the parties) which is relevant. This is often referred to as the 'substance over form' approach. This 'substance over form' approach applies in all cases to determine whether the relationship is properly one of employment and who the employer is.

12. This substance over form approach can lead to a conclusion that the employer under the formal contract of employment should not be regarded as the employer of the individual for the purposes of the short-term visit exception. This may occur, for example, if:

- the conduct of the parties is not consistent with the terms of the written contract of employment or another contract with a third party including instances where such terms are ambiguous; or
- under the contractual terms, the true nature of the relationship(s) between the parties are misrepresented or disguised.

Key indicators of employment relationship

13. Under Australian common law, the factors listed below are considered in determining whether an employment relationship exists in respect of particular arrangements. As stated in paragraph 7, the Commissioner will consider these factors in determining who should be the employer for the purposes of the short-term visit exception:

- Who exercises ultimate control over the employee – the right to control in terms of the ability to withdraw a worker from an assignment and/or terminate the relationship with the worker;

- Who exercises day-to-day control over the worker – that is, the degree of actual control exercised in terms of, for example, how, when and what is to be done;
- Integration – the nature of the services rendered by the worker and whether they are an integral part of the business activities carried on by the enterprise to which the services are provided;
- The terms of engagement – for example, entitlements to leave and who has obligations to deduct PAYG tax, pay superannuation contributions and workers' compensation insurance;
- Who is responsible for payment of remuneration for the worker's services;
- Who bears the responsibility or risk for the results produced by the worker;
- Whether or not the contract is for the achievement of a specified result;
- Who provides or maintains the necessary equipment and resources to perform the work; and
- Whether or not the work can be delegated by the worker.

14. The relevance of and weighting given to a particular factor may vary according to the circumstances. No one factor is determinative.

Disagreements and application of the exception

15. In accordance with paragraph 8.12 of the Commentary on Article 15 of the OECD Model, where a disagreement between States arises as to whether an employment relationship exists, the Australian competent authority will endeavour to resolve it by having regard to the relevant principles and examples in paragraphs 8.13 to 8.27 of the Commentary.

16. The availability of the short-term visit exception may be denied in abusive cases, as contemplated by paragraphs 8.9 and 8.10 of the Commentary on Article 15 of the OECD Model.

Examples

17. In the examples below, the non-resident individual is in an employment relationship. As a result, the Income from Employment Article in Australia's tax treaties deals with the remuneration derived by the non-resident individual. These examples seek only to illustrate in particular instances analysis of the factors to be taken into account in determining the identity of the employer of the non-resident individual for the purposes of the short-term visit exception.

18. The facts contained in these examples are based on the examples in paragraphs 8.16 to 8.27 of the Commentary on Article 15 of the OECD Model. In each of the examples, Australia and State H have entered into a tax treaty that contains an Income from Employment Article that is on the same terms as that in the Finnish Agreement, the terms of which are set out at paragraphs 52 and 54.

Example 1 – Accounting services to client enterprise – Employer is non-resident services company.

19. *Accounting Co, a company which is a resident of State H, contracts with Mano Co, an Australian resident company that is a manufacturer in Australia, to provide accounting services. Accounting Co specialises in providing accounting services and Mano Co wishes to use those services. Peter, a resident of State H who works for Accounting Co, is assigned by Accounting Co to work for Mano Co pursuant to the contract between Accounting Co and Mano Co.*

20. *Accounting Co is responsible for Peter performing the work to an acceptable standard and within the terms required under the contract between Accounting Co and Mano Co. Accounting Co bears the responsibility or risk for Peter's work.*

21. *Peter performs work at Mano Co's premises under the day-to-day direction of Mano Co.*

22. *Peter's contract with Accounting Co specifies the nature of the services to be provided, the period the services are to be provided, rate of pay and other benefits to be paid whilst in Australia.*

23. *Accounting Co pays Peter weekly and charges a fee for the services to Mano Co. The fee includes employment costs for Peter plus a percentage mark up to cover profits, overheads and other administration costs of Accounting Co.*

24. *The ultimate authority over Peter in the performance of his work rests with Accounting Co even though day to day control is with Mano Co.*

25. *The accounting services Peter provides to Mano Co are integral to the business activities of Accounting Co.*

26. *Peter is employed by Accounting Co and provides the accounting services to Mano Co on behalf of Accounting Co.*

27. *Accounting Co is the employer of Peter for purposes of the short-term visit exception in the Income from Employment Article of the tax treaty between State H and Australia.*

28. *Thus, as the remuneration is paid by Accounting Co who is the non-resident employer of Peter, the second condition in the short-term visit exception is satisfied. However, the short-term visit exception will only apply if all the conditions for its operation are satisfied.*

Example 2 – Labour hire arrangement – Employer is Australian enterprise, not non – resident labour hire company.

29. *Construct Co is an Australian resident company which provides construction services. Kevin is a non-resident engineer resident of State H who has provided services under an employment contract with Construct Co for the past three months.*

30. *Hire Co is a company which is a resident of State H and carries on business providing highly specialised personnel to clients to meet their temporary needs.*

31. *Construct Co arranges with Hire Co to enter into an agreement with Kevin for the provision of engineering services to Construct Co for the next four months. The terms of the agreement between Hire Co and Kevin are, in all material respects, the same as or similar to the previous employment contract between Kevin and Construct Co. Hire Co pays Kevin on the basis of time sheets provided to both Hire Co and Construct Co.*

32. *Under a separate contract between Construct Co and Hire Co, Construct Co will pay Hire Co the amount of Kevin's remuneration, social contributions, travel expenses and other employment benefits and charges plus a percentage for Hire Co's services. Under the contract, Construct Co has the right to determine whether, where and when Kevin will work. Construct Co provides Kevin with the necessary tools and equipment to complete these tasks. Hire Co is not responsible and incurs no financial penalties if Kevin does not attend work or fails to perform work to an acceptable standard.*

33. *Construct Co does not only exercise the day-to-day or practical control over Kevin but also has the ultimate or legal control over Kevin. Kevin provides engineering services while Hire Co is in the business of filling short-term business needs. The services rendered by Kevin are an integral part of the business activities of Construct Co and Construct Co bears the responsibility or risk for the results produced by Kevin.*

34. *In substance and reality, the relationship between Kevin and Construct Co has not been altered by the interposition of Hire Co.*

35. *Accordingly, Construct Co is the employer for the purposes of the short-term visit exception in the Income from Employment Article of the tax treaty between State H and Australia. Thus, as Kevin's employer is not 'a resident of the other State', the short-term visit exception does not apply.*

Example 3 – Arrangement between two similar enterprises – Employer is Australian user enterprise.

36. *Big Tech Co is a company resident of State H specialising in providing engineering services. Big Tech Co employs several engineers on a full time basis.*

37. *Small Tech Co is a smaller engineering company that is an Australian resident. It needs the temporary services of an engineer to complete a contract on a construction site in Australia.*

38. *Big Tech Co agrees with Small Tech Co that Mary, one of Big Tech Co's engineers who is a resident of State H, will work in Australia for 2 months on Small Tech Co's contract.*

39. *Big Tech Co continues to pay Mary during this period including an amount for travel expenses. Small Tech Co reimburses Big Tech Co in respect of Mary's salary and travel expenses plus a 5% commission.*

40. *Mary will be working as part of a team under the direct supervision and control of one of Small Tech Co's senior engineers. Small Tech Co controls her day to day work but also has the authority to sanction Mary if her work performance is inadequate. Small Tech Co also agrees to be liable for any claims related to Mary's work performed in Australia.*

41. *The work performed by Mary on the construction site in Australia is performed on behalf of Small Tech Co, rather than Big Tech Co.*

42. *Small Tech Co exercises not only practical day to day control over Mary but also has ultimate authority over Mary's performance. In addition, Mary's work is integral to the business activities of Small Tech. The responsibility and risk in relation to her work is with Small Tech Co.*

43. *These are factors that support a conclusion that, from Australia's perspective, Small Tech Co is Mary's employer for the purposes of the short-term visit exception in the Income from Employment Article in the tax treaty between State H and Australia.*

44. *Accordingly, Small Tech Co is the employer for the purposes of the short-term exception in the Income from Employment Article of the tax treaty between State H and Australia. Thus, as Mary's employer is not 'a resident of the other State', the short-term visit exception does not apply with respect to the remuneration for the services Mary will render in Australia.*

Example 4 – Intra-group centralised corporate services – Employer is non-resident services company.

45. *Foreign Co, a company that is a resident of State H, and Aust Co, an Australian resident company, are part of the same multinational group of companies. A large part of the activities of that group are structured along function lines, which requires employees of different companies of the group to work together under the supervision of managers who are located in different States and employed by other companies of the group.*

46. *Caitlin is a resident of State H. She is employed by Foreign Co and is a senior manager in charge of supervising human resources functions within the multinational group. Since Caitlin is formally employed by Foreign Co, Foreign Co acts as a cost centre for the human resource costs of the group; periodically, these costs are charged out to each of the companies of the group on the basis of a formula that takes account of various factors such as the number of employees of each company. Caitlin is required to travel frequently to other States where other companies of the group have their offices. During the last year, Caitlin spent 3 months in Australia dealing with human resources issues at Aust Co. Whilst she is in Australia, Caitlin continues to report to and receive instructions from her Director at Foreign Co.*

47. *The work performed by Caitlin is part of the activities that Foreign Co performs for its multinational group. Although Caitlin's day to day work whilst she was in Australia may be determined by the Australian entity, Foreign Co has the ultimate authority in regard to her work and performance. In addition, the work that Caitlin performs is an integral part of the business of Foreign Co. in managing the resource functions of the group. The responsibility and risk for Caitlin's work and performance whilst she is in Australia remains with Foreign Co.*

48. *The services that Caitlin renders to Aust Co are rendered on behalf of Foreign Co under the contractual arrangements for services concluded between the enterprises of the multinational group of companies, not under a contract of service between Caitlin and Aust Co.*

49. *Accordingly, the short-term visit exception applies to the remuneration derived by Caitlin for her work in Australia provided that the other conditions for that exception are satisfied.*

Date of effect

50. When the final Ruling is issued, it is proposed to apply both before and after its date of issue. However, the Ruling will not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Ruling (see paragraphs 75 to 77 of Taxation Ruling TR 2006/10).

Commissioner of Taxation
23 May 2012

Appendix 1 – Explanation

This Appendix is provided as information to help you understand how the Commissioner's preliminary view has been reached. It does not form part of the proposed binding public ruling.

Background

51. Australia's tax treaties contain an article that allocates source and residence country taxing rights in respect of income derived from employment. The relevant article is on the same terms as or based on Article 15 of the OECD Model.

52. Paragraph (1) of Article 14 of the Finnish agreement[5] (and its equivalents in Australia's other tax treaties) states:

> Subject to the provisions of Articles 15, 17, and 18,[6] salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of an employment shall be taxable only in that State unless the employment is exercised in the other Contracting State. If the employment is so exercised, such remuneration as is derived therefrom may be taxed in that other State.

53. This paragraph states the general rule that income from employment derived by an individual who is a resident of one of the Contracting States may be taxed in the other Contracting State (the State of source) if the employment is exercised, that is the services are rendered, in that State.

54. Paragraph (2) of Article 14 of the Finnish agreement (and its equivalents in Australia's other tax treaties) state as follows:

> Notwithstanding the provisions of paragraph 1, remuneration derived by a resident of one of the Contracting States in respect of an employment exercised in the other Contracting State shall be taxable only in the first-mentioned State if:
>
> (a) the recipient is present in that other State for a period or periods not exceeding in the aggregate 183 days in any 12 month period commencing or ending in the year of income of that other State, and
>
> (b) the remuneration is paid by, or on behalf of, an employer who is not a resident of the other State, and
>
> (c) the remuneration is not borne by a permanent establishment which the employer has in the other State.[7]

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[5] The Agreement between the Government of Australia and the Government of Finland for the avoidance of double taxation with respect to taxes on income and the prevention of fiscal evasion and the protocol to that agreement [2007] ATS 36.

[6] Each dealing with directors' fees, pensions and annuities and government service respectively.

[7] Some of Australia's tax treaties may also contain a fourth condition for exception. For example, Australia's treaty with Austria contains the following additional condition in Article 15(2)(d):

55. This paragraph establishes the short-term visit exception from taxation in the State of source. All the conditions prescribed in paragraph (2) must be satisfied for the remuneration to qualify for the short-term visit exception. However, given that the Income from Employment Article in a tax treaty is subject to certain other specified articles,[8] this exclusion applies only to the extent that the remuneration of the non-resident is not dealt with by another one of the Articles specified, such as those applying to government services or entertainers and sportspersons.[9]

56. The first condition is that the short-term visit exception is limited to periods less than or equal to 183 days in any 12 month period.[10]

57. The second condition is that the employer paying the remuneration, or on whose behalf it is paid, must not be a resident of the State in which the employment is exercised.[11]

58. Under the third condition, if the employer has a permanent establishment in the State in which the employment is exercised, the remuneration must not be borne by the permanent establishment which it has in that State.

The meaning of the term 'employer'

59. The term 'employer' is not defined in Australia's tax treaties. Article 3(2) of the Finnish agreement, which deals with undefined terms and is on the same terms as Article 3(2) of the OECD Model, provides:

> As regards the application of the Agreement at any time by a Contracting State, any term not defined therein shall, unless the context otherwise requires, have the meaning that it has at that time under the law of that State concerning the taxes to which the Agreement applies, any meaning under the applicable tax law of that State prevailing over a meaning given to the term under other law of that State.

> the remuneration is, or upon the application of this Article will be, subject to tax in the first-mentioned State.

[8] For example, see Article 14(1) of the Finnish agreement at paragraph 52 above.

[9] 'Artistes and Sportsmen' is the heading of Article 17 of the OECD Model. Equivalent Articles in Australia's tax treaties may state other headings, such as 'Entertainers', or have no heading at all.

[10] The number of days and the time period within which the number of days are counted in some treaties may vary. For example, the number of days is 90 days in the Papua New Guinea, Fijian and Kiribati agreements. Examples of variations of the period of time referred to above include: '183 days in the year of income or fiscal year …' in Article 15(2)(a) of the Netherlands agreement, '183 days in any 12 month period commencing or ending in the taxable year of the other Contracting State' in Article 14(2)(a) of the Japanese convention. Article 14(2)(a) of the German agreement refers to 'year of income or the assessment period' during which the employment is exercised.

[11] Some of Australia's tax treaties provide that the employer must be a resident of the same State as the individual deriving the income from employment. For example, Article 15(2)(b) of the Mexican agreement states:

> the remuneration is paid by, or on behalf of, an employer who is a resident of the first mentioned State.

60. In ascertaining the meaning of undefined terms in a tax treaty, this draft Ruling uses the approach set out in paragraphs 63 to 76 of Taxation Ruling TR 2001/13 *Income Tax: Interpreting Australia's Double Tax Agreements* (TR 2001/13). Paragraph 74 of TR 2001/13 states:

> … reliance cannot necessarily be placed on an undefined term in a DTA being interpreted according to its domestic law meaning; the context of its use in the DTA may indicate that such a meaning is inappropriate, in that it would not be an accurate representation of the 'bargain' or '*consensus ad idem*' which objective evidence shows has been reached by the negotiating countries.

61. In relation to interpreting a treaty term, Article 31(1) of the *Vienna Convention on the Law of Treaties* (Vienna Convention)[12] states that a treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.[13] Also, *Thiel v. Federal Commissioner of Taxation* (1990) 171 CLR 338; [1990] HCA 37; (1990) 64 ALJR 516; (1990) 94 ALR 647; 90 ATC 4717; (1990) 21 ATR 531 supports consideration of the Commentaries to the OECD Model in interpreting tax treaties.[14]

62. The object and purpose of those subparagraphs in the short-term visit exception containing the term 'employer[15] are set out in paragraph 6.2 of the Commentary on Article 15 of the OECD Model as follows:

> The object and purpose of subparagraphs *b)* and *c)* of paragraph 2 are to avoid the source taxation of short-term employments to the extent that the employment income is not allowed as a deductible expense in the State of source because the employer is not taxable in that State as he neither is a resident nor has a permanent establishment therein. These subparagraphs can also be justified by the fact that imposing source deduction requirements with respect to short-term employments in a given State may be considered to constitute an excessive administrative burden where the employer neither resides nor has a permanent establishment in that State.

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[12] The Vienna Convention which entered into force internationally on 27 January 1980. Article 31 (and 32) of this Convention is applied as a matter of practice when interpreting any of Australia's tax treaties (see paragraph 96 of TR 2001/13).

[13] Specifically in the Australian context, paragraph 38 of *McDermott Industries (Aust) Pty Ltd v. Commissioner of Taxation* [2005] FCAFC 67; (2005) 142 FCR 134; (2005) 219 ALR 346; 2005 ATC 4398; (2005) 59 ATR 358 *(McDermott)* which, in summarising the principles applicable to the interpretation of tax treaties, states amongst other things:

> The courts must, however, in addition to having regard to the text, have regard as well to the context, object and purpose of the treaty provisions. The approach to interpretation involves a holistic approach.

[14] See also paragraphs 101 - 108 of Taxation Ruling TR 2001/13.

[15] That is, subparagraphs (b) and (c).

63. Having regard to the object and purpose stated above, the meaning given to 'employer' in the context of the Article seeks to ensure that the short-term visit exception does not apply in unintended situations. For example, this object and purpose would be defeated if:

- the user enterprise is the employer and it deducts the payment to a non-resident intermediary (including the remuneration of the non-resident individual) as a cost incurred in carrying on business in the source country to earn assessable income for the purposes of section 8-1 of the *Income Tax Assessment Act 1997* (ITAA 1997); and
- the non-resident individual is not taxed in the source country on the remuneration he receives.

64. Consistent with the undefined terms provision in Australia's tax treaties, paragraphs 8.4 of the Commentary on Article 15 of the OECD Model states (in part):

> Subject to the limit described in paragraph 8.11 [that disregarding a formal contractual relationship can only be done on the basis of objective criteria] and unless the context of the particular convention requires otherwise, it is a matter of domestic law of the State of source to determine whether services rendered by an individual in that State are provided in an employment relationship and that determination will govern how that State applies the Convention.

65. The Commentary extracted above refers to it being a matter of domestic law to determine whether services rendered by an individual are provided in an employment relationship subject to the limitation and potential exception specified. However, from paragraph 61 and as a matter of tax treaty interpretation,[16] Australia's domestic law is not the only consideration in determining the meaning of the term 'employer' and, as a consequence, the identity of the employer for the purposes of short-term visit exception. The context, object and purpose of the short-term visit exception, subparagraphs b) and c) in particular, are also to be considered in interpreting the term 'employer'.

66. Paragraphs 70 to 125 of the explanation to this draft Ruling contain an analysis of the underlying principles and factors arising from Australia's domestic law. These are applied to the facts and circumstances of particular arrangements in determining whether an individual is rendering services in an employment relationship and, in some cases, who the employer is. The Commissioner considers that these underlying principles and factors constitute from Australia's perspective, the 'various … jurisprudential rules' and 'objective criteria' referred to in paragraph 8.4 and 8.11 respectively of the Commentary on Article 15 of the OECD Model.

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[16] See, for example, Article 31(1) of the Vienna Convention referred to at paragraph 61 and paragraph 38 of *McDermott* referred to in footnote 13.

67. Where there is a contractual relationship between particular parties that is one of employment; one of the parties will be the employer in the relationship. The employer for the purposes of the short-term visit exception is, from Australia's perspective, the enterprise to which a non-resident individual renders his or her services in what is considered an employment relationship.

Determining the employer

68. In determining who the employer is for the purposes of the short term visit exception, the Commissioner will in each case have regard to:

- the underlying principles and factors at paragraphs 70 to 125 arising from Australian domestic law; and
- the context, object and purpose of the short-term visit exception, especially subparagraphs b) and c).[17]

69. Application of the underlying principles and factors at paragraphs 70 to 125 is, of itself and in most instances, unlikely to result in the short-term visit exception being applied so as not to be in accordance with its object and purpose.

70. The discussion below of the law as to who is an employer is a summary of the underlying principles to be considered as it relates to the short-term visit exception.[18]

71. Under Australian domestic law, the relationship between an employer and an employee is contractual.[19] It is often referred to as a *contract of service*.

The existence of a contract

72. An employment relationship cannot exist in the absence of a contract, whether that contract is express or implied. This includes instances where there are three or more parties to an arrangement as a contract must exist between, for example, the non-resident individual and either a non-resident intermediary or an Australian resident end-user. The existence of such a contractual relationship is determined by applying the ordinary principles of contract law.[20] The importance of both of these matters are illustrated in cases such as *Building Workers' Industrial Union of Australia and Others v. Odco Pty Ltd* (1991) 29 FCR 104; (1991) 99 ALR 735 *(Odco)*; *Drake*

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[17] In relation to the object and purpose of these subparagraphs, see paragraph 62.
[18] A fuller discussion in the context of who is an employee for the purposes of the *Superannuation Guarantee (Administration) Act 1992* is set out in Superannuation Guarantee Ruling SGR 2005/1 *Superannuation guarantee: who is an employee?* and Superannuation Guarantee Ruling SGR 2005/2 *Superannuation guarantee: Work arranged by intermediaries.*
[19] *Byrne & Anor v. Australian Airlines Limited* (1995) 185 CLR 410 at 436, per McHugh and Gummow JJ.
[20] For example, an intention to be legally bound, offer and acceptance and consideration.

Personnel Ltd & Ors v. Commissioner of State Revenue [2000] VSCA 122; 2000 ATC 4500; 44 ATR 413 *(Drake)*; *Swift Placements Pty Limited v. Workcover Authority of New South Wales* [2000] NSWIRComm 9 *(Swift Placements)* and *Damevski v. Guidice* [2003] FCAFC 252 *(Damevski)*.

73. As was stated by the Industrial Relations Commission of New South Wales in *Swift Placements*, the initial requirement is the creation of a legal relationship between the parties concerned for the performance of work. It is only then that there is a need to ascertain whether the relationship so created be one of employment (under a contract of service) or of some other kind (such as, principal – independent contractor or principal – agent).[21]

74. See also *Dalgety Farmers Ltd. t/as Grazcos v. Bruce* (1995) 12 NSWCCR 36, Kirby A.-C.J. at pp.47-48:

> In determining whether a contract of service has been entered, and if so with whom, it is necessary to look to the circumstances of the engagement and to ascertain who it was that offered employment, and whether the worker accepted that offer. To determine whether what then ensued was indeed employment (in the sense of a contract of service) it is necessary to look to the whole of the relationship.

75. The contract may be written, oral, partly written and partly oral or it may be implied from the parties' actions.[22]

76. As Marshall J stated in *Damevski,*[23] contracts are not to be implied lightly. The court may imply a contract by concluding that the parties intended to create contractual relations after examining extrinsic evidence, including what the parties said and did.

77. Marshall J found that although there was no formal offer of a new employment contract, it could be implied that the parties[24] had informally re-entered an arrangement in the nature of a contract of service on the same terms and conditions which had governed their previous employment relationship.[25]

78. In *Wilton & Cumberland v. Coal & Allied Operations Pty Ltd* [2007] FCA 725 *(Wilton),* the Federal Court considered whether workers provided to a coal mining company through an on-hire employee arrangement were employees of that company. The workers were initially employed by the labour hire agency. However, the workers claimed that it should be implied from their dealings with the coal mining company that they were employees of the company. The Federal Court was not satisfied that there was an employment relationship between the workers and the coal mining company. The company and the workers did not discuss or consider essential contractual terms. The workers did not act in a way that indicated they regarded themselves as being employed by the coal mining company.

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[21] [2000] NSWIRComm 9 at paragraph 33.
[22] Graw, S 2005, *An Introduction to the Law of Contract*, 5th edn, Lawbook Co, p 28.
[23] [2003] FCAFC 252 at paragraph 82.
[24] Endoxos and Mr Damevski.
[25] *Damevski v. Giudice* [2003] FCAFC 252 at paragraph 89.

The nature of the contractual relationship

79. Determining that the nature of the relationship between the relevant parties to the contract is one of employment and the identification of the respective parties depends on the proper characterisation of the contractual arrangements. The existence of a contractual relationship and an employment relationship, in any given set of circumstances, is ultimately a question of law.[26]

80. In ascertaining the proper characterisation, the totality of the relationship between the parties must be considered.[27]

81. In characterising the relationship, both the express terms of the contract and the substance or reality of the contractual relations (in other words, the actual behaviour of the parties) are relevant. In short, the approach under Australian common law is to find the true substance of the relationship. This approach is within the substance over form rules referred to in paragraph 8.4 of the Commentary on Article 15 of the OECD Model. Furthermore, the approach is consistent with the approach set out in paragraphs 8.13 to 8.15 of the Commentary on Article 15 of the OECD Model.

82. This approach applies to all cases to determine who the employer is for the purposes of the short-term visit exception. In this regard, paragraph 8.1 of the Commentary on Article 15 of the OECD Model states:

> While the Commentary previously dealt with cases where arrangements were structured for the main purpose of obtaining the benefits of the exception of paragraph 2 of Article 15, it was found that similar issues could arise in many other cases that did not involve tax-motivated transactions and the Commentary was amended to provide a more comprehensive discussion of these questions.

83. Following from paragraphs 62 – 63 above, it would be contrary to the object and purpose of the short-term visit exception to prohibit the source country from taxing the remuneration of a non-resident individual when in substance he or she is employed by the user enterprise which deducts the cost instead of the non-resident intermediary.

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[26] Per Marshall J in *Damevski v. Giudice* [2003] FCAFC 252 at paragraph 60.

[27] *Stevens v. Brodribb Sawmilling Company Pty Ltd* (1986) 160 CLR 16; [1986] HCA 1; (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 Pty Ltd* (2001) 207 CLR 21; [2001] HCA 44; (2001) 47 ATR 559; 2001 ATC 4508 (*Hollis v. Vabu*).

84. Even though, as stated above, it has been recognised judicially that an employment contract is not to be implied lightly,[28] the substance over form approach may lead to a conclusion that an entity other than the party specified in the written contract of employment should be regarded as the employer for the purposes of the short-term visit exception where:

- the conduct of the parties is not consistent with the terms of the written contract of employment or another contract with a third party, including instances where such terms are ambiguous; or
- under the contractual terms, the true nature of the relationship(s) between the parties are misrepresented or disguised.

85. The terms and conditions of the contract, whether express or implied, are of considerable importance to the proper characterisation of the relationship.[29]

86. However, the parties cannot deem the relationship between themselves to be something that it is not.[30] The parties to an agreement cannot alter the true substance of the relationship by simply giving it a different label.[31]

87. As Gray J stated in *Re Porter: re Transport Workers Union of Australia:*

> 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.[32]

88. In *Damevski*, the Federal Court found that a worker remained an employee despite his employer's attempt to end the employment relationship and deal with the employee as a contractor through a labour hire agency. In this case, the interposition of the labour hire agency was not genuine. The true nature of the relationship was that the worker remained an employee of his former employer because the labour hire agency did nothing more than pay his wages, while the employer continued to direct the employee

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[28] See, for example, Marshall J in *Damevski v. Giudice* [2003] FCAFC 252 at paragraph 82. Also, Conti J in *Wilton & Cumberland v. Coal & Allied Operations Pty Ltd* [2007] FCA 725 at paragraph 182 refers to the 'controversial notion of implied relationships of employment and the significance thereof' in the labour hire context deriving from the UK Court of Appeal decision in *Brook Street Bureau (UK) Ltd v. Dacas* [2004] EWCA Civ 217, [2004] IRLR 358 being an association that is at best doubtful.
[29] See *Stevens v. Brodribb* (1986) 160 CLR 16 at 37, per Wilson and Dawson JJ.
[30] *Hollis v. Vabu* (2001) 207 CLR 21 at 45.
[31] *Massey v. Crown Life Insurance Co* [1978] 1 WLR 676; [1978] 2 All ER 576.
[32] (1989) 34 IR 179.

89. In some circumstances, an intermediary firm may perform an agency role to bring about a contractual relationship between the worker and end user. In this case, the worker will be an employee of the user enterprise, not the intermediary. However, the manner in which the relationship is described is not conclusive of the nature of the legal relationship between the parties. In *Swift Placements*, the Industrial Relations Commission rejected the categorisation by counsel for Swift Placements that the relationship between Swift Placements and the worker was one of agency, notwithstanding that the business of Swift Placements was described as an employment agency.

Key indicators of employment relationship

90. While the factors discussed below are key indicators of whether an individual is an employee or independent contractor at common law, they are also relevant in determining who should be regarded as the employer for the purposes of the short term visit exception.

91. No one factor is determinative and not all factors will be relevant in a particular case. Wilson and Dawson JJ in *Stevens v. Brodribb* stated.[33]

> The modern approach is, however, to have regard to a variety of criteria. This approach is not without its difficulties because not all of the accepted criteria provide a relevant test in all circumstances and none is conclusive. Moreover, the relationship itself remains largely undefined as a legal concept except in terms of the various criteria, the relevance of which may vary according to the circumstances.

Control

92. An important factor to consider is the degree of control which an enterprise engaging an individual to perform work has over that individual in terms of what, how and where work is to be done. In this regard, Wilson and Dawson JJ in *Stevens v, Brodribb*[34] stated:

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

93. However, the importance of control lies in the right of the employer to exercise it, rather than its actual exercise,[35] even though the actual exercise can still be relevant.

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[33] (1986) 160 CLR 16 at paragraph 9.
[34] (1986) 160 CLR 16 at 36.
[35] *Zuijs v. Wirth Bros Proprietary Ltd (1955) 93 CLR 561 at 57.1*

94. The Full Bench held in *Swift Placements* that control over a worker did not merely relate to the on-the-job situation, but rather the ultimate or legal control over the worker. It stated:

> …control by an employer over an employee is not to be viewed merely in the on-the-job situation in directing a person what to do and how to do it, but rather in the sense of the ultimate or legal control over the person to require him to properly and effectively exercise his skill in the performance of the work allocated…[36]

95. In *Forstaff and Ors v. The Chief Commissioner of State Revenue* [2004] NSWSC 573; 2004 ATC 4758; (2004) 56 ATR 302 *(Forstaff)*, McDougall J recognised that, historically, the control test had been considered in the context of a bilateral rather than trilateral or multi-lateral relationship. He stated.[37]

> …in the cases that do involve a trilateral relationship (*ACC v. Odco, BWIU v. Odco and Brook St*[38]) the control test has not been regarded as dispositive… in a changing workforce with evolving relationships … the concept of control is not readily susceptible of analysis according to the traditional master/servant matrix.

96. From the cases including *Stevens v. Brodribb,*[39] *Mason & Cox Pty Ltd v. McCann* (1999) 74 SASR 438; [1999] SASC 544 (*Mason and Cox)*, *Swift Placements* and *Drake*, it is the ultimate or legal control over the individual non-resident which is most relevant, rather than practical control.

97. Ultimate control would, amongst other things, enable the relevant entity to withdraw the worker from an assignment and terminate the contract with the worker.[40]

98. However, specifying in detail how contracted services are to be performed does not of itself necessarily imply an employment relationship.

99. Similarly, in international labour hire arrangements, it will not necessarily be inferred that the user enterprise is the employer for the purposes of the short-term visit exception merely because the user enterprise exercises practical control over the individual by having the work performed at the premises of the user enterprise and under their direction.[41]

100. The Commissioner will also have regard to the contract between the labour hire firm and the user enterprise.

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[36] *Swift Placements* [2000] NSWIR Comm 9 at paragraph 44.
[37] [2004] NSWSC 573 at paragraph 114.
[38] *Brook Street Bureau (UK) Ltd v. Dacas* [2004] EWCA Civ 217; [2004] IRLR 358.
[39] (1986) 160 CLR 16; 63 ALR 513 Per Mason J at paragraph 16.
[40] For example, see the judgment of McDougall J in *Forstaff* [2004] NSWSC 573; (2004) 56 ATR 302 at paragraph 115.
[41] For example, this was the result in *Mason & Cox.*

Integration

101. It is relevant to consider the nature of the services rendered by the individual and whether they are an integral part of the business activities carried on by the enterprise to which the services are provided.

102. In describing the 'integration test', the majority of the High Court in *Hollis v. Vabu*[42] quoted the following statement by Windeyer J in *Marshall v. Whittaker's Building Supply Co*:[43]

> … 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.'[44]

103. In *Hollis v. Vabu,*[45] the High Court considered this distinction (and other aspects including control) and concluded that the bicycle couriers in that case were the employees of another, rather than working on their own account. The majority 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.

104. Where the facts indicate that individuals are not working on their own account, this points to the relationship being one of employment.

105. Furthermore, Mason J in *Stevens v. Brodribb*[46] described the relevance of the integration test:

> In the present case it was argued that Gray was part and parcel of Brodribb's organization in that his snigging activities were integral to the supply of timber necessary for Brodribb's sawmilling operations at Orbost. The relevance of this submission was said to be that it added weight to the inference that Gray was subject to the control of Brodribb and therefore that the relationship between them was one of employment. In short, the contention was that the organization test is relevant to the issue of control. But this is not to use the concept as a criterion for determining a legal issue or legal liability. It is merely to use the fact that A is part of B's business organization as additional material from which to infer that B has legal authority to control what A does. No doubt in some circumstances, depending on the nature of the organization and the part that A plays in its activities, it is legitimate to have regard to that fact in drawing an inference as to B's control of A in the performance of a relevant activity. However, here there are other facts which bear more cogently on the issue of control and negate the inference which is sought to be drawn.
>
> ….For my part I am unable to accept that the organization test could result in an affirmative finding that the contract is one of service

[42] Hollis v. Vabu (2001) 207 CLR 21 at 41.
[43] (1963) 109 CLR 210; [1963] HCA 26.
[44] *Hollis v. Vabu* (2001) 207 CLR 21 at 39, per Gleeson CJ, Gaudron, Gummow, Kirby and Hayne JJ.
[45] *Hollis v. Vabu* (2001) 207 CLR 21 at paragraph 47 (to 57).
[46] (1986) 160 CLR 16 at paragraphs 15 and 16.

> when the control test either on its own or with other indicia yields the conclusion that it is a contract for services. Of the two concepts, legal authority to control is the more relevant and the more cogent in determining the nature of the relationship.

106. In relation to international labour hire arrangements, it will not necessarily be inferred that the user enterprise is the employer for the purposes of the short-term visit exception merely because the work is being performed for the benefit of the user enterprise rather than the intermediary. In *Swift Placements*, the Full Bench adopted and applied a passage from the judgment of Kitto J in *Attorney-General for NSW v. Perpetual Trustee Co. (Ltd)*[47] which explained the essential elements of an employer-employee:

> …the statement that the doing of work must be for the benefit of the master does not mean, of course, that the direct benefit from the work itself must necessarily accrue to the master; he may, without altering the relationship, direct his servant to do work which will benefit another.[48]

107. Accordingly, a non-resident individual engaged by an intermediary may be directed to work for the benefit of the user enterprise without the user enterprise becoming the employer for the purposes of the short-term visit exception.

Remuneration

108. The identity of the entity paying remuneration to an employee for their work is a factor to consider in determining the identity of the employer.

109. In *Wilton*, MES (the hiring agency) made the payments referred to as wages to the applicants directly on a weekly basis and before any payment was made by CAO (the user enterprise for present purposes) to MES. Income tax was deducted and superannuation contributions were made. CAO argued and the Court accepted that CAO did not remunerate the applicants for their work and that CAO was not the employer. In *Forstaff*, the Court concluded that the user enterprise (Forstaff's client in that case) was not the employer. Amongst other things, Forstaff paid the workers and the remuneration was 'subject to all relevant provisions of any appropriate Award, Site or Enterprise Agreement', in other words, the remuneration was prescribed under an award or agreement for employees.

[47] (1952) 85 CLR 237; [1952] HCA 2.
[48] *Swift Placements* [2000] NSWIRComm 9 at 32; (2000) 96 IR 69.

110. However, as stated in the joint judgment of Wilcox J, Burchett J and Ryan J in *Odco:*[49]

> ...payment of wages by a third party, or what Woodward J called an 'intermediary', is not fatal to the existence of a contract of employment between a worker and a putative employer.

111. The identity of the entity that determines the amount of the remuneration will also be relevant. In *Mason & Cox* and in *Drake*, the fact the labour hire agency determined the remuneration was relevant. By contrast, in *Damevski*, the intermediary in that case played no role in determining the rates payable other than for the inclusion of its administrative charge. This was one of the indicators in that case pointing to the user enterprise being the employer.

Terms of engagement

112. As was stated by Wilson and Dawson JJ in *Stevens and Brodribb,*[50] the actual terms and terminology in the contract will be of considerable importance to the proper characterisation of the relationship between the parties, particularly where the criteria are balanced. In *Forstaff,*[51] where the parties characterised their relationship as one of employment, McDougall J stated:

> In circumstances where the criteria are balanced, I think that it is appropriate, as the Full Court did in *BWIU v. Odco*, to pay close regard to the way in which the parties have characterised their relationship.

113. However, how the arrangement between the parties is labelled in a written contract is not conclusive of the nature of the legal relationship. For example, in *Forstaff*, McDougall J stated.[52]

> If the facts were inconsistent with the parties' characterisation of their relationship, then the characterisation could not prevail.

114. Terms of engagement also refers to such matters as length of assignment and the relevant role of the worker, rates of pay, workers compensation insurance, deduction of PAYG, superannuation contributions and other employee benefits.

Risk

115. A key consideration of whether there is an employment relationship is who bears the responsibility or risk for the individual's work.

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[49] (1991) 29 FCR 104 at 119; (1991) 37 IR 380; (1991) 99 ALR 735; [1991] ATPR 41-092; (1991) 33 AILR 163 and referred to by Merkel J in *Damevski* [2003] FCAFC 252 at paragraph 172.
[50] (1986) 160 CLR 16; 63 ALR 513 at paragraph 11.
[51] [2004] NSWSC 573; 2004 ATC 4758 at paragraph 120.
[52] [2004] NSWSC 573; 2004 ATC 4758 at paragraph 121.

116. In *Hollis v. Vabu,*[53] the majority said:

> In general, under contemporary Australian conditions, the conduct by the defendant of an enterprise in which persons are identified as representing that enterprise should carry an obligation to third persons to bear the cost of injury or damage to them which may fairly be said to be characteristic of the conduct of that enterprise. In delivering the judgment of the Supreme Court of Canada in *Bazley v. Curry*, McLachlin J said of such cases that 'the employer's enterprise [has] created the risk that produced the tortious act' and the employer must bear responsibility for it …. McLachlin J termed this risk 'enterprise risk' and said that 'where the employee's conduct is closely tied to a risk that the employer's enterprise has placed in the community, the employer may justly be held vicariously liable for the employee's wrong'.

117. However, in *Mason and Cox*, Doyle CJ stated:[54]

> Nor is it to the point that Mason & Cox might have been vicariously liable for an act of negligence by the plaintiff while working at their premises. The vicarious liability of *Mason & Cox* would arise out of the control exercised over the plaintiff, not from a contract of employment: see *Denhan v. Midland Employees Mutual Insurance Ltd* [1955] 2 QB 437 and *McNiece*.

Results

118. The notion of 'payment for result' is a strong (but not conclusive) indication that the contract is one for services, rather than of service. In *World Book (Australia) Pty Ltd v. FC of T*,[55] 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...

119. However, this notion is not necessarily inconsistent with a contract of service. Cases such as *FC of T v. Barrett & Ors*, *Hollis v. Vabu* and *Commissioner of State Taxation v. Roy Morgan Research Centre Pty Ltd* [56] are examples of purported contracts for results involving employment relationships. Given the emphasis that the courts have placed on the control test (discussed above); the production of a given result is not determinative. This is consistent with paragraph 14 above which states that no one factor is determinative.

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[53] (2001) 207 CLR 21; 2001 ATC 4508 at paragraph 42.
[54] [1999] SASC 544 at paragraph 30.
[55] 92 ATC 4327; (1992) 23 ATR 412.
[56] The High Court in *FC of T v. Barrett & Ors* (1973) 129 CLR 395; 73 ATC 4147 at 4153; (1973) 4 ATR 122; found that land salesmen, who were engaged by a firm of land agents to find purchasers for land entrusted to the firm for sale and who were remunerated by commission only were employees and not independent contractors. The High Court in *Hollis v. Vabu* (2001) 207 CLR at 21; [2001] HCA 44; 2001 ATC 4508; (2001) 47 ATR 559 considered that payment to the bicycle couriers per delivery, rather than per time period engaged, was a natural means to remunerate employees whose sole purpose is to perform deliveries. Further, the Full Court of the Supreme Court of South Australia in *Commissioner of State*

120. To the extent such a contract involves an employment relationship, who determines the results to be achieved can be a factor to take into account in determining the identity of the employer.

Provision of tools and equipment and payment of business expenses

121. The provision of assets, equipment and tools and the incurring of expenses and other overheads by an individual have been held to be an indicator that the individual is an independent contractor.[57]

122. 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.[58]

123. The weight or emphasis to be placed on this factor in determining the nature of the contractual relationship depends on the particular circumstances. For example, in *Wilton*, CAO (the user enterprise) rather than the labour hire agency provided the necessarily mining equipment, whilst the agency provided other work gear (goggles, helmets etcetera). In weighing up all the factors and despite CAO providing significant equipment for the workers to perform their job, the Federal Court concluded there was no employment relationship between the workers and CAO.

Delegation

124. The power to delegate or subcontract (in the sense of the capacity to engage others to do the work, or parts of the work) is a significant factor to determine whether a worker is an employee or an independent contractor.[59] For example, if a worker is required contractually to perform work personally, then this is an indication that the worker is an employee.

Taxation v. Roy Morgan Research Centre Pty Ltd [2004] SASC 288; (2004) 57 ATR 148; (2004) 2004 ATC 4933 found that interviewers who were only paid on the completion of each assignment, not on an hourly basis, were employees and not independent contractors.

[57] See, for example, *Stevens v. Brodribb* and *Vabu Pty Ltd* v. *FC of T* 96 ATC 4898; (1996) 33 ATR 537.

[58] (2001) 207 CLR 21 at 41 to 42. 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.

[59] *Stevens v. Brodribb* (1986) 160 CLR 16 at 26 per Mason J.

125. In international labour hire arrangements, the power of delegation may be relevant in determining the nature of the relationship between the intermediary and the worker. The contract between the labour hire agency and the worker in most cases would require the worker to perform the relevant work for the client themselves with no ability to delegate the work to others. In *Odco,*[60] the Federal Court found that the workers in question were not employees of either the labour hire agency or the host business. However, whether the worker was able to delegate any of the work assigned was not discussed.

Disagreements and application of the exception

126. Where there is a disagreement between States about whether services rendered by an individual who is not a resident of the source country may properly be regarded by that State as rendered in an employment relationship, then Paragraph 8.12 of the Commentary on Article 15 of the OECD Model states:

> Any disagreement between States as to whether this [services rendered by an individual may properly be regarded by a State as rendered in an employment relationship] is the case should be resolved having regard to the following principles and examples [those stated at paragraphs 8.13 to 8.27]….

127. Paragraphs 8.13 to 8.15 of the Commentary on Article 15 of the OECD Model set out the approach the OECD uses in such circumstances. These paragraphs are attached at Appendix 3.

128. It is possible for the State applying the convention to deny the application of the short term visit exception in abusive cases. Paragraph 8.9 of the Commentary on Article 15 refers to paragraph 9.5 of the Commentary on Article 1, which states the guiding principle as being:

> that the benefits of a double tax convention should not be available where a main purpose for entering into certain transactions or arrangements was to secure a more favourable tax position and obtaining that more favourable treatment in these circumstances would be contrary to the object and purpose of the relevant provisions.

129. Furthermore it is noted in paragraph 8.9 of the Commentary on Article 15 that it should not be lightly assumed that this is the case.

130. Accordingly, the availability of the short-term visit exception may be denied in abusive cases, subject to there being no disagreement between the Contracting States. In such instances, the country of residence of the non-resident individual must relieve double taxation under the Elimination of Double Taxation Article, or its equivalent, in Australia's tax treaties.

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[60] (1991) 29 FCR 104.

Permanent establishment (PE) or a fixed base

131. In international labour hire arrangements, the user enterprise may be either a resident entity of the source country (for present purposes, Australia) or a PE (in Australia) of a non-resident. The analysis so far in this draft ruling has proceeded on the basis that:

- the user enterprise is a resident; and
- any remuneration paid to the non-resident individual is not deductible in determining the profits of a PE or a fixed base which a non-resident intermediary may have in Australia.

132. Where in a particular instance, a resident user enterprise is the employer; the condition in subparagraph (b) of Article 15(2) (that the employer is not a resident of the other State) would not be satisfied.

133. The same result will apply for the purposes of subparagraph (c) if the user enterprise is the employer for the purposes of the short-term visit exception and is a PE or fixed base of a non-resident in the source country. In such instances, any remuneration paid to the non-resident individual is borne by the PE or fixed base the user enterprise has in Australia.

134. If the non-resident intermediary has a PE or a fixed base in Australia through which the services of the worker are provided to the non-resident individual, the remuneration paid to the non-resident individual would normally be deductible in determining the taxable profits attributable to the PE or the fixed base of the non-resident intermediary. In these circumstances, the requirement under subparagraph (c) of Article 15(2) would not be satisfied in relation to the intermediary. As a result, the exception under Article 15(2) would not be available even if the intermediary is the employer.

The application of short-term visit exception and source of income

135. Where it is concluded that the user enterprise in Australia is the employer of the non-resident individual for the purposes of the short-term visit exception, the conditions of the short-term visit exception in the Income from Employment Article in Australia's tax treaties will not be satisfied. Where the short-term visit exception does not apply, taxing rights over the payments or income received by the non-resident individual in respect of employment exercised in the source country are allocated to that country.

136. In these circumstances, the 'source of income' articles contained in most of the tax treaties of Australia (see, for example, Article 21 of the Finnish agreement) have the effect of deeming such income to have its source in Australia for domestic tax law purposes. As a result, the non-resident individual will be subject to source country tax on the employment income under the normal assessment rules applicable to non-residents. If in a particular case the relevant tax treaty does not contain a source rule that has this effect, the assessment of the employment income of the non-resident will depend on the application of the common law source rules for employment income.[61]

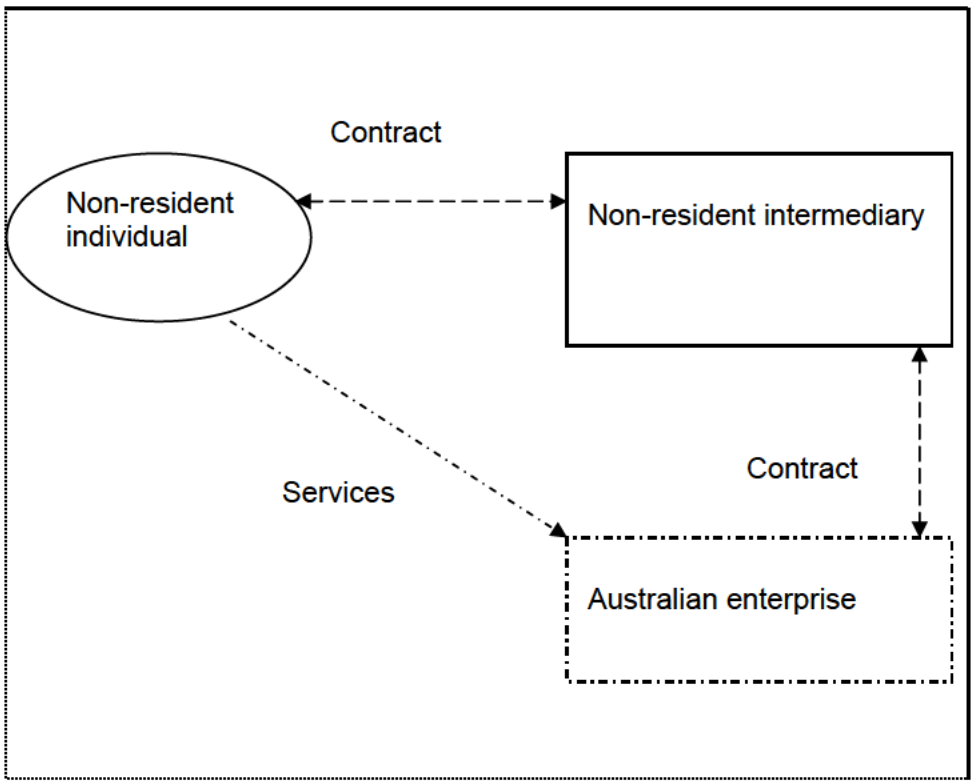
137. Where the application of the Income from Employment Article in a tax treaty leads to the income of the individual being assessable to tax in Australia, the country of residence of the individual must grant relief for double taxation under the Elimination of Double Taxation Article (or its equivalent) in the relevant tax treaty.

[61] Refer to *FC of T v. Mitchum* (1965) 113 CLR 401; 39 ALJR 23; 13 ATD 497; 9 AITR 559 and *FC of T v. French* (1957) 98 CLR 398; 11 ATD 288; 7 AITR 76.

Appendix 2 – Glossary of terms

138. This glossary provides an explanation or description of a number of the terms used in this draft ruling:

> **'intermediary'** refers to an entity which enters into a contractual agreement with a non-resident individual to provide a salary, wages or other similar remuneration in return for that individual providing his or her labour or personal services. The intermediary of the non-resident individual may or may not be the employer for the purposes of the short-term visit exception.
>
> '**international labour hire arrangements'** include circumstances where a non-resident individual(s) are either hired out or seconded to the user enterprise in Australia by a non-resident intermediary. In some instances, the non-resident intermediary may be the only intermediary. In others, there may be more than one intermediary. The arrangement is shown in the diagram below.



'short-term visit exception'[62] refers to the provisions in the Income from Employment Article (or equivalent ones) in Australia's tax treaties that, from the perspective of the country where the work is performed, prohibit taxation by that country of remuneration derived by a non-resident working there.

'user enterprise' refers to the enterprise to which a non-resident individual's services are rendered whether or not the enterprise has entered into a formal contract with that individual. The enterprise may be a resident of the source country or a permanent establishment of a non-resident of that country.

[62] This term has been used in this draft Ruling because it is descriptive of the true nature of paragraph 2 of the Income from Employment Articles and its equivalent provisions in Australia's tax treaties as an exception to the general rule in paragraph 1 of the same Article. This term 'exception' is also used in the Commentary to Article 15 of the OECD Model.

Appendix 3 – Extract from the Commentary to Article 15 of the OECD Model

139. Extracted below are paragraphs 8.13 to 8.15 of the Commentary on Article 15 of the OECD Model:

> 8.13 The nature of the services rendered by the individual will be an important factor since it is logical to assume that an employee provides services which are an integral part of the business activities carried on by his employer. It will therefore be important to determine whether the services rendered by the individual constitute an integral part of the business of the enterprise to which these services are provided. For that purpose, a key consideration will be which enterprise bears the responsibility or risk for the results produced by the individual's work. Clearly, however, this analysis will only be relevant if the services of an individual are rendered directly to an enterprise. Where, for example, an individual provides services to a contract manufacturer or to an enterprise to which business is outsourced, the services of that individual are not rendered to enterprises that will obtain the products or services in question.
>
> 8.14 Where a comparison of the nature of the services rendered by the individual with the business activities carried on by his formal employer and by the enterprise to which the services are provided points to an employment relationship that is different from the formal contractual relationship, the following additional factors may be relevant to determine whether this is really the case:
>
> - who has the authority to instruct the individual regarding the manner in which the work has to be performed;
> - who controls and has responsibility for the place at which the work is performed;
> - the remuneration of the individual is directly charged by the formal employer to the enterprise to which the services are provided (see paragraph 8.15 below);
> - who puts the tools and materials necessary for the work at the individual's disposal;
> - who determines the number and qualifications of the individuals performing the work;
> - who has the right to select the individual who will perform the work and to terminate the contractual arrangements entered into with that individual for that purpose;
> - who has the right to impose disciplinary sanctions related to the work of that individual;
> - who determines the holidays and work schedule of that individual.

8.15 Where an individual who is formally an employee of one enterprise provides services to another enterprise, the financial arrangements made between the two enterprises will clearly be relevant, although not necessarily conclusive, for the purposes of determining whether the remuneration of the individual is directly charged by the formal employer to the enterprise to which the services are provided. For instance, if the fees charged by the enterprise that formally employs the individual represent the remuneration, employment benefits and other employment costs of that individual for the services that he provided to the other enterprise, with no profit element or with a profit element that is computed as a percentage of that remuneration, benefits and other employment costs, this would be indicative that the remuneration of the individual is directly charged by the formal employer to the enterprise to which the services are provided. That should not be considered to be the case, however, if the fee charged for the services bears no relationship to the remuneration of the individual or if that remuneration is only one of many factors taken into account in the fee charged for what is really a contract for services (e.g. where a consulting firm charges a client on the basis of an hourly fee for the time spent by one of its employee to perform a particular contract and that fee takes account of the various costs of the enterprise), provided that this is in conformity with the arm's length principle if the two enterprises are associated. It is important to note, however, that the question of whether the remuneration of the individual is directly charged by the formal employer to the enterprise to which the services are provided is only one of the subsidiary factors that are relevant in determining whether services rendered by that individual may properly be regarded by a State as rendered in an employment relationship rather than as under a contract for services concluded between two enterprises.

Appendix 4 – Your comments

140. You are invited to comment on this draft Ruling. Please forward your comments to the contact officer by the due date.

141. A compendium of comments is also prepared for the consideration of the relevant Rulings Panel or relevant tax officers. An edited version (names and identifying information removed) of the compendium of comments will also be prepared to:

- provide responses to persons providing comments; and
- publish on the Tax Office website at www.ato.gov.au.

Please advise if you do not want your comments included in the edited version of the compendium.

Due date:	**6 July 2012**
Contact officer:	**Bart Commandeur or Kevin O'Shaughnessy**
Email address:	**Bart.Commandeur@ato.gov.au Kevin.O'Shaughnessy@ato.gov.au**
Telephone:	**(03) 9285 1403 (03) 9285 2571**
Facsimile:	**(03) 9285 2606**
Address:	**Australian Taxation Office 3rd Floor North 990 Whitehorse Road BOX HILL VIC 3128**

Appendix 5 – Detailed contents list

142. The following is a detailed contents list for this Ruling:

References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2001/13; TR 2006/10;
SGR 2005/1; SGR 2005/2

Previous Rulings/Determinations:

TR 2003/11

Subject references:

- double tax agreements
- employment relationship
- international tax

Legislative references:

- Income Tax Assessment Act 1997 8-1
- Superannuation Guarantee (Administration) Act 1992
- Agreement between Australia and the Republic of Austria for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income [1988] ATS 21 (Austrian agreement)
- Agreement with the Government of Finland for the Avoidance of Double Taxation with Respect to Taxes on Income and the Prevention of Fiscal Evasion, and Protocol [2007] ATS 36 (Finnish agreement)
- Convention between Australia and Canada for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income [1981] ATS 14, as amended by the Canadian protocol (No. 1) [2002] ATS 26
- Agreement between Australia and Fiji for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income [1990] ATS 44
- Agreement between the Commonwealth of Australia and the Federal Republic of Germany for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and capital and to certain other taxes, and Protocol [1975] ATS 8
- Convention between Australia and Japan for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income, and Protocol and Exchange of notes [2008] ATS 21
- Agreement between Australia and the Republic of Kiribati for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income [1991] ATS 34.
- Agreement between Australia and the Kingdom of the Netherlands for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income, and Protocol [1976] ATS 24, as amended by the Netherlands protocol (No. 2) [1987] ATS 22.
- Agreement between Australia and the Independent State of Papua New Guinea for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income [1989] ATS 37
- Agreement between the Government of the Commonwealth of Australia and the Government of the Republic of Singapore for the

avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income [1969] ATS 14, as amended by the Singaporean protocol (No. 1) [1990] ATS 3 and the Singaporean protocol (No. 2) [2010] ATS 26

- Agreement between the Government of Australia and the Government of the United Mexican States for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income [2004] ATS 4 (Mexican agreement)
- Vienna Convention on the Law of Treaties 31
- Vienna Convention on the Law of Treaties 32

Case references:

- Attorney-General for NSW v. Perpetual Trustee Co (Ltd) (1952) 85 CLR 237; [1952] HCA 2
- Brook Street Bureau (UK) Ltd v. Dacas [2004] EWCA Civ 217, [2004] IRLR 358
- Building Workers' Industrial Union of Australia and Others v. Odco Pty Ltd (1991) 29 FCR 104; (1991) 99 ALR 735
- Byrne & Anor v. Australian Airlines Limited (1995) 185 CLR 410; [1995] HCA 24; (1995) 131 ALR 422; (1995) 69 ALJR 797
- Commissioner of State Taxation v. Roy Morgan Research Centre Pty Ltd [2004] SASC 288; (2004) 57 ATR 148; (2004) 2004 ATC 4933
- Dalgety Farmers Ltd. t/as Grazcos v. Bruce (1995) 12 NSWCCR 36
- Damevski v. Guidice [2003] FCAFC 252
- Drake Personnel Ltd & Ors v. Commissioner of State Revenue [2000] VSCA 122; 2000 ATC 4500; 44 ATR 413
- FC of T v. Barrett & Ors (1973) 129 CLR 395; (1973) 4 ATR 122; (1973) 73 ATC 4147
- FC of T v. French (1957) 98 CLR 398; 11 ATD 288; 7 AITR 76
- FC of T v. Mitchum (1965) 113 CLR 401; 39 ALJR 23; 13 ATD 497; 9 AITR 559
- Forstaff and Ors v. The Chief Commissioner of State Revenue [2004] NSWSC 573; 2004 ATC 4758; (2004) 56 ATR 302
- Hollis v. Vabu (2001) 207 CLR 21; [2001] HCA 44; 2001 ATC 4508; (2001) 47 ATR 559
- McDermott Industries (Aust) Pty Ltd v. Commissioner of Taxation [2005] FCAFC 67; (2005) 142 FCR 134; (2005) 219 ALR 346; 2005 ATC 4398; (2005) 59 ATR 358
- Marshall v. Whittaker's Building Supply Co (1963) 109 CLR 210; [1963] HCA 26
- Mason & Cox v. McCann (1999) 74 SASR 438; [1999] SASC 544
- Massey v. Crown Life Insurance Co [1978] 1 WLR 676; [1978] 2 All ER 576
- Re: Porter: re Transport Workers Union of Australia (1989) 34 IR 179
- Stevens v. Brodribb Sawmilling Company Pty Ltd (1986) 160 CLR 16; [1986] HCA 1; 63 ALR 513
- Swift Placements Pty Limited v. Workcover Authority of New South Wales [2000] NSWIRComm 9; (2000) 96 IR 69
- Thiel v. Federal Commissioner of Taxation (1990) 171 CLR 338; [1990] HCA 37; (1990) 64 ALJR 516; (1990) 94 ALR 647; 90 ATC 4717; (1990) 21 ATR 531
- Vabu Pty Ltd v. FC of T 96 ATC 4898; (1996) 33 ATR 537.
- Wilton & Cumberland v. Coal & Allied Operations Pty Ltd [2007] FCA 725

- World Book (Australia) Pty Ltd v. FC of T 92 ATC 4327; (1992) 23 ATR 412.
- Zuijs v. Wirth Bros Proprietary Ltd (1955) 93 CLR 561; [1955] HCA 73

Other references:

- Graw, S. 2005, An Introduction to the Law of Contract, 5th ed., LBC.
- OECD Model Tax Convention on Income and on Capital, condensed version, 22 July 2010

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