

***PPS Bulletin 11 - The meaning of the term 'payment'
for PPS purposes***

PPS Bulletin

Number 11

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About this Bulletin

This Bulletin identifies and explains the broad class of contracts referred to in the definition of *payment*, other than payments of exempt income and payments to or by a trustee of the estate of a bankrupt, or the liquidator of a company that is being wound up.

A *prescribed payment* is defined to mean payments made under a particular class or category of contract. The payments that are currently prescribed are:

- certain payments within nine specified industries (see PPS Bulletins 1-9 for information on how these industries are affected by PPS); and
- any other payment that the payer and payee have agreed will be a prescribed payment (see PPS Bulletin 10 – *Voluntary Agreements*).

What is a 'payment' for PPS purposes?

The term *payment* is defined (as relevant to this Bulletin) to mean:

A payment that is made, or is liable to be made, under a contract the performance of which, in whole or in part, involves the performance of work (whether or not by the person to whom the payment is made or is liable to be made), but does not include:

- a payment of salary or wages to an employee.¹

From this definition it can be seen that the word 'payment' is not itself defined. It therefore takes on its ordinary and commonly understood meaning of discharging a debt, obligation or promise by giving or doing something.

The definition limits the payments that might be subject to PPS by restricting the term to payments made under a particular class of contract. There are two key aspects to the above definition that determine or identify the relevant class, namely:

- performance of the contract; and
- performance of work.

What is meant by 'performance of the contract'?

In this context, the word 'performance' is taken to refer to fulfilment of the payee's obligation (promise or undertaking) to the payer under the contract. That is, it refers to the essential action required of the payee to complete their side of the bargain. In this case the required action must involve, at least in part, the performance of work.

This is to be distinguished from performance that requires the passing of property (transfer of title) in goods. Performance of a contract for the sale of goods involves the transfer of title rather than the performance of work. There may be a great deal of work required to facilitate the transfer of title. This work is done for the payee in pursuance of an undertaking to the payer to transfer title in goods, rather than work done for the payer (or another party) in pursuance of an undertaking to the payer to perform some work.

Whether a contract is for the sale of goods or not is determined by examining the substance of the contract.² For example, when a consumer purchases a custom-made lounge suite direct from the manufacturer, the substance of the contract is to transfer title in the goods to the consumer. The contract is for the sale of goods. The work that the manufacturer undertakes to create the item, while no doubt reflected in the price of the item, is done to enable the manufacturer to meet the obligation to transfer title in a lounge suite.

What is important is the primary objective of the contract. Where the primary objective of the contract is to transfer title in goods it is usually characterised as a contract for the sale of goods. Therefore, any payment made under the contract is beyond the scope of the term 'payment' for PPS purposes.

What is meant by 'performance of work'?

The term 'work' is a concept often identified with personal exertion or labour. To ensure that its interpretation is not limited to notions of physical labour, work is defined to specifically include:³

- services;
- work of a professional, technical, skilled or artistic kind;
- activities that consist of the performance or presentation by a person (or the participation by a person) in any music, play, dance, entertainment, address, sport, display, promotional activity, exhibition or any similar activity involving the exercise of intellectual, artistic, musical, physical or other personal skills or the performance of any services in connection with any such activity; and
- activities that consist of the performance of services by a person in, or in connection with, the making of any film, tape or disk or of a television or radio broadcast.

Work may be performed for another person through a contract of service (ie as a common law employee) or through a contract for services (ie as an independent contractor). However, the payment of salary or wages to an employee is excluded from the definition of payment. The payment of salary or wages to an employee is subject to the PAYE collection system, and can not be subject to PPS. Only those payments made under contracts for services (including contracts described as being for work and materials) come within the definition of 'payment' and may be prescribed for PPS purposes.

Contracts for work and materials

Whether a contract is for the sale of goods or for work and materials (in whole or in part involving the performance of work) is a question of fact and degree. All the terms of the contract must be viewed objectively to determine the substance of the contract. For example, an engineering firm may have a contract to service helicopters and ensure that safety standards are met. In the course of servicing the helicopters parts are provided and installed. The contract is predominantly for the performance of engineering services. The renewal of parts is incidental although an important feature of the obligations under the contract.⁴ Also, when a contract provides for the provision of services of a person together with the hire of equipment then a prescribed payment arises.⁵

Another example is where a manufacturer requests the development of plastic furniture drawers from an engineering company. According to the contract between the engineering company and the manufacturer, the engineering company must design and produce the mouldings of a drawer which will then be used for mass production. While the engineering firm must perform work to design and produce the mouldings it is incidental to performance of the contract which involves transfer of title in goods. The contract is for the sale of goods.⁶

When determining whether a contract is for the sale of goods or for work and materials you should consider all the terms of the contract to ascertain whether the substance of the contract is the transfer of title or hire of the goods or for providing skill and experience. Only payments made under those contracts properly characterised as being for work and materials are payments for PPS purposes. In these circumstances, all of the payments are subject to the PPS provisions.

Do you need more information?

If you have any questions or need more information, please contact the Tax Office

- by **a Fax from Tax**, our 24 hour fax information service. Simply call **13 28 60** (local call cost) on your phone or fax and follow the voice prompts
- at our **Internet** website, **ATOassist**, at **www.ato.gov.au**
- by phone on our national enquiry number **13 28 66** (local call cost)
- in person by visiting the enquiry counter at the Tax Office. Addresses are listed in *TaxPack* and the *White Pages* telephone directory.

Endnotes

1. *Income Tax Assessment Act 1936* subsection 221YHA(1)
2. *Robinson V Graves* [1935] 1 KB 579
3. *Income Tax Assessment Act 1936* subsection 221YHA(1)
4. *Helicopter Sales Pty Ltd V Rotorwork Pty Ltd* (1974) 132 CLR 1
5. *Case V129 88 ATC* 817
6. *Deta Nominees Pty Ltd V Viscount Plastic Products Pty Ltd* [1979] VR 167

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