

Global Employer Services (GES)

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## GES NewsFlash

# Australia — Increasing focus on employment tax and immigration requirements



May 19, 2014

### Overview

Over the past few months, Deloitte has seen the Australian Taxation Office (ATO), Department of Immigration and Citizenship, (DIAC) and the Offices of State Revenue (OSRs) focus on various employment tax and immigration requirements. Amongst numerous other ongoing compliance obligations, our clients are now seeing the practical flow-on implications of previously legislated superannuation reforms coming into play. They are increasingly recognizing tax and immigration risks associated with expatriate employees and are keen to mitigate penalties relating to inappropriately classified contractor arrangements. We also know that ESS reporting, despite having been a requirement since 2009, is still causing headaches prior to year-end.

To assist you in understanding the current state of play, we discuss each of these areas below and hope that our GES insights provide you with some key takeaways that may be relevant for your business.

### SG — Division 293 Notices

In the 2012 budget, Bill Shorten (then acting in his capacity as Minister for Financial Services and Superannuation) announced an intention to implement measures that created a “reduction of higher tax concession for contributions of very high income earners.” As a result, Division 293 tax of the Income Tax assessment Act 1997 (ITAA97) was introduced by the bill titled Tax and Superannuation Laws Amendment (Increased Concessional Contributions Cap and Other Measures) Act 2013, which received Royal Assent on 28 June 2013. The legislation was drafted to have retrospective application and, therefore, Division 293 tax can apply in respect of superannuation contributions made from 1 July 2012.

In January 2014, the ATO commenced issuing Division 293 tax notices of assessment in respect of superannuation contributions made within the year ended 30 June 2013. Given the complex nature of the legislative provisions, our clients have experienced various technical and administrative issues, which we address below.

### What is Division 293 tax?

Generally, concessional (pretax) contributions made to a superannuation fund are able to access a 30% concession from the top marginal rate of tax, bringing the effective tax rate on these contributions to 15% (i.e., 45% to 30%) within the fund. What Division 293 of the ITAA97 seeks to do is reduce this concession to 15%

where the contributions are made by a high-income earner.

In practice, this means that Division 293 tax is usually a reference to the additional 15% tax charged on 'taxable contributions' made for high-income earners. In this context, high-income earners are individuals who have income for surcharge purposes (disregarding reportable employer superannuation contributions) and 'low-tax contributions' greater than \$300,000.

Low-tax contributions are in essence the concessional contributions (including SG and salary sacrifice), less any contributions subject to excess contribution tax, plus contributions for defined benefit interests.

The Division 293 tax applies to the lesser of the low-tax contribution and the amount above the \$300,000 threshold.

## Assessment and payment

The ATO collates information from the individual's income tax return and their relevant superannuation fund (or funds). The amount of Division 293 tax is assessed by the ATO and will generally be due and payable within 21 days from the date the notice of assessment is issued by the ATO. Individuals are authorized to have amounts released from their superannuation benefits for the payment of Division 293 tax (or reimbursed if the individual has already paid the tax), but this must occur within 120 days of the date of issue of the notice of assessment. The due date for payment of the tax remains the date advised on the notice of assessment.

## Specific rules

There are specific rules for defined benefit interests (particularly in relation to determining the amount of the contribution for surcharge calculation purposes and when the surcharge needs to be paid), constitutionally protected state's higher-level office holders, certain commonwealth judicial officers, and temporary residents who depart Australia.

Individuals are entitled to a refund of any Division 293 tax paid if:

- They made a Division 293 tax payment,
- They received a Departing Australia Superannuation Payment (DASP), and
- They applied to the Commissioner of Taxation in the approved form for the refund.

The amount of the refund will be the sum of all payments made towards any Division 293 tax assessments an individual made while a temporary resident in Australia. However, if the individual becomes a permanent resident during an income year, and a payment is made towards a Division 293 tax liability in that income year, that payment will not be refunded.

### Deloitte's view

It has become clear in our interactions with the ATO that not all processes, forms, and technical positions relating to the Division 293 tax have been entirely formalized. This has been particularly evident in relation to the interaction between DASP provisions and the availability of refunds under Division 293.

Given this is the first year the Division 293 notice of assessments have been issued, we would recommend that employers consider:

- Whether their employee population is aware of these changes and, if not, how best to communicate the message effectively
- How the additional tax may increase the cost of employment, particularly where individuals are subject to tax-equalization arrangements
- What administrative processes have been implemented to assist in the payment of such liabilities

Deloitte will be monitoring the progress of these notices closely and, therefore, should you wish to confirm what impact Division 293 may have on your business, please do not hesitate to contact your local Deloitte representative for further information in relation to the Division 293 tax.

## SG contributions caps

The ATO has released the new indexed superannuation contribution caps that will apply from 1 July 2014.

In summary, the contribution caps will be as follows:

Year ending	Concessional contribution cap	Concessional contribution cap	Nonconcessional contributions cap	Three years bring-forward cap
	Under 50 years	50 years and over		
30 June 2015 and onwards	\$30,000	\$35,000	\$180,000	\$540,000

## Concessional contribution caps

The concessional contribution cap for the 2014–2015 income year will now be increased from \$25,000 to \$30,000.

The concessional contribution cap for an individual who is aged 49 years or over on 30 June 2014, remains at \$35,000 in the 2014–2015 income year. There is no indexation increase applied to this cap.

## Nonconcessional contribution caps

The following nonconcessional caps have also been increased:

- Annual nonconcessional contribution cap increases from \$150,000 to \$180,000.
- Nonconcessional contribution cap under the three years' bring-forward provision increases from \$450,000 to \$540,000.

### Deloitte's view

Due to these changes, existing contribution strategies may need to be revised to benefit fully from the increased contribution caps, particularly, the \$90,000 increase under the three years' bring-forward provision.

If the three years' bring forward is triggered in the 2014 income year, the three-year cap will remain at \$450,000 for the period 30 June 2016. The bring forward is triggered if more than \$150,000 of nonconcessional contributions are made.

Accordingly, for individuals who will be aged 64 or less at 1 July 2014, and who have not triggered the bring-forward provision in the 2012–2013 or 2013–2014 income years, consideration should be given to postponing the trigger event (i.e., not contributing more than \$150,000 in the 2013–14 income year) until 1 July 2014, at the earliest to take full advantage of the increased cap.

For individuals who turn 65 during the 2013–2014 income year, the trigger event for the three years' bring forward cannot be postponed beyond the 2014 income

year. Employers and employees should also be aware that existing salary sacrifice arrangements may need to be altered should the relevant individual intend to “top up” concessional contributions to fully utilize the concessional contributions cap.

## **PAYG variation**

Employers with employees who are on foreign payrolls have indicated that they find it administratively difficult to meet their PAYG withholding and remittance obligations within the set time periods. In recognition of this administrative burden, for many years, the ATO used its discretion to reduce to nil the PAYG withholding that needed to be remitted in respect of these employees where tax was paid by the employer upon assessment of the employee’s personal income tax return.

Of late, the ATO’s perception is that not all of the Australian income taxes due have been accounted for through the employees’ Australian income tax returns. Accordingly, the ATO has tightened the criteria relevant for determining whether such a PAYG withholding variation may be utilized.

## **Implications for current PAYG withholding variations**

The ATO will honor any existing PAYG withholding variations until 30 June 2014.

Furthermore, the ATO will accept PAYG withholding variation applications under the current provisions until 30 June 2014. This will be pertinent for employers who have employees on a foreign payroll who arrive in Australia before this tax year-end.

## **New PAYG withholding variations**

If an employer wishes to continue to have a nil withholding variation for payments to employees who are on a foreign payroll, the employer will need to apply for a new variation and provide a list of:

- All relevant employees’ names
- The tax file numbers of all relevant employees
- The countries of origin of all relevant employees

Employers are required to provide an update to the ATO of any additional relevant employees during the course of the applicable tax year. The ATO has indicated that they would expect an update to occur each time a new employee is added.

The new PAYG withholding variations will be valid for two years, after which, the employer will need to apply for a new variation.

## **No PAYG withholding variation**

In the absence of a PAYG withholding variation from 1 July 2014, the employer will be required to register for PAYG withholding by applying for a withholding payer number. Furthermore, the employer will be required to:

- Withhold taxes from the relevant employees,
- Report and remit the withheld taxes to the ATO,
- Provide the employees with a payment summary each tax year, and
- Lodge a payment summary annual report with the ATO by 14 August each tax year.

## **Alternative approach to meeting the employer PAYG obligation**

In order to meet their PAYG obligations, employers who have employees paid through a foreign payroll will generally operate a ‘shadow/mirror’ payroll. Under a shadow/mirror payroll arrangement, the employee’s pay is delivered through the home country payroll; the salary is then converted to Australian dollars and used to calculate the PAYG due and remittance is processed through the Australian payroll.

This approach is popular as it addresses the PAYG obligation on a current-year basis and simplifies the process of meeting the employer's other obligations (e.g., payroll tax, superannuation, and workers' compensation insurance). In addition, due to the availability of foreign tax credits, it can be a more tax-efficient approach for employers with U.S. employees.

#### Deloitte's view

The PAYG withholding variation is designed to reduce the administrative burden for employers in meeting their PAYG withholding obligations for employees on a foreign payroll and, at first glance, it looks like an attractive concession on the part of the ATO. At a minimum, it provides cover for employers, with employees on foreign payroll, should they be unable to meet the PAYG obligations, thereby reducing their exposure to penalties, including potential criminal prosecution of both the payer and relevant company directors.

That being said, the PAYG withholding variation does not alleviate the administrative burden associated with the employer's other obligations. Given that the information required and the process needed for meeting the employer's PAYG and other obligations are broadly the same, employers need to consider:

- Whether or not having to maintain two processes — one for PAYG and a second for their other employer obligations — is actually increasing their risk in failing to meet one or both obligations
- What is the additional administrative burden, if any, of operating a shadow payroll to simplify the process of meeting the employer's PAYG and other obligations and how can this additional burden be alleviated?
- How are you going to administratively track and ensure that all new employees subject to the variation are appropriately disclosed to the ATO?

Whether a PAYG variation is appropriate given a set assignee population needs to be determined on a case-by-case basis. As such, should you wish to proceed with an application/renewal, we would recommend that you contact your Deloitte representative.

#### 457 integrity review

Over recent years, there have been several major reforms to the subclass 457 visa program through the introduction of the Migration Legislation Amendment (Worker Protection Act) 2008, the Migration Amendment (Temporary Sponsored Visas) Act 2013, and changes to the Migration Regulations 1994.

The 457 visa program plays an important role in the Australian economy by allowing employers to fill temporary skill shortages. Given the importance of the program to business, the Government has announced a review with the following aims:

- Determine the level of noncompliance by sponsors in the subclass 457 program, both historically and under the current regulatory framework.
- Evaluate the regulatory framework of the subclass 457 program and determine whether the existing requirements appropriately balance a need to ensure the integrity of the program with potential costs to employers in accessing the program.
- Report on the scope for deregulation, while maintaining the integrity in the program.
- Review and advise on the current state of compliance and the appropriateness of existing sanctions.

The review will be conducted by an external panel appointed by the Assistant Minister for Immigration and Border Protection. Submissions addressing the terms of reference can be made up to the end of 30 April 2014.

#### Deloitte's view

Deloitte welcomes the 457 program review and the opportunity it provides to Australian businesses to participate in its further development.

Deloitte believes that the level of compliance of sponsors using the 457 program has been and continues to be high. A Senate hearing in May 2013 showed that out of approximately 29,100 active sponsors, only 170 sponsors had received formal sanctions for breaches. The level of noncompliance is low and this is an area of the program that receives undue focus.

It is in areas outside of compliance and sanctions that Deloitte believes the review should have the most impact. Issues, such as Labor Market Testing, the composition of the Consolidated Sponsored Occupations Lists, and the Temporary Skilled Migration Income Threshold (TSMIT), should have a strong focus in the review.

Deloitte is also strongly recommending the reintroduction of regional concessions for the 457 program. Employers in regional areas struggle with the TSMIT, especially those within the tourism, agribusiness, and aged and personal-care sectors. As growth industries identified in Deloitte's report positioning for prosperity? Catching the next wave, these industries are currently in a position where they are unable to access the program and ones that are facing urgent labor shortages.

## Contractors

Engaging contractors can be advantageous for employers as they can provide greater flexibility and often demand fewer entitlements than employees (e.g., leave), but this does not mean that they can be simply ignored when it comes to the spectrum of employer tax obligations.

In order to understand the relevant employment tax obligations, it is firstly important to understand the distinction between independent contractors and employees. The distinction is a matter of substance over form and it is not an uncommon scenario for a contractor's engagement conditions to be similar to those of the employer's ordinary employees. At the extreme end of the spectrum, this even includes 'sham arrangements,' whereby both parties have a common intention to disguise the actual nature of the arrangement. An example of this is an employee who terminates their employment to be immediately reengaged as a contractor subject to substantially identical conditions. Contractors found to be employees under common principles are likely to be subject to all employment tax obligations.

A common mistake with employers who engage contractors is a failure to consider whether the contractors will be "deemed employees." Deeming provisions are especially relevant for payroll tax, SG, and workers' compensation insurance purposes, and the application of each may vary considerably.

There are more and more instances of SG shortfalls for contractors who are deemed employees for SG purposes. Contractors are increasingly learning about their legislative entitlements, often by word of mouth from similar contractors, and are approaching employers asking for their superannuation entitlements. In some cases, contractors are approaching the ATO, who are obliged to investigate the matter, and are exposing employers to the risk of a wider audit.

Deloitte has found that many employers are also at risk when it comes to maintaining sufficient documentation and substantiating their positions. This may be as fundamental as keeping any accessible records of contractors engaged and extends to employers who have correctly applied the law, but their substantiation is lacking.

The OSRs are taking an increasingly aggressive approach to payroll tax positions that cannot be substantiated. Recent payroll tax audit activity has highlighted that the OSRs expect employers to have a far more in-depth understanding of the contractors they engage.

The key is to get in early and ensure that records are maintained in the first place.

Exercises, such as mock audits, are invaluable for employers to test their readiness for any revenue authority audits and identify areas for improvement.

#### Deloitte's view

Given that hundreds of employers were issued a "request for information" relating to contractors late last year, it is clear that this is, and will continue to be, a focus area for both the ATO and OSRs.

There is almost no question that, at some point, this issue will be raised within your organization and, when it is, you will want to be sure that all risks have been mitigated. In order to do this, employers may wish to:

- Review current human resource policies surrounding the engagement of contractors;
- Consider the contractors who have been 'on your books' for a significant period of time; and
- If you are using the ATO contractor decision tool, be aware that this will not necessarily provide a correct result for SG, payroll tax, or workers' compensation insurance. It is a guide, not a comprehensive analysis, and should only be used as such.

### ESS reporting

Broadly, the provider of an ESS interest (such as share awards and share options) is required to report any ESS income taxation events during the tax year. The taxation event is reported to the employee on an ESS statement by 14 July, and to the ATO on an ESS annual report by 14 August, following the 30 June year-end. This report may be prepared via paper or electronically.

### Who is an employee?

For these purposes, the term "employee" has a wide scope. It includes employees and associates of employees of both the company and its subsidiaries (including past and prospective employees). Individuals, such as directors, contractors, and consultants, may also be treated as employees for ESS purposes.

If an ESS interest has been provided to any of the above persons, and an ESS income taxation event has occurred during the tax year, then the provider is required to report ESS income for that person.

### Who is a provider?

An ESS provider can be a foreign headquartered company or an Australian company. For example:

- Where share awards/options are offered by a non-Australian-tax-resident company to employees of its Australian subsidiary, the foreign parent is considered to be the provider. The Australian subsidiary is not the provider.
- Where share awards/options are offered by a non-Australian-tax-resident company to its mobile employees who have an Australian service period, the foreign parent is considered to be the provider.
- Where share awards/options are offered by an Australian-tax-resident company to its own employees or employees of its Australian subsidiaries, the Australian company is the provider.

### Recent changes indicating an ATO focus on "foreign providers"

Many non-Australian-based parent companies are still not meeting their ESS reporting obligations in Australia. The Australian subsidiary is often not aware of the ESS interests awarded by the non-Australian-based parent company to employees now living and working in Australia. Therefore, the ATO has increased its scrutiny surrounding the compliance of foreign providers with ESS reporting obligations. This has been demonstrated by a number of recent changes:



- The ESS annual report paper form has been updated to contain a tick box for companies that do not have an Australian Business Number (ABN) (i.e., foreign companies).
- The ATO's electronic ESS Bulk Load Excel Spreadsheet allows for the ABN field to be completed with a zero if an overseas address is entered (intended for foreign companies).
- The ATO has ensured that its website and communications refer to the "provider" rather than "employer" where ESS reporting is concerned.

## Sourcing for mobile employees

In 2013, the ATO also released an announcement clarifying its position in respect of participants who are taxable only on a portion of the gain in Australia as a result of being resident in another country during the life of the award.

Where the provider is able to calculate the portion of the gain assessable to a mobile employee, the provider should report the actual assessable amount of the gain (after taking into account foreign service).

If the actual amount cannot be reported by the due date, the provider should:

- Report the gross amount by the due date, and
- When known, report the actual amount on an amended ESS statement to the employee and an amended ESS annual report to the ATO.

Providers should ensure that they report the actual assessable amount (taking into account any period of foreign service) where possible. This will avoid mismatches arising when the ATO subsequently compares data from ESS annual reports with employees' tax returns.

### Deloitte's view

Companies should determine who the provider is for the purposes of ESS reporting and ensure that ESS reporting is carried out correctly and on an annual basis.

If there have been failures to report ESS taxable events, a provider should, within 30 days, issue ESS statements to employees and lodge any outstanding ESS annual reports with the ATO. If there are changes to or omissions in any information previously provided either to employees or the ATO, then the provider should amend the ESS statements and ESS annual reports.

Companies should ensure that their systems for completing the ESS reporting in Australia are adequate. If you need any assistance with this or if you would like to receive information about Deloitte's automated tool for ESS reporting, your Deloitte contact would be pleased to help you.

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