



www.contractworld.com.au
office@contractworld.com.au
ABN: 54 403 453 626

General Manager
Superannuation, Retirement and Savings Division
The Treasury
Langton Crescent
Parkes ACT 2600

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Submitted by email: simplersuper@treasury.gov.au

Please find attached a submission from Independent Contractors of Australia (ICA) on the plan to simplify and streamline superannuation. For information on ICA, please see Attachment A to our submission.

We are grateful for the opportunity to make a submission and appreciate the time that has been given to allow for genuine consultation on this important issue. We agree to the submission being treated as public, with full publication on your website. We will be making the submission available on our own website immediately. (<http://www.contractworld.com.au>).

Should you wish to discuss any of the matters raised, please contact our chairman, Angela MacRae (contact details outlined below).

Angela MacRae
Chairman
Independent Contractors of Australia
Ph/fax: 03 9859 9620
Mob: 0425 708 945
Email: angela@macraedxa.net

1. General comment

The proposals raised in the plan to simplify and streamline superannuation ('the Plan') are strongly supported by ICA, though we consider that in some areas the proposals do not go far enough. We see simplicity being the major benefit in the proposals as they stand. We strongly favour the maintenance of that simplicity. The only suggestions we make in our submission would add further measures to streamline and simplify the rules for superannuation.

For many years, policy-making in the superannuation arena has focused almost entirely on equity measures that have led to an unwieldy and complex system. That complexity has had the perverse effect of contributing to inequity—particularly for unsophisticated taxpayers. We strongly endorse the approach taken in the Plan to cut through much of the complexity.

We consider that there is a high risk that many submissions may lose sight of the ultimate objective of simplifying the rules for superannuation and will call for a myriad of changes that will reintroduce complexity into the system. We would urge the Government to strongly resist such calls and remain focused on the ultimate goal of a simpler superannuation regime. Already, the rules have been complicated in response to lobbying on the original proposals (for example, the way the rules work for the three year 'averaging' on post-tax contributions is unnecessarily complex—particularly in the application of the work test for those who make 'bring forward' contributions and then retire).

From the perspective of contractors, we believe that one of the major hurdles to greater self-provision of retirement income is the complexity (and associated cost to secure competent financial advice) of the existing superannuation arrangements. If the rules can be genuinely simplified and streamlined, this should go a long way to encouraging greater participation in superannuation by many contractors.

Key points:

- ICA strongly supports the measures proposed in the Plan, but considers further simplification can be made.
- ICA stresses that simplicity should be the main goal of the Plan—submissions calling for more complex rules should be resisted at all costs.

2. Giving the self-employed a level playing field

While ICA supports the measures proposed in the Plan as a whole, we particularly emphasise our endorsement of the proposal to allow for the full deductibility of contributions made by the self-employed. Independent contractors are, by definition, self-employed. We consider that the existing treatment of self-employed contributions discriminates against the self-employed. Reform in this area is long overdue.

The existing restrictions on the deductibility of contributions by the self-employed is especially galling when this is one group that needs the most incentive to provide for their own retirement. The self-employed are less likely than employees to be covered by the compulsory superannuation arrangements (though some contractors are covered for some contracts for super guarantee purposes) and there is good evidence

to suggest that many self-employed people plough all their resources into their business. While this may provide a good outcome for some, it does not allow for the diversification into superannuation that makes good sense from a financial perspective.

We also strongly endorse the extension of the government co-contribution to the self-employed. This will remove another feature of the current system that discriminates against the self-employed.

In short, allowing the self-employed the same access to deductibility of contributions that can be accessed by employees, and to the co-contribution, is strongly endorsed.

However, this measure does not go far enough. A barrier to the participation of contractors in superannuation remains. Apparently, the non-deductibility of contributions made by those self-employed people whose employment income is more than 10 per cent of their total income is to be retained (the so-called 'self-employed' rule). We can see no good reason for the retention of the 'self-employed' rule:

- We have been unable to establish any policy basis for this restriction on contributions by the self-employed—to retain such bias against the self-employed is inconsistent with other recent initiatives taken by the Government to protect them, such as the Independent Contractors Act.
- Under the proposed arrangements, there is a cap of \$50,000 per annum on pre-tax contributions for those people who are either fully employed, or fully self-employed—there is no reason why this cap would not work equally well to provide a sufficient limit on pre-tax contributions by those with a mix of employment and self-employment.
- The rule appears little more than arbitrary—why 10 per cent?
- The self-employed rule can create perverse outcomes that could not possibly be consistent with the intent of the restriction. For example, it is a well known strategy under the existing rules for an employed person who can so arrange their affairs to take a minimal wage, salary sacrifice the balance of their salary directly to super, and get a deduction for a personal contribution as well (provided they have sufficient investment income to ensure that their wage is less than 10 per cent of their total income). Hence, they can get a deduction for personal contributions, even though they are not self-employed at all. Hence, employed people have exploited the 'self-employed' rule, while many genuine contractors have been denied a deduction in circumstances which would make a deduction far more reasonable than the case just described.
- The self-employed rule adds complexity to the system—especially for those contractors that may not know what their mix of employment/contract work will be until the end of the year.
- The rule undermines the attractiveness of contributions by the self-employed—a group at risk of making inadequate superannuation provision because of lower super guarantee coverage and a tendency to put all their eggs in one basket—their business.

Should the government wish to restrict access to deductible contributions to those who maintain a link with the workforce, it would be simpler, more consistent and

more equitable to use the proposed eligibility criteria for the co-contribution—that is, they must earn 10 per cent or more of their income from carrying on a business, eligible employment or a combination of both.

Key points:

- ICA strongly endorses the proposal to make contributions by the self-employed fully deductible and to give the self-employed access to the government co-contribution.
- To further simplify the system, and to provide policy consistency, ICA considers the current restriction on the deductibility of contributions by the self-employed who earn more than 10 per cent of their income from employment should be abolished.
- If necessary, a simpler and fairer rule could be introduced to replace the ‘self-employed’ rule. The rule could match the proposed co-contribution criteria—that is, they must earn 10 per cent or more of their income from carrying on a business, eligible employment or a combination of both.

3. Further simplifying the rules for contractors

While potentially outside the scope of the Plan, ICA would also like to suggest a further simplification to the superannuation regime for contractors. We strongly endorse the proposal made by the Taskforce on Reducing the Regulatory Burdens on Business to align the definitions of ‘employee’ and ‘contractor’ for PAYG withholding purposes and superannuation guarantee purposes. An excerpt from the Taskforce Report, *Rethinking Regulation*, supporting this proposal, is at Attachment B.

Key point:

- ICA would like to see the definitions of ‘employee’ and ‘contractor’ aligned for PAYG withholding purposes and superannuation guarantee purposes.

4. Conclusion

ICA supports the measures outlined in the Plan, particularly the proposed full deductibility of contributions by the self-employed and access by the self-employed to the government co-contribution.

However, to further simplify the rules and to take this proposal to its logical policy conclusion, the existing restriction on contributions by the self-employed who earn more than 10 per cent of their income from employment should be abolished. If necessary, this ‘self-employed’ rule could be replaced with criteria matching those for the co-contribution—that is, they must earn 10 per cent or more of their income from carrying on a business, eligible employment or a combination of both.

Further, greater simplicity would be achieved by aligning the definitions of ‘employee’ and ‘contractor’ for PAYG withholding purposes and superannuation guarantee purposes.

Finally, we see great merit in the simplicity offered by the proposals in the Plan. Any consideration of changes to the proposals should make the creation of further simplicity paramount. To ensure this, we strongly urge that any changes be subject to the good regulation-making process that the Government has recently accepted following recommendations from the Taskforce on Reducing the Regulatory Burdens on Business. We stress, in particular, that the range of feasible policy options needs to be assessed within a cost-benefit framework—including analysis of compliance costs, and that only the option that generates the greatest net benefit for the community, taking into account all the impacts, should be adopted.

We also want to acknowledge that we appreciate the opportunity to make this submission and stress that there needs to be effective consultation at all of the key stages as these major reform options proceed to legislation and implementation.

Attachment A Independent Contractors of Australia Background

ICA is the first (and probably only) organisation in Australia exclusively dedicated to the interests and rights of independent contractors.

ICA was formed in July 2001 and incorporated as a non-profit organisation under the South Australian *Associations Incorporation Act*. ICA has three principal aims:

- 1) To conduct education campaigns to assist independent contractors and the community at large to understand the legitimate status of independent contractors and the important issues relating to them.
- 2) To act as a network for industries structured around or dependent upon independent contractors.
- 3) To lobby for the rights of independent contractors.

ICA operates through its Website at www.contractworld.com.au.

ICA is truly a 'virtual' organization. Through its Website:

- The public can access significant quantities of information about independent contracting, including submissions made by ICA to government reviews.
- People can subscribe (\$50 per year) and access the 'subscribers only' section of the site, where core legal, tax and other information is stored.
- Subscribers can engage in discussion on independent contractor issues and have policy input.
- Subscribers and interested registered persons can receive regular e-mail alerts on independent contractor issues.

The ICA committee is drawn from across Australia with representatives from a range of industries including farming, IT, housing/construction, transport, labour hire and others.

ICA came into existence in response to the needs of the 28 per cent of the private-sector workforce who work but are not employed. ICA is dedicated to exploring the issues and interests of this significant, growing, but largely unrepresented sector of the working population.

Attachment B

(From *Rethinking Regulation* by the Taskforce on Reducing the Regulatory Burdens on Business)

Definition of employee

The Taskforce considers that the definitions of 'employee' and 'contractor' should be aligned for PAYG withholding purposes and superannuation guarantee purposes. The definitional boundary between employee and contractor was a common issue raised by business.

Under the superannuation guarantee legislation, the definition of employee includes a person engaged under a contract where more than half the value of the contract is for the person's labour (although the rule does not apply if the contractor is engaged to produce a result or is free to engage other people to perform the work). There is almost certainly a high level of non-compliance with this aspect of the law as many employers are not aware that contractors should be covered in this way.

A lady ... a genuine operator ... hadn't appreciated there was actually a different definition when it came to superannuation and she hadn't been paying approximately \$30 000 worth to staff. She was horrified. She was a genuine player who went to all the courses ... so that definitional thing is quite an issue.

Steve Jamieson, Business Enterprise Centres Australia, at the Small Business Roundtable, November 2005

Most employers are well aware of their PAYG withholding obligations, so aligning the PAYG and superannuation guarantee definitions of employee would reduce compliance costs and also help to overcome the problem of unwitting non-compliance.

Altering the superannuation guarantee definition would mean that some contractors currently covered would fall outside the system. But the impact would be relatively small because:

- there is probably a high level of non-compliance with the existing rules; and
- only unincorporated contractors would be affected, as those who are incorporated would be employees of their own company, and so caught by the superannuation guarantee rules.

Redefining the term 'employee' for the purposes of the superannuation guarantee may also remove a barrier to using independent unincorporated contractors (currently some larger companies may not take on unincorporated contractors because of superannuation guarantee and other liabilities).

Recommendation 5.44

The Australian Government should align the definitions of 'employee' and 'contractor' used for superannuation guarantee and PAYG withholding purposes.