

**INQUIRY INTO APPLICATION OF THE CONTRACTOR
AND EMPLOYMENT AGENT PROVISIONS IN THE
PAYROLL TAX ACT 2007**

Organisation: NSW Small Business Commissioner
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The Hon. Jeremy Buckingham, MLC
Chair – Portfolio Committee No.1 – Premier and Finance
Inquiry into the application of the contractor and employment
agent provisions in the Payroll Tax Act 2007
Legislative Council
Parliament of NSW

By online submission: [Lodge a Submission](#)

Dear Chair

Thank you for the opportunity to make a submission to the Portfolio Committee No.1 - Premier and Finance in relation to its Inquiry into the *Application of the contractor and employment agent provisions in the Payroll Tax Act 2007*, self-referred by the Committee on 26 November 2024.

The NSW Small Business Commissioner (the Commission) is an independent statutory office of the NSW Government. It provides strategic advice, advocacy, and affordable dispute resolution services across NSW.

As the Committee would be aware, small businesses are generally exempt from payroll tax, either because they fall below the threshold or because payments made to them under bona fide arrangements qualify for a relevant contractor exemption. However, the Commission is aware of circumstances where some small businesses may be concerned about potential obligations or impacts arising from the contractor provisions of the *Payroll Tax Act 2007* (the Act).

Representations from small businesses to the Commission indicate ambiguity and confusion around interpreting and applying the contractor provisions of the Act. Recent court decisions have clarified how these provisions apply to certain arrangements, including those involving small businesses. However, the Commission is aware that some stakeholders remain concerned about whether current arrangements align with policy intent because they may capture service contracts involving small businesses in a manner perceived to be inconsistent with the broader exemptions of the Act.

The Commission recognises the importance of appropriate safeguards to prevent illegitimate contractual arrangements designed solely to avoid tax obligations. However, the Commission supports the principle of exempting small businesses from the payroll tax system; a principle which is mostly embodied in existing legislation through both the payroll tax threshold and contractor exemptions.

The Commission welcomes review of the legislation and its administration to ensure it does not inadvertently capture arrangements the community considers ought not be subject to payroll tax, especially where it discourages efficient and innovative business models that improve productivity.

‘Relevant contracts’ and exemptions

The contractor provisions were introduced to address tax avoidance strategies where several types of contractor arrangements were used to disguise an employer-employee relationship for the purposes of avoiding payroll tax. The legislature took a broad approach to defining ‘relevant contract’ expansively,

with specific exclusions which were intended to catch genuine independent contractor relationships.¹ The effect of the contractor provisions was to impose payroll tax on payments to contractors who work predominantly or exclusively for a single entity, where the primary purpose of the contract is to secure the contractor's labour.

The definition of a "relevant contract" in the Act has remained largely unchanged for the past forty years, despite significant shifts in business models and contractor engagement practices. While minor amendments have been made, primarily to narrow the scope of exemptions by removing industry-specific exclusions or imposing stricter qualifying criteria, the provisions have arguably not kept pace with modern business structures. Since the provisions were first introduced, only one new exemption has been added, specifically for owner-drivers, highlighting the limited adaptability of the framework to evolving work arrangements and contemporary contractor relationships.

The Act's definition of a "relevant contract" encompasses most service contracts by default. Specific exemptions are outlined to determine whether a contractor is operating as a genuine independent business. However, these exemptions do not universally exempt service contracts involving legitimate independent contractors, and contracts can be liable for payroll tax where they do not satisfy the criteria.

This issue was highlighted in the case of *Loan Market Group Pty Ltd v Chief Commissioner of State Revenue* [2024] NSWSC 390. In this case, the NSW Supreme Court ruled that agreements between Loan Market and its brokers constituted "relevant contracts" under the Act, making the company liable for payroll tax on commissions paid to its brokers. The court acknowledged that the legislation's broad drafting captured genuinely independent businesses, leading to outcomes that could be considered "harsh."

Impact of NSW Court decisions

The Commission understands there is broad concern about how recent NSW Supreme Court decisions² may impact modern business models, particularly tripartite structures. These structures often involve intermediaries that connect contractors with end-users while also handling payment processing on behalf of contractors. Although these arrangements primarily engage genuine independent contractors, they often fail to meet the strict exemption criteria, resulting in unforeseen payroll tax liabilities.

These business models are especially prevalent in industries reliant on specialised contract labour, such as healthcare and financial services. In the growing on-demand economy, many platform-based enterprises have adopted this approach to form contractual partnerships with self-employed gig workers. The rise of digital technologies, evolving regulatory requirements, and the need for operational efficiency has driven the expansion of these commercial frameworks.

From the perspective of small businesses, these arrangements exist to reduce transaction costs (such as the costs of contracting, payment processing, and compliance) and are not artificially structured to avoid tax liabilities.

The Commission notes the NSW Government introduced a Bulk Billing Support Initiative to provide a payroll tax rebate for bulk billing general practitioners in medical centres. This followed court decisions finding arrangements of this nature were liable for payroll tax.

¹ *Bridges Financial Services* at [218]-[219]; *Downer EDI Engineering Pty Ltd v Chief Commissioner of State Revenue* [2019] NSWSC 743 at [101]-[110].

² *Bridges Financial Services Pty Ltd v Chief Commissioner of State Revenue* [2005] NSWSC 788; *Thomas and Naaz Pty Ltd v Chief Commissioner of State Revenue* [2021] NSWCATAD 259; and *Loan Market Group Pty Ltd v Chief Commissioner of State Revenue* [2024] NSWSC 390.

Feedback from businesses

The Commission regularly surveys NSW small businesses on matters affecting their performance and operations. In December 2024 and January 2025, the Commission surveyed businesses³ who provide administrative and financial services to small businesses, seeking feedback on the application of the contractor and employment agent provisions in the Act.

Of these businesses that assist in managing payroll tax obligations, one in four respondents (26 per cent) reported difficulty in determining whether a contractor payment is 'for the performance of work' and therefore, subject to the contractor provisions of the Act.⁴

Respondents who answered 'yes' to experiencing difficulties were invited to describe their experiences. A summary of feedback is provided below.

- **Complexity and uncertainty** - The rules governing payroll tax and contractor versus employee distinctions are seen as complex and unclear. Respondents referred to what were perceived as "grey areas" and expressed difficulty understanding the exemption categories. Comments also highlighted that the provisions have not considered or kept pace with the changing nature of business activities in specific industries.
- **Need for simplicity** – Respondents called for simplification of the rules, with suggestions for clearer, more straightforward approaches to reducing the burden of determining contractor status and tax obligations.
- **Guidance** – Respondents suggested opportunities to improve guidance and a perception of inconsistent advice from official sources, adding to the confusion and lack of clarity.
- **Impact on business operations** - The administrative burden and potential financial risks associated with misclassification or non-compliance are highlighted as significant concerns for business owners. The perceived complexity and risk lead to higher operational costs as businesses may over-comply to avoid potential penalties.
- **Demand for tools and reforms** - Respondents suggest the need for tools such as a definitive calculator to help determine contractor status more easily. Calls for tax reform at both state and federal levels indicated a desire for an overhaul of the taxation framework to ease the burden on businesses.

Administrative burden and potential for over-taxation

The survey also explored the challenges businesses face in determining payroll tax liabilities for contractor payments, particularly when proving exemption status is difficult or time-consuming. Survey feedback suggests proving the exemptions can be difficult, even when they may meet the requirements of a relevant exemption, such that they default to treating contractor payments as taxable rather than risk non-compliance.

The Commission recognises that this can be a concern for small businesses, particularly where the payroll tax liability is passed onto them either directly through contractual arrangements or indirectly through reduced capacity for them to be paid for their services. One in four respondents that assist in managing payroll tax obligations (24 per cent) reported observing cases where businesses treated

³ Survey respondents by industry: Professional, Scientific and Technical Services 52 per cent; Financial and Insurance Services 32 per cent; and Administrative and Support Services 16 per cent.

⁴ 260 respondents in total, with 155 respondents indicating they support other businesses to manage their payroll tax obligations or handle payroll taxes for their own business.

contractor payments as taxable without considering an exemption and subsequently passed the payroll tax liability onto the contractor.

Effectiveness of the exemptions

When questioned about the effectiveness of the current contractor exemptions, some respondents found exemptions useful, while others found them difficult to apply, ambiguous, or ineffective. Common challenges reported include:

- Ambiguity in definitions leading to inconsistent interpretation.
- Difficulty obtaining documentation from contractors to prove exemptions.
- The exemptions fail to apply to many businesses that should qualify.
- Inconsistent interpretation by auditors.

Many survey respondents conveyed significant difficulties in determining whether contractor payments qualify for payroll tax exemptions, largely due to limited visibility into a contractor's business operations. Respondents highlighted challenges in verifying whether contractors serve multiple clients or employ staff, making it impractical to prove exemptions.

To address these issues, some respondents suggested there should be more streamlined ways for contractors to support the hiring business in determining eligibility for an exemption. Additionally, there were calls to expand exemptions to automatically capture contractors that meet predefined criteria, including the development of a centralised online verification system, similar to the Australian Business Register (ABR), to streamline the exemption process.

A summary of feedback is provided in relation to the contractor exemptions is provided below:

- **Services not ordinarily required for your business** – Some respondents highlighted confusion around what qualifies as "ordinary for business" and uncertainty in cases where services are essential within a business. One respondent noted that many clients likely overpay due to this uncertainty, opting to pay when in doubt.
- **Services required for less than 180 days during the financial year** - Respondents found the 180-day exemption difficult to track, particularly in cases where service needs are unpredictable. Many noted confusion when interpreting the exemption alongside the 90-day rule, with discrepancies between how the law is written and how it is interpreted. Some expressed concerns about its application to IT, repairs, and delivery services, while others found it challenging to determine eligibility. Overall, tracking and clarity were the main issues.
- **Services provided for 90 days or less** - Most respondents found tracking the 90-day exemption onerous as service frequency is often uncertain and hard to anticipate. Feedback found the 90-day threshold arbitrary not reflecting realistic timelines for contemporary projects. Some indicated confusion around the rules, while others reported working with Revenue NSW to clarify their position.
- **Services performed by two or more people** – Few respondents reported administrative challenges associated with the exemption for services performed by two or more people. However, some noted challenges in knowing if multiple individuals are involved, as contractors do not always disclose this information.

Services provided by an owner driver – Few respondents reported challenges with the owner-driver exemption, but some found it difficult to determine whether an owner-driver was involved, as this information is not always clear on invoices.

Contractor who works for the public generally in the financial year – Some respondents noted that clients typically assume contractors meet this criterion without proper verification and that it is difficult to determine the extent of a contractor's client base. Respondents expressed the view that the evidence to support this exemption is not readily available and typically held by the contractor who may not wish to disclose it due to commercial sensitivities. This creates significant uncertainty under a taxing provision that relies on such evidence.

Review and reform

There is merit in ongoing review of the Act to ensure it continues to meet legislative intent in light of recent developments and the Commission welcomes this inquiry as a first step.

The Commission does not have specific recommendations in relation to the Act, however encourages consideration of different approaches to ensure small businesses are not unintentionally captured as new and innovative business models emerge.

The Commission notes that in 2018, the NSW Productivity Commissioner undertook a review of payroll tax administration in NSW. The purpose of the Review was to identify options to reduce the costs employers face in meeting NSW payroll tax obligations. That review noted some of the same challenges considered in this submission.⁵ The Commission would welcome deeper analysis to further explore whether existing arrangements could be streamlined.

The Commission notes the terms of reference for this inquiry do not explicitly seek feedback on the payroll tax threshold, rate or broader opportunities for tax reform. However, the Commission notes general sentiments from survey respondents which indicate that payroll tax is widely seen as a disincentive to business growth and a tax that penalises employment, with many advocating for its abolition or reform.

Thank you for the opportunity to make a submission. If you require further information, please contact my Executive Officer, Megan Bennett, at either _____ or _____

Yours sincerely

Mark Frost
Acting Commissioner
NSW Small Business Commission

Date: 07-02-2025

⁵ Pages 17-20, <https://www.productivity.nsw.gov.au/sites/default/files/2022-04/NSW-PC-to-Treasurer-Review-of-payroll-tax-administration.pdf>