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ACCOUNTANTS & ADVISERS

NEWS UPDATE

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What makes or breaks Christmas?

The cost of living has eased over the past year but consumers are still under pressure. For business, planning is the key to managing Christmas volatility.

The countdown to Christmas is on and we're in the midst of a headlong rush to maximise any remaining opportunities before the Christmas lull. Busy period or not, Christmas causes a period of dislocation and volatility for most businesses. The result is that it is not 'business as usual' and for many, volatility can create problems.

Added to this dislocation are cost of living pressures impacting consumers. Employee households are the hardest hit experiencing mortgage cost fuelled increases – spiked by the rollover of fixed rate loans to higher variable rate loans. While there has been some relief from energy subsidies and a reduction in fuel prices, underlying inflation remains persistently above the RBA's target rate. Services inflation - the cost of your rent, insurance, your hairdresser, etc. – is sitting at around 5%. With the Reserve Bank of Australia (RBA) Board keeping rates on hold for now and hinting that it will be some time yet before they are comfortable reducing rates, consumers want a reason to spend based on value for money. The irony is that if we all

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spend up big, which a recent Roy Morgan poll suggests we are, there is a risk this elevated spending will further delay rate cuts. But, while we might spend more, some of this increase is simply to compensate for inflation - we need to spend more to buy at the same level as previous years.

The discounting trend

Consumers expect a bargain and can generally find one. If you choose to discount stock (or the market forces you to), it's essential to know your profit margins to determine what you can afford to give away. A business with a 20% gross profit margin that offers a 15% discount, needs a 300% increase in sales volume simply to maintain the same position. Worst case scenario is that a business trades below its breakeven point and generates losses.

Increased sales from discounting can be great if you know your numbers, have excess or older stock that needs to be moved, generates demand, or drives new customers to you.

Also think about how you create value; it does not always have to be a direct discount on a product. Packaging might be a better option than a straight discount where you can increase sales of multiple items, even better if you can combine higher demand with lower demand stock. Quantity discounts, value added are also options.

The Christmas cost hangover

Costs tend to go up over Christmas. More staff, lower efficiency, downtime from non-trading days, increased promotional costs, all mean that the cost of doing business increases. It's great to get into the Christmas spirit as long as you don't end up with a New Year hangover. Cost control is important.

Many businesses also bring in casual staff. It's essential that you pay staff at the correct rates and meet your Superannuation Guarantee obligations.

Check the pay calculator to make sure you have it right.

New Year cashflow crunch

The New Year often leads into a quieter trading and tighter cashflow period. The March quarter is often the toughest cashflow quarter of the year. You will need a cash buffer. Don't over commit yourself in the run up to the end of the year and start the new Year with a problem.

Take a lesson from Scrooge

If you work with account customers, start your debtor follow up early. If your customers are under cashflow pressure, the Christmas period will only exacerbate it. The creditors that chase debt hard and early will get paid first. Don't be the last supplier on the list; the bucket might be empty by then.

Christmas is a great time of year. Just don't get caught up in the rush and forget about the basics.

Trading stock headaches

If business activity spikes over the Christmas period and you sell goods, then there is a temptation to increase stock levels. That makes sense as long as you don't go too far. Too much stock post the Christmas period and you will either be carrying product that is out of season, or you will have too much cash tied up in trading stock. Try to work with suppliers that can supply on short notice.

Managing your trading stock is not just about managing cost. If your customers are in your store but can't find what they need, have an online option available in store to take the sale.

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When overseas workers are Australian employees

The Fair Work Commission has determined that a Philippines based "independent contractor" was an employee unfairly dismissed by her Australian employer.

Like us, you are probably curious how a foreign national living in the Philippines, who had an 'independent contractors' agreement with an Australian company, could be classified as an Australian employee by the Fair Work Commission?

The recent case of *Ms Joanna Pascua v Doessel Group Pty Ltd* highlights just some of the issues Australian businesses face when working with overseas contractors and staff.

What underpinned the Fair Work decision?

Ms Pascua worked under contract as a legal assistant, investigating credit claims on clients' behalf, for a specialist credit repair legal firm based in Queensland between 21 July 2022 until 20 March 2024. She worked from home in the Philippines, using her own computer, a firm email address and a PBX phone system that gave the appearance that she was calling from the legal office.

The contract described the relationship as one of an independent contractor, with the standard clauses that the firm will not be liable for any other benefits or remuneration other than what was specified and that the firm was not liable for taxes, worker's compensation, unemployment insurance, employer's liability, social security or other entitlements. Ms Pascua also bore a liability in the event that something went awry with her work.

For her work, Ms Pascua was paid "AUD$18 per hour Salary all inclusive as a Full Time Employee," capped at 8 hours per day, 5 days per week, excluding breaks. While working with the firm, Ms Pascua used a firm supplied pro forma invoice to bill 83 weekly invoices at the full hours allowable and 28 other invoices for lesser amounts when she worked less than 40 hours in the week.

For the first 12 months of her time with the legal firm she was supervised by a solicitor. Within 12 months, her work was unsupervised, and in the last 7 months of the relationship, she was the only person conducting investigative work.

Underpinning the Fair Work Commission's decision were the recent High Court cases that changed the way in which disputes over the nature of employment relationships are determined (*CFMMEU v. Personnel Contracting Pty Ltd* and *ZG Operations Pty Ltd and Jamsek).* Whereas once the courts looked at the substance of the overall arrangement (let's call it the 'if it walks like a duck and talks like a duck, then it's a duck' principal), now greater weight is given to the contract, with reference to the rights and duties created by that contract.

To determine this case, the FWC stepped through the contract clause by clause to evaluate whether it suggested an employment or independent contractor relationship, and looked at how these clauses were brought into effect.

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In this case, on weight, the FWC determined Ms Pascua was an employee because the contract indicated that Ms Pascua was required to perform work "in the business of another", instead of for her own enterprise. The contract suggested that:

- Despite being described as a paralegal, she did not appear to be working in a distinct profession, trade or distinct calling. Her contract outlined administrative tasks and ad hoc duties.
- The contract did not enable her to assign the work to another.
- While there were daily targets in the contract – a result that she was expected to achieve – these tasks referenced weekly requirements and often could be carried over, suggesting ongoing work.
- There was a level of control exerted by the legal firm over how Ms Pascua performed her work that suggests she was not running her own enterprise – the PBX phone system, the email address, the level of direction in the tasks to be performed in the daily instruction she received.
- Despite being invoiced by Ms Pascua, the hourly rate described in the contract was that of a full-time employee, and the invoices were to be forwarded weekly for the previous week's work. The FWC also noted that the most likely rate for Ms Pascua as an employee would be $30.95 per hour (the casual rate for level 2 legal clerical work). To this, the FWC noted that genuine independent contractors would normally specify a fee that was greater, not less, than the minimum wage.

The FWC found that the description of the arrangement as that of independent contractor belied the actual nature of the contract.

When it came to the clauses excluding matters such as the payment of income tax, workers compensation, annual and personal leave relied on by the legal firm as confirmation of an independent contractor arrangement, the FWC referred to the *Deliveroo Australia Pty Ltd v Diego Franco* case and others. That is, the FWC considers, "the statements in the contract about meeting the obligations consequent upon the labelling of the arrangement as one of independent contractor to have little weight in determining the true nature of the relationship."

The new definition of *employee* and *employer*

In August 2024, a new definition of what is an employee and employer came into effect in the Fair Work Act. This new definition extends the High Court's decision in *CFMMEU v. Personnel Contracting Pty Ltd* and *ZG Operations Pty Ltd and Jamsek* to rely on the *nature* of the contract between the parties, not just what the contract says. The intent of the legislative change appears to be to ensure that clever drafting of a contract alone will not be sufficient to define an independent contractor arrangement.

The Fair Work Act now requires that the true relationship between the parties is, "determined by ascertaining the real substance, practical reality and true nature of the relationship between the individual and the person." The totality of the relationship needs to be considered including how the contract is performed in practice.

What does this decision mean for employers?

The FWC's decision in *Ms Joanna Pascua v Doessel Group Pty Ltd* highlights how cautious employers should be about the nature of employment relationships. Just because you label an arrangement as that of an independent contractor, does not mean it is. And if you get it wrong, beyond the industrial relations impact, you might be liable for the tax, payroll tax and workers compensation payments that should have been made.

What makes this decision unusual is how an international employment arrangement can be drawn into the national workplace system. Regardless of the geographic location of an employee, if your business is an Australian national system employer (bound by the Fair Work Act), and the individual is deemed to be an employee, the same rights and obligations may apply to that employee as to other employees located in Australia.

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While not addressed in this case, the FWC also referred to the minimum wage for a paralegal performing work such as that undertaken by Ms Pascua. While not applicable to this case, from 1 January 2025, wage theft will become a criminal offence - where an employer is required to pay an amount to an employee but intentionally underpays. For international employees where rates might be significantly different to Australian expectations, it is more important than ever to ensure you have characterised the employment relationship correctly.

Tax obligations and international workers

We're often asked about the implications of working with overseas, non-resident workers who are working for a resident Australian company.

Let's say you want to engage the services of a non-resident individual.

Contactor or employee?

The first step is to ensure that the arrangement is correctly classified. As we have seen from the *Ms Joanna Pascua v Doessel Group Pty Ltd* case, this really depends on the specific situation. From a tax perspective, the ATO has outlined their guidance in Employee or independent contractor, but you might need specific advice if you are uncertain.

Implications of an employment relationship

If the worker is classified as an employee and they are a non-resident for Australian tax purposes, then they should only be taxed in Australia on income that has an Australian source. However, you need to check whether a double tax agreement (DTA) could impact on the outcome – Australia has around 45 bilateral DTAs. For example, if the employee was a resident of say the Philippines, then Article 15 of the double tax agreement (DTA) between Australia and the Philippines generally prevents Australia from taxing the employment income unless the work is performed in Australia.

Pay as you go (PAYG) withholding should not generally apply if the worker is a non-resident employee and is only deriving foreign sourced income. Generally, PAYG does not need to be withheld under the PAYGW rules from a payment of salary / wages to someone if the payments are not taxed in Australia.

Superannuation guarantee should not apply if all the work is performed overseas, and the worker is a non-resident.

It will be important to get specialist advice in the employee's country of residency to determine whether there are any obligations that need to be satisfied under local tax or super systems (e.g., withholding, superannuation or superannuation like contributions, etc).

Tax implications of independent contractors

If the worker is classified as a genuine independent contractor (or they are working through a trust or company) and they are a non-resident, then they should only be taxed in Australia on Australian sourced income. Using the same example, if the contractor is a resident of the Philippines, then Article 7 of the DTA would generally prevent Australia from taxing their business profits or income unless they relate to a permanent establishment that the contractor has in Australia (see *Will a foreign worker mean your business is carrying on a business overseas?* below).

PAYG withholding should not apply as long as:

- The contractor provides an ABN; or
- A DTA prevents the income from being taxed in Australia; or
- The contractor does not carry on an enterprise in Australia. If the contractor performs all their work overseas, they don't have any physical presence or employees in Australia, then it might be possible to argue that they don't carry on an enterprise in Australia. The company could ask the contractor to complete a statement by supplier.

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Payments to foreign contractors might need to be reported to the ATO on the taxable payment annual report (TPAR) if your business provides building and construction, cleaning, courier and road freight, IT or security, investigation or surveillance services.

Will a foreign worker mean your business is carrying on a business overseas?

By having foreign workers, there is a risk that the business will be considered to be carrying on a business through a permanent establishment in the relevant foreign country. This could potentially expose an Australian business to tax in the foreign country on some of its business profits.

A permanent establishment is generally defined in Australia's double tax agreements as being a fixed place of business through which the business of the enterprise is carried on in whole or part. Each DTA is a unique document which means that the definition of permanent establishment might be different depending on which foreign country you are dealing with.

This area can become complex very quickly and it is a good idea to get advice to ensure that you have certainty about your obligations.

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Quote of the month

"We cannot solve our problems with the same thinking we used when we created them."

Albert Einstein

Are student loans too big?

Australian voters tend to reject US style education favouring more egalitarian systems where income does not determine access.

In the US, average student debt is USD $37,693 (public and private debt) taking an average of 20 years for individuals to repay. But, students often have a gap not fulfilled by loans.

For Australian domestic students, the cost of completing a bachelor degree is generally between $20,000 and $45,000, excluding some of the higher value courses. HECS-HELP loans are available for eligible students to cover the cost of tuition up to $121,844 for most degrees, and $174,998 for higher value degrees like medicine. The average higher education student debt in Australia is around $27,000 and on average takes just over 8 years to repay. Close to 3 million Australians have a student loan debt with debt totalling over $81 bn. Over 7 million have loans above $100,000.

Currently, student loans start to be paid back when an individual's income reaches $54,435, with a repayment rate that scales according to income ranging from 0% to 10% when income reaches $159,664.

The Government has announced a series of changes to HECS-HELP including:

- **Indexation rate calculation change to the lower of consumer price index (CPI) or wage price index (WPI)** – currently CPI. Intended to be backdated to student loans on 1 June 2023, effectively removing the 7.1% spike that occurred in 2023.
- **Increased minimum repayment threshold** to $67,000 in 2025-26. The repayments will also be calculated on the income above the new $67,000 threshold rather than total annual income.
- **20% loan reduction** for all study and training support loans before 1 June 2025 (around $16bn).

These changes are subject to the passage of legislation and are not yet law.