

Reporting of Taxable Payments for Contractors in the Building and Construction Industry

Consultation Paper
May 2011

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CONSULTATION PROCESS

REQUEST FOR FEEDBACK AND COMMENTS

The Government is seeking your feedback and comments on the design details of the Government's 2011-12 Budget announcement to introduce a reporting regime for contractors in the building and construction industry.

While submissions may be lodged electronically or by post, electronic lodgement is preferred. For accessibility reasons, please email responses in a Word or RTF format. An additional PDF version may also be submitted.

All information (including name and address details) contained in submissions will be made available to the public on the Treasury website, unless you indicate that you would like all or part of your submission to remain in confidence. Automatically generated confidentiality statements in emails do not suffice for this purpose. Respondents who would like part of their submission to remain in confidence should provide this information marked as such in a separate attachment. A request made under the *Freedom of Information Act 1982* (Commonwealth) for a submission marked 'confidential' to be made available will be determined in accordance with that Act.

Closing date for submissions: **27 June 2011**

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FOREWORD



I am pleased to release this discussion paper on the Government's proposal for the reporting of taxable payments for contractors in the building and construction industry.

In the 2011-12 Budget, the Government announced important changes to the tax law to introduce a reporting regime requiring certain businesses to report details of payments made to contractors in the building and construction industry. The introduction of this reporting regime will help ensure that all contractors comply with their taxation obligations and pay their fair share of tax.

By helping to improve compliance, this measure will also help create a level playing field in the building and construction industry. No longer will tax evaders be able to undercut honest competitors on price. Indeed, improving compliance is likely to improve fairness and promote competition in the industry.

I'm pleased many parts of the industry have already expressed their support for these measures. These improvements will be of great assistance to those contractors and businesses in the building and construction industry who do the right thing but who face a competitive disadvantage compared to those who do not pay their fair share of tax.

I look forward to receiving the community's views.

The Hon Bill Shorten MP

Assistant Treasurer and Minister for Financial Services and Superannuation

INTRODUCTION

On 10 May 2011, the Government announced the 'Improving Tax Fairness and Compliance' package as part of the 2011-12 Budget. This package includes three measures that are targeted at creating a more level playing field for taxpayers, thereby supporting the Government's ongoing commitment to ensure that everyone pays their fair share of tax.

A measure entitled 'Reporting Taxable Payments' forms part of this package and requires certain businesses to report annually, to the Australian Taxation Office (ATO), payments they make to contractors in the building and construction industry (BCI), along with the contractor's Australian Business Number (ABN). This new reporting regime will start on 1 July 2012.

The aim of the reporting regime is to improve compliance with taxation obligations of contractors in the BCI by providing the ATO with sufficient information to allow data matching for review and targeted audits. The information will also allow the ATO to focus their resources in order to provide assistance and education to those identified as having a problem with compliance, based on a lack of knowledge or awareness.

This discussion paper outlines the proposed design of the reporting regime and poses questions to provide interested parties with an opportunity to comment on the final design and implementation of this measure.

The Government is committed to well-designed regulation that achieves the policy objective in a manner that minimises costs for business and the community.

1. BACKGROUND

There are more than one million independent contractors currently operating throughout Australia.¹ These contractors operate as self-employed businesses across an array of industries, with high concentrations in building and construction, financial and insurance services, agriculture and other professional services industries.

Compliance with taxation obligations that flow from running a self-owned and operated business is often a difficult task for taxpayers, but for some contractors the difficulty can be compounded by poor administrative practices along with a general lack of understanding of their obligations.

Unlike most individual (non-business) taxpayers, contractors sometimes deal with the more complex aspects of income tax including capital gains tax, business deductions and, additional reporting and record keeping requirements. Some contractors may also be liable to remit and account for Goods and Services Tax (GST).

While the ATO has made an effort over the years to educate and support contractors in respect of their taxation obligations, ATO data nevertheless indicates that compliance with taxation obligations by contractors is poor and presents a systemic risk to revenue collection.

Academic research supports the hypothesis that 'compliance [with taxation obligations] is likely to be higher when taxpayers perceive there to be a higher probability of being caught along with anticipated adverse consequences'² and has found that compliance often becomes a casualty of business pressures for small businesses where there is no third party reporting of income and the chances of detection are low.³ Reducing the levels of non-compliance within an industry such as the BCI has the potential to provide wider improvements to competitiveness and fairness. For these reasons the Government has decided to strengthen compliance and improve fairness in the BCI.

1.1 THE NON-COMPLIANCE PROBLEM

Non-compliance with taxation obligations is not a problem unique to contractors. However, the ATO has identified a high level of non-compliance by contractors in the BCI, particularly in relation to lodgment, correct reporting and payment. There are also associated problems with contractors not complying with GST requirements, record keeping requirements and the personal services income rules.

Non-compliance is a key problem for compliant businesses. In an industry with high levels of non-compliance, compliant taxpayers are often at a competitive disadvantage, being undercut by competitors who are able to charge less for their goods or services because they pay less or no tax. This creates an uneven playing field and can contribute to compliant businesses failing or becoming non-compliant themselves leading to a higher barrier to entry for new businesses.

1 Australian Bureau of Statistics (2010) 'Forms of Employment' Release 6359.0, November 2009, p 32.

2 Ahmed, E & Braithwaite, V (2005) 'Understanding small business taxpayers: Issues of deterrence, tax morale, fairness and work practice', International Small Business Journal, Vol 23, Issue 5, pp 539-568 at p 540.

3 Ahmed, E & Braithwaite, V (2005) at p 543.

1.1.1 The extent of the problem

The ATO recently undertook compliance analysis on data from the 2006 and 2009 income years for the six largest industries in the micro market⁴ (based on population size). These included the following broad industry groups:

- building and construction;
- financial and insurance services;
- professional, scientific and technical services;
- rental, hiring and real estate services;
- agriculture, forestry and fishing; and
- retail trade.

The analysis revealed that the BCI was the least compliant of the six largest industries in the micro market.

ATO analysis also showed that the construction industry accounts for \$1.58 billion (or 20.73 per cent) of all debt owed to the ATO in the micro market and 60 per cent of all debt cases held by the ATO in the micro market (146,084 cases).

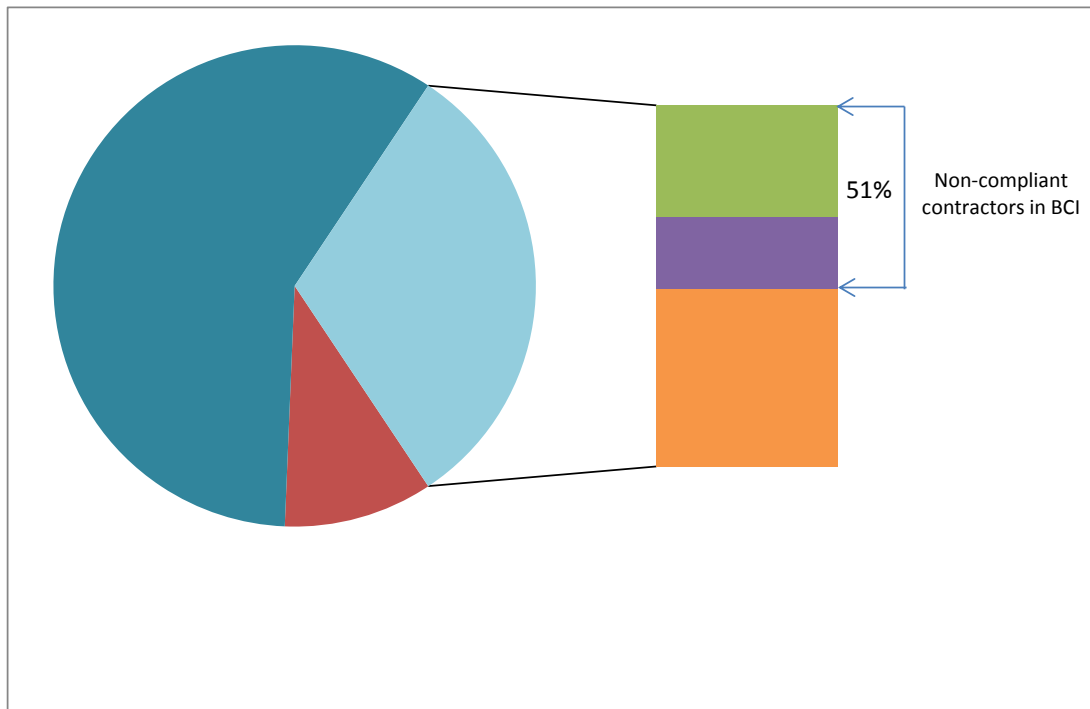
The ATO's current audit program, under the *Level Playing Field — Strategic Budget Initiative*, was established to target businesses engaging entities as contractors that may actually be employees (otherwise known as 'sham contracting'). The ATO also used the audit program to check whether contractors were properly reporting their income, by matching the details of income paid to contractors for the 2008, 2009 and 2010 income years with ATO records.

The audit program revealed significant compliance problems with contractors in the BCI who had not correctly reported payments received in tax returns or activity statements.

From this program, it was found that based on the 2009 data, approximately 10 per cent of all tax invoices could not be matched to a payee on ATO systems due to non-quotation or invalid quotation of an ABN. Of the approximately 11,500 matched entities in the initial analysis, 34 per cent were contractors in the building and construction industry. It was found that 31 per cent of those contractors that were matched to ATO records had not lodged a tax return, with a further 20 per cent having lodged but omitting all or part of their income (see Figure 1).

4 The ATO defines the micro market as businesses that have an annual turnover of less than \$2 million.

Figure 1: Audit program results — snapshot of contractors audited including BCI compliance.



KEY

- Non-matched entities
- Matched entities – not BCI
- Matched entities - BCI

KEY

- BCI – did not lodge
- BCI – omitted all or part of income
- BCI - compliant

1.1.2 What factors contributed to the problem?

The high levels of non-compliance with taxation obligations by contractors in the BCI could be due to a range of factors.

For instance, some contractors operating in the BCI lack the capacity to comply with their taxation obligations due to the complex nature of the business tax system (coupled with a lack of tax knowledge) and pressures on time and resources. However, the entrenched non-compliance by contractors in the BCI may indicate that it is the contractors’ unwillingness to comply that contributes to the higher rates of non-compliance. This leads to the existence of the ‘cash economy’.

Where non-compliance is entrenched within an industry, it acts as a disincentive for new entrants to the industry to comply with their taxation obligations. This is especially the case where non-compliant contractors are able to constantly undercut or outbid compliant rivals.

A related, but nevertheless separate issue is that, in practice, many contractors appear to approach their work as if they were employees rather than contractors, either unaware of, or disregarding, their broader business tax obligations. As a result, some contractors can find themselves with a considerable tax debt, which often results in business failure.

Non-compliance with taxation obligations can also arise from factors external to the contractor or industry. Legislative amendments to existing taxation obligations can lead to additional

responsibilities. Inadequate notification or education of these changes may reduce the contractors' ability to comply with these new obligations.

1.1.3 Efforts already made to solve the problem

Since identifying the high levels of non-compliance with tax obligations by contractors in the BCI, the ATO has made increased efforts to address the problem. This included increasing resources for audit activities and providing numerous education programs and avenues for assistance to contractors in the BCI.

These activities have been met with only limited success, with many contractors still failing to show a willingness or ability to comply. The Government has reviewed the result of the ATO's activities and has concluded that longer-term improvement in voluntary compliance in the BCI is unlikely to come from these approaches.

While targeted compliance and audit funding has a role in addressing entrenched non-compliance, short-term improvements following compliance intervention are generally not sustained, and this approach is costly to apply on a wide scale.

2. OVERVIEW OF THE PROPOSED REPORTING REGIME

The measure proposed in the 2011-12 Budget involves the introduction of a reporting regime that will require businesses to report annually to the ATO any amounts paid to contractors in the BCI, along with each contractor's ABN. The information that businesses are required to provide in these annual reports is information that they should already commonly collect or record under existing business record keeping requirements.

No private individual who hires a contractor will be required to report payments under this regime. The proposal will be confined to business-to-business transactions (contractors).

The introduction of a reporting regime is expected to significantly reduce non-compliance with taxation obligations by ensuring that amounts received for services are detected by the ATO in a timely and coherent manner. For those contractors who are willing to comply but do not have the capacity or are erroneously underreporting their income, the reporting regime would provide the ATO with data that would alert them to this situation. ATO resources could then be directed towards assisting the contractor to comply and ensuring that they are able to meet their taxation obligations in the future.

2.1 REGULATORY STRUCTURE OF THE REPORTING REGIME

The reporting regime can operate through the existing Payment, ABN and identification verification system (PAIVS) in Part 5-30 in Schedule 1 to the *Taxation Administration Act 1953* (TAA 1953). The PAIVS was introduced in 2000 as part of the *A New Tax System* changes. Given the policy objectives of this measure, the PAIVS is considered the most suitable legislative platform to deliver the proposed reporting regime.

The explanatory memorandum (EM) to the *A New Tax System (Tax Administration) Act 1999* (ANTS Act) details the policy intent underlining the creation of the PAIVS. Paragraph 4.1 of the EM states that:

'The system [PAIVS] is intended to be used in areas where non-compliance with the taxation laws is entrenched. The main objective of the new system is to ensure that business participants meet their tax obligations and that any current or future competitive advantage resulting from non-compliance is minimised.'

The PAIVS has not been activated yet, as *'components of the new compliance system will only be used in areas where there is entrenched non-compliance and when the Government is convinced that it is necessary.'*⁵

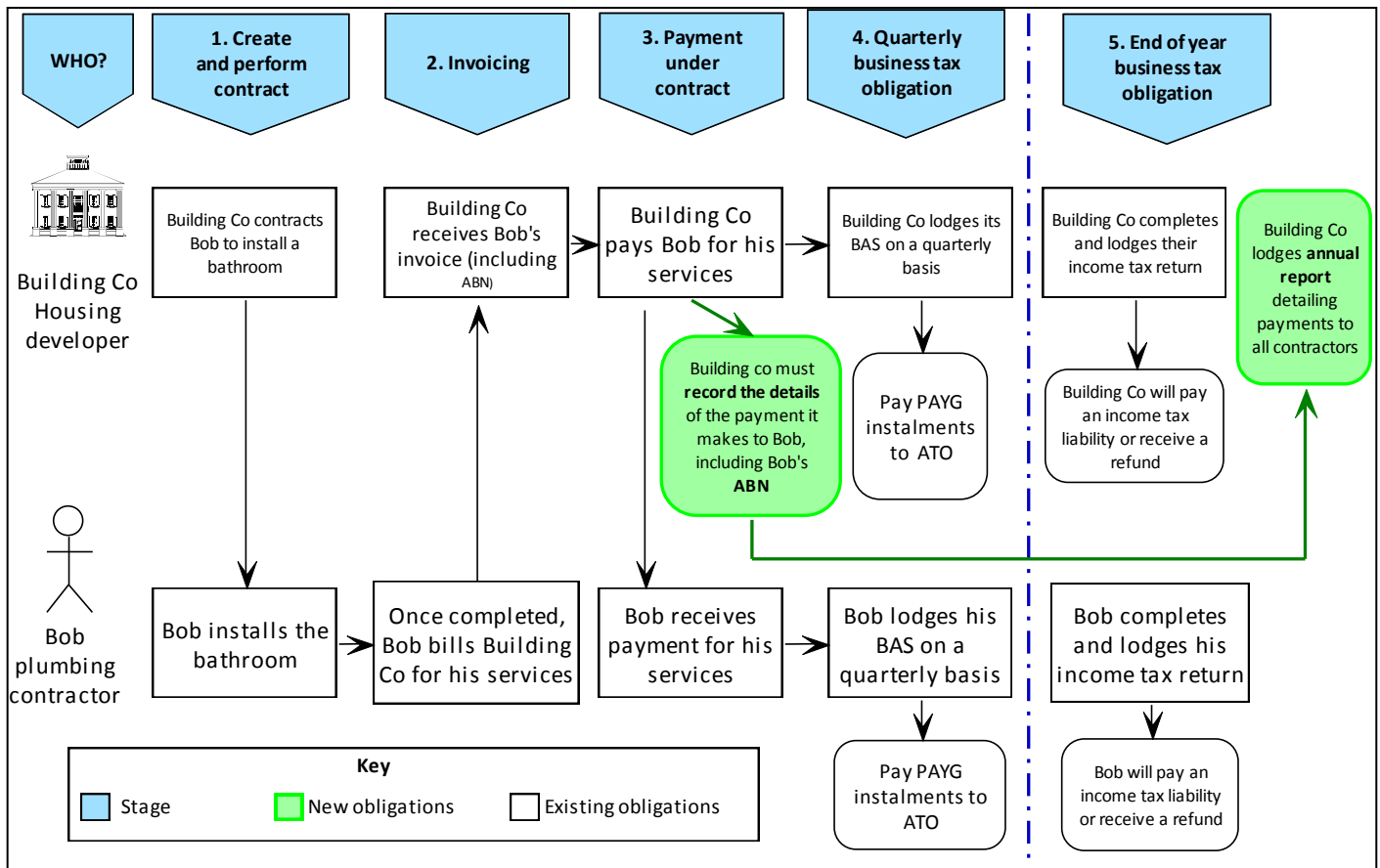
This measure will utilise the 'transaction reporting by purchasers' component of the PAIVS (Division 405 in Schedule 1 to the TAA 1953). Under this component, the measure will adopt the terminology within the legislation and operate to require a 'purchaser' to report details to the ATO of 'suppliers' who they have paid for a 'supply'.

5 EM at paragraph 4.3.

Combining the elements within the PAIVS, the reporting regime would operate to require businesses ('purchaser') to report any payments for work undertaken ('supply') by contractors in the BCI ('supplier'). Further detail on the proposed meaning for these terms and the administrative structure of the regime are set out in the next section.

Figure 2 below provides an example of the proposed reporting regime and how the regime would operate in conjunction with existing basic taxation obligations. In Figure 2, Building Co is the 'purchaser', Bob is the 'supplier' and the payment for the installation of the bathroom is the payment for a 'supply'.

Figure 2: Example of the proposed reporting regime



Note: the requirement to record the details of the payment and ABN in Figure 2 is technically a new legal obligation for this reporting regime. However, businesses already collect and record this information for different reasons under the existing record keeping obligations.

To apply the PAIVS to contractors in the BCI, regulations will be inserted into the *Taxation Administration Regulations 1976* defining the key terms of 'purchaser', 'supplier' and 'supply'.

The existing structure of the PAIVS legislation will be utilised and the existing penalty provisions within the PAIVS system (currently 20 penalty units) provide the incentive for purchasers to meet their reporting obligations. For that reason, there are no legislative amendments foreseen as part of this measure.

While the PAIVS legislation is currently structured to require quarterly reporting of payments, under this measure, it is proposed that businesses will only be required to report annually. To give effect to this, the Commissioner can exercise a discretion under section 388-55 in Schedule 1 of the TAA 1953 to change the reporting cycle from quarterly to annually (see section 3.4 of this paper).

3. DETAILED DESIGN OF THE PROPOSED REPORTING REGIME

Division 405 in Schedule 1 to the TAA 1953 is the primary legislation under which the reporting regime will operate.

Determining the detailed design of the proposed reporting regime requires examination of the core parameters within Division 405, which are:

- what payments are subject to reporting;
- who is required to report;
- who will be reported on; and
- what is required to be reported and how will this occur.

3.1 'SUPPLY' — WHAT PAYMENTS ARE SUBJECT TO REPORTING

Summary

The payments that are subject to reporting are payments for a supply, which in this context is a supply made under a contract that is in whole, or in part, for the supply of building and construction services.

However, this **does not** include payments that are solely for the supply of goods or materials, or payments of salary and wages for employees.

Section 405-5 in Schedule 1 to the TAA 1953 states that Division 405 applies to any payments that are made, or are liable to be made, for a 'supply' where the supply is specified in regulations made for the purpose of the section. A payment is liable to be made if the obligation to make the payment is notified in an invoice.

Subsection 405-5(4) in Schedule 1 to the TAA 1953 further explains that the regulations may specify a supply by reference to:

- the goods or services supplied; or
- the supplier; or
- the purchaser.

Payments which constitute a 'supply' under Division 405, are then called 'Division 405 payments'.

3.1.1 Tax law definition of 'supply'

'Supply' is defined in section 9-10 of the *A New Tax System (Goods and Services Tax) Act 1999* (GST Act) as, any form of supply whatsoever, including but not limited to:

- a supply of goods;
- a supply of services;
- a provision of advice or information;
- a grant, assignment or surrender of real property;
- a creation, grant, transfer, assignment or surrender of any right;
- a financial supply;
- an entry into, or release from, an obligation:
 - to do anything; or
 - to refrain from an act; or
 - to tolerate an act or situation;
- any combination of any two or more of the matters listed above.

3.1.2 Supplies within the scope of the proposed reporting regime

For the purposes of this measure, it is proposed that a 'supply' will include a supply under a contract that in whole or in part, involves a supply of building and construction services.

Supplies that will **not** be covered include:

- a supply that consists of only a supply of goods or materials; or
- a supply of labour under a common law employment contract where PAYG withholding applies.

'In whole or in part'

The reference to 'in whole or in part' means that the 'supply' may include a supply under a contract for services only, or may include a supply under contract for a supply of services, together with the supply of goods.

Example

Beatrice is a plumber who has been contracted to install several toilets in a housing estate. Her contract includes payment for her labour and payment for the toilet parts and fittings.

Beatrice's contract would constitute a 'supply' under this measure, as it is a contract in part for a supply of services.

'Supply of building and construction services'

The term 'supply of building and construction services' is not defined in the current tax law, however the concept of 'building and construction services' has been considered in both the GST context and also previously formed part of the now repealed Prescribed Payment System (PPS).

The definition of 'building work' and 'construction work' has also been defined outside of the taxation context in the *Building and Construction Industry Improvement Act 2005* (Cth) and in New South Wales under the *Building and Construction Industry Security of Payment Act 1999* (NSW).

The definition that is ultimately adopted for the term 'supply of building and construction services' in the new reporting regime could borrow concepts from both the GST and PPS contexts as well as the activities defined in the non-taxation context.

Ordinary meaning

Under its ordinary meaning, the term 'supply of building and construction services' should cover services supplied which are commonly determined as building and construction activities. From a broad perspective, this should include but not be limited to activities such as:

- bathroom or kitchen fitting / installation;
- alarm installation and home security;
- carpentry and joinery;
- electrical work and plumbing;
- fencing erection and installation;
- landscaping and paving;
- painting and decorating;
- pest control and termite inspection;
- air conditioning / heating installation;
- glazier work;
- tiling, plastering and concreting;
- door, window frame and screen fitting;
- brick laying / masonry;
- building;
- cabinet making / furniture;
- concrete supply and formwork;
- demolition / renovation;
- swimming pool construction;
- excavation and earthmoving;
- roofing and roof construction;
- insulation supply and installation; or
- scaffold supply and erection.

GST context

The concept of ‘building and construction services’ has been considered by the ATO in the Goods and Services Tax Ruling GSTR 2000/18⁶. In that ruling, the ATO explained the concept of ‘construction and building services’ as meaning:

‘those services supplied in respect of a building or civil engineering work. Construction and building services include, but are not limited to bricklaying, carpentry, plumbing, tiling, electrical, painting, air conditioning installation, lift installation, or any combination of these.’⁷

The ruling then goes on to state that, ‘[i]n some circumstances a supplier may enter into an agreement to design and construct. Where these services are supplied under the same agreement then the design component is considered to be part of the construction and building service.’

The GST context offers a constructive explanation of the concept and given the integration of the concept of supply, provides a practical definition that could be utilised for the purposes of defining ‘supply’ under this measure.

PPS context

The concept of ‘building and construction services’ was also explored and defined through regulations as part of the former PPS. The PPS was a type of withholding system that applied to certain payments under a contract which in whole or in part included the performance of work. The PPS was repealed with the introduction of the *A New Tax System* in 2000. The regime applied to, among other services, the provision of building and construction services of a professional nature (including the preparation of plans and specifications)⁸.

This included work on any structure, road work or thoroughfare where the activity included:

- construction;
- erection;
- installation;
- alteration;
- modification;
- improvement;
- demolition;
- destruction;
- repair;
- dismantling; or
- removal⁹.

Examples of these activities included:

- painting, decorating, proofing or other treatment of internal or external surfaces;
- the installation, fixing or fitting in, to any structure of:

6 Goods and Services Tax Ruling GSTR 2000/18 – ‘Goods and services tax: construction and building services which span 1 July 2000’.

7 Paragraph 15, of GSTR 2000/18.

8 Former paragraph 126(3)(e) of the *Income Tax Regulations 1936* (ITR 1936).

9 Former subregulation 126(2) of the ITR 1936.

- heating, cooking, refrigeration, insulation, lighting, power supply, water supply, irrigation, sanitation, drainage, fire or security protection, sound communication, air conditioning, ventilation or any other systems or devices;
 - walls, ceilings, linings or floors;
 - roof tiles, ceramic tiles, quarry tiles, stone, or other interior or exterior cladding or covering;
 - built-in-furniture, electrical or plumbing fittings; or
 - swimming pools.
- internal or external cleaning carried out in the course of any of the above activities and cleaning of the building prior to occupation;
 - any other activity on a structure, road works or thoroughfare, or on land which these are located. Includes work preparing, forming part of, or completing any of the above activities as well as:
 - site clearance;
 - earth moving;
 - excavation;
 - laying foundations;
 - erection of scaffolding;
 - site restoration;
 - landscaping; or
 - access works¹⁰.

Partly because the PPS system sought a different goal (namely to secure withholding from payments akin to payments for labour), the following activities were excluded:

- architectural, engineering, surveying or other professional building and construction activities¹¹;
- delivery **only** of goods and materials in connection with the above activities, except in circumstances where tied drivers are contracted;
- sign writing (where no structural work is done); or
- the production of murals and similar works¹².

Non-taxation context

Outside of the taxation context, the concept of ‘building and construction services’ is defined through the terms ‘building work’ and ‘construction work’ in various State and Territory legislation. For example, the definitions of ‘building work’ and ‘construction work’ in the *Building and Construction Industry Improvement Act 2005* (Cth) and the *Building and Construction Industry*

¹⁰ Former subregulation 126(2) of the ITR 1936.

¹¹ However, these payments for these services/activities were covered under a separate regulation in the PPS.

¹² Former paragraph 126(2)(d) of the ITR 1936.

Security of Payment Act 1999 (NSW) are substantially similar to the definition of 'building and construction services' in the PPS.

The definition of 'building work' in the *Building and Construction Industry Improvement Act 2005* (Cth) includes the following activities:

- the construction, alteration, extension, restoration, repair, demolition or dismantling of buildings, structures or works that form, or are to form, part of land, whether or not the buildings, structures or works are permanent;
- the construction, alteration, extension, restoration, repair, demolition or dismantling of railways (not including rolling stock) or docks;
- the installation in any building, structure or works of fittings forming, or to form, part of land, including heating, lighting, air-conditioning, ventilation, power supply, drainage, sanitation, water supply, fire protection, security and communications systems; or
- any operation that is part of, or is preparatory to, or is for rendering complete, work covered by the activities listed above, for example:
 - site clearance, earth-moving, excavation, tunnelling and boring;
 - the laying of foundations;
 - the erection, maintenance or dismantling of scaffolding;
 - the prefabrication of made-to-order components to form part of any building, structure or works, whether carried out on-site or off-site;
 - site restoration, landscaping and the provision of roadways and other access works.

However, the definition does not include any of the following activities:

- the drilling for, or extraction of, oil or natural gas;
- the extraction (whether by underground or surface working) of minerals, including tunnelling or boring, or constructing underground works, for that purpose;
- any work that is part of a project for:
 - the construction, repair or restoration of a single-dwelling house; or
 - the construction, repair or restoration of any building, structure or work associated with a single-dwelling house; or
 - the alteration or extension of a single-dwelling house, if it remains a single-dwelling house after the alteration or extension.

Questions for consultation

1. Should the definition of 'supply of building and construction services' be developed from a more principled perspective, or should it attempt to list the activities/services covered?
2. What types of activities would fundamentally be considered activities that are commonly undertaken by contractors in the BCI?
3. Are there any building and construction activities that are not listed above that should be included in the reporting regime?
4. Are there any building and construction activities that are listed above that should not be included in the reporting regime?

3.2 'PURCHASER' — WHO IS REQUIRED TO REPORT

Summary

The 'purchaser' is the entity required to report and in this context the 'purchasers' are entities that are businesses, including sole traders or contractors that are wholly or principally engaged in the BCI.

However, this **does not** include private individuals, such as householders or owner builders.

Subsection 405-10(1) in Schedule 1 to the TAA 1953 states that any entity (the 'purchaser') that makes, or is liable to make a 'Division 405 payment' must report to the Commissioner.

This measure is aimed at business-to-business transactions, targeting only those payments made by businesses or contractors in the BCI, to contractors (or sub-contractors) in the BCI. For that reason, the definition of 'purchaser' would include any business, including a sole trader or a contractor that is wholly or principally engaged in the BCI.

3.2.1 'Wholly or principally engaged in the BCI'

A business that is 'wholly or principally engaged in the BCI' is a business that predominantly undertakes building and construction activities as defined as a 'building and construction service'. Therefore, under this measure a 'purchaser' would be a business whose core activity is the provision or procurement of building and construction services.

Example

FYBK Pty Ltd is a small tier bricklaying company that supplies and lays bricks for housing developments. As it is a business and its core activity is the supply and laying of bricks (which is a building and construction service), it is considered a 'purchaser' under this regime.

Example

Ralph & Zucchini Pty Ltd is a fashionable clothing company in Melbourne that is engaging contractors to build an extension on their premises. Although Ralph & Zucchini Pty Ltd is a business, and is engaging a contractor from the building and construction industry to build the extension, the business's core activity is selling clothing, and therefore it is not a 'purchaser' under this regime.

A 'purchaser' does not include an individual in a domestic capacity, such as a 'householder' who undertakes a private or domestic construction project and pays a builder or someone else (under a contract) to organise sub-contractors on their behalf for all or part of the project.

This exemption from the definition of 'purchaser' also includes any individuals who are 'owner builders' that undertake a private or domestic construction project, and organise their own contractors for all or a large part of the project¹³.

Example

Kerrie and her husband Justyn are building their dream home. In order to save money they have decided to not engage a builder, but instead engage contractors themselves. As they are 'owner builders', they are not a 'purchaser' under this regime.

Question for consultation

5. Are there any entities that would be captured within the proposed definition of 'purchaser', that should not be required to report under this regime?

In addition to the proposed definition of 'purchaser' set out above, comments and feedback are sought to consider whether it is appropriate to extend the definition of 'purchaser' any further, such as to 'connected businesses'.

Such an extension would bring into scope those businesses that are not necessarily wholly or principally engaged in the BCI, but are sufficiently connected to it to warrant inclusion in the scheme.

For example, it may bring in retailers of building and construction products, such as a hardware store, that regularly contract tradespeople to install their products, such as kitchens, tiles and paving, security screens and doors, and air-conditioners.

¹³ The term 'owner builder' is defined differently in each State or Territory jurisdiction and certain permit conditions apply.

Question for consultation

6. Is it desirable to extend the scope of the proposed definition of ‘purchaser’ to include those entities which may not be engaged predominantly in the BCI, but are sufficiently connected to the BCI?
7. Are there any other businesses or entities that should be caught within the proposed definition of ‘purchaser’?

3.3 ‘SUPPLIER’ — WHO WILL BE REPORTED ON

Summary

The entities that will be reported on include any contractor or sub-contractor who is engaged in the BCI, quotes their ABN to the purchaser and receives a ‘Division 405 payment’.

Under the PAIVS framework, the ‘supplier’ is the entity who receives the ‘Division 405 payment’, supplies the goods or services and is the subject of the reporting regime. As the ‘supplier’ is only being reported on under this measure, they do not have any obligations under the PAIVS framework.

For the purposes of this measure, the ‘supplier’ will be any contractor or sub-contractor (individual or non-individual) who is engaged in the BCI with an ABN and receives a ‘Division 405 payment’.

Where a contractor engages another contractor to undertake work on their behalf, the parties would generally be known as a contractor (or principal contractor) and a sub-contractor respectively.

Based on ATO estimates, in total there are currently 451,000 contractors and sub-contractors in the building and construction industry that could be ‘suppliers’ under this measure.

As the proposed definition of ‘supplier’ requires the contractor to quote their ABN, a contractor will not be subject to the proposed reporting regime where they fail to provide a ‘purchaser’ with an ABN. However, under the current law¹⁴, a purchaser is already required to withhold an amount from a payment made for a supply where the supplier has failed to quote their ABN to the purchaser, and report the transaction to the ATO. Accordingly, the two regimes will work together so that if payment data (including an ABN) is not provided to the ATO, tax is paid through withholding.

To further streamline the operation of these two regimes, the ATO will consult with industry and software developers on the form and method of reporting, including how to report payments for which no ABN has been quoted.

¹⁴ Section 12-190 in Schedule 1 to the TAA 1953 provides for withholding where an entity does not quote their ABN in respect to a payment for a supply.

3.4 ADMINISTRATION — WHAT IS REQUIRED TO BE REPORTED AND HOW WILL THIS OCCUR

Summary

Entities required to report will need to lodge an annual report which is an approved form.

Generally, the annual report ('Division 405 report') will contain information that identifies the 'supplier' and 'Division 405 payments' made to the 'supplier' in the reporting period.

The ATO will consult with industry about the form and method of reporting.

For 'purchasers' that make a 'Division 405 payment', section 405-10 in Schedule 1 to the TAA 1953 requires them to make a 'Division 405 report'. This report is a written statement and is required to be made in an approved form¹⁵.

3.4.1 Content of 'Division 405 report'

The 'Division 405 report' will contain information including:

- name of the 'supplier';
- the supplier's ABN (if known by the 'purchaser'¹⁶);
- the total of the 'Division 405 payments' that the purchaser made or was liable to make in that reporting period;
 - Including those payments that were notified in an invoice during the period, or were made during the period but for which no invoice has been received; and
- any other information relevant to the payment that the Commissioner requires.

Under section 405-10 in Schedule 1 to the TAA 1953, the Commissioner also has the power to require particular information to be included in a 'Division 405 report' if the request is made in writing to the 'purchaser' or class of 'purchasers'. The Commissioner also has the power, by written notice, to change the reporting requirements under section 405-10 for a 'purchaser' or class of 'purchasers'.

Questions for consultation

8. Is the information that is proposed to be included in the 'Division 405 report', information that businesses currently collect and/or record?
9. If not, what changes to business systems will be required to collect the information proposed for the 'Division 405 report'?

15 The requirements for an approved form are set out in section 355-50 in Schedule 1 to the TAA 1953.

16 The ABN would only be unknown to the purchaser where the supplier has failed to provide it. In that case, as discussed earlier, no-ABN withholding would apply and the purchaser would be required to withhold 46.5 per cent from the payment made to the supplier.

3.4.2 Lodgment of 'Division 405 report'

Whilst Division 405 currently requires quarterly reporting, it is considered that annual reporting would be adequate for this measure. Under section 388-55 in Schedule 1 of the TAA 1953, the Commissioner has an unfettered discretion to defer the time within which an approved form is required to be given. Accordingly, it is proposed that no legislative amendment be made to Division 405.

3.4.3 Lodgment process for 'Division 405 report'

Businesses will be able to lodge these reports electronically or manually, depending on which is most compatible with businesses' natural systems. Administratively, the ATO has a number of manual and online lodgment channels that could be utilised for this reporting function which will provide businesses and contractors with different options for fulfilling their reporting obligations.

The ability to automate parts of the reporting process will help to reduce compliance costs. In a 2008 report commissioned by the ATO entitled *'Profiling the micro business segment communication and information needs'* it was found that 85 per cent of micro businesses used accounting and reporting software (14 per cent did not use any, and 1 per cent did not know). For those businesses and contractors without an accounting software package there is likely to be a cost associated with establishing record keeping and reporting systems, however, these will be minimised as much as possible.

To implement this reporting regime it may be possible to use the Standard Business Reporting (SBR) Program to automate some of the requirements. This would allow SBR compatible businesses to avoid manual reporting of payments. As is currently the case, use of the SBR Program would not be mandatory, allowing those who wish to report manually to do so.

Currently, only those businesses that use SBR compatible software and use, or are willing to use, electronic record keeping practices will be able to use automated reporting. It is expected that the SBR may be most useful at the business or 'principal' contractor reporting level, as smaller contractor businesses and sub-contractors may not currently use the SBR platform. The degree of effectiveness of the SBR program in minimising compliance costs under this proposal should be revealed during consultation.

Question for consultation

10. Are there any other administrative arrangements or mechanisms that could be adopted for this measure to reduce the compliance burden on businesses and contractors?