F Legal issues relating to self-directed funding

F.1 Employment obligations under self-directed funding

The administrative and compliance obligations for employment of people under self-directed funding depend on the nature of the employment arrangement. Any such obligations affect the likelihood that people use self-directed funding to employ people, and whether any statutory changes are required or desirable.

The tax treatment of payments for 'work' depends, among other things, on whether a person providing services to a people with disability was deemed to be a volunteer, employee or independent contractor. The issue involves considerable legal uncertainties. Tax laws do not define an 'employee', but resort to the ordinary common law meaning, which by nature is contextual. Any court decision looks at the whole of the relationship between the parties, and balances the various criteria that support a person being in one 'employment' category against the criteria supporting the person being in another.

PAYG tax withholding

Tax withholding obligations are associated with any contract for an ordinary employee hired by a business. However, there are several important exemptions that are relevant to the kind of 'employment' arrangements that are likely to be fostered under self-directed funding. No tax withholding would be required:

- where the work was legally classed as volunteering. While, there is no legal definition of a volunteer for tax purposes (ATO 2008), the decisive test is that a genuine volunteer would not work under a contractual obligation for remuneration and would not be an employee or independent contractor. For example, this could include voluntary respite care, when a neighbour or friend took a person with a disability to a recreational activity (ATO tax determination TD 2004/D66). The 'worker' could still be reimbursed for out-of-pocket

expenses (for example, the costs associated with transport, food and drink, and recreational activities) or/and receive an honorarium, and still be classified as a volunteer. A person deemed a volunteer would not have to pay tax on payments or benefits received. This provides a degree of flexibility for people using self-directed funding, so long as they are not implicitly paying a wage to someone providing support

- where the employment most resembled a contract *for* service (an arrangement with an independent contractor), as distinct from a contract *of* service (ATO Tax Ruling 2005/D3, Batalha 2006, ATO 2005). Where it is the former, there are few obligations so long as the contractor provides an Australian Business Number (ABN). Some of the tests for establishing this would be whether the worker provided the necessary equipment to do the job (a mower, a car), was free to accept or refuse work, was paid for results achieved (a fully mowed lawn) rather than by the hour, would not get paid leave, and would not work hours set by an agreement or award. My Place (sub. 217, p. 2) indicated that one of the options under its 'shared management' arrangements for self-directed funding was for the people with disability or carers to engage the support worker as an independent contractor
- even when no ABN was provided, so long as *any* of the following applied:
  - the worker was paid for 'private or domestic' work, such as attendant care or cleaning in the home of the people with disability. This was another option noted by My Place (sub. 217, p. 2). This type of arrangement was seen as the most usual case applying to the employment of support workers by Perth Home Community Services (2010, p. 16). This was because support work is often flexible and provided in limited periods of time, which may remain the same each week for some time, and then change to suit the family's needs, say, in holiday time or when someone is ill
  - the payment was $75 or less (which would often apply to the sporadic engagement of a neighbour or friend for a task)
  - the supplier was an individual aged under 18 years and the payment to them did not exceed $120 a week
  - several other conditions apply, but that are less relevant to self-directed funding.

However, as noted by Perth Home Community Services (2010, p. 17), where people and families receive large funding packages and have support staff working regular

and substantial lengths of time then it is likely that PAYG withholding payments would need to be made to the ATO.[1]

Superannuation obligations

In many cases, there would be no requirement for superannuation payments to a support worker. The two most relevant exclusions for self-directed funding occur where the support worker is:

- engaged in tasks that are wholly or principally of a domestic or private nature for not more than 30 hours per week (ATO Superannuation Guarantee Ruling SGR 2005/1). (The person is deemed not to be an employee in relation to that work.)
- paid less than $450 in any calendar month.

Occupational health and safety

In one area of regulation and law — health and safety — there appears to be limited compliance costs for people with disability employing support workers, once all Australian jurisdictions adopt a uniform law for work health and safety (due to be in operation on 1 January 2012). The intent of the new model law is not to encompass domestic arrangements that are inherently between a consumer and a person providing services (rather than between a business and another party). Accordingly, beyond their common law obligations, a householder paying an electrician to fix a power point would not have health and safety obligations to that worker. Equally, the law would not aim to pick up arrangements for a paid babysitter or a support worker paid directly by the person with disability. Given that, many of the informal 'employment' arrangements described above are not likely to invoke health and safety requirements.

Workers' Compensation obligations

The various laws about workers' compensation suggest a person with disability or their proxy would generally be required to cover workers' compensation for support workers, often even where that worker was an independent contractor (for example, Workcover Western Australia 2010; Perth Home Care Services 2010, pp. 19–20).

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1 Notably, in the United States, where similar legal principles apply, the Internal Revenue Service has determined that directly hired home-based service workers are employees, and has taken enforcement action against states who classified such workers as independent contractors (Crisp et al. 2010).

Industrial relations issues

Industrial relations issues add additional levels of complexity. For instance, if a person was deemed an employee, their conditions would have to meet some minimum national conditions, such as the minimum wage. Other entitlements would depend on whether the Federal employment law or the employment laws of a State covered the employee, and whether they were a casual. In the majority of cases, an intermittently employed support worker would be a casual employee, and if covered by the national workplace relations system, would have relatively limited entitlements under the National Employment Standards.

Implications

'Employing' a support worker involves enough complexity that most people will need at least advice in doing so. In many cases, people will be able to craft relatively simple arrangements by paying workers' compensation payments and public liability, but without superannuation or tax withholding requirements. In other cases, more complex arrangements will be required. Chapter 8 examines some of the solutions to this.

In theory, to make things simpler, various workers' compensation laws and the *Income Tax Assessment Act 1997* (ITAA) could be modified to provide general exemptions from withholding taxes and workers' compensation where an employee was hired under a defined self-directed funding arrangement. However, removing access to workers' compensation would put at risk workers in the scheme. An exemption from withholding taxes could be implemented, but would add just another degree of complexity to the ITAA, but without very large gains, since PAYG withholding would not apply to many workers. These considerations suggest legislative conservatism in this area.

F.2 Interactions with the taxation and welfare system

Depending on the context, direct payments made to people under self-directed funding may be subject to income tax and affect eligibility for, or amounts of, income support and other welfare benefits. This would have unintended impacts on the viability of self-directed funding.

The determining factor is whether direct payments are ordinary 'income'. Payments made under self-directed funding are subject to ambiguous treatment for tax and welfare purposes, with possible unintended consequences.

Were funds to be seen as ordinary income, the accompanying increases in taxation and reductions in social security income would:

- erode the available funds for people with disability, reducing their incentives to take greater control over their lives
- divert disability resources from state and territory governments to the Australian Government, weakening the incentives for jurisdictions to adopt individualised funding.

In principle, direct funding should not be seen as income as the payments are social insurance payments to meet the costs associated with a disability. Notably the *Social Security Act 1991* (SSA) exempts private insurance trauma payments from income for defining eligibility for social security payments.[2] Similarly, under section 54 of the ITAA, annuities or lump sums paid to injured people are not assessed for tax so long as the payments are not for income replacement. In both of these instances, the Australian Government does not require the injured person to prove that any spending of injury payments was only on medical expenses.

However, without some constraints over the use of direct payments, it appears that the SSA and ITAA would currently treat the money as assessable income. The greater the freedom given to a recipient to spend the funds to meet their individual needs, as is typical for ordinary income, the more likely that funds would be treated as income for tax and welfare purposes. For this reason, and because of the need, in any case, for reasonable levels of accountability, jurisdictions have structured self-directed funding to avoid it being defined as ordinary income. They have done so by characterising users as agents for the relevant government department, rather than the other way around, with the person with a disability treating their own interests as subservient to the interests of the department. Governments have sought tax rulings to confirm their success in doing this.[3] On the face of it, this approach is antithetical to the underlying principles of self-directed funding.

Moreover, the current arrangements require a jurisdiction to seek tax rulings for any new form of self-directed funding or even small variations in existing arrangements as rulings relate only to the 'precise scheme' identified. For instance, the Victorian Government had to seek a new tax ruling (CR 2009/50 cf CR 2006/84) when it developed a new individualised funding scheme that allowed people to use the support package to employ his or her own support workers directly. Requirements

2 Social Security Act, section 8(1) and SS Guide 4.3.2.30.

3 The tax ruling for the South Australian self-managed funding scheme is typical, noting that the funding would not be subject to tax because 'clearly guards against abuse by the recipient. … The fiduciary [person with disability or proxy] must treat his or her own interests as subservient to the interests of the principal, in this case the DFC' (ATO Tax Ruling CR2010/12).

for new rulings take some time and resources, creating a barrier against change in self-directed funding arrangements.

Further, it is arguably better for the agency overseeing the design of the self-directed funding to develop the appropriate probity, accountability and other restrictions, and not be hamstrung by the incidental obligations of the ITAA and SAA.

For these reasons, there are grounds for the Australian Government to revise ITAA and the SSA legislation so that self-managed disability funding approved by the relevant government disability agency would not have implications for income tax or welfare payments.[4] As noted above, there are already exemptions in associated compensation areas and, more generally, the ITAA has multiple income tax exemptions, so that the addition of another would not represent any radical re-casting of the Act.

It is also important not to overdramatise the risks entailed by these exemptions. The relevant government disability agency would have risk management processes in place. Moreover, most spending by people with disability and their carers relate to attendant care, aids and appliances, home and vehicle modifications, respite and accommodation services, and not to those areas of expenditure arousing controversy.

F.3 Release of superannuation

The issue of the definition of income under the ITAA and SAA is also relevant to the taxation of superannuation released early on compassionate grounds (Mathew Dexter, sub. 94, p. 1).

In the context of disability, APRA administers the 'compassionate grounds' for early release of superannuation under sub-regulation 6.19A(1) of the *Superannuation Industry Supervision Regulations 1994*. These grounds include circumstances where a person may not have the financial capacity to meet expenditure to modify their home or vehicle to accommodate a disability and the services are not available through publicly-funded means. This may include the

[4] In the United States, similar issues arose with self-directed funding under the Cash and Counseling demonstration programs. The US Government provided waivers so that the payments were not counted as income or assets for eligibility for various welfare payments (Doty et al. 2007, p. 383).

alleviation of a disability through early specialist intervention. An early release needs to be independently substantiated by appropriately qualified professionals.[5]

Few people with a disability or their carers attempt to use the early release option to meet these expenses. In 2009-10, there were around 300 instances where APRA gave an approval for early release of funds for disability-related home or vehicle modifications, with an average release of about $13 300 per case.[6] There were approximately 2700 instances of early release for medical treatment expenses and a further 700 (approximate) instances that were consistent with the grounds for early release. These two groups also potentially include some disability-related cases, for example, an early intervention program for autism or certain therapies for acquired brain injuries[7]….

A national disability scheme may reduce the need for people to access their superannuation early because it would limit the rationing pervading the current arrangements. Nevertheless, early access to superannuation may sometimes provide families with an additional capacity to seek individual approaches to disability supports that are in excess of what might be allowable under a publicly-funded scheme. For example, this might include a new therapy or a wheelchair with special features.

However, the power people have to use superannuation amounts effectively is affected by its tax and welfare treatment. Where a person accesses super:

- and a person is 60 years or more years old, no tax is payable
- and a person is under 60 years old, tax is not imposed on the proportion of the benefit financed by personal contributions to the scheme, but tax is imposed on the remaining amount. These taxes — and any welfare payment reductions associated with the treatment of super as income — dilute the resources available for disability services.

Taxation concessions given to superannuation are intended to encourage people to add to their superannuation accounts to meet their retirement needs. So, in normal circumstances, were similar tax concessions given to income reserved for current consumption then those savings incentives would be diminished.

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[5] Regulation 6.19A of the *Superannuation Industry (Supervision) Regulations 1994*.

[6] This information was provided by APRA and relates to APRA approvals only, and not to actual releases by superannuation funds.

[7] APRA does not keep statistics on the individual medical conditions for which early release of superannuation is approved.

The release of funds on compassionate grounds are not normal circumstances. In theory, there could still be concerns if someone were able to game the rules for compassionate early release or it were to have unintended impacts on their incentives. That said, while that risk may be present for some of the areas where compassionate grounds exist,[8] these are unlikely to exist for expenditures relating to disability. There is a limited capacity to contrive extreme disability and expenditures on disability have little value for people without disability. (Disability could be defined by the assessment tool used by the NDIS, so there would not be a need for a separate assessment tool.)

So once compassionate grounds for eligible disability expenditures have been substantiated, arguably the tax treatment of those savings used for pre-approved disability purposes should be neutral with respect to taking the savings out when over 60 years old. This is especially the case where privately-funded interventions might provide cost offsets for governments and society by reducing government funding obligations. It is notable that access to super when someone has a terminal medical condition is tax free regardless of age (section 303.10 of the ITAA), so it is clearly practical from a legislative perspective to create special waivers. There are grounds for an amendment to the ITAA along the lines of section 303.10 for early release of superannuation for disability expenditures.

8 For example, the current capacity to access super to prevent forfeiture of a dwelling arising from mortgage stress might sometimes decrease people's prudence when taking on debt commitments. A tax on early access would provide some disincentive for this. It should be noted that people have at times exploited other aspects of the super system (involving self-managed superannuation funds) to try to access funds early, so concerns about the risks of gaming can be real.