Personal services income

Fast facts

What is PSI?

Income is classified as personal services income (PSI) when more than 50% of the income you've received from a contract is a reward for your personal efforts or skills.

You can receive PSI in almost any industry, trade or profession. Common examples include but are not limited to financial professionals, information technology consultants, engineers, construction workers, and medical practitioners.

If you earn PSI and the PSI rules apply, then there are special rules to ensure that this income is attributed to you and not diverted to other individuals or entities.

Working out if income is PSI

Income is classified as PSI when more than 50% of the income you've received from a contract is a reward for your personal efforts or skills, rather than being generated by the use of assets, the sale of goods, from a business structure.

When working out if your income is PSI, you need to look at the income you've received from each contract separately. The terms and conditions of the contract, as well as invoices and written agreements that detail the work

arrangement, are important in working out if the income is PSI. They can help you to work out what percentage of income from each contract is for:

- your labour, skills, knowledge, expertise or efforts, and
- anything else, such as the materials supplied or tools and equipment used.

If 50% or less of the income received from a contract was for your personal efforts or skills, then none of the income from that contract is PSI.

Income that is not PSI

Certain types of income are not PSI:

- supplying or selling goods
- supplying or using an income-producing asset
- income from a business structure.

Whose PSI is it?

Once you have identified PSI is being earned, you then need to work out whose PSI it is. In working out who is earning the PSI, it is important to review the contract and consider all the facts and circumstances of the contractual arrangements between all parties involved. Part of this process involves working out who provides the principal work.

'Principal work' is work that is central to meeting your obligations under an agreement or contract. Principal work does not include associated clerical or administrative work (such as bookkeeping and answering phones) unless the principal work is administrative in nature.

Individuals can earn PSI either directly as a sole trader, or through another entity such as company, partnership or trust which is referred to as a ‘personal

services entity' (PSE).

Working out if the PSI rules apply

Once you have worked out that PSI has been generated through your business contracts, and you have identified who the PSI belongs to, the next step is to work out whether the PSI rules apply to that income.

To do this, you need to work out if you're a personal services business (PSB) in the year that you received PSI. If you self-assess as a PSB the PSI rules do not apply to your PSI.

You can self-assess as a PSB if you:

- meet the results test in relation to at least 75% of your PSI, or
- meet one of the other PSB tests (Unrelated clients test, the Employment test, the Business premises test) and less than 80% of your PSI is from the same entity and its associates.

If you're a company, partnership or trust and you have more than one individual generating PSI, the self-assessment rules and PSB tests need to be applied to each individual.

It is possible for one individual to conduct a PSB but not another.

If you're unable to self-assess as a PSB for a particular income year, you may be able to apply for a PSB determination (PSBD) in some circumstances. A PSBD is a notice from the Commissioner of Taxation which states that one of the PSB tests has been met for the relevant income year.

If you self-assess as a PSB, or have a PSBD, then the PSI rules will not apply to the PSI you receive in that income year.

If you're unable to self-assess as a PSB, and do not have a PSBD for the relevant income year, the PSI rules will apply.

Obtaining work through an agency

Obtaining work through an agency (for example, a labour hire firm, group training organisation or employment agency) can affect whether the PSI rules apply to your income.

If you're contracting through an agency, where the agency provides your services to a client, the agency will ultimately be responsible for the payment for your services.

There are many factors you need to consider when working out if the PSI rules apply. Obtaining your contracts through an agency may prevent you from passing some of the PSB tests.

Apply for a PSB determination

A personal services business determination (PSBD) is a notice from the Commissioner of Taxation which states that one of the PSB tests has been met for the relevant income year.

Where a PSBD is issued, the PSI rules will not apply to that income for the income year.

PSBDs are only issued in relation to one 'test' individual. If multiple individuals are earning PSI through another entity such as a company, partnership or trust (which the ATO refer to as a personal services entity or PSE), the entity will need to apply for a PSBD for each individual.

You can apply to the ATO for a PSBD if:

- you're unsure whether you have passed one of the PSB tests
- unusual circumstances prevented you from passing one of the PSB tests, or
- you met the unrelated clients test but unusual circumstances prevented you from meeting the 80% rule.

There are 2 ways to apply for a PSBD:

1. Use the ATO Personal services income tool
2. Complete the Personal services business determination application.

What to do when the PSI rules apply

When the PSI rules apply to the PSI you received, you will need to complete certain questions in your tax return, and the deductions you can claim may be affected.

As a sole trader, when the PSI rules apply you:

- won't be able to claim certain deductions against your PSI
- will need to complete additional PSI related questions in your tax.

You'll need to be aware of the following if you operate through a company, partnership or trust and the PSI rules apply.

You won't be able to claim certain deductions against your PSI

The PSI your business receives needs to be allocated (or 'attributed') to each individual who performed the services (after being reduced by certain deductions), and the individual declares the income in their individual tax return.

You'll have PAYG obligations for amounts that you pay as salary and wages to an individual who performed the services and for other amounts attributed (treated as belonging) to each individual.

Your business, as well as each individual who performed the services, has tax return obligations for the PSI received.

Completing your tax return

If you're earning PSI, then you need to report this as PSI in your tax return even if you're a PSB and the PSI rules don't apply to you.

How you report your PSI depends on whether the PSI rules apply to your income, and whether you operate as a sole trader, company, partnership or trust.

You will also need to complete reconciliation labels in a company, partnership or trust tax return if the PSI rules apply to your income.

What to do if the PSI rules don't apply

Even when the PSI rules don't apply, you still need to declare any PSI amounts at the relevant labels on your tax return.

If you received PSI but found that the rules do not apply, there are no changes to the deductions you can claim against the income.

Although the PSI rules don't apply, if you've entered into an arrangement where the dominant purpose is to obtain a tax benefit, the general anti-avoidance rules may apply.

Record keeping for PSI

You need to keep records explaining all transactions that relate to your tax affairs, including PSI.

Generally, you need to keep records of most transactions, in English, for 5 years. The 5 years starts from when you prepared or obtained the records or

completed the transactions (or acts they relate to), whichever is the later.

When working out if you receive PSI, you need to keep records that show:

- whether the income is PSI
- how you worked out if the PSI rules apply
- which expenses apply to any PSI received, and
- the deductions you can claim against the PSI.

If more than one individual is generating PSI, you need to keep records relating to each individual.

Help for PSI

This tax ruling may help you to clarify how the PSI rules apply to you or your business - Taxation Ruling TR 2022/3 Income tax: personal services income and personal services businesses.

If you're still unsure about how the PSI rules apply to you or your business, you may need to seek professional advice from a registered tax professional. The ATO can also provide tailored technical assistance in some circumstances.

If you want written clarification on an issue other than if the PSI rules apply, you should apply for a private ruling from the ATO.

For more information refer to Private ruling application.

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