



AUSTRALIAN
CONSTRUCTORS
ASSOCIATION

JOINT SUBMISSION
ON
FRINGE BENEFITS TAX REFORM:
LIVING-AWAY-FROM-HOME BENEFITS

**The Australian Industry Group & the Australian Constructors
Association**

February 2012

Introduction

The Australian Industry Group (Ai Group) is a peak industry association in Australia which along with its affiliates represents the interests of more than 60,000 businesses in an expanding range of sectors including: manufacturing; engineering; construction; automotive; food; transport; information technology; telecommunications; call centres; labour hire; printing; defence; mining equipment and supplies; airlines; and other industries. The businesses which we represent employ more than 1 million employees.

The Australian Constructors Australia (ACA) represents the nation's leading construction contracting organizations. ACA is dedicated to making the construction industry safer, more efficient, more competitive and better able to contribute to the development of Australia. Association members operate globally, with member companies operating in Australasia, Europe, Asia, North and South America and the Middle East. Collectively ACA member companies have a combined annual revenue in excess of \$50 billion and employ over 100,000 people in their Australian and international operations.

Our organisations recognise the importance of an efficient, simple and equitable tax system that keeps distortions to commercial decision-making to a minimum. We also recognise the importance of stability of taxation arrangements and the need to keep to a minimum the degree to which changes to tax law disrupt existing contracts, practices and commercial arrangements.

More specifically, we support the initiative to address any misuse of the tax treatment of Living-Away-From-Home (LAFH) allowances and benefits. We have three major concerns:

- The proposed treatment of temporary residents who not maintain a home for their own use in Australia would infringe the principle of horizontal equity and would deny this class of taxpayers access to the same tax treatment proposed for other taxpayers.
- At present there is no attention given to transitional provisions. The proposed changes to the taxation of LAFH arrangements will mean a higher tax burden on LAFH allowances and benefits that, over a long period, have been accepted by the taxation authorities and in many cases are embedded in current industrial awards and employment arrangements. Further, many current commercial contracts have been negotiated on the basis of the existing tax treatment of LAFH allowances and benefits. Transitional arrangements are needed to accommodate existing contracts.
- The proposed approach will impose substantial new compliance costs and will introduce new areas of uncertainty that will need to be resolved in consultation between the tax authorities and taxpayers. We recommend the Government not introduce changes to the treatment of LAFH allowances and benefits until 1 July 2013 to allow an orderly resolution of new definitions and design of new procedures.

The proposed changes

The Government proposes to:

- Restrict eligibility for the new tax treatment of LAFH allowances and benefits to residents and to temporary residents who maintain a home for their own use in Australia;
- Require all eligible employees (that is employees who are residents or who are temporary residents who maintain a home in Australia for their own use) to substantiate their LAFH expenses.

In the case of LAFH allowances paid to eligible employees, the Government proposes to:

- Remove the current Fringe Benefits Tax (FBT) exemption;
- Include LAFH allowances in the assessable income of employees;
- Allow eligible employees to claim deductions for actual and substantiated LAFH expenses;
- Vary PAYE withholding obligations of employers so that PAYE tax need not be withheld where eligible employees are expected to incur deductible LAFH expenses.

In the case of LAFH benefits (either reimbursements or direct provisions) for eligible employees, the Government proposes to:

- Retain an exemption from FBT for actual LAFH expenses (subject to the statutory food amount);
- Require the employer to obtain documentary evidence that the employee is living away from home (or, in the case of temporary residents are maintaining a home in Australia for their own use);
- In the case of reimbursements, require the employer to obtain documentary evidence of actual LAFH expenses incurred.

Impacts of the proposed changes

The proposed changes would have significant ramifications.

- They would increase the tax paid on many negotiated salary packages and will reduce the attractiveness of many existing salary packages.
- They would raise the costs to employers of employing temporary residents.
- In many cases they would raise the costs of employing Australian residents currently receiving LAFH allowances and benefits (if LAFH allowances and benefits currently received are in excess of those expenses allowed under the proposed regime).
- They would shift amounts currently paid as LAFH allowances to normal remuneration thus increasing a range of other costs to employers including

- For many resident employees currently receiving LAFH allowances, the changes would reduce entitlements to some government benefits such as Family Tax Benefit.

Where the existing tax treatment (i.e. the FBT exemption) for LAFH allowances and benefits is reflected in employment arrangements that extend beyond 1 July 2012, including through specification in industrial awards, pressures to renegotiate salary packages would arise as employees seek to maintain their after-tax income levels. There is a possibility of industrial unrest and disputation.

Existing commercial contracts may reflect a pattern of costs based on the current tax treatment of LAFH allowances and benefits. Across a project, the changed tax treatment could have a material impact on profitability. Whether the proposed change in tax treatment of LAFH allowances and benefits qualifies under variation clauses would vary from contract to contract and be subject to considerable dispute.

The proposed changes would significantly increase administrative and compliance costs for businesses and employees. New withholding arrangements would need to be designed and implemented. Employers would require evidence from employees to apply these withholding arrangements. New compliance burdens would be associated with the changed rules governing the FBT exemption.

Impacts on costs and competitiveness

The proposed changes would raise the costs of employment in Australia or would reduce the ability of Australian businesses to attract employees. This would reduce the competitiveness of Australian businesses.

The prospect of higher costs is particularly evident in relation to businesses that employ temporary residents for whom a special tax treatment is proposed. Australia competes internationally for temporary residents including in internal labour markets of global enterprises. To continue to attract temporary residents salary packages will need to increase to offset the new tax treatment. The higher salary package (and additional on costs) may not be justifiable and, particularly where skills are highly specialised and equivalently skilled employees are not available in Australia, there may be a loss of economic activity.

Costs would also rise and competitiveness would also fall as a consequence of the changed tax treatment of LAFH allowances and benefits for residents (and temporary residents who maintain a home for their own use in Australia). This will occur for two reasons.

- Where existing LAFH allowances and benefits are in excess of those that will qualify for deductions or FBT exemptions under the proposed regime, at least some of the incidence of the changed tax treatment would fall on employers.
- In relation to all allowances (including allowances against which employees would be able to claim deductions) employers would also face higher superannuation guarantee and payroll tax liabilities and higher workers compensation premiums.

Temporary residents

The Foreword to the Government's November 2011 Consultation Paper states:

The LAFH benefits are intended to compensate employees for additional costs they incur when they are temporarily relocated by their employer for their work.

It further notes that:

A particular concern is the growing use of the concession by employers ... to allow temporary resident workers coming to Australia to convert their taxable salary into a tax-free allowance. This provides them with an unfair advantage over local Australian workers.

The proposed policy response in relation to temporary residents who do not maintain a home for their own use in Australia does not accord with the stated intention; it is anomalous and it is inequitable. It proposes to deny to these taxpayers the same tax relief available to other taxpayers in respect of expenses associated with living away from home.

In relation to temporary residents who do not maintain a home for their own use in Australia, the Government's proposal does much more than target the concern about the conversion of taxable salary into a tax-free allowance. This is the same concern that exists in relation to resident employees. Yet there is a different approach proposed for the two groups of taxpayers. There is no explanation for this anomalous approach and there is no consideration of why the same approach proposed for resident taxpayers would not address the concern in relation to residents who do not maintain a home for their own use in Australia.

Ai Group and ACA strongly recommend that the Government change its proposed approach to remove the anomalous treatment proposed for temporary residents who do not maintain a home for their own use in Australia. Instead, the Government should devise a non-discriminatory approach that targets the concerns at hand. This would also simplify the proposed arrangements by removing the need for employers to distinguish between different groups of taxpayers.

Transitional arrangements

At present there are no transitional arrangements to accommodate the fact that existing employment agreements that extend beyond the proposed start date of 1 July 2012 contain salary, allowance and benefit levels that have been negotiated on the basis of the existing tax treatment.

If the proposed tax arrangements been in place when these agreements were negotiated it is very likely that different salary, allowance and benefit levels would have been negotiated. The proposed change in tax treatment will create pressures to reopen these negotiations at great cost and inconvenience and at the risk of opportunistic bargaining over a range of other matters.

Further, commercial contracts are in place where costs and quotes have been negotiated on the basis of the existing tax treatment of LAFH allowances and benefits. In some cases there may be contract variation clauses. However, in many of these cases there is considerable uncertainty about whether the proposed changes would qualify as a cause for negotiation of variations in contract terms and conditions.

While acknowledging that transitional provisions would add some complexity to the proposed arrangements, Ai Group and ACA strongly recommend that such provisions be developed to ensure that existing contractual arrangements are allowed to run their course are not disrupted by the proposed changes.

Complexity and compliance costs

The new arrangements would add considerable complexity and compliance costs for businesses and for employees. The new arrangements will require new definitions and new guidance from the taxation authorities. New data collection and reporting arrangements will need to be developed and put into place.

Ai Group and ACA recommend that, to facilitate an orderly transition to the new arrangements and to permit a reasonable degree of consultation between the authorities and taxpayers over new definitions and procedures, the Government defer the proposed start date by one year to 1 July 2013. This orderly transition should include the development of transitional arrangements to ensure that contracts entered into before a specified date can are not affected by the changes to the tax treatment of LAFH allowances and benefits.