Submission 27

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BY EMAIL

Committee Secretary
Standing Committee on Economics
PO Box 6021
Parliament House
CANBERRA ACT 2600

Dear Sir

Submissions on Tax Laws Amendment (2012 Measures No. 4) Bill 2012

Thank you for the opportunity to comment on the Tax Laws Amendment (2012 Measures No. 4) Bill 2012 (the "**Bill**"), in relation to the amendments to be made to the Living-Away-From-Home Allowances ("**LAFHA**").

This letter details our comments on selected aspects of the Bill.

1. SUMMARY

(a) The proposed method of splitting the taxation of the food and drink LAFHAs between the fringe benefits provisions and the income tax provisions is unnecessarily complex and will have flow-on compliance costs for employers and employees. It is submitted that the approach adopted in the Exposure Draft preceding the Bill (ie the taxation of LAFHAs is dealt with wholly within the income tax legislation) is more appropriate.

(b) If the approach in the Bill is retained, amendments need to be made to section 30 of the Bill to ensure it operates as intended and does not result in all food and drink LAFHAs being subject to fringe benefits tax.

2. LAFHA FOOD AND DRINK BENEFITS AS TAXABLE FRINGE BENEFITS

Under the Bill, the tax treatment of food and drink LAFHAs are split between the fringe benefits tax and income tax regimes. We submit that structuring the tax treatment of LAFHAs is unnecessarily complex and will increase compliance costs.

2.1 Current tax treatment of food and drink LAFHAs

Currently, when employers determine the amount of an allowance to be paid to an employee for food and drink expenses while the employee is required to work away from home, they will generally either:

(a) deduct from the allowance their employee's eligible statutory food amount (which is now referred to in Bill as 'ordinary weekly food and drink expenses'); or

(b) make no such deduction.

The statutory food amount is intended to be a proxy for the expenditure that the employee might reasonably be expected to have incurred if they resided at their usual place of residence. If the first calculation method is applied (ie the statutory food amount is deducted) the food and drink allowance would generally be exempt from fringe benefits tax ("**FBT**"). If the second calculation method is used (no deduction), the statutory food amount would generally be subject to fringe benefit tax.

The tax treatment of the allowance is illustrated in the Worked Example provided in the Appendix, by comparing the two calculation methods.

2.2 Technical issues with the proposed FBT provisions

Under the Exposure Draft released prior to the Bill being tabled in Parliament, the tax treatment of the LAFHA food benefits was to be wholly encompassed in the *Income Tax Assessment Act 1997* (Cth) ("**ITAA**"). The Exposure Draft resulted in a food and drink LAFHA being included in the employee's assessable income, but allowed employees to deduct expenses for food and drink, in excess of their "ordinary weekly food and drink expenses". These payments did not fall under the fringe benefits regime.[1] The changes were intended to move the LAFHAs from the scope of fringe benefits and broadly reinstate the tax treatment of LAFHAs before the introduction of FBT.[2]

This approach in the Exposure Draft was changed in the Bill, which proposes that food and drink LAFHAs be partially taxable as fringe benefits and partially subject to income tax.

Proposed section 30 of the *Fringe Benefits Tax Assessment Act 1986* (Cth) ("**FBTAA**"), set out in the Bill, provides that any food and drink LAFHA paid by employers "which does not exceed an employee's ordinary weekly food and drink expenses... constitutes a benefit provided by the employer".[3] This component of the food and drink LAFHA will be a taxable fringe benefits. The remaining food and drink LAFHA is treated as assessable income of the employee under the ITAA.[4]

The Explanatory Memorandum (**"EM"**) accompanying the Bill notes that this treatment is consistent with the treatment of most allowances[5] and that the component "representing 'ordinary weekly food and drink expenses' will continue to be treated as a fringe benefit".[6]

In relation to the latter statement, as outlined above and as demonstrated in the Worked Example contained in the Appendix, under the current law the "ordinary weekly food and drink expenses" or "statutory food amount" component of a food and drink LAFHA will not always be treated as a taxable fringe benefit, depending on how the allowance has been calculated. Practically, most employers would deduct the "statutory food amount" so that the entire LAFHA food component is exempt from FBT. Accordingly, we submit that the provisions of the Bill which seek to partly tax LAFHAs as fringe benefits are not consistent with the current FBT treatment of food and drink LAFHAs and is based on a misunderstanding of how the current law is applied.

Accordingly, the approach under the Exposure Draft of the Bill (to deal with LAFHAs wholly within the income tax regime) should be readopted.

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[1] Explanatory Materials, Reform of the Living-Away-from-Home Allowance and Benefit Rules, House of Representatives, 11.

[2] Ibid, [2.12].

[3] s 30 Tax Laws Amendment (2012 Measures No. 4) Bill 2012.

[4] Explanatory Memorandum, Tax Laws Amendment (2012 Measures No. 4) Bill 2012, [1.19].

[5] Ibid.

[6] Ibid, [1.20].

2.3 Increased complexity

It is submitted that the general approach of splitting the tax treatment of food and drink LAFHAs between the FBT and income tax regimes should be abandoned as it is overly complex.

Not only will employers be subject to a fringe benefits tax liability in relation to the "ordinary weekly food and drink expenses" component of food and drink LAFHAs (as outlined above), the application of the FBT provisions is entirely dependent on whether the employees gives the employer a declaration that they meet the highly prescriptive requirements to deduct accommodation, food or drink expenses as set out in subsection 25-115(1) of the ITAA, and that this declaration remains in force.

If an employee does not give such a declaration or a declaration ceases to be in force, the tax treatment of food and drink LAFHAs will then fall outside the FBT regime. This means that the application of the law between individual LAFHAs will also be inconsistent.

If a declaration is provided, employees will need to monitor whether these declarations remain valid and will be exposed to a criminal offence if they do not notify their employer that they cease to comply with the relevant requirements. For example, an employee who is not an eligible fly-in fly-out worker, is required to notify their employer within 7 days if:

- their usual place of residence ceases to be available for their immediate use and enjoyment;
- they cease to have an expectation that they will resume living in that residence at the end of the period they are required to live away from it; or
- the first 12-month of the period they are required to live away from home ends.

It is therefore possible for the tax treatment of food and drink LAFHAs to go in and out of the FBT regime a number of times depending on the employee's circumstances.

In our submission such a system is likely to be unworkable in practice, will significantly increase compliance costs for employers and employees and will give rise to uncertainty.

3. AMENDMENTS TO SECTION 30

If the Committee recommends a retention of the current approach of splitting the tax treatment of LAFHAs between FBT and income tax, it is submitted that amendments still need to be made to the proposed section 30 of the FBTAA to ensure it operates in a manner consistent with the current law. That is, food and drink LAFHAs should only be subject to FBT to the extent that an employee's ordinary weekly food and drink expenses have not been deducted in calculating the amount of an employee's LAFHA.

Yours sincerely

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APPENDIX

Worked Example

In the example below, an employee is required to live away from their usual place of residence by their employer. The employee is living away from their usual place of residence, with their spouse.

In determining an allowance for additional food and drink expenses that the employee will incur as a result of being required to live away from their usual place of residence, the employer relies on the Commissioner of Taxation's determination of an amount that represents a reasonable food component for the fringe benefit tax year beginning 1 April 2012, being $400 for 2 adults (refer Tax Determination TD 2012/5).

The statutory food amount or ordinary weekly food and drink expenses amount is $42 per week per adult, being $84 in total for the purposes of this example.

The employee is paid a LAFHA food allowance based on the reasonable food component determined by the Commissioner, for both the employee and their spouse. The statutory food amount or ordinary weekly food and drink expenses amount is $42 per week, per adult.

It is assumed that the employee will meet the requirements in proposed subsection 25-115(1) of the ITAA.

There are two possible scenarios under this situation.

	Scenario 1 Employer does not make a deduction for ordinary weekly food and drink expenses	**Scenario 2** Employer does make a deduction for ordinary weekly food and drink expenses
Applying the current law	*Employer* Food allowance = $400.00 Taxable fringe benefit = $42.00 x 2 = $84.00 Taxable amount = $157.00 Therefore **FBT ≈ $73.00** *Employee* **No tax** as allowance is non-assessable, non-exempt income	*Employer* Food allowance = $400.00 – ($42.00 x 2) = $316.00 As deduction for ordinary weekly food and drink expenses made. Food allowance is wholly exempt, **no FBT payable**. *Employee* **No tax** as allowance is non-assessable, non-exempt income
Applying the proposed Bill	*Employer* Food allowance = $400.00 First $84.00 is a taxable fringe benefit Therefore **FBT ≈ $73.00**	*Employer* Food allowance = $400.00– ($42.00 x 2) = $316.00 First $84.00 is a taxable fringe benefit Therefore **FBT ≈ $73.00**[1]

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	Employee Non-assessable, non-exempt income: $84.00 Assessable income: $316.00 Deductible amount: $316.00 **$0.00**	*Employee* Non-assessable, non-exempt income: $84.00 Assessable income: $232.00 Deductible amount: $316.00 **Net deductible amount: ($84.00)**
Applying the approach in the Exposure Draft	*Employer* **No FBT payable.** *Employee* Assessable income: $400.00 Deductible income: $316.00 **Net assessable amount: $84.00**[2,3]	*Employer* **No FBT payable.** *Employee* Assessable income: $316.00 Deductible income: $316.00 **Net assessable amount: $0.00**

Notes:

[1] There is no "otherwise deductible" rule, therefore FBT is not reduced even though the employee can claim a deduction for expenditure which the allowance is compensating the employee for.

[2] Net assessable amount taxed at employee's marginal rate of tax.

[3] Tax on this amount may be collected through the PAYG system.

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