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15 July 2012

Dear Parliamentary Committee Members

Submission on Schedule 1 to the Tax Laws Amendment (2012 Measures No. 4) Bill 2012

PwC is pleased to make a submission in relation to the proposed reforms to the Fringe Benefits Tax (FBT) treatment of living-away-from-home (LAFH) benefits pursuant to Schedule 1 of the *Tax Laws Amendment (2012 Measures No. 4) Bill 2012* (the Bill).

Our submission is in two sections:

1. Impact on Australian business
2. Submission on the Bill

We also attach our prior submissions in relation to the proposed reforms as many of the matters raised in these submissions remain relevant in relation to the Bill.

In this submission, references to "LAFH benefits" are to LAFH accommodation and food benefits.

PwC would welcome the opportunity to discuss this submission. Please contact Jim Lijeski on (02) 8266 8298 or Norah Seddon on (02) 8266 5864 with any queries in relation to our submission.

Yours sincerely

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1. Impact on Australian business

We believe the proposed reforms in the Bill will have a significant negative impact on Australian business and therefore on the Australian economy.

In summary, the negative impacts include:

1. higher costs to business including higher labour costs for mobile employees along with additional payroll tax, superannuation and workers compensation costs;

2. business needing to address these higher costs through moving contracts and projects offshore, additional costs being passed onto customers (and ultimately consumers) or contracts being terminated because the profits on the contracts have become uncommercial; and

3. a significant negative impact on Australia's competitiveness in the global talent war resulting in current employees leaving Australia because of the removal of the LAFH benefits and creating difficulties in attracting talent and key skills to Australia because of our remoteness from the rest of the World and the high cost of living (including tax rates) as compared to other countries.

The proposed reforms make a distinction between employees who are temporary residents and those that are not. The first two impacts above are relevant for both types of employees and the third is mainly relevant for temporary resident employees.

In June 2012, PwC conducted a survey of *Business response to reforms to Living Away from Home rules* to understand the impact of the proposed reforms on business. The survey had 121 respondent organisations and showed that of the participants:

- 77% expected additional costs to arise to their business;
- 44% expected to have difficulty in retaining talent (14% of the survey participants had already had someone go home as a result of the proposed reforms);
- 55% expected to have difficult in attracting new talent;
- 14% expected that current projects may not be viable; and
- 41% expected that Australia would be less competitive in comparison to other countries.

The survey results support the impacts listed above.

Australian business needs people to be mobile within Australia and inbound into Australia to address skills shortages in certain industries and regions and to meet short and medium term business needs. The need for mobility is a business need. As a result, the additional costs of compensating employees who are required to be mobile to meet short to medium term business needs (2+ years) should be recognised as a legitimate and necessary business expense and afforded concessional treatment, rather than giving rise to additional tax costs to the employer and/or employee. This recognition existed at the time of introduction of living away from home concessions into the FBT legislation however it appears to have been overlooked in the reasons being given for the need for the reform of the LAFH rules.

The personal impact for foreign and Australian employees living away from home in Australia is always significant for both the employee and their family. The removal of the taxation concessions for LAFH benefits for many employees will merely add to the reasons for the employee not to be mobile, unless the cost is fully met by their employer. Currently, the additional cost it often 'shared' by the employer and employee. Where the cost is met by the employer, this increases the cost to and complexity for business. For example, business will need to decide how will the cost be met – an additional allowance, the employer paying the relevant costs directly, a one –off mobility premium or another approach- and each of these alternatives have associated Human Resource and administrative complexities. The LAFH reforms remove an incentive for people to be mobile and will make mobility more costly for business.

If business needs cannot be met by appropriately skilled people, this will have a negative impact on the Australian economy. The flow-on effects of the proposed reforms need to be fully considered.

2. Submission on the Bill

Transitional rules – Temporary residents & non-residents

We are disappointed that there are no transitional rules for temporary residents and non-residents. We believe that it would be fair and equitable to have transitional rules for such employees similar to the transitional rules for permanent residents.

While temporary resident employees have been aware since 29 November 2011 that there would be future changes in relation to LAFH benefits they were receiving, they and their employers hoped that there would be transitional rules for a period of time after the final form of the changes was available.

These temporary residents made good faith decisions to come to Australia based on LAFH benefits that have consistently been available since 1945 and they are here currently contributing to the Australian economy.

The employers of temporary resident employees have also budgeted for the cost of having such employees here temporarily and these budgeted costs have been taken into account in business decisions including those regarding contract pricing. In the case of many fixed price contracts, these additional costs in relation to existing employees cannot be passed onto customers. As a result of the additional cost to business, other business decisions need to be made (e.g. does the contract need to be terminated? Do some of the services currently being provided by employees in Australia need to be moved offshore?).

While the proposed LAFH provisions will not apply until 1 October 2012, temporary residents still have to make arrangements and decisions in relation to the LAFH reforms in the Bill. These arrangements and decisions are having a significant impact on temporary residents, their families and their employers. We believe that temporary residents will consider returning home (and the PwC survey results show that some already have returned home) as a result of the LAFH reforms and their employers are also considering the impact on their business in deciding the employer's response to the changes.

The absence of transitional rules for temporary residents is disappointing and is also likely to have a significant negative impact on Australian business and the economy.

Transitional rules – "Permanent residents"

Transitional rules apply to permanent residents who have employment arrangements for LAFH benefits in place at 7:30pm (AEST) on 8 May 2012. "Permanent residents" are taxpayers who are not temporary residents or non-residents for Australian income tax purposes.

The conditions for LAFH benefits in the Bill to:

- Maintain a home in Australia for the employee's use and enjoyment; and
- Limit the concessional treatment to a maximum of 12 months;

will not apply to permanent residents until the earlier of 1 July 2014, when the employee ceases to be living away from home, the date a new employment arrangement is entered into or the date an eligible employment arrangement is varied or renewed.

Based on paragraph 1.81 of the Explanatory Memorandum, the term "varied" refers to any **material** variation to an "eligible employment arrangement". Paragraph 1.81 of the Explanatory Memorandum also seeks to explain what a "material variation" would be.

In the context of the transitional rules for permanent residents, we submit that a "material variation" to an employment contract should only occur where there is a variation that changes the requirement for the employee to live away from home for the purposes of their employment.

We also submit that changes to the living away from home benefits (e.g. changing from a reimbursement to an allowance or vice versa, changing accommodation benefits as a result of a change in rent, changing food and drink allowances as a result of the change in the reasonable food amounts each year) should not be a material variation that would result in the transitional rules ceasing to apply to an employee.

Paragraph 1.81 of the Explanatory Memorandum specifically includes an extension of time to an existing contract, change in the salary of an employee and change in the working hours of the employee as examples of material variations to an employment arrangement. We address each of these in turn below.

1. *Extension of time*

Consider an employee who is required to live away from home for a 12 month period in relation to a specific project. If:

- The project is running late and, as a result, the employee's assignment contract is extended by another 6 months after which the employee still intends to return home, we submit that the extension should not be a material variation to the employee's contract for the purposes of the transitional rules because there has been no change to the requirement for the employee to live away for home for the purposes of their employment; or
- The project becomes an ongoing project and the employee's contract is varied so that their employment in the project location is indefinite, then we submit that such a variation should be treated as a material variation and the employee should no longer be able to claim the transitional rules.

2. Change in salary

In our discussions with Treasury, they have indicated that pay rises should not generally represent a material variation to an employment arrangement however promotions could represent a material variation to an employment arrangement for the purposes of the transitional rules. It is unclear from the Explanatory Memorandum that pay rises are not intended to trigger the new provisions and that only promotions are meant to trigger the new LAFH benefit provisions.

As a promotion would lead to the new LAFH benefit provisions being triggered, this may lead to dilemmas for employers that may face difficulties in being able to award or agree to a promotion with those employees that are eligible to access the transitional provisions for LAFH benefits.

We submit that neither a pay rise nor a promotion should result in a material change to an employment arrangement unless it changes the nature of the employee's employment such that it changes the requirement for the employee to be living away from home. There is no reasonable basis for ceasing entitlement to the transitional provisions for LAFH benefits based on changes that are unrelated to an individual's LAFH arrangement.

For example, if an employer:

- Has sent an employee on assignment and during that assignment it gives a pay rise to the employee, if the requirement for the employee to live away from home has not changed as a result of the pay rise, then we submit that the pay rise should not be a material variation of an employment contract for the purposes of the transitional rules.

- Promotes an employee while the employee is on assignment and the promotion is in the ordinary course of the business of the employer (e.g. as part of a regular review process), as long as the promotion does not change the requirement for the employee to live away from home, then we submit that this should not be a material variation of an employment contract for the purposes of the transitional rules. Where the promotion is significant (e.g. from a more junior role that is for a fixed term to become the Chief Executive Officer of a company on an employment contract without a defined term) and the new role does not require the employee to live away from home, then we submit that this should be a material variation to an employment contract for the purposes of the transitional rules.

Summary

We submit that paragraph 1.81 of the Explanatory Memorandum should be updated and expanded to provide more guidance and make it clear that material variations are only those that change the requirement for the employee to live away from home.

Whether a material variation has taken place is a question of fact and should be considered in light of the existing circumstances. For the purposes of the transitional rules, a variation should only be material where it changes the employer's requirement for the employee to live away from home. Any changes in salary by way of a pay rise or promotion, changes in the working hours and any administrative changes to an employment arrangement where the employer still requires the employee to live away from home should not represent a material variation in the employment arrangement and therefore the employee should still qualify for the transitional rules.

Food & drink allowances

The proposed new rules for food and drink allowances separate a reasonable food and drink weekly allowance into:

a) the ordinary weekly food and drink expenses (being $42 for an adult and $21 for a child under 12 years) which, subject to the employee giving the employer a declaration in force under new section 30A of the *Fringe Benefits Taxation Assessment Act 1986* (FBTAA), is a taxable fringe benefit in new section 30 of the FBTAA; and

b) the excess above the ordinary weekly food and drink expenses will be an assessable allowance under income tax rules where the employee satisfies paragraphs 25-115 (1) (a) to (e) of the 1997 Act. The employee may claim an allowable deduction for expenses in excess of the ordinary weekly food and drink expenses if the requirements of new section 25-115 of the *Income Tax Assessment Act 1997* Act (1997 Act) are met.

For example, the reasonable food allowance for one adult for the FBT year ending 31 March 2012 is $250 per week according to Tax Determination TD 2012/5. Under the proposed new rules, the weekly ordinary food and drink expenses are $42 and will be subject to FBT which is $36.50. The balance of $208 is an assessable allowance to the employee and he or she may claim an income deduction for expenses in accordance with new section 25-115 of the 1997 Act.

The current rules in the FBTAA treat the amount of $208 as an "exempt food component" (see definition in subsection 136 (1) FBTAA) for which the taxable value may be reduced to nil under s31 of the FBTAA (subject to the employee providing the employer with a LAFH declaration by the declaration date).

It is common practice for employers in providing LAFH benefits to eligible employees under the current FBT rules, to pay a food allowance which is equal to the "exempt food component" (and is described accordingly) and does not include an allowance for the ordinary food and drink amount. This addresses the administrative and practical problems for an employer in dealing with benefits which would otherwise be partly subject to FBT.

The proposed new rule operates by deeming the ordinary weekly food and drink expenses of a reasonable food allowance to be a taxable fringe benefit. This ensures tax is paid upon the ordinary weekly food and drink expense either because FBT is paid thereon by the employer or the employee authorises the employer to deduct those expenses from his or her post-tax monthly salary (which means income tax rates apply to those expenses).

The absence of a new rule similar to the "exempt food component" will serve to **increase** remuneration costs for an employer.

In the example above, the employer paying $208 has an immediate problem from 1 October 2012 (the proposed start date for the new rules). In order to provide the employee with a $208 weekly food and drink allowance for which an income tax deduction is available, the employer's costs will increase to $286.50 as follows.

	Scenario 1 (employer meets FBT cost)	Scenario 2 (employee bears income tax cost)
Reasonable allowance paid to employee	$250.00	$250.00
Add FBT	$36.50	
Less amount repaid by employee	Nil	($42.00)
Total cost to employer	**$286.50**	**$208.00**
Net amount received by employee	**$250.00**	**$208.00**

The costs above do not include for example, the increased State and Territory Government Payroll Taxes (around 6%) or, if applicable, 9% superannuation contributions.

Our suggestion is that a new version of the "exempt food component" rules should be considered by Treasury and employers should be permitted to pay an allowance to employees that does not include an amount in relation to the ordinary weekly food and drink amount (i.e. the $42). This would involve making the reasonable food allowance limits only in respect of the additional food costs over normal costs (that is, in relation to the above example, the reasonable limit would be $208, down from $250).

Time cap on LAFH benefits

Under the proposed reforms, where an employee is living away from home, LAFH benefits will only be available for a maximum 12 month period. We submit that the 12 month cap is too low for many projects and business requirements where an employee is required to live away from home and suggest that a 2 year period would reflect more situations where there is a short to medium term employer requirement for an employee to live away from home.

The limitation under the "once-only 12 month rule per location" is that an employee, who is temporarily transferred to another work location, may only avail themself of the LAFH concession for that location for one occasion. No concession is available for any later temporary transfers to that same location. We submit that the "per location" is changed to a "per assignment" test. Where employees return to a previous location to which they have been on assignment previously, we suggest that the integrity of the concession would be maintained with the inclusion of a requirement that the employee resumes living in their usual place of residence for a minimum period between the assignments to the same location of (say) 6 months.

Usual place of residence is available for use and enjoyment

Another condition that must be met for the LAFH benefits to be claimed is that employees who are temporarily transferred to another work location are not eligible for the LAFH concession unless they are living away from an Australian home which at all times is kept available for their immediate use and enjoyment.

This requirement raises many additional (non-tax) issues. For example, where the home is left vacant for 12 months, the costs of maintaining the home can increase with all the associated and attendant insurance and maintenance problems or where the spouse and family have to stay behind for the first 12 months in order to maintain the home there can be a significant impact on the family.

We reiterate that the LAFH benefits should be an incentive for employees to be mobile and having additional costs and issues to address in keeping a usual place of residence available for use and enjoyment is a significant disincentive for employees to be mobile.

The requirement also adds significant complexity for employers in meeting their obligations as, if the employer is paying for the accommodation and other expenses in the assignment location, the employer needs to understand the details of the employee's personal arrangements in order to comply with the employer's tax obligations.

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3 February 2012

Dear Sir

Submission on the Consultation Paper Fringe Benefits Tax Reform Living-Away-From-Home Benefits

PricewaterhouseCoopers welcomes the opportunity to make a submission in relation to the proposed reforms to the fringe benefits tax (FBT) treatment of Living Away From Home (LAFH) benefits as announced by the Government on 29 November 2011.

Our submission is in three sections:

1. Impact on Australian business
2. Alternative approaches
3. Questions for consultation

In this submission, references to "LAFH benefits" are to LAFH accommodation and food benefits.

The key conditions for an allowance to qualify as a LAFH benefit (including accommodation and food allowances) are:

1. The payment is an allowance paid by the employer to an employee in respect of the employee's employment; and

2. the whole or a part of the allowance is in the nature of compensation to the employee for additional expenses (not being deductible expenses) incurred by the employee and any other additional disadvantages arising to the employee during a period because that the employee is required to live away from the employee's usual place of residence in order to perform the duties of employment.

1. Impact on Australian business

Based on our discussions with clients, other interested parties and on the impact on PwC's own business, the proposed reforms will have a significant impact on Australian business.

LAFH benefits have been and are currently provided to employees to attract people with key skills and experience to Australia either on a short term basis (e.g. a 6 month assignment for a specific customer contract) or on a medium term basis (e.g. a 2-4 year secondment to the Australian business to bring a specific skills set or knowledge to the business). Many of these positions are advertised both within Australia and overseas and are usually filled on a fixed short or medium term basis.

In our experience, LAFH benefits are provided to employees on all types of salaries and not just to executives in senior positions. LAFH benefits are also provided by employers in many industries.

In many sectors in Australia, there is a critical skills shortage and there is therefore a need to attract and retain skilled employees from overseas. In competing for employees, the LAFH benefits are seen to offset the high headline tax rate (46.5%) and cost of living for which Australia is well known internationally. As such, LAFH benefits are a key attraction and retention tool for Australian business and are provided to compensate employees for additional costs because they are in Australia for a short or medium term assignment.

It is also worth noting that some of the employees that come to Australia on a short or medium term basis ultimately decide to apply for permanent residency in Australia. They then contribute to Australia's skills base and contribute to government revenues through paying income tax on a long term basis.

The impacts on Australian business are expected to include:

1. Significantly higher costs to Australian business as additional amounts will need to be paid by employers so as to leave affected employees in the same after tax position once the proposed reforms are introduced – as outlined above, many temporary residents are needed by Australian business to address the skills shortage in Australia and therefore business will need to ensure that the employee is not disadvantaged upon the introduction of the proposed reforms;

2. The higher cost of labour in Australia resulting from the removal of the LAFH benefits for temporary residents may result in:

    a. Contracts and projects being moved offshore to lower labour cost countries either because of cost to the business or because business cannot attract employees to Australia with the necessary skills. If contracts and projects are moved offshore there is likely to be an impact on both the business concerned and on the Australian employees that would have been employed to work on the contracts or projects;
    b. The additional costs being passed onto customers (including consumers and government); and
    c. The profits on current contracts and projects becoming uncommercial and therefore the contract and project being terminated;

3. Where the reforms are implemented there is a real possibility that a large number of temporary residents will leave Australia soon after 1 July 2012 as a result of the increased cost of residing in

Australia, which makes employment offers from overseas companies more attractive and competitive than Australian businesses can offer; and

4. There will also be significantly higher costs for business as a result of the proposed change due to additional payroll tax, superannuation and workers compensation expenses arising because of the move of LAFH accommodation and food benefits moving from being fringe benefits to being salary and wages.

All of the above impacts are likely to result in lower taxable income of Australian businesses and therefore lower corporate taxes being paid.

In summary, the proposed reforms will have a significant negative impact on Australian business and therefore on the Australian economy.

2. Alternative approaches

We believe that retaining the currently LAFH accommodation and food benefits is in the best interest of Australian business and therefore the Australian economy.

That said, we have outlined below alternative approaches that may assist the government in achieving the stated aims of the proposed reforms. The Forward to the Consultation Paper states that: the changes will ensure a level playing field exists between hiring an Australian worker or a temporary resident worker living at home in Australia, in the same place, doing the same job.

We also believe that these alternatives also allow Australia to address the requirements of the non-discrimination articles in its Double Taxation Treaties (this is discussed in more detail in Question 3 of the Questions for Consultation below).

We are happy to discuss these alternatives in more detail.

Inspector-General of Taxation Report – January 2007

If there are concerns in relation to how the LAFH benefits have been administered in the past, we suggest that Recommendation 2 in the *Review of Tax Office's management of complex issues — Case study on living-away-from-home allowances*, a report by the Inspector-General of Taxation to the Minister for Revenue and Assistant Treasurer dated 24 January 2007 is implemented.

We note that this report did not even consider a distinction between temporary and non-temporary residents in relation to how the LAFH provisions should be administered.

Recommendation 1 was that the Commissioner of Taxation reach a conclusion whether the Australian Taxation Office should advise Treasury that a legislative change was needed to the LAFH provisions. Recommendation 2 then stated that:

> In the absence of the Tax Office providing such formal advice to Treasury or any legislative change, then the Tax Office should issue a new public ruling to replace Miscellaneous Taxation Ruling MT 2030. The new public ruling should provide community-wide guidance and certainty on the Tax Office's interpretation, administration and practical application of the LAFHA provisions, and should include clarification of the key technical issues arising from this review such as:

- usual place of residence;
- meaning of the term 'additional';
- factors the Tax Office would take into consideration in determining what was 'reasonable' for the purposes of a LAFHA including guidance on methods which would be acceptable to the Tax Office;
- causation between employment and entitlement to receive a LAFHA, in particular, whether there is a requirement for a pre-existing employee/employer relationship for a LAFHA entitlement.

Requirement to return to a specific home

Where a temporary resident worker is maintaining a home in their home country and also paying for accommodation in Australia, there is not a level playing field between an Australian worker and a temporary resident worker in the same place, doing the same job. The temporary resident worker is incurring additional expenses that the Australian worker is not. This is especially the case for workers in Australia on a short term basis (e.g. a 6 month assignment) where giving up their home in their home country is not practical.

LAFH benefits are the way in which a temporary resident (and any other employee that is LAFH) is compensated for these additional expenses. Given that benefits cannot qualify as LAFH benefits unless they are in the nature of compensation to the employee for additional expenses of and disadvantages arising to the employee during a period because that the employee is required to live away from the employee's usual place of residence in order to perform the duties of employment, by their very nature, LAFH benefits level the playing field where an actual home is maintained by the temporary resident worker.

With the above as background, we believe that the stated aims of the proposed reforms could be achieved through maintaining LAFH benefits for temporary resident workers however, for accommodation benefits, all workers (temporary resident or not) would need to maintain a home in their home location (country or state) rather than only having an intention to return to a specific city or district. The worker would need to substantiate that the property was their home and guidance would be needed from the Australian Taxation Office as to appropriate documentation to substantiate this statement.

Reimbursements only for LAFH accommodation

Another alternative to achieve the stated outcome of a level playing field is to operate the LAFH accommodation benefit on a reimbursement basis only.

Historically, allowances have been paid to employees for administrative simplicity and efficiency rather than to allow employees to "pocket" the excess allowance as tax-free income. Many Australian businesses require employees to show them a copy of a signed lease as evidence of the allowance being reasonable and equivalent to what the employee actually pays in rent.

While paying allowances would still be simpler and more efficient, operating LAFH accommodation allowances on a reimbursement basis only would address the concern in the Consultation Paper that "the concessions currently allow some employees to access large amounts of tax-free remuneration through allowances that are well in excess of the actual costs incurred by the employee".

Again, this change would apply to all workers, not just temporary resident workers.

3. Questions for Consultation

The specific questions for consultation in the paper are:

1. Are there any unintended consequences from the proposed reforms?

We believe that the significant impacts on business as outlined in Section 1 of this submission are likely to be unintended consequences of the proposed reforms. As a result, we respectfully submit that the alternative approaches in Section 2 should be considered in order to achieve the aims of the proposed reforms as outlined in the Consultation Paper.

2. What practical aspects of the proposed reforms need further consideration?

The practical aspects that need further consideration are outlined below.

Determining whether an employee is a temporary resident

In order to determine who can receive LAFH benefits, employers will need to understand whether the individual is a "temporary resident" as defined. This will also be relevant when an employee requests a PAYG withholding variation (see below).

To determine whether someone is a "temporary resident" as defined is not as simple as just checking whether or not the employee has a section 457 temporary work visa sponsored by the Australian employer. A temporary resident is both a section 457 temporary visa holder lawfully in Australia and a foreign national whose spouse, or former spouse, is not, and has never been, an Australian citizen or permanent resident. Spouse includes both legal and de facto relationships and, from 1 April 2009 de facto relationships include both opposite sex and same-sex relationships. From this definition it can be seen that employers may need to ask questions that employees may not wish to answer from a privacy perspective.

Consideration should therefore be given to the Australian Taxation Office providing statements in an approved form that employees can give to their employers in relation to their Temporary Resident status and on which the employer can rely.

PAYG variations

Example 1 in Section 2.2 of the Consultation Paper gives an example of Ciara, an employee who is LAFH that intends to claim income tax deductions for her accommodation and food expenses while she is LAFH. The Example states that "Ciara's employer does not have to withhold tax from the LAFHA because she indicates to them that she will be claiming a deduction."

Guidance is requested on how Ciara will "indicate" to her employer that she will be claiming a deduction and what the employer will need to do to approve a PAYG withholding variation in these circumstances.

Substantiation that a unit of accommodation is available

Under the proposed reforms, a temporary resident will only be eligible for LAFH benefits while living away from an Australian home provided that home is available for their personal use and enjoyment at all times. The Consultation Paper makes clear at paragraph 2.1.5 that the unit of accommodation cannot be rented out or sub-let while the temporary resident is LAFH. Under the proposed reforms, temporary residents in this situation will be required to provide documentary evidence to their employers that they are maintaining a home for their own use.

The documentary evidence will be difficult to produce as the evidence will be "proving a negative fact" rather than "proving a positive fact". Guidance should be provided by Treasury or the Australian Taxation Office as to examples of appropriate documentary evidence.

Move from FBT to Income Tax provisions

Moving the LAFH provisions from the *Fringe Benefits Taxation Act 1986* will increase the compliance burden on individual employees in relation to complex provisions. Under the current provisions, this compliance burden sits with the employer who commonly has guidelines and policies on which advice has been sought to ensure compliance with the relevant provisions.

Guidance from the ATO to individual employees would be appreciated as the LAFH provisions can be complex to apply.

3. Are there any interactions with other areas of the tax law that need to be addressed?

A key part of Australia's taxation laws are Australia's Double Taxation Treaties. Many of these treaties (for example, the United Kingdom and the United States) have non-discrimination articles. Under a non-discrimination article, nationals of the foreign country cannot be worse off under taxation or connected laws than an Australian national in the same circumstances.

The proposed reforms will result in a temporary resident employee who is LAFH being denied deductions for accommodation and food expenses. An Australian resident employee who is not a temporary resident and who is also LAFH will be able to claim such deductions. This is in clear contradiction to the requirements of the non-discrimination articles in Australia's Double Taxation Treaties.

Another potential contravention of the non-discrimination clause could arise where a foreign national who is a temporary resident (as defined) is LAFH but is denied deductions for accommodation and food benefits whereas another foreign national who has an Australian spouse (and is therefore not a temporary resident as defined) is LAFH and can claim such deductions.

The OECD model convention article and commentary for the non-discrimination article are shown below and the non-discrimination article in the treaties with the United Kingdom and the United States are shown in Appendix 1 to this submission.

Paragraph 1 of Article 24 of the OECD Model Convention states that:-

> Nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith, which is other or more burdensome than the taxation and connected requirements to which nationals of that other State in the same circumstances, in particular with respect to residence, are or may be subjected. This provision shall, notwithstanding the provisions of Article 1, also apply to persons who are not residents of one or both of the Contracting States.

Paragraph15 of the OECD commentary for paragraph 1 of Article 24 states the following:

> Subject to the foregoing observation, the words ". . . shall not be subjected . . . to any taxation or any requirement connected therewith which is other or more burdensome . . ." mean that when a tax is imposed on nationals and foreigners in the same circumstances, it must be in the

same form as regards both the basis of charge and the method of assessment, its rate must be the same and, finally, the formalities connected with the taxation (returns, payment, prescribed times, etc.) must not be more onerous for foreigners than for nationals.

We strongly suggest that the alternative approaches outlined in Section 2 of this submission are considered as we believe that these address the requirements of the non-discrimination articles.

4. As the statutory food amount is intended to reflect the ordinary costs incurred by an Australian in 2011, what should the statutory food amount be updated to?

It would be appropriate for the Government to conduct a survey through a reputable information provider to be used as the basis for determining the appropriate statutory food amount.

5. Should the statutory food amount be indexed annually to ensure that it remains up to date?

The statutory food amount should be reviewed regularly to ensure that it remains up to date.

The statutory food amount should either:

- be indexed annually and updated with a formal survey through a reputable provider on a regular basis (say every 5 years); or

- be updated with a formal survey through a reputable provider on a more regular basis than the first option (say every 3 years).

6. What transitional arrangements would be appropriate for the community sector?

This question for consultation focuses solely on the community sector. As the implications of the proposed reforms will impact almost all industries in Australia, any transitional arrangements should be for all affected taxpayers and not just those in the community sector.

Suggested transition arrangements could include:

- employees currently receiving LAFH benefits could continue to receive the full LAFH benefit for the period of their fixed term employment contract where this period is of no more than 4 years (say) in total;

- employees currently receiving LAFH benefits to receive a capped LAFH benefit for a period of their fixed term employment contract where this period no more than 4 years (say) in total. The cap could be determined by the ATO and could either a specified percentage of the employee's total remuneration package (including salary, superannuation and other fringe benefits) or a specified amount. If an amount was specified, we suggest that a survey is conducted through a reputable provider on the appropriate amount for relevant cities; or

- for all affected taxpayers who, as at 29 November 2011, were LAFH, were claiming accommodation benefits under the LAFH provisions and who were in a fixed term lease, where the fixed term for this lease ends after the proposed implementation date of the reforms of 30 June 2012, transitional rules should permit these taxpayers to continue to claim accommodation benefits under the LAFH provisions until the end of the fixed term lease. This transitional approach would be consistent with the recent transitional

arrangements for motor vehicles and the changes to the *Fringe Benefits Taxation Act 1986*.

Without such transitional rules there will be significant financial hardship for individual taxpayers who made the decision to enter into the fixed term lease or employment contract based on the taxation laws that existed (and had existed since 1945) at the time that the decision was made.

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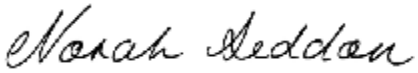
PricewaterhouseCoopers would welcome the opportunity to discuss this submission with Treasury. Please contact Jim Lijeski on 02 8266 8298 or Norah Seddon on 02 8266 5864 with any queries in relation to the contents of this submission.

Yours sincerely



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APPENDIX 1

United Kingdom

ARTICLE 25
Non-discrimination

1 Nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith, which is other or more burdensome than the taxation and connected requirements to which nationals of that other State in the same circumstances, in particular with respect to residence, are or may be subjected.

2 The taxation on a permanent establishment which an enterprise of a Contracting State has in the other Contracting State shall not be less favourably levied in that other State than the taxation levied on enterprises of that other State carrying on the same activities in similar circumstances.

3 Except where the provisions of paragraph 1 of Article 9, paragraph 8 or 9 of Article 11, paragraph 6 or 7 of Article 12, or paragraph 4 or 5 of Article 20 of this Convention apply, interest, royalties and other disbursements paid by an enterprise of a Contracting State to a resident of the other Contracting State shall for the purpose of determining the taxable profits of such enterprise, be deductible under the same conditions as if they had been paid to a resident of the first-mentioned State.

4 Enterprises of a Contracting State, the capital of which is wholly or partly owned or controlled, directly or indirectly, by one or more residents of the other Contracting State, shall not be subjected in the first-mentioned State to any taxation or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which other similar enterprises of the first-mentioned State in similar circumstances are or may be subjected.

5 Nothing contained in this Article shall be construed as obliging a Contracting State to grant to individuals who are residents of the other Contracting State any of the personal allowances, reliefs and reductions for tax purposes which are granted to individuals so resident.

6 This Article shall not apply to any provision of the laws of a Contracting State which:

(a) is designed to prevent the avoidance or evasion of taxes;

(b) does not permit the deferral of tax arising on the transfer of an asset where the subsequent transfer of the asset by the transferee would be beyond the taxing jurisdiction of the Contracting State under its laws;

(c) provides for consolidation of group entities for treatment as a single entity for tax purposes provided that Australian resident companies that are owned directly or indirectly by residents of the United Kingdom can access such consolidation treatment on the same terms and conditions as other Australian resident companies;

(d) provides deductions to eligible taxpayers for expenditure on research and development; or

(e) is otherwise agreed to be unaffected by this Article in an Exchange of Notes between the Government of Australia and the Government of the United Kingdom.

7 The provisions of this Article shall apply to the taxes which are the subject of this Convention.

United States

ARTICLE 23
Non-discrimination

(1) Each Contracting State in enacting tax measures shall ensure that:

(a) citizens of a Contracting State who are residents of the other Contracting State shall not be subjected in that other State to any taxation or any requirement connected therewith which is more burdensome than the taxation or connected requirements to which citizens of that other State who are residents of that other State in the same circumstances are or may be subjected;

(b) except where the provisions of paragraph (1) of Article 9 (Associated enterprises), paragraph (4) of Article 11 (Interest) or paragraph (5) of Article 12 (Royalties) apply, interest, royalties and other disbursements paid by a resident of a Contracting State to a resident of the other Contracting State shall, for the purpose of determining the taxable profits of the resident of the first-mentioned State, be deductible under the same conditions as if they had been paid to a resident of the first-mentioned State;

(c) a corporation of a Contracting State, the capital of which is wholly or partly owned or controlled, directly or indirectly, by one or more residents of the other Contracting State, shall not be subjected in the first-mentioned State to any taxation or any requirement connected therewith which is more burdensome than the taxation or connected requirements to which other similar corporations of the first-mentioned State in the same circumstances are or may be subjected; and

(d) the taxation on a permanent establishment which a resident of a Contracting State has in the other Contracting State shall not be less favorably levied in that other State than the taxation levied on residents of that other State that carry on the same activities in the same circumstances.

(2) Nothing in this Article relates to any provision of the taxation laws of a Contracting State:

(a) in force on the date of signature of this Convention;

(b) adopted after the date of signature of this Convention but which is substantially similar in general purpose or intent to a provision covered by sub-paragraph (a); or

(c) reasonably designed to prevent the avoidance or evasion of taxes;

provided that, with respect to provisions covered by sub-paragraphs (b) or (c), such provisions (other than provisions in international agreements) do not discriminate between citizens or residents of the other Contracting State and those of any third State.

(3) Without limiting by implication the interpretation of this Article, it is hereby declared that, except to the extent expressly so provided, nothing in the Article prevents a Contracting State from distinguishing in its taxation laws between residents and non-residents solely on the ground of their residence.

(4) Where one of the Contracting States considers that the taxation measures of the other Contracting State infringe the principles set forth in this Article the Contracting States shall consult together in an endeavor to resolve the matter.

* * * * * * * * * * * * * *

The Manager
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29 May 2012

Dear Sir,

Submission on the Exposure Draft of the Tax Laws Amendment (2012 Measures No. 3) Bill 2012: Deducting expenses for living away from home

PwC welcomes the opportunity to make a submission in relation to the Exposure Draft legislation (ED) of the Tax Laws Amendment (2012 Measures No. 3) Bill 2012: deducting expenses for living away from home and associated Explanatory Materials (EM).

In this submission, references to "LAFH benefits" are to Living Away from Home (LAFH) accommodation and food allowances and reimbursements.

Our submission is in two sections as follows:

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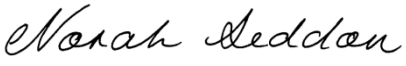

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1. Impacts on Australian business

We believe the changes in the ED will have a significant negative impact on Australian business and therefore on the Australian economy.

In our submission of 3 February 2012, we detailed these impacts in relation to the removal of LAFH benefits for temporary residents and these impacts still arise under the ED. In summary, the negative impacts include:

1. higher costs to business including higher labour costs for mobile employees along with additional payroll tax, superannuation and workers compensation costs;

2. business needing to address these higher costs through moving contracts and projects offshore, additional costs being passed onto customers (and ultimately consumers) and contracts being terminated because the profits on the contracts have become uncommercial; and

3. a significant negative impact on Australia's competitiveness in the global talent war resulting in current employees leaving Australia because of the removal of the LAFH benefits and creating difficulties in attracting talent and key skills to Australia because of the high cost of living (including tax rates) as compared to other countries.

Subject to certain transitional rules, the changes in the ED now place limitations on LAFH benefits for non-temporary ("permanent") residents. Where a permanent resident is living away from home, LAFH benefits will only be available for a maximum 12 month period for where the employee lives away from and maintains an Australian home for their use and enjoyment.

We believe that the impacts outlined above in paragraphs 1. and 2. will also arise in relation to the proposed changes in relation to permanent residents. In addition, we believe that the proposed changes in relation to permanent residents will inhibit employee mobility within Australia. This mobility should be encouraged in light of the skills shortage in many areas and industries within Australia. The limitations on LAFH benefits will mean that there will often be little incentive for employees to offset the disincentives of being mobile (for example, relocating families and lives, getting used to a new location and working environment, making new friends, the costs associated with maintaining family links in the home location).

In relation to the transitional rules in the ED, we welcome the transitional rules for permanent residents but are disappointed that there were no transitional rules introduced for temporary residents (other than temporary residents who were living away from an Australian home at 7.30pm on 8 May 2012).

These temporary residents made good faith decisions to come to Australia based on LAFH benefits that have been in place since 1945 and they are here currently contributing to the Australian economy. Temporary residents have been given 53 days (from Budget Night to 30 June 2012) to make arrangements and decisions in relation to the changes in the ED. These arrangements and decisions are having a significant impact on temporary residents, their families and their employers. We believe that temporary residents will consider returning home as a result of the changes in the ED and their employers are also considering the impact on their business in deciding the employer's response to the changes.

While temporary resident employees have been aware since 29 November 2011 that there would be future changes in relation to LAFH benefits they were receiving, they and their employers hoped that there would be transitional rules for a period of time after the final form of the changes was available.

The Australian economy needs employee mobility both domestically and internationally in order to meet the needs that arise as a result of the skills shortage in certain areas and industries. The changes in the ED remove a key incentive for employees to be mobile and will therefore have a significant impact on Australian business and the economy. The absence of transitional rules for temporary residents is disappointing and is also likely to have a significant negative impact on Australian business and the economy.

2. Submission on the Exposure Draft

2.1 12 month time limit for living away from home deduction

Proposed new subsection 25-115 (1) of the 1997 Act provides that "you can deduct an amount for an accommodation, food or drink expense you incur.....while living away from an Australian home where under new subparagraph 25-115 (1) (e) (i) .....the expense relates to all or part of the first 12 months that you live away from that residence as required by your employer".

While paragraph 2.50 of the Draft Explanatory Materials ('EM'), explains the 12 month period commences the first day the employee begins living away from home and paragraph 2.51 states the 12 month period pauses if the employee temporarily relocates to their usual place of residence, further guidance in the EM would be helpful as to:

- whether the day (or days) of travel to and from the usual place of residence count towards the 12 month period;
- when the 12 month period starts where a permanent resident has commenced an assignment during the period between Budget Night (8 May 2012) and the effective date of the changes in the ED (1 July 2012) – on the actual start date or 1 July 2012; and
- whether commuters (whose usual place of residence is say Sydney, and they work in say Melbourne on week days spending the weekend back home) should count the weekend days as a "pause".

In respect of commuters, the exception to the 12 month rule in subparagraph 25-115 (1) (e) (iii) suggests that commuters as described above may not be subject to the 12 month rule. The EM does state at paragraph 2.10 that the deduction will be limited to a period of 12 months (other than fly-in and fly-out workers). The inclusion of two subparagraphs in 25-115 (1) (e) for fly-in and fly-out workers indicates both remote and non-remote areas are meant to be carved out of the 12 month rule. Subparagraph (iii) is capable of being read so as to include interstate (and other) commuters. We suggest that an example is included in the EM in relation to commuter arrangements and how Treasury intends the changes in the ED to apply to such arrangements.

The EM makes clear that the 12 month period restarts if the employee's work location changes, that is, if the employee is required by their employer to move to another location to perform the duties of

employment and it would be unreasonable for the employer to require their employee to commute to the new location from the earlier location.

What is not clear is whether an employee can claim LAFH again if they are required by the same employer to work temporarily again at that same work location (perhaps many years later). It appears that as long as the employee has resumed living in their usual place of residence, the 12 month period should start again for the second assignment however we suggest that an example of such a situation and how the rules apply should be included in the EM.

Where the employer requires an employee to work at a new location, the EM states that the 12 month period will start again where it would be unreasonable for the employer to require their employee to commute to the new location from the earlier location. We suggest that a rule of thumb in relation to distance or travel time as to when it would be "unreasonable" for the employer to expect the employee to travel should be included in the EM.

We also note that there are genuine situations where employees will travel on business trips to a location and then subsequently start living away from home at that location. We believe that the 12 month rule should apply from the first date that the employee is living away from home however we ask that clarity is provided on this point in the EM. In addition, guidance on the difference between business trips and living away from home (e.g. length, type of accommodation, nature of work) should be provided.

2.2 Transitional provisions

Transitional rules apply to permanent residents who have employment arrangements for LAFH benefits in place at 7.30 pm (AEST) on 8 May 2012.The conditions in the Budget to:

- Maintain a home in Australia; and
- Limit the concessional treatment to a maximum of 12 months;

will not apply to permanent residents until the earlier of 1 July 2014 or the date a new employment arrangement is entered into.

Eligible employment arrangements

While the ED itself makes clear transitional rules apply to an eligible employment arrangement which cannot be varied or renewed, the EM does not actually provide any illustrative examples on what is meant by "your employer or a connected of your employer commits to provide you with an allowance or benefit for your accommodation, food or drink while you are required to live away from your usual place of residence".

In particular, neither the ED nor the EM address the situation where an employer has made an offer of employment to an employee that includes a commitment to provide LAFH benefits prior to 8 May 2012 but the offer is only accepted by the employee after 8 May 2012. Also, neither the ED nor the EM outlines whether an "eligible employment arrangement" includes company policies that commit to providing LAFH benefits to employees that are living away from home prior where both the employee was living away from home and such policies were in place on or prior to 8 May 2012.

Guidance is therefore requested in relation to whether these would qualify as an "eligible employment arrangement".

The ED and EM also do not define the terms "varied" or "renewed" for the purpose of the transitional provisions. As a result, it is unclear whether a change to the amount of rent charged under an existing arrangement or a change in the method that a LAFH benefit is delivered to an employee (i.e. from payment of an allowance to a reimbursement of rental expenses incurred) would effectively vary or renew an eligible employment arrangement for the purpose of the transitional provisions. We assume that such changes would not mean that the transitional rules cease to apply however guidance is requested from Treasury on these points.

When is an employee's "tax status" tested?

Consideration should also be given by Treasury as to when an employee must be a permanent resident for the purpose of the transitional provisions (that is, not a temporary or foreign resident). The transitional rules do not apply to a temporary resident or a foreign resident (and both of these terms are defined).

A foreign resident (being a non-resident taxpayer) can become an Australian tax resident (but not a temporary resident) and a temporary resident can cease to be a temporary resident where they fail the "however" provision in the definition in subsection 995-1 of the 1997 Act. For example a temporary resident who acquires an "Australian spouse" through marriage or a de facto relationship will cease to be a temporary resident from that time.

There is no guidance in the ED or the EM as to when an employee's "tax status" is to be measured. The following are examples of situations where an employee's "tax status" changes and guidance is requested on such situations in relation to the application of the transitional rules where someone becomes a permanent resident.

> Example 1: A temporary resident living away from a foreign home on 8 May 2012, marries an Australian citizen on 1 June 2012, but still maintains their usual place of residence overseas. On 1 July 2012, they are a permanent resident. They should get transitional relief from both the home requirement and the 12 month requirement provided their eligible employment arrangement is not changed or varied prior to 30 June 2012.
>
> Example 2: A temporary resident living away from a foreign home on 8 May 2012, marries an Australian citizen on 1 August 2012, but still maintains their usual place of residence overseas. On 1 July 2012, they are a temporary resident. They should get transitional relief from both the home requirement and the 12 month requirement from 1 August 2012 provided their eligible employment arrangement is not changed or varied prior to 30 June 2012.

2.3 Non-discrimination article

An integral part of Australia's taxation laws are Australia's Double Taxation Treaties. Many of these treaties (for example, the United Kingdom and the United States) have non-discrimination articles whereby nationals of the foreign treaty country cannot be worse off under taxation or connected laws than an Australian national in the same circumstances.

The ED will result in an employee being denied deductions for accommodation and food expenses unless the employee maintains a residence for their use and enjoyment in Australia during a period

they are living away from that residence. A temporary resident employee is still required to maintain a residence for their use and enjoyment in Australia before accessing the concessions for LAFH benefits.

The transitional provisions however allow a "permanent resident" employee covered under an eligible employment arrangement at 7:30pm (AEST) on 8 May 2012 to access the concessions for LAFH benefits. Except for temporary residents who were living away from an Australian home at 7.30pm (AEST) on 8 May 2012 covered by an eligible employment arrangement, there are no transitional rules for temporary or foreign resident employees.

In substance rather than perhaps in form, the requirement to maintain an Australian home may be seen to be discriminating against non-Australians as typically temporary and foreign residents claiming LAFH benefits are living away from a foreign home.

The transitional rules however are in clear contradiction to the requirements of the non-discrimination articles in Australia's Double Taxation Treaties.

The OECD model convention article and commentary for the non-discrimination article are shown below.

Paragraph 1 of Article 24 of the OECD Model Convention states that:

> *Nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith, which is other or more burdensome than the taxation and connected requirements to which nationals of that other State in the same circumstances, in particular with respect to residence, are or may be subjected. This provision shall, notwithstanding the provisions of Article 1, also apply to persons who are not residents of one or both of the Contracting States.*

Paragraph15 of the OECD commentary for paragraph 1 of Article 24 states the following:

> *Subject to the foregoing observation, the words ". . . shall not be subjected . . . to any taxation or any requirement connected therewith which is other or more burdensome . . ." mean that when a tax is imposed on nationals and foreigners in the same circumstances, it must be in the same form as regards both the basis of charge and the method of assessment, its rate must be the same and, finally, the formalities connected with the taxation (returns, payment, prescribed times, etc.) must not be more onerous for foreigners than for nationals.*

The following countries have a non-discrimination article in their Double Taxation Treaty with Australia:

Chile
Finland
Japan
New Zealand
Norway
South Africa
Turkey
United Kingdom
United States

We submit that Treasury should revise the transitional provisions to apply to both permanent residents and temporary residents with eligible employment arrangements in place at 7.30pm on 8 May 2012 in order to meet the requirements of the non-discrimination articles in Australia's treaties.

We also submit that Treasury should consider whether the requirement to be living away from an Australian home (rather than a home anywhere in the world) could raise issues under the non-discrimination clauses in the above treaties.

Where the ED becomes law, it is likely that nationals from the above list of countries will rely on the non-discrimination article to ensure that they are not faced with a more burdensome taxation requirement than Australian citizens are.

2.4 Other

Other aspects that need further consideration are outlined below.

Ordinary weekly food and drink expenses

Section 25-115(3)(b) of the draft legislation states that the ordinary weekly food and drink expenses for a child aged under 12 during a 7-day period for the 2011-12 income year is $44. However, per paragraphs 2.40, 2.42 and 2.43 of the EM, the ordinary weekly food and drink expenses for a child aged under 12 during a 7-day period for the 2011-12 income year is $55.

We assume that the correct amount is $55 however the ED and the EM should be consistent.

Substantiation that a residence is available for use and enjoyment

The ED and EM state that an employee would only be eligible for LAFH benefits if they live away from an Australian home. We further note that under paragraph 2.28 of the EM, the employee's home has to be available for their use and enjoyment at all times during a period the employee is required to live away from that home.

Documentary evidence will be difficult to produce as the evidence will be "proving a negative fact" rather than "proving a positive fact". Guidance should be provided by Treasury or the Australian Taxation Office (ATO) as to what would constitute appropriate documentary evidence of the employee's home being available for their use and enjoyment.

ATO determinations re: reasonable food allowances

The move from FBT rules to the income tax regime for LAFH allowances does mean the ATO food determinations for year ending 31 March 2013 will not be relevant post 30 June 2012. The ATO will need to publish guidance BEFORE 30 June 2012 as to reasonable food allowances for interstate (and intrastate) temporary transfers for the 12 months to 30 June 2013.

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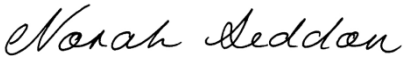

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The EM makes clear that the 12 month period restarts if the employee's work location changes, that is, if the employee is required by their employer to move to another location to perform the duties of

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2.2 Transitional provisions

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- Maintain a home in Australia; and
- Limit the concessional treatment to a maximum of 12 months;

will not apply to permanent residents until the earlier of 1 July 2014 or the date a new employment arrangement is entered into.

Eligible employment arrangements

While the ED itself makes clear transitional rules apply to an eligible employment arrangement which cannot be varied or renewed, the EM does not actually provide any illustrative examples on what is meant by "your employer or a connected of your employer commits to provide you with an allowance or benefit for your accommodation, food or drink while you are required to live away from your usual place of residence".

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Guidance is therefore requested in relation to whether these would qualify as an "eligible employment arrangement".

The ED and EM also do not define the terms "varied" or "renewed" for the purpose of the transitional provisions. As a result, it is unclear whether a change to the amount of rent charged under an existing arrangement or a change in the method that a LAFH benefit is delivered to an employee (i.e. from payment of an allowance to a reimbursement of rental expenses incurred) would effectively vary or renew an eligible employment arrangement for the purpose of the transitional provisions. We assume that such changes would not mean that the transitional rules cease to apply however guidance is requested from Treasury on these points.

When is an employee's "tax status" tested?

Consideration should also be given by Treasury as to when an employee must be a permanent resident for the purpose of the transitional provisions (that is, not a temporary or foreign resident). The transitional rules do not apply to a temporary resident or a foreign resident (and both of these terms are defined).

A foreign resident (being a non-resident taxpayer) can become an Australian tax resident (but not a temporary resident) and a temporary resident can cease to be a temporary resident where they fail the "however" provision in the definition in subsection 995-1 of the 1997 Act. For example a temporary resident who acquires an "Australian spouse" through marriage or a de facto relationship will cease to be a temporary resident from that time.

There is no guidance in the ED or the EM as to when an employee's "tax status" is to be measured. The following are examples of situations where an employee's "tax status" changes and guidance is requested on such situations in relation to the application of the transitional rules where someone becomes a permanent resident.

> Example 1: A temporary resident living away from a foreign home on 8 May 2012, marries an Australian citizen on 1 June 2012, but still maintains their usual place of residence overseas. On 1 July 2012, they are a permanent resident. They should get transitional relief from both the home requirement and the 12 month requirement provided their eligible employment arrangement is not changed or varied prior to 30 June 2012.
>
> Example 2: A temporary resident living away from a foreign home on 8 May 2012, marries an Australian citizen on 1 August 2012, but still maintains their usual place of residence overseas. On 1 July 2012, they are a temporary resident. They should get transitional relief from both the home requirement and the 12 month requirement from 1 August 2012 provided their eligible employment arrangement is not changed or varied prior to 30 June 2012.

2.3 Non-discrimination article

An integral part of Australia's taxation laws are Australia's Double Taxation Treaties. Many of these treaties (for example, the United Kingdom and the United States) have non-discrimination articles whereby nationals of the foreign treaty country cannot be worse off under taxation or connected laws than an Australian national in the same circumstances.

The ED will result in an employee being denied deductions for accommodation and food expenses unless the employee maintains a residence for their use and enjoyment in Australia during a period

they are living away from that residence. A temporary resident employee is still required to maintain a residence for their use and enjoyment in Australia before accessing the concessions for LAFH benefits.

The transitional provisions however allow a "permanent resident" employee covered under an eligible employment arrangement at 7:30pm (AEST) on 8 May 2012 to access the concessions for LAFH benefits. Except for temporary residents who were living away from an Australian home at 7.30pm (AEST) on 8 May 2012 covered by an eligible employment arrangement, there are no transitional rules for temporary or foreign resident employees.

In substance rather than perhaps in form, the requirement to maintain an Australian home may be seen to be discriminating against non-Australians as typically temporary and foreign residents claiming LAFH benefits are living away from a foreign home.

The transitional rules however are in clear contradiction to the requirements of the non-discrimination articles in Australia's Double Taxation Treaties.

The OECD model convention article and commentary for the non-discrimination article are shown below.

Paragraph 1 of Article 24 of the OECD Model Convention states that:

> *Nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith, which is other or more burdensome than the taxation and connected requirements to which nationals of that other State in the same circumstances, in particular with respect to residence, are or may be subjected. This provision shall, notwithstanding the provisions of Article 1, also apply to persons who are not residents of one or both of the Contracting States.*

Paragraph15 of the OECD commentary for paragraph 1 of Article 24 states the following:

> *Subject to the foregoing observation, the words ". . . shall not be subjected . . . to any taxation or any requirement connected therewith which is other or more burdensome . . ." mean that when a tax is imposed on nationals and foreigners in the same circumstances, it must be in the same form as regards both the basis of charge and the method of assessment, its rate must be the same and, finally, the formalities connected with the taxation (returns, payment, prescribed times, etc.) must not be more onerous for foreigners than for nationals.*

The following countries have a non-discrimination article in their Double Taxation Treaty with Australia:

Chile
Finland
Japan
New Zealand
Norway
South Africa
Turkey
United Kingdom
United States

We submit that Treasury should revise the transitional provisions to apply to both permanent residents and temporary residents with eligible employment arrangements in place at 7.30pm on 8 May 2012 in order to meet the requirements of the non-discrimination articles in Australia's treaties.

We also submit that Treasury should consider whether the requirement to be living away from an Australian home (rather than a home anywhere in the world) could raise issues under the non-discrimination clauses in the above treaties.

Where the ED becomes law, it is likely that nationals from the above list of countries will rely on the non-discrimination article to ensure that they are not faced with a more burdensome taxation requirement than Australian citizens are.

2.4 Other

Other aspects that need further consideration are outlined below.

Ordinary weekly food and drink expenses

Section 25-115(3)(b) of the draft legislation states that the ordinary weekly food and drink expenses for a child aged under 12 during a 7-day period for the 2011-12 income year is $44. However, per paragraphs 2.40, 2.42 and 2.43 of the EM, the ordinary weekly food and drink expenses for a child aged under 12 during a 7-day period for the 2011-12 income year is $55.

We assume that the correct amount is $55 however the ED and the EM should be consistent.

Substantiation that a residence is available for use and enjoyment

The ED and EM state that an employee would only be eligible for LAFH benefits if they live away from an Australian home. We further note that under paragraph 2.28 of the EM, the employee's home has to be available for their use and enjoyment at all times during a period the employee is required to live away from that home.

Documentary evidence will be difficult to produce as the evidence will be "proving a negative fact" rather than "proving a positive fact". Guidance should be provided by Treasury or the Australian Taxation Office (ATO) as to what would constitute appropriate documentary evidence of the employee's home being available for their use and enjoyment.

ATO determinations re: reasonable food allowances

The move from FBT rules to the income tax regime for LAFH allowances does mean the ATO food determinations for year ending 31 March 2013 will not be relevant post 30 June 2012. The ATO will need to publish guidance BEFORE 30 June 2012 as to reasonable food allowances for interstate (and intrastate) temporary transfers for the 12 months to 30 June 2013.

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