



21 August, 2012

Mr Stephen Boyd
Secretary
House of Representatives Standing Committee on Economics
Parliament House
Canberra ACT 2600

Dear Mr Boyd

REVIEW OF THE TAX LAWS AMENDMENT (2012 MEASURES NO. 4) BILL 2012

Please find enclosed a response from the Treasury to the additional questions on notice received from the House of Representatives Standing Committee on Economics on 14 August 2012 regarding the above Bill.

Should you have any further questions, please don't hesitate to contact me on 02 6263 4353.

Yours sincerely

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HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON ECONOMICS

Review of the Tax Laws Amendment (2012 Measures No. 4) Bill 2012

ADDITIONAL QUESTIONS ON NOTICE FROM SCOTT MORRISON MP

- a) In answer to Question 2, Treasury noted that *"given the uncertainty around how individuals choose to respond to the policy, there is a high degree of uncertainty about the respective contribution of different revenue components to the total fiscal impact"*.
- i) Does the Department agree therefore that its figures for collective revenue are also uncertain, given the unpredictability of the components? Isn't it therefore also possible that the Treasury's estimates are significantly underestimated and that the total fiscal impact is likely to be \$551 million per year, based on Scenario 2 assumptions proposed in Question 12?

Response:

- i) Treasury agrees there is a degree of uncertainty around the LAFHA costings (as there are to varying degrees for all revenue costings). We do not consider that a total fiscal impact for 457 visa holders of \$551 million per year is likely, and such an estimate is not supported by the actual usage and prevalence of LAFH allowances or benefits observed from ATO data.

QUESTION TO TREASURY AND TO THE ATO

- b) In answer to Question 2, Treasury noted that *"the relative composition of revenue impacts is dependent on how individuals choose to respond to the policy. in estimating this composition, the scenarios considered by Treasury included: individuals being paid more cash salary by their employer instead of the fringe benefit; individuals moving completely out of the LAFH system and not receiving additional pay; and individuals staying within the system and incurring additional fringe benefits tax"*.
- i) Of the 50,000 457 visa holders Treasury estimates are accessing LAFH, for modelling purposes how many of these individuals were predicted to move completely out of the LAFH system and not receive additional pay?
- ii) For modelling purposes, how many individuals did Treasury assume would be paid more cash salary by their employer instead of the fringe benefit?
- iii) For modelling purposes, how many individuals did Treasury assume would stay within the system and incur additional FBT?

Response:

- i) That information is not publically available.
- ii) That information is not publically available.
- iii) That information is not publically available.

QUESTION TO TREASURY AND TO THE ATO

- c) Treasury indicated in Answer to Question 3 that an estimate of the number of 457 visa holders accessing LAFHA – 50,000 – was *“derived based on data provided by the ATO”*.
- i) What data was provided by the ATO and used as a basis for these calculations? How was that data gathered and when – ie through questionnaires or annual returns?
 - ii) In answer to question 3, Treasury noted that “DIAC data was looked at but due to LAFH allowance and benefit limitations could not be fully utilised”. To what extent was DIAC data utilised and how did this inform or alter assumptions made based on solely ATO data?

Response:

- i) Fringe benefits tax returns for 2010-11 and earlier and FBT compliance intelligence for 2010-11.
- ii) Due to those aforementioned limitations DIAC data was not able to be fully utilised. Rather, it could only be used as an upper bound check on what the ATO data was imputing.

QUESTION TO TREASURY AND TO THE ATO

- d) In answer to Question 4, Treasury stated that “the revenue from 457 visa holders is not expected to increase significantly year on year”.
- i) Why does the Department expect that revenue for 457 visa holders will not increase significantly year on year?
 - ii) With the granting of 457 visas dependent on market demand, did the Department model predicted revenue with variations in the number of 457s expected to access LAFH allowances and benefits, or simply on a constant 50,000?

Response:

- i) The reforms will have a greater effect on 457 visa holders initially than it will on permanent residents. The effects are such that they will effectively be constant from the start date onwards, allowing for rental increases and the like.
- ii) A constant 50,000 was used.

QUESTION TO TREASURY AND TO THE ATO

- e) Treasury indicated in their Answer to Question 7 that *“for the purpose of modelling it was assumed that around 50 per cent of employees will convert LAFH allowances and benefits into salary wages”*.
- i) What rationale did Treasury and/or the ATO follow to arrive at the assumption that around 50 per cent of employees would convert LAFH allowances and benefits into salary wages?
 - ii) If more than 50 per cent of employees do convert LAFH allowances and benefits into salary wages, how would this affect Treasury’s revenue estimates?
 - iii) If the data and/or assumptions were based on ATO advice, please provide the Committee with a copy of the ATO assumptions and/or advice.

Response:

- i) That assumption detailed in the answer to question 7 was in reference to those employees who will have a straight conversion with no gross up for PAYG(W) for 457

visa employees. Employees who would have their LAFHA converted into cash salary and be compensated for PAYG(W) were an additional group. It was based on the expectation that grossing up will not be possible in some circumstances, and that certain employment contracts will not allow for it.

- ii) As noted above, Treasury has estimated that around 50 per cent will be paid additional cash salary or use alternative FBT concessions – it is just that around 50 per cent were assumed to not be paid additional compensation.
- iii) Estimating behaviour is inherently difficult, particularly when precedents for changes resulting in observed behaviour are not available, as in this case. Treasury consulted with the ATO in the course of preparing the costings.

QUESTION TO TREASURY AND TO THE ATO

- f) In answer to Question 6, Treasury stated that *"the costing was modelled on the notion of an average rate of LAFH allowances or benefit, which reflected a range of family compositions"*.
 - i) In its modelling, what did Treasury/ATO consider to be the average rate of LAFH allowances?
 - ii) How many different family compositions were considered in determining the average rate of LAFH allowances?
 - iii) Were these family compositions informed by Department of Immigration and Citizenship data or ATO data?

Response:

- i) The average rate of LAFH allowances was derived by comparing the level of total allowances and benefits employees were receiving (estimated from ATO data) divided by the estimated number of employees in receipt of these allowances and benefits.
- ii) As an average was used based on data across the LAFHA population, it implicitly takes account of the different family compositions across the LAFHA population.
- iii) Not applicable.

QUESTION TO TREASURY AND TO THE ATO

- g) In answer to Question 8, Treasury indicated that assumptions were made that employers would compensate their employees by grossing up allowances for the additional PAYG tax payable.
 - i) What assumptions were made? How many employers did Treasury/ATO assume would compensate their employees by grossing up allowances?
 - ii) For the 50,000 457 visa holders Treasury/ATO predicted were accessing LAFH, how many employers does Treasury/ATO associate with that group?

Response:

- i) This information is not publically available. Assumptions made were done at an employee level, rather than the employer level.
- ii) A prediction of how many employers were employing the estimated 50,000 457 visa holders was not calculated.

QUESTION TO TREASURY AND TO THE ATO

- h) In answer to Question 9, Treasury stated their costing in relation to food allowances “was based on data provided by the ATO which includes the food component and consideration was also given to reasonable food allowances”.
- i) What assumptions did the ATO make in relation to the average food allowance paid to employees?
- j) What data was provided by the ATO to Treasury in relation to the food component and what was the source of this data? ie questionnaire or return data? Information sought from employers or employees? If this data was obtained by questionnaire, what was the size of the test pool and how many respondents were recorded?
- iii) Is it possible to disaggregate the value of LAFH benefits provided by means other than an allowance from a Fringe Benefit Tax return? If so, can you provide that value to the Committee?

Response:

- i) The ATO did not make any assumptions in relation to the average food allowance paid to employees.
- j) The fringe benefits tax return data completed by employers.
- iii) The fringe benefits tax return does not disaggregate to that level.

QUESTION TO TREASURY AND TO THE ATO

- k) In answer to Question 10, Treasury indicated that “assumptions in relation to accommodation amounts were made based on observed arrangements, informed by data provided by the ATO”.
- i) What arrangements were observed by the ATO?
- ii) What was the assumed weekly accommodation allowance used by Treasury in its calculations?
- iii) Were these arrangements determined to be ‘reasonable’?

Response:

- i) Details of specific LAFH arrangements were collected in the data referred to in the answer for question (c). This data was able to identify those individuals who were 457 visa holders or not. The data provided the total LAFH allowances or benefits provided, but did not break it up any further (for example, into accommodation or food components).
- ii) An assumed percentage of the LAFH allowances referred to in question (f) was used, based on consultation with the ATO and a collective view of what would be reasonable.
- iii) Yes, reasonable for costing purposes.

QUESTIONS TO TREASURY AND TO THE ATO

- l) What marginal tax rate has Treasury/ATO assumed in its modelling would be paid by employees on their newly taxable allowance?

Response: A conservative average marginal tax rate for individuals was assumed, consistent with other estimates where actual data is not reliably known.

- m) What proportion of allowances are likely to be taxed at higher marginal tax rates? At what cost to employees?

Response: The use of the average marginal tax rate means that some allowances will be taxed higher, and some lower. Exact proportions are not known, but could be expected to be balanced out for the average rate approach.

- n) In answer to Question 11, Treasury noted that “data was requested and received from DIAC on 457 visa holders, however DIAC only collects information on total remuneration and the LAFH allowance and benefit component is not able to be separately identified”.

- i) Was DIAC consulted in relation to the ATO data that was used in place of its own data and ways their shortcomings could be overcome? If so, can you provide the committee with the advice that was received and if not, why not?
- ii) Was any DIAC data used in conjunction or to inform equations or assumptions involving ATO data? If so, which data and how?

Response:

- i) No.
- ii) Please see answer to question (c)(ii).

- o) In answer to Question 14, Treasury stated “*employer and employee behavioural assumptions were incorporated to account for how individuals and employers will possibly react to the new system. This included some employees converting LAFH allowances and benefits into salary and wages, some employers paying extra remuneration, some people staying in the FBT system and some alternative FBT concessions being accessed. The net result of these changes was then computed.*”

- iv) For the purposes of modelling, what other employer and employee behavioural assumptions were included in modelling?
- v) For the purposes of modelling, what percent of employers did Treasury assume would pay extra remuneration?
- vi) For the purposes of modelling, what percent of people did Treasury predict would stay in the FBT system?
- vii) For the purposes of modelling, what percent of people did Treasury assume would access alternate FBT concessions?

Response:

- iv) Assumptions around the proportions of employees maintaining or not maintaining a usual place of residence, the amount of consumed food subject to GST, the amount of allowances being paid over actual expenses, the estimated growth rate in LAFHA over the forward estimates, the amount of LAFHA not being reported on FBT returns, the propensity of employees to move work locations at the end of contracts and average contract lengths.

- v) No assumptions were made regarding the percentage of employers – assumptions were made regarding the percentage of employees.
 - vi) That information is not publically available.
 - vii) That information is not publically available.
- p) In answer to Question 15, the Department noted that “any increases in employment costs as a result of these changes will be different for each employer. Assumptions on increased costs of remuneration were made in line with the answer to question 8.”
- i) What assumptions did Treasury/ATO make on the cost of remuneration?
 - ii) How many employers did Treasury/ATO assume would compensate their employees by grossing up allowances for the additional PAYG tax payable?
 - iii) Of the 50,000 457 visa holders used in the modelling, what percentage of employers did Treasury/ATO model would compensate their employees by grossing up allowances and at what cost to the employer?

Response:

- i) Remuneration, in terms of cash salary, would increase by the assumed amount of LAFH allowances and benefits being paid to employees that would be compensated for the additional PAYG(W). For those employees continuing to provide the benefits as fringe benefits and incurring FBT, the increase would be at the FBT rate, excluding that FBT which is already being paid.
 - ii) Grossing up assumptions were based on employees.
 - iii) Grossing up assumptions were based on employees.
- q) In answer to question 17 concerning the impact of transitioning the measure over a two year period, Treasury said “There are no publically available estimates for this proposal.”
- i) Was the Department/ATO asked to privately model the transitioning of this measure over a two year period?
 - ii) Did the Department/ATO model any other time frame transitions? If so, what were those models and can you provide them to the Committee? If not, why not?

Response:

- i) A two-year transition period was provided for the LAFHA reforms announced at Budget. In line with past practice, Treasury does not disclose information in regards to policy development processes.
 - ii) In line with past practice, Treasury does not release information in regards to policy development processes.
- r) In answer to question 18 concerning modelling for transitional provisions for 457 visa holders, Treasury noted it did “not have a costing for the scenarios”.
- i) Did the Government at any stage request Treasury/ATO to undertake modelling for a transitional period for 457 visa holders?
 - ii) In Treasury’s consultation with DIAC, did DIAC ever make any suggestion to Treasury/ATO concerning the possibility of a parallel transitional arrangement for 457 visa holders? If so, what were those parallel arrangements?

Response:

- i) In line with past practice, Treasury does not disclose whether requests for advice were received from the Government.
- ii) No.