

Chapter 1

Background and overview of the bills

1.1 On 13 October 2016, the Senate referred the provisions of four bills which form part of the government's working holiday maker reform package ('the reform package') to the Senate Economics Legislation Committee for inquiry and report by 7 November 2016.¹ The four bills in the reform package are the:

- Income Tax Rates Amendment (Working Holiday Maker Reform) Bill 2016;
- Treasury Laws Amendment (Working Holiday Maker Reform Bill) 2016;
- Superannuation (Departing Australia Superannuation Payments Tax) Amendment Bill 2016; and
- Passenger Movement Charge Amendment Bill 2016.

1.2 There are a number of measures in the reform package relating to working holiday makers (WHMs)—that is, individuals visiting Australia on Working Holiday visas (Subclass 417) and Work and Holiday visas (Subclass 462). These measures include:

- changes to the income tax rates that apply to WHMs—whereas WHMs can currently access the \$18,200 tax free threshold if they are residents for tax purposes, the reform package will apply a 19 per cent income tax rate to taxable income on amounts up to \$37,000 for all WHMs, with ordinary tax rates for taxable income exceeding this amount;
- an increase to the rate of the departing Australia superannuation payments (DASP) tax to 95 per cent for WHMs;
- protections for WHMs from unfair employment arrangements—including allowing the Commissioner of Taxation (Commissioner) to disclose information that is relevant to ensuring an entity's compliance with the *Fair Work Act 2009* to the Fair Work Ombudsman;

1 Two parts of the reform package will be progressed through the next round of Appropriation Bills following Mid-Year Economic and Fiscal Outlook (MYEFO) 2016–17: a \$10 million Tourism Australia advertising campaign and \$10 million for the Fair Work Ombudsman and the Australian Taxation Office (ATO) to 'establish the employer register and assist with ongoing compliance initiatives and to address workplace exploitation of working holiday makers'. A measure to provide greater flexibility to employers of working holiday makers by allowing working holiday makers to stay with one employer for up to 12 months providing the second six months is worked in a different location, is being progressed separately by the Department of Immigration and Border Protection. This measure does not have a fiscal impact. Explanatory Memorandum, *Income Tax Rates Amendment (working Holiday Maker Reform) Bill 2016 [and related bills]*, (hereafter 'Explanatory Memorandum'), p. 7; Media release, 'Better working holiday maker tax arrangements', 27 September 2016, <http://sjm.ministers.treasury.gov.au/media-release/104-2016/>, accessed 24 October 2016.

- a requirement for employers of WHMs to register with the Commissioner, which will allow such employers to withhold tax at income tax rates applying to WHMs;
- a requirement for the Commissioner to give the Treasurer, for presentation to the Parliament, a report on WHMs;
- a reduction in the visa application charges for WHMs; and
- an increase to the passenger movement charge (PMC) from \$55 to \$60 (which will affect all passengers departing Australia, not just WHMs).

Conduct of the inquiry

1.3 The committee advertised the inquiry on its website and social media, and wrote directly to a range of individuals and organisations inviting written submissions by 21 October 2016. The committee received 56 submissions, which are listed at Appendix 1.

1.4 The committee held three public hearings: Canberra on 26 October 2016, Cairns on 31 October 2016, and Launceston on 2 November 2016. The names of witnesses who appeared at the hearing are at Appendix 2.

1.5 The committee thanks all participants in the inquiry.

Background

Working holiday maker program and taxation of WHMs

1.6 The WHM program commenced in 1975, and aims to foster tourism and cultural exchange between Australia and partner countries. The program comprises two visa classes: Subclass 417 (Working Holiday) and Subclass 462 (Work and Holiday). It allows people aged between 18 and 30 years of age from 38 partner countries to work in Australia during an extended holiday of up to 12 months (Subclass 417 visa holders can apply for a second year visa).²

1.7 The income tax that applies to WHMs depends on their residency status for taxation purposes (which, as explained further below, WHMs self-assess). Australia has long had different rates of income tax for individuals who are residents and non-residents for tax purposes. The tax-free threshold was removed for non-residents in 1982, and non-residents pay 32.5 per cent on all earnings up to \$80,000 (the first income tax bracket for non-residents is therefore \$0–\$80,000). In contrast, residents for tax purposes pay nil tax on income up to \$18,200 (the tax-free threshold), and 19 per cent for earnings between \$18,201 and \$37,000. For income over \$37,000, tax rates for both residents and non-residents are the same and increase at the same rate (see Table 1, below).

2 Explanatory Memorandum, p. 41; Joint Standing Committee on Migration, 'Seasonal change: Inquiry into the Seasonal Worker Programme' (May 2016), p. 45.

Table 1: Comparison of current tax rates for residents and non-residents³

Taxable income	Residents tax rate	Non-residents tax rate
\$0 – \$18,200	Nil	32.5 per cent
\$18,201 – \$37,000	19 per cent	
\$37,001 – \$80,000 ⁴	32.5 per cent	
\$80,001 – \$180,000	37 per cent	37 per cent
\$180,001 and over	45 per cent	45 per cent

1.8 Currently, WHMs who satisfy the tax residency criteria receive the benefit of the \$18,200 tax-free threshold.⁵ WHMs who are non-residents for tax purposes are taxed at 32.5 per cent from their first dollar of income (and, consistent with marginal tax rates for resident taxpayers, 37 per cent for income over \$80,000 and 45 per cent for income over \$180,000).⁶

Residency status for tax purposes

1.9 WHMs self-assess their residency status for tax purposes.⁷ The Australian Taxation Office (ATO) provides information on residency tests on its website and how these tests apply in common situations. For example, a person visiting Australia for more than six months who for most of that time lives in the same place, and who establishes ties in the local community, will generally be considered an Australian resident for tax purposes. However, a person visiting for more than six months who

3 The table does not include the Medicare Levy of 2 per cent that residents for tax purposes pay (non-residents are not required to pay the levy), or the Temporary Budget Repair Levy of 2 per cent for incomes over \$180,000.

4 The Treasury Laws Amendment (Income Tax Relief) Bill 2016, currently before the Parliament, proposes increasing the upper limit of the third bracket to \$87,000. The lower limit of the fourth bracket would increase to \$87,001. The bill would also increase the upper limit of the first income tax bracket for non-residents to \$87,000.

5 If a working holiday maker's income is \$37,000 or less, they will also receive the full benefit of the low income tax offset of \$445. This means that, in effect, working holiday makers do not pay tax until their income exceeds \$20,542. The low income tax offset reduces by 1.5 cents for every dollar over \$37,000, and cuts out entirely if income is \$66,667 or above. Explanatory Memorandum, p. 42; Australian Tax Office, webpage, 'Low income earners', <https://www.ato.gov.au/individuals/income-and-deductions/offsets-and-rebates/low-income-earners/>, accessed 17 October 2016.

6 Explanatory Memorandum, p. 10.

7 Explanatory Memorandum, p. 42.

spends most of that time travelling and working in various locations in Australia will generally be considered a foreign resident for tax purposes.⁸

1.10 Determining tax residency is not always straight-forward, and the ATO has identified that many WHMs are incorrectly assessing themselves as residents for tax purposes (and thereby avoiding the higher income tax rates that apply to WHMs who are non-resident for tax purposes). The Explanatory Memorandum explains that recent findings by the Administrative Appeals Tribunal (AAT) are of particular relevance in this regard:

In particular, many WHMs have been relying on their presence in Australia for six months as sufficient to be an Australian tax resident. Administrative Appeals Tribunal (AAT) decisions that were handed down in 2015 clarified the law. The AAT cases confirmed that applying the '183 day' test alone was not sufficient, and that an assessment of the full facts and circumstances must be applied to ascertain residency status.

The AAT decisions mean that most transient WHMs do not satisfy the tax residency tests and should be taxed as non-residents. However, WHMs that stay in one place and establish ties with their local community may be considered tax residents under the existing law, notwithstanding the fact that holidaying is the primary purpose for their visit.⁹

1.11 Appearing before the committee, a representative of the ATO provided the following insight into the complexity of the residency question for WHMs, and noted there was some confusion on the matter:

We need to administer the law around residency for working holiday-makers in the sense that we believe that a number of working holiday-makers are self-assessing themselves as residents when they are non-residents. And to support this we are aware of tax agents in the community who specialise in backpacker tax returns advertising, 'As long as you are here for more than six months we can get all your tax back.' We have some recent AAT cases, some tribunal cases, which show that if someone is a transient working holiday-maker—they are moving from farm to farm, for example, with different employers and moving around—then they are more likely to be non-residents. In fact, the cases concluded that people were non-residents regardless of the length of time that they were here in Australia. We do have some confusion out in the community on this point.¹⁰

8 Australian Taxation Office, webpage, 'Work out your tax residency', <https://www.ato.gov.au/Individuals/International-tax-for-individuals/Work-out-your-tax-residency/>, accessed 18 October 2016.

9 Explanatory Memorandum, p. 42.

10 Mr Michael Ingersoll, Assistant Commissioner, Individuals, Australian Taxation Office, *Proof Committee Hansard*, 26 October 2016, p. 33.

1.12 As the law currently stands, WHMs who are travelling and working in various locations around Australia would generally be considered non-residents for tax purposes, and as such subject to 32.5 per cent tax for income earned in Australia. While many WHMs have been incorrectly self-assessing as residents for tax purposes, the ATO confirmed to the committee that if the bill was not passed it would apply the current law:

We consider that most working holiday makers are non-residents due to their pattern of working and holidaying while in Australia.

We will help working holiday makers understand Australia's self-assessment tax system, so that they correctly advise their employers of their residency status and have correct tax withheld. We will also work to ensure that working holiday makers correctly prepare their tax returns. This will include working with tax agents so that their advice is consistent with the ATO view, as confirmed by recent Tribunal decisions. It will also include some checking of returns.¹¹

WHMs as a source of labour

1.13 For WHM visa holders, work must not be the main purpose of their visit to Australia.¹² However, as the Explanatory Memorandum explains:

While not the original intention, the WHM program has been acknowledged as being a strong contributor of supplementary labour, particularly to the tourism and agriculture industries which are heavily reliant on seasonal labour.¹³

1.14 In 2015–16, 214,547 working holiday visas were granted (195,673 Subclass 417 visas, and 18,910 Subclass 462 visas), down from a peak of 258,248 visas granted in 2012–13.¹⁴

1.15 As explained in the next chapter, the importance of WHMs as a labour source for agricultural and tourism industries has led to some concerns that imposing higher rates of taxation on WHMs would lead to a decline in WHMs visiting and working in Australia.¹⁵

2015–16 Budget announcement and the government's subsequent review

1.16 The 2015–16 Budget announced a measure to treat all WHMs as non-residents for tax purposes, thus taxing them at 32.5 per cent from the first dollar of income like other non-resident taxpayers. As such, WHMs would no longer be able to

11 Australian Taxation Office, *Submission 54*, p. 1.

12 Explanatory Memorandum, p. 41.

13 Explanatory Memorandum, p. 43.

14 Explanatory Memorandum, p. 44.

15 Explanatory Memorandum, p. 45.

claim residency for tax purposes and access the tax-free threshold of \$18,200. It was estimated that the measure would result in an increase to revenue of \$540 million over the then forward estimates period (2015–16 to 2018–19).

1.17 As the Treasurer noted in his second reading speech for the current reform package bills, the proposed measure led to concerns being raised about its possible effect on 'our global competitiveness as a backpacker destination'.¹⁶ In response to these concerns, on 17 May 2016 the Minister for Small Business and Assistant Treasurer announced that the government would undertake a review of the broad range of issues affecting the supply and taxation of WHMs. The government also announced that it would defer the 2015–16 Budget measure by six months, to start from 1 January 2017.¹⁷

1.18 The Deputy Prime Minister and Minister for Agriculture and Water Resources, the Hon Barnaby Joyce MP and the Assistant Minister to the Deputy Prime Minister, the Hon Luke Hartsuyker MP, announced the commencement of the government's review of the WHM visa program on 15 August 2016.¹⁸ As part of government's review of the WHM visa program, the Department of Agriculture and Water Resources (DAWR) invited and received more than 1700 written submissions.¹⁹ Deloitte Touche Tohmatsu (Deloitte) was appointed to conduct an independent stakeholder engagement process as part of the government's review of the WHM program.²⁰

1.19 Deloitte's stakeholder engagement process consisted of two main streams:

- workshops in all states and territories, with industry groups, welfare bodies, unions and labour hire companies invited to participate; and
- the abovementioned written submissions process run by DAWR, which passed on all submissions to Deloitte for inclusion in its review.²¹

16 The Hon Scott Morrison, Treasurer, second reading speech, *House of Representatives Proof Hansard*, 12 October 2016, p. 5.

17 Explanatory Memorandum, p. 6.

18 Media release, 'Working holiday maker visa review no underway', 15 August 2016, <http://minister.agriculture.gov.au/joyce/Pages/Media-Releases/working-holiday-maker-visa-review.aspx>.

19 Department of Agriculture and Water Resources, 'Submissions received', <http://www.agriculture.gov.au/ag-farm-food/working-holiday-maker-review/submissions>, accessed 24 October 2016.

20 Department of Agriculture and Water Resources, 'Working holiday maker visa review', <http://www.agriculture.gov.au/ag-farm-food/working-holiday-maker-review>, accessed 24 October 2016.

21 Deloitte, 'Independent stakeholder engagement on the Working Holiday Maker Visa review', September 2016, p. 1.

1.20 A number of central themes and arguments emerged in Deloitte's stakeholder engagement process, including:

- the importance of WHMs as a labour source in both the agriculture and tourism sectors, particularly in seasonal work in those sectors;
- the role of WHMs in increasing tourism in Australia;
- Australia's competitiveness as a destination for WHMs would be damaged by the proposed tax increase; and
- the proposed tax increase would create further incentives for workers to enter into the black/cash-in-hand economy and exacerbate the current exploitation of temporary visa holders.²²

1.21 The Treasurer advised in his second reading speech that the government had listened to stakeholders who had raised concerns.²³ The revised reform package was announced by the Treasurer on 27 September 2016.²⁴ According to the Treasurer, the revised package:

...acknowledges the importance of ensuring the integrity of the tax base in relation to what is an important area of growth in the economy, but also that this is done in an appropriate way that addresses the concerns of stakeholders that have arisen.²⁵

1.22 The primary difference between the 2015–16 Budget proposal and the reform package is that the latter would apply a 19 per cent tax rate on the earnings of WHMs up to \$37,000, as opposed to a 32.5 per cent tax rate. The reform package also reduces the cost of WHM visas by \$50 to \$390.²⁶ These and other measures in the reform package are summarised below.

Overview of the reform package

Tax rate changes

1.23 The Income Tax Rates Amendment (Working Holiday Maker Reform) Bill 2016 will set the tax rate that applies to WHMs at 19 per cent from their first

22 Deloitte, 'Independent stakeholder engagement on the Working Holiday Maker Visa review', September 2016, pp. 2–7.

23 The Hon Scott Morrison, Treasurer, second reading speech, *House of Representatives Proof Hansard*, 12 October 2016, p. 5.

24 Media release, 'Better working holiday maker tax arrangements', 27 September 2016, <http://sjm.ministers.treasury.gov.au/media-release/104-2016/>, accessed 24 October 2016.

25 The Hon Scott Morrison, Treasurer, second reading speech, *House of Representatives Proof Hansard*, 12 October 2016, p. 5.

26 Media release, 'Better working holiday maker tax arrangements', 27 September 2016, <http://sjm.ministers.treasury.gov.au/media-release/104-2016/>, accessed 24 October 2016.

dollar of income up to \$37,000. Annual income above this amount will be subject to ordinary marginal income tax rates. The new tax rate will apply from 1 January 2017.

1.24 DAWR explained the relevance of the abovementioned AAT decisions on the residency status of WHMs to the current package:

The Administrative Appeals Tribunal has affirmed the existing income tax rate for most WHMs is 32.5% (AAT 2015a-c). Despite this, it is clear that many WHMs have been, and continue to, declare themselves as 'residents' for tax purposes, and do not pay income tax on earnings below the tax free threshold.

The legislation before the committee is to change the law to an alternative tax rate of 19% for WHMs on income up to \$37,000, with standard marginal rates thereafter. Without change the existing law would remain.²⁷

Changes to the departing Australia superannuation payments (DASP) tax

1.25 When a temporary resident who has been working in Australia departs the country, they are able to claim their superannuation as a departing Australia superannuation payment (DASP).²⁸ As the Explanatory Memorandum explains, the DASP tax applies to the superannuation balance paid to eligible temporary visa holders (including Subclass 417 and Subclass 462 visa holders) where the individual has left Australia and their visa has expired or is cancelled.²⁹ The DASP tax is currently 38 per cent for the element of the payment taxed in the fund, and 47 per cent for untaxed elements.³⁰

1.26 The Superannuation (Departing Australia Superannuation Payments) Bill 2016 increases the rate of the DASP tax for WHMs to 95 per cent for those components of the payment that are currently subject to the tax. The change will take effect from 1 July 2017.³¹ The changes to the DASP tax rate only apply to WHMs.

Registration of WHM employers, protection of WHMs and periodic reporting by the Taxation Commissioner

1.27 The Treasury Laws Amendment (Working Holiday Reform) Bill 2016 establishes a framework requiring employers of WHMs to register with the

27 Department of Agriculture and Water Resources, *Submission 23*, p. 3.

28 Australian Taxation Office, webpage, 'Super for temporary residents departing Australia', <https://www.ato.gov.au/individuals/international-tax-for-individuals/in-detail/super/super-information-for-temporary-residents-departing-australia/>, accessed 2 November 2016.

29 Explanatory Memorandum, p. 10.

30 Explanatory Memorandum, p. 48. Any tax-free component of superannuation, which is generally made up of after-tax contributions, is taxed at 0 per cent when claimed as a DASP. Explanatory Memorandum, p. 11.

31 Explanatory Memorandum, pp. 13, 30.

Commissioner of Taxation. Registered employers will be able to apply reduced rates of PAYG Withholding to withholding payments made to WHMs.³²

1.28 If an employer registers as an employer of WHMs, the amount the employer is required to withhold from their withholding payments to WHM employees would be based on the rates of income tax that apply to income derived by WHMs (including the 19 per cent rate for income up to \$37,000). If an employer is not registered as a WHM employer with the Commissioner, then they would be required to withhold from their withholding payments to WHM employees the higher rate of income tax that applies to non-residents (32.5 per cent on all income up to \$80,000).³³

1.29 A WHM's income tax rate would not depend on whether their employer is registered or not. As the Explanatory Memorandum explains, following the assessment of a WHM's taxable income on lodgement of their tax return, the Commissioner refunds any excess PAYG Withholding amount—'that is, any amount that is not required to cover the working holiday maker's income tax liability'.³⁴ This means that if the higher PAYG Withholding rate has been applied by a non-registered employer, the WHM will be unable to access any excess PAYG Withholding amount until their income has been assessed on lodgement of their tax return. The Explanatory Memorandum states:

Employers that are registered as registered working holiday maker employers are able to apply reduced PAYG Withholding rates to payments made to their working holiday maker employees compared to the rates that would apply if the employer was not registered. This concessional treatment is designed to provide additional incentives for an employer to register as a registered working holiday maker employer, as access to this withholding treatment may result in them being considered as more attractive employers by working holiday makers.³⁵

1.30 In registering as an employer of WHMs, an entity will also be required to make a declaration to the Commissioner, stating that:

- if the entity is carrying on a business, the entity has a genuine business requirement to employ one or more WHMs (such as a labour shortage);
- the entity agrees to comply with the requirements of the *Fair Work Act 2009* in relation to its employment of any individual who is a WHM; and

32 Explanatory Memorandum, p. 13.

33 PAYG Withholding schedules are determined by the Commissioner. It is expected that the Commissioner will exercise his power to make PAYG Withholding schedules to provide different treatment based on whether an employer of a WHM is registered as a WHM employer. Explanatory Memorandum, p. 24.

34 Explanatory Memorandum, p. 24.

35 Explanatory Memorandum, p. 25.

- the entity agrees to check that any individual it employs as a WHM holds a visa that qualifies that person to be a WHM.³⁶

1.31 In addition, the Treasury Laws Amendment (Working Holiday Reform) Bill 2016 will provide greater protection for WHMs by allowing for:

- the Commissioner to cancel the registration of an employer under certain circumstances;
- the date on which an entity's registration or cancellation of registration takes effect to be made publically available on the Australian Business Register, making it easy for WHMs and others to check the registration status of a potential employer³⁷; and
- the Commissioner to disclose information to the Fair Work Ombudsman relevant to ensuring an entity's compliance with the *Fair Work Act 2009*.³⁸

1.32 As soon as practicable after 30 June each year, the Commissioner will be required to provide an annual report to the Minister regarding the taxation of WHMs, including statistics derived from the employer register.³⁹

Visa and passenger movement charge changes

1.33 The Treasury Laws Amendment (Working Holiday Reform) Bill 2016 and the Passenger Movement Charge Amendment Bill 2016 make the following changes to visa and passenger movement charges:

- a \$50 reduction in the visa application charge for Subclass 417 (Working Holiday) visas and Subclass 462 (Work and Holiday) visas from \$440 to \$390; and
- a \$5 increase in the PMC from \$55 to \$60.

Financial impact

1.34 As noted above, the original proposal to change the tax rates that apply to WHMs, as announced in the 2015–16 Budget, was estimated to increase revenue by \$540 million over the then forward estimates period (2015–16 to 2018–19). The deferral of the package for six months until 1 January 2017 had an estimated revenue cost of \$40 million.⁴⁰

36 Explanatory Memorandum, p. 22.

37 Explanatory Memorandum, p. 23.

38 Explanatory Memorandum, p. 13.

39 Explanatory Memorandum, p. 16.

40 Explanatory Memorandum, p. 6.

1.35 The cost to the Budget of the changes in the package to the income tax rate that applies to WHMs, as compared to the rate proposed in the 2015–16 Budget, is offset by increases to the DASP tax for WHMs and to the PMC for all passengers departing Australia.⁴¹

Structure of this report

1.36 The next three chapters in this report consider the views expressed by inquiry participants on the various aspects of the reform package.

- Chapter 2 considers the importance of WHMs to the Australian economy—both as a source of tourism dollars and a source of seasonal and temporary labour, particularly in the agricultural and tourism industries.
- Chapter 3 addresses the establishment of a register for employers of WHMs, and considers related issues of employer compliance.
- Chapter 4 examines the evidence received regarding the proposed increase in the PMC.

41 Explanatory Memorandum, pp. 6–7.

