AUSTRALIAN INDUSTRY

GROUP

Submission to

The House Standing Committee on Economics'

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

Proposed changes to the taxation of

Living-away-from-home Allowances and Benefits

13 July 2012

About Ai Group

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

Summary

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

Ai Group supports the initiative in Tax Laws Amendment (2012 Measures No. 4) Bill 2012 (the Bill) to address any misuse of the tax treatment of Living-away-from-home (LAFH) allowances and benefits. We have the following major concerns with the Bill:

- The proposed changes to the tax treatment of LAFH allowances and benefits go well beyond addressing misuse of living away from home allowances and benefits and will impact on a wide range of businesses and employees who have not been misusing the present arrangements.

- The proposed changes are unfair to temporary residents who maintain a home in their country of origin.

- The transitional provisions proposed by the Government including the deferral of the start date to 1 October, while welcome, do not apply to a large proportion of the proposed changes and do not adequately address the difficulties for employers and employees where existing arrangements have been negotiated on the basis of the previous tax treatment.

We note also that the proposed changes will have widespread implications both for employers and employees that do not appear to have been acknowledged by the Government and which we take to be unintended consequences. These include the flow-on costs to employers associated with payroll tax, superannuation contributions and workers' compensation premiums and the impacts on the entitlements of employees' families to payments such as the Family Tax Benefit.

The proposed changes will impose substantial new compliance costs and will introduce new areas of uncertainty that will need to be resolved in consultation between the tax authorities and taxpayers. While the deferral of the start date to 1 October will assist, we doubt it will be sufficient and recommend the Government not introduce changes to the treatment of LAFH allowances and benefits until 1 July 2013 to allow an orderly resolution of new definitions and design of new procedures.

Proposed Changes Go Beyond Addressing "Misuse"

The Government's stated intention in changing the tax treatment of LAFH allowances and benefits is to address areas of misuse.

Thus in his Media Release of 29 November 2011 when announcing the initial round of changes to LAFH allowances and benefits, the Deputy Prime Minister and Treasurer stated:

> The Government will introduce reforms to stop individuals from being able to exploit the tax exemption for living-away-from-home allowance and benefits.
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> This tax exemption is being increasingly misused by a narrow group of people, particularly highly-paid executives and foreign workers, at the expense of Australian taxpayers.
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> Rorting of this tax exemption was one of the issues raised at the Tax Forum, and has seen the total amount of tax-free living-away-from-home allowance reported by employers to the Australian Taxation Office increase from $162 million in 2004-05 to $740 million in 2010-11.[1]

In the Foreword to the Consultation Paper released by the Government in November 2011[2], the then Assistant Treasurer, the Hon. Bill Shorten MP stated:

> The LAFH benefits are intended to compensate employees for additional costs they incur when they are temporarily relocated by their employer for their work.
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> However, the LAFH benefit concessions are now being widely exploited in a manner that is outside the original policy intent. Some employers do not have to pay FBT and employees do not pay tax on income claimed to be spent on accomodation and food for those living away from home. From 1 July 2012, employers and employees will need to substantiate these claims.
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> A particular concern is the growing use of the concession by employers (including through labour hire and contract management companies) to allow temporary resident workers coming to Australia to convert their taxable salary into a tax-free allowance. This provides them with an unfair advantage over local Australian workers.
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> There have been attempts in the past to restrict the exemption, such as in the 1995 cost of compliance review and by the Australian Taxation Office (ATO) through the issue of public rulings. The Inspector General of Taxation has also reported on the misuse of this concession. The rorting of the LAFH benefits concessions was also raised at the 2011 Tax Forum.

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[1] The Hon Wayne Swan MP, Deputy Prime Minister and Treasurer, Media Release, *Tax Measures in Mid-Year Economic and Fiscal Outlook*, 29 November 2011.
[2] Commonwealth of Australia, *Fringe Benefits Tax (FBT) reform: Living away from home benefits*, November 2011.

> In recognition of the increasing cost to revenue, the inequitable treatment that has arisen between employees and the growing community concern regarding the operation of the LAFH benefits concessions, the Government has decided to act to reform the concessions.
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> 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. The Government welcomes temporary resident workers, but our skilled migration program is a better way of making sure temporary resident workers go to sectors of the economy where they are needed most.
>
> No permanent resident receiving LAFHA for genuine reasons will lose any existing entitlement under the changes. This means that residents who are currently receiving LAFH benefits that can be substantiated, employees operating under fly-in, fly-out arrangements and community sector employees who are not currently using all of their FBT exemptions cap will not be affected by the reforms.

Ai Group supports the Government's objective of addressing misuse of the present tax treatment of LAFH allowances and benefits. In our estimation, the changes to substantiation requirements announced in November 2011 together with changes relating to the need to maintain a home will address the concerns over misuse.

In contrast, the changes requiring temporary residents to maintain a home in Australia and the changes constraining the availability of the tax treatment of LAFH allowances and benefits for a period of one year go well beyond any reasonable definition of misuse. These additional changes will also mean that the impact of the measures will extend to hundreds of thousands of employees and will go well beyond what the Treasurer identified "as narrow group of people."

The changes announced in the May 2012 Budget mark a significant leap in the Government's definition of the "misuse" of the existing tax treatment of LAFH allowances and benefits. In limiting the availability of the tax treatment to periods of twelve months, the Government has decided to shift the definition of misuse from the definition it employed last November. As a result, the statement of last November by the former Assistant Treasurer that "no permanent resident receiving LAFHA for genuine reasons will lose any existing entitlement under the changes" cannot be made in relation to the changes announced on 8 May. All of a sudden an arbitrary period of one year is proposed to demarcate between "legitimate use" and "misuse".

While the current tax treatment of living away from home allowances and benefits has attracted the criticism that it has become subject to misuse, the many businesses and their employees that are not misusing the current treatment stand to be unfairly disadvantaged by the Government's proposed changes. These changes would extend far beyond addressing misuse. In many cases they would unfairly impact on employees and employers where employment arrangements have been negotiated on the basis of the existing tax treatment.

The current tax treatment of living away from home allowances has helped business in a wide range of industries attract and relocate staff. The changes proposed will raise costs, reduce competitiveness and act as a barrier to attracting and relocating staff. They are also likely to give rise to industrial disruption.

These changes will have very widespread impacts and will extend to the many businesses and employees in non-mining trade exposed industries that are under such intense pressures in the face of the strong dollar among other factors. The impacts will also extend to many businesses and employees in those parts of the construction sector under intense pressures posed by current market conditions.

Businesses caught by the extension of the proposed changes beyond addressing areas of abuse will be impacted if the Bill is enacted in its present form in the following ways:

- It will be more expensive for businesses to attract and retain the temporary residents who help many businesses address skill shortages across a very wide range of industries and occupations;

- It will be more expensive for businesses to relocate their resident workforce and therefore increase the costs associated with adapting to the rapid changes in industrial composition and the location of economic activity; and

- It will raise costs and intensify skilled labour shortages in the, already stretched, engineering construction sector.

Unfair to Temporary Residents Who Maintain a Home in their County of Origin

The Explanatory memorandum to the Bill quotes (at 1.8) the Explanatory Note when the original tax concession for LAFH allowance was introduced in 1945:

> "The allowance is paid to compensate the employee for the additional expenditure he is obliged to incur in providing board and accommodation for himself at his place of employment while, at the same time, maintaining his home elsewhere."

The proposed changes in the Bill go well beyond this and will only extend the current tax treatment to temporary residents if they maintain a home *in Australia*. This is unfair on temporary residents who maintain a home in their country of origin. There is no question that such an employee would be incurring expenses while "at the same time, maintaining his home elsewhere". Yet the changed proposed in the Bill will discriminate against this employee and require him or her to maintain a second home in Australia.

It is far from clear why additional expenses incurred in Australia by a temporary resident from New Zealand working in Townsville should not receive the same tax treatment as similar additional expenses incurred in Australia by a Melbournian working in Perth.

Inadequate Transitional Provisions

The Bill fails to put forward an adequate solution to the difficulties of the transition to the new tax treatment of LAFH allowances and benefits.

Transitional provisions should extend for the duration of existing employment arrangements so that bargains struck on the basis of the existing tax treatment (both between employers and employees and between businesses) can run their course without disputation and/or renegotiation.

The Bill does partly recognise the need for transitional provisions in respect of one set of changes but does not introduce transitional provisions in respect of other changes. Both the changes announced in November and the changes announced in May should incorporate adequate transitional provisions.

The inadequacy of transitional provisions substantially raises the probability of industrial disputation in relation to existing employment arrangements as employees and employers jostle over the incidence of the greater tax burdens proposed.

Unintended Consequences

The proposed changes to the tax treatment of LAFA allowances and benefits would have important unintended consequences beyond those already mentioned.

Firstly, in changing the composition of employee remuneration, the proposed changes would raise the salary component of remuneration. This will:

- Impose additional liabilities for employers in respect of payroll tax, workers compensation premiums and superannuation contributions when amounts currently provided as fringe benefits are paid as taxable allowances against which employees can claim deductions; and,

- Reduce disposable incomes for employees including through their entitlements for family tax benefit and other income support programs.

Proposals

Ai Group proposes that adequate transitional provisions be adopted so that existing employment and commercial contracts negotiated on the basis of the existing tax treatment are allowed to run their course without the need for disputation and/or renegotiation.

We propose that the scope of the proposed changes be narrowed to concentrate more effectively on the misuse of the existing tax treatment by concentrating on substantiation arrangements and on a consistent and non-discriminatory approach (as between residents and non-residents) to “living away from home”.

We propose a start date of 1 July 2013 to allow an orderly transition to the new arrangements.