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17 March 2006

Mr Russell Chafer
Committee Secretary
Joint Committee of Public Accounts and Audit
Parliament House
Canberra ACT 2600

e-mail: jcpa@aph.gov.au

Dear Mr Chafer

INQUIRY INTO ASPECTS OF TAX ADMINISTRATION

The Taxation Institute of Australia (Taxation Institute) is pleased to provide you with its response (see Appendix A) to the Joint Committee of Public Accounts and Audit's call for submissions to its inquiry into the Australian Taxation Office's (ATO) administration of the certain aspects of the income tax laws announced on 8 December 2005 (the Inquiry).

In commenting on the issues raised within the terms of reference, the Taxation Institute draws on the experience of our 10,000 members, who range from tax advisers in the small, medium and large enterprise sectors to senior tax practitioners in the legal and accounting professions. Taken together with their clients, our members' views reflect the concerns and opinions of many tens of thousands of businesses throughout Australia.

Set out below are the Taxation Institute's comments on the scope of the Inquiry and an overview of the key difficulties with self assessment, followed by a summary of our key recommendations.

Scope of the Inquiry

The Taxation Institute has some reservations about limiting the scope of the Inquiry to the administration by the ATO of the Income Tax Assessment Act 1936 and Income Tax Assessment Act 1997, with particular reference to compliance and the rulings regime. As the Federal Government's principal revenue collection agency, the ATO is not only responsible for administering income tax. It is also responsible for administering Pay As You Go (PAYG) instalments, fringe benefits tax (FBT), goods and services tax, the Australian Business Number and Australian Business Register, excise duty, superannuation (including the superannuation guarantee and self managed superannuation funds), higher eduction funding (jointly with other Government agencies) and grants and schemes in relation to diesel and alternative fuels. The ATO is also required to support the delivery of community benefits, with

roles in other areas (such as private health insurance, family assistance and cross-agency support).
Given the breadth of the ATO's administrative responsibilities, we appreciate the need to circumscribe the scope of the review. However, it is also important to acknowledge that the ATO carries a significant administrative burden in relation to the collection of revenue that extends well beyond the income tax legislation itself and embraces administrative issues that interface directly or indirectly with the administration of the income tax laws.
In particular, to the extent that the penalty, General Interest Charge, Shortfall Interest Charge and the Pay As You Go (PAYG) provisions were once part of the income tax acts and now reside in the *Taxation Administration Act 1953*, the Taxation Institute assumes that discussion of these measures is within the scope of this Inquiry.
We are also disappointed that although a self assessment system applies in respect of Fringe Benefits Tax (FBT), the administration of FBT was not included in the Inquiry. Further, given the existence of a further ruling system for indirect taxes (the Goods and Services Tax (GST), wine and luxury car taxes), it is also disappointing that the administration of these were not part of the Inquiry, particularly given that the ruling and penalty provisions are also contained in the *Taxation Administration Act 1953*.

Key difficulties with self assessment

It is clear that the move to self assessment was driven by the desire to increase the cost efficiency of revenue collection by liberating assessing resources within the ATO to audit activities. However, the impact of self assessment has been to shift the compliance obligation and the resultant compliance cost and risk back to taxpayers.

Such a system requires that the ATO issue information and advice. However this has resulted in the issuance of a plethora of different rulings, interpretative decisions, facts sheets, etc at such a rate that the volume of guidance is overwhelming, making it difficult if not impossible for taxpayers and their advisors to read, comprehend and comply. For example the ATO issued 3,666 interpretative decisions between 2002 and 2005.
This mass of information is a direct result of overly complex legislation introduced in the period from 1999. In this period we have seen almost 300 tax related bills drafted. These laws are complex and detailed and only pay lip service to the plain English style. The preoccupation with the "time value of money" and anti-avoidance resulted in the continued adoption of global solutions. Many laws involved the removal of commonly accepted concepts and terminology and adoption of "new speak" concepts in the law (eg the term "depreciation" no longer has a place in Australian tax law). It is not surprising then that self assessing taxpayers are struggling under the weight of the laws, but also under the weight of explanatory material.

Key recommendations

The Taxation Institute's key recommendations are as follows:

- There is a need to assess current levels of compliance imposed on taxpayers in a self assessment environment with a view to identifying and reducing/eliminating any unnecessary compliance burdens on taxpayers (Recommendation 1);

- The ATO to review its compliance activities to ensure that its officers have understanding of the operation of particular industries and businesses in those industries, such that they can communicate effectively with the taxpayers to ensure that taxpayers know the nature of a compliance activity (whether it is an audit or not) and the scope of the ATO's inquiry. (Recommendation 2);

- Greater clarity and consistency is required around ATO processes for imposing and calculating the level of penalties imposed, with particular reference to substantiating

how the ATO has paid due regard to whether a taxpayer has a reasonably arguable case or special circumstances in setting the level of penalty (Recommendation 3);

- The absence of appeal rights where the shortfall interest is less than 20 percent should be reviewed; there should be no monetary limit to a review of the Commissioner's discretion in these circumstances (Recommendation 4);

- There is a need to simplify the administration of the PAYG system by imposing a system similar to provisional tax with a figure which is uplifted. A recalculation option would be available where a taxpayer's circumstances have dramatically varied (Recommendation 5);

- In order to ensure taxpayers are not adversely affected in situations where the law is unclear and the ATO has adopted a contentious view, then:

  - taxpayers should be granted a lodgment deferral until the issue is clarified, thereby allowing lodgment of correct returns; or
  - where taxpayers have relied on the alternate view in these circumstances, then they should be entitled to remission of all penalties, GIC and SIC (Recommendation 6);

- In circumstances where the Government introduces retrospective legislation to overcome an adverse court decision arising from the Commissioner challenging a taxpayer's position (e.g., Marana Holdings and Coleambally cases), then, to ensure equity, that legislation should enable those taxpayers to get the benefit of those retrospective changes (Recommendation 7);

- Before the ATO proposes any changes to tax returns, particularly those that require taxpayers to provide additional information, the Taxation Institute recommends that the ATO should be compelled to undertake compliance cost studies to support any such changes (Recommendation 8);

- Similarly, the Government should also be required to undertake appropriate compliance cost studies to support any proposed changes, amendments, additions or deletions to the tax laws (Recommendation 9).

- The tax liability for fringe benefits be transferred from employers to employees with the tax being collected under the PAYG system, accompanied by a simplification of the fringe benefits rules (reducing the categories of benefits subject to FBT and simplifying the calculation processes) (Recommendation 10);

- The "double taxation" arising from the intersection of fringe benefits tax and family tax benefits is due to the top marginal tax rate being used both for the calculation of the gross up of benefits and the FBT payable and that overstated gross up figure being used to reduce entitlement to family tax benefit. By adopting recommendation 10 above, this "double tax issue" would disappear. The alternative solution of valuing fringe benefits based upon the marginal tax rate of the individual would impose further adverse compliance costs on the business community (Recommendation 11); and

- In the absence of changing the current FBT regime to shift the liability to the employee, the Committee should support a joint body submission dated 4 August 2004, sent to the then Assistant Treasurer and Minister for Taxation, the Hon Mal Brough MP, calling for the following legislative changes aimed at both simplification and reducing compliance costs (see Appendix B)(Recommendation 12).

The Taxation Institute is happy to give evidence before the committee to elaborate on the issues raised in our submission.

Should you have any queries in relation to any of the matters raised in our submission, please contact at first instance the Taxation Institute's Senior Tax Counsel, Dr Michael Dirkis, on (02) 8223 0011.

Yours faithfully

John de Wijn QC
President

APPENDIX A

Submission by the Taxation Institute of Australia to the Joint Standing Committee on Public Accounts and Audit

Inquiry reviewing a range of taxation issues within Australia

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ADDRESSING THE TERMS OF REFERENCE

The Taxation Institute has identified the following key issues that need to be highlighted as part of this inquiry. We have addressed these issues in accordance with the Committee's terms of reference as follows:

Part A — Inquiry into the administration by the ATO of the Taxation Laws, with particular reference to compliance and the rulings regime

- A1 The impact of the interaction between self-assessment and complex legislation and rulings.
- A2 The application of common standards of practice by the ATO across Australia.
- A3 The level and application of penalties, and the application and rate of the General Interest Charge and Shortfall Interest Charge.
- A4 The operation and administration of the Pay As You Go (PAYG) system.
- A5 Other administrative issues

Part B — The application of the fringe benefits tax regime, including any "double taxation" consequences arising from the intersection of fringe benefits tax and family tax benefits.

PART A INQUIRY INTO THE ADMINISTRATION BY THE ATO OF THE TAXATION LAWS, WITH PARTICULAR REFERENCE TO COMPLIANCE AND THE RULINGS REGIME

A1 The impact of the interaction between self-assessment and complex legislation and rulings

The Taxation Institute believes that it is essential that for any tax system to operate effectively it should be *perceived* as equitable, both in the way tax is levied and in the administration of the system. It will be remembered that the Asprey Committee, in considering the essential aims of efficiency, fairness and simplicity in a tax system, noted:

> ". . . that revenue-raising [must] be 'by means that are not unduly complex and do not involve the public or the administration in undue difficulty, inconvenience or expense".[1]

It is clear that the move to self assessment was driven by the desire to increase the cost efficiency of revenue collection by liberating assessing resources within the ATO to audit activities. However, the impact of self assessment has been to shift the compliance obligation and the resultant compliance cost and risk back to taxpayers. Self assessment has imposed on taxpayers disproportionate additional expenses and burdens to get the law right or face significant penalties (including SIC and GIC) if their view of the uncertain and complex law is not consistent with that found by the ATO.

Although the Review of Self Assessment goes some of the way in addressing those concerns by:

- increasing the range of statements that can be relied upon (and arguably the number of statements taxpayers can be penalised for not following);
- shortening the term for when an assessment can be reopened; and
- introducing a lower "shortfall interest charge" for the period between assessment and audit adjustment;

there remains a perception in the community that the onus for getting it right, even where the law is unclear, still lies unfairly on the least resourced member of the ATO/taxpayer relationship - *the taxpayer*. In light of the complexity that underlies our income tax laws, this burden remains and the Taxation Institute is of the view that this burden should be shared more equally.

Even in applying for a ruling the ATO is unable, due to internal guidelines, to indicate whether a ruling request is likely to proceed, even where a fundamental weakness is evident from the beginning. As a result tax payers continue to waste money continuing with an application that is "dead in the water" and the business opportunity, reliant on a positive outcome of the ruling is often lost.

Recommendation 1

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[1] Preliminary Report of the Taxation Review Committee (Asprey Committee) June 1974 at para 3.6. See also Review of Business Taxation (Ralph Committee) July 1999 at pp 15-17

There is a need to assess current levels of compliance imposed on taxpayers in a self assessment environment with a view to identifying and reducing/eliminating any unnecessary compliance burdens on taxpayers.

A2 The application of common standards of practice by the ATO across Australia

There exist some wide spread general concerns about the consistency of the current ATO compliance practices. The April 2005 report by Kevin Burges on the outcomes of one-on-one interviews with large corporate representatives, who had expressed concern about their audit experience, identified the following areas of concern:

- difficulties in obtaining advice;
- audit and investigation procedural concerns;
- inadequate understanding of the company's business;
- risk assessment review issues;
- key client manager issues;
- the general interest charge;
- ATO staff attitudes inimical to cooperative compliance; and
- a balanced view.

Similarly, the Taxation Institute has similar concerns expressed by members. These include:

- the considerable confusion at present about whether an ATO compliance activity constitutes an audit or not, with ramifications for whether a taxpayer can make a voluntary disclosure and seek to minimise the impact of any penalties. The ATO needs to put in place protocols for advising taxpayers about whether or not a particular compliance activity is an audit, and if so, when the audit commences. Although work has progressed in the ATO, resolution has stalled;

- the lack of understanding of the operation of particular industries and businesses in those industries leads to a lack of consistency in the management of audit activity by ATO officers once a compliance activity commences. Whilst it is appreciated that the actual conduct of a compliance activity is greatly influenced by what is being investigated and the taxpayer's particular circumstances, there is a need for ATO officers conducting those audits to communicate effectively with the taxpayers to ensure that a taxpayer knows the nature of a compliance activity (whether it is an audit or not) and the scope of the ATO's inquiry. They should also provide regular progress reports to the taxpayer;

- the fact that, despite the ATO making advances in client risk profiling, the ATO compliance activity in some parts of its operations appears to be still based upon procedural checking rather than more sophisticated identification of taxpayers with high risk profiles. In our opinion there needs to be a more consistent method of communication in relation to audits that not only provide the detail on the nature of the audit to be carried out but also the process involved. This would include a confirmation in writing at the conclusion of the audit on the matters to be addressed or that the audit has in fact finished;

- that during the course of a compliance activity, feedback suggests that the ATO does not always allow sufficient time for taxpayers to provide information requested by the ATO. Concerns have been expressed about the level of technical competency of some ATO audit officers and of problems experienced with the change of audit personnel during the course of an audit and the lack of proper hand-over from one ATO officer to another. This impacts adversely on the compliance process in terms of costs for the taxpayer and the time taken to complete a compliance activity; and

- that there is some evidence to suggest that some ATO compliance activities are too open ended, leaving the taxpayer with no expectation about closure on a particular ATO compliance activity. In many cases, it is up to the taxpayer to inquire of the ATO officer whether or not a compliance activity has been concluded and what the outcome is.

Recommendation 2

The ATO to review its compliance activities to ensure that its officers have an understanding of the operation of particular industries and businesses in those industries such that they can communicate effectively with the taxpayers to ensure that taxpayers know the nature of a compliance activity (whether it is an audit or not) and the scope of the ATO's inquiry.

A3 The level and application of penalties, and the application and rate of the General Interest Charge and Shortfall Interest Charge

There is a perennial problem in respect of the imposition of penalties imposed by the ATO. Often they are imposed arbitrarily, without due regard to whether a taxpayer has a reasonably arguable case or special circumstances. Penalties are seen by advisors to corporate taxpayers as an opening gambit in negotiations with the ATO, whereby the ATO will seek to get its contentious position accepted through bargaining the penalties down to the appropriate level that reflects the ATO's perceptions of the taxpayer's true "guilt".

This view is reflected in many court and AAT cases where the level of penalty is reduced on appeal. It appears that it is mainly in egregious scheme cases that the courts and the AAT uphold the penalties imposed.

There also remains a problem with remission of shortfall interest. The absence of appeal rights where the shortfall interest is less than 20 percent of the tax shortfall is harsh (see s 280-170 of *Taxation Administration Act 1953 (Cth)*, Schedule 1). The justification for exclusion (at paragraphs 2.76 to 2.81 of the *Explanatory Memorandum to the Tax Laws Amendment (Improvements to Self Assessment) Bill (No 1) 2005*) based upon the cost of an appeal does not ring true (eg 19 percent of a one million adjustment is a substantial amount that should be open to review). There should be no monetary limit to a review of the Commissioner's discretion, just as there is no monetary limit in respect of an objection to an ordinary assessment.

Recommendation 3

The ATO to provide greater clarity and consistency around the process of calculating the level of penalties imposed, with particular reference to substantiating how the ATO has paid due regard to whether a taxpayer has a

reasonably arguable case or special circumstances in setting the level of penalty.

Recommendation 4

The absence of appeal rights where the shortfall interest is less than 20 percent should be reviewed; there should be no monetary limit to a review of the Commissioner's discretion in these circumstances.

A4 The operation and administration of the Pay As You Go (PAYG) system.

The PAYG system is an example of a preoccupation with the economic theory of what is known as the "time value of money". This preoccupation has resulted in the bringing forward of revenue collection that outstrips the ability of taxpayers to supply the supporting information in a cost effective manner.

In particular the system (which is merely a more aggressive form of provisional tax) does not allow adequate time for businesses, particularly those with complex affairs, to collect the data necessary. This time is shorter than many other regulatory systems require. For example, large public companies are given only 21 days to collect, compile and calculate liability where other agencies allow greater time for the provision of similar data. As a result taxpayers, unable to comply, will overpay to avoid penalties.

Although the ATO has attempted to alleviate some of the difficulties, the system continues to impose a high compliance burden on businesses by adding compliance costs and imposing compliance obligations well beyond those existing in business systems. Even simple things such as the order in which the ATO applies refunds to other debts remains a constant area of confusion.

Recommendation 5

There is a need to simplify the administration of the PAYG system by imposing a system similar to provisional tax with a figure which is uplifted. A recalculation option would be available where a taxpayer's circumstances have dramatically varied.

A5 Other administrative issues

There are two categories of concern with ATO administration, being contentious interpretations and unnecessary compliance obligations.

Contentious interpretations

Often ATO interpretations of the law will impose high compliance costs on taxpayers, even though the ATO's interpretation is contentious. There are two recent examples, one involving the application of the absorption costing method and the other the GST input tax treatment of residential property.

Application of the absorption costing method

In Practice Statement PS LA 2003/13 and draft Taxation Ruling TR 2005/D11, the ATO is implementing the contentious position of requiring the absorption costing method for valuing trading stock for taxpayers in the retail and wholesale industries.

Contrary to a popular misconception that taxpayers with a gross operating turnover of less than $10 million do not have to implement the absorption costing method, this Practice Statement and draft Ruling only operate to remove strict compliance with the mandated absorption costing regime because, as stated in paragraph 1 of PS LA 2003/13:

> "[t]axpayers not covered by this practice statement will still be expected to use a reasonable and practical basis to correctly bring to account their trading stock",

and in paragraph 27 of TR 2005/D11, the ATO indicates that

> "[t]axpayers with a gross operating turnover of less than $10 million may make an appropriate estimate of the additional costs to be absorbed which need not be based on detailed records of all expenses".

PS LA 2003/13 and draft Taxation Ruling TD 2005/D11 result in the ATO arbitrarily creating rules that are too costly for small business to comply with:

- given that the focus of a practice statement should be upon ensuring that ATO practice meets that of the community, it is difficult to see how the ATO can justify imposing additional compliance costs on small business merely arising from a contentious interpretation and application of accounting standards; and
- in these circumstances, we do not believe the ATO has done an appropriate cost benefit analysis including:(i) the cost of compliance impact on small business in having to take "reasonable and practical" steps to "make an appropriate estimate of the additional costs to be absorbed"; (ii) the revenue to be gained from effectively imposing the absorption costing method on small business; and (iii) the impact of the ATO's proposals on the overall viability of small business and their capacity to be able to comply with the ATO's requirements.

GST input tax treatment of residential property

The second issue is in the GST context where the Full Federal Court in the *Marana Holdings Pty Ltd v FCT* [2004] FCAFC 307 dismissed an appeal by the taxpayer concerning a commercial redevelopment of motel premises and the meaning of the term "residential premises". Although the ATO was successful in this litigation the reasoning in the decision of the Court was in conflict with GST Ruling 2000/20.

Despite undertaking to rewrite the ruling the ATO failed to do so for over 18 months. In fact the ATO indicated as late as 15 February 2006 that a revised Ruling was due for release on 22 March 2006.

On 27 February 2006, the Minister for Revenue and Assistant Treasurer, Peter Dutton, announced that the Government proposed to amend the GST law to continue the GST treatment as contemplated by the original ruling, it being stated that the ATO's victory in *Marana Holdings* was not consistent with the intention of the law. The amendment is proposed to be retrospective. While the proposed amendments may restore the original intent of the GST law, the important issue is why should the amendment be retrospective?

Retrospective tax legislation is almost always inappropriate but especially so in the context of transaction taxes, like the GST. It will mean that taxpayers who entered into commercial arrangements consistent with and relying on the decision of the Full Court in *Marana Holdings* are now to be retrospectively denied input credits to which they expected they would be entitled on the basis of the decision of the Full Court.

Recommendation 6

In order to ensure taxpayers are not adversely affected in situations where the law is unclear and the ATO has adopted a contentious view, then:

- ***taxpayers should be granted a lodgment deferral until the issue is clarified, thereby allowing lodgment of correct returns; or***
- ***where taxpayers have relied on the alternate view in these circumstances, then they should be entitled to remission of all penalties, GIC and SIC.***

Recommendation 7

In circumstances where the Government introduces retrospective legislation to overcome an adverse court decision arising from the Commissioner challenging a taxpayer's position (e.g., Marana Holdings and Coleambally cases), then, to ensure equity, that legislation should enable those taxpayers to get the benefit of those retrospective changes.

Unnecessary compliance obligations

Often the ATO in pursuit of other worthwhile goals will impose costs on taxpayers.

For example, the ATO put forward a proposal to put a compulsory label in the 2005 Partnership and Trust Returns requiring information relating to the disclosure of certain financial arrangements that provided a tax deduction, capital loss, or foreign tax credit.
The ATO was motivated to recommend this as a means of obtaining early information on potential schemes.

Given concerns about the targeting of the questions and the resultant compliance costs (which were conservatively valued at $45 million, affecting some 900,000 returns), the Taxation Institute wrote to the Commissioner of Taxation on 25 February 2005 and raised the issue at the 15 March 2005 National Tax Liaison Group meeting.

The Commissioner advised that after reviewing the submission on the inclusion of the new compulsory label the Tax Office has decided not to go ahead with this for the 2005 year return forms. However, the issue will be reconsidered for 2006.

This is an example of the growth in unnecessary and costly tax return compliance proposals being put forward by the ATO. This trend should be halted.

Before the ATO proposes any changes to tax returns, particularly those that require taxpayers to provide additional information, the Taxation Institute recommends that the ATO should be compelled to undertake compliance cost studies to support any such changes. These studies should model both the transitional and operative compliance costs in collecting data and the ATO should then be required to raise a

compelling case in support of imposing administratively those additional compliance costs.

However, in most cases it is the Government, wearing a whole of Government hat which imposes unnecessary compliance costs. A great example is the superannuation surcharge system which was so poorly designed that the compliance costs almost out weighed revenue collected. Even after its demise, despite the ATO having all the residual information, the Government will continue to impose compliance costs by requiring superannuation providers to report details of employer contributions to the ATO on an annual basis.

Worst still, these reports will be due by 31 October each year, despite the fact that most other reporting obligations are tied to the lodgment of the return. Such different dates impose unnecessary compliance costs as taxpayers information has to be reviewed twice.

Recommendation 8

Before the ATO proposes any changes to tax returns, particularly those that require taxpayers to provide additional information, the Taxation Institute recommends that the ATO should be compelled to undertake compliance cost studies to support any such changes.

Recommendation 9

Similarly, the Government should also be required to undertake appropriate compliance costs studies to support any proposed changes, amendments, additions or deletions to the tax laws.

PART B THE APPLICATION OF THE FRINGE BENEFIT TAX REGIME, INCLUDING ANY "DOUBLE TAXATION" CONSEQUENCES ARISING FROM THE INTERSECTION OF FRINGE BENEFITS TAX AND FAMILY TAX BENEFITS.

Overview

Australia's fringe benefits tax regime is complex and resource intensive for employers. In particular, the structure of the rules is scattergun, ie the rules seek to tax all benefits (any right, including rights in real and personal property, privilege, service or facility) provided to an employee or to an associate of the employee by the employer, an associate or an arranged person in respect of the employment of the employee, except where it is expressly excluded.

This untargeted approach is another example of lazy policy design driven by a preoccupation focused on "taxing every last cent". Such rules are overly complex and thereby impose higher taxpayer compliance costs on the whole taxpaying community. This complexity has resulted in wholesale non-compliance in the SME sector.

As a result, the Taxation Institute continues to support recommendation 5.44 of the Review of Business Taxation (in *A Tax System Redesigned* (1999) that the tax liability for fringe benefits be transferred from employers to employees with that tax being collected under the PAYG system.

However, the Institute believes that this change should be accompanied by a simplification of the fringe benefit rules, by targeting the major benefits (car, loans, etc) and simplifying the calculation methods.

Under this approach, fringe benefits would be taxed as ordinary income (as they are taxed in all OECD countries other than New Zealand) with the simplified valuation rules inserted into the income tax law.

Recommendation 10:

The tax liability for fringe benefits be transferred from employers to employees with the tax being collected under the PAYG system, accompanied by a simplification of the fringe benefits rules (which would reduce the categories of benefits subject to FBT and simplify the calculation processes).

Fringe benefits tax and family tax benefits

In commenting on this term of reference, it is assumed that the "double taxation" consequences, arising from the intersection of fringe benefits tax and family tax benefits, identified by the Committee occurs, as the gross up of benefits is based upon the top marginal tax rate while persons receiving the family tax benefit will have a lower marginal income tax rate. This means the grossed up value of the benefit received is overstated and this overstatement in turn reduces the amount of family tax benefit entitlement by that larger amount (ie so-called "double tax").

If benefits were taxed in the hands of the individual then it is possible to modify the gross up to reflect the individual's marginal rate such that only the actual benefit received is subject to tax. However, to introduce a variable FBT rate under the current regulatory regime would seem to counter the policy driver for FBT, that is, the cashing out of non-cash benefits. It would also increase compliance costs.

Recommendation 11

By adopting recommendation 10 above, this "double tax issue" would disappear. The alternative solution of valuing fringe benefits based upon the marginal tax rate of the individual would impose further adverse compliance costs on the business community.

Compliance cost reduction

If no change was to occur, at a minimum, the Committee should support a joint body submission dated 27 October 2004, sent to the then Assistant Treasurer and Minister for Taxation, the Hon Mal Brough MP, calling for the following legislative changes aimed at both simplification and reducing compliance costs:

(a) Car Parking: An optional standard valuation for car parking benefits could be provided for in the legislation.

(b) Travel Costs for Employees working in one city and living in another: These should be exempt from FBT altogether as they are not remuneration related but a business cost of getting the right employees in the right place.

(c) Optional 50/50 split for recreational expenditure: employers should have the option to adopt the 50/50 split method in respect of all recreation expenditure, as is the case for meal entertainment and entertainment leasing facility benefits.

(d) Reportable Benefits confined to Remuneration benefits only: Only benefits that are part of a remuneration package or award should be reported on payment summaries. The excluded benefits would include the travel costs referred to in (b) above. In addition, the law should be amended to provide for an exception from the usual reporting rules where it is impossible to fairly allocate the value of a fringe benefit to individual employees. At a bare minimum as a short-term solution, clearer guidance is required as to an acceptable set of rules for the valuation and attribution of shared cars between employees.

As an alternative or in addition to the above recommendations, the following are suggestions:

- where a car is used by more than one employee, the employer be given the option to calculate the statutory formula for the car separately for each employee based on the annualised kilometres for the period of use by each employee; and

- in many instances, employees only obtain a marginal benefit from the occasional use of a car to drive home when they use a car predominantly for employment purposes only. It is suggested that the unnecessary compliance costs arising from calculating a potential fringe benefits tax liability in this type of situation would be alleviated by extending the current work related exemption for the use of utilities and panel vans to all cars, with appropriate safeguards to prevent the non-work related use of such cars.

Note that the above two recommendations are for fringe benefits tax generally and not just for reportable benefits.

(e) Reportable Fringe Benefits and Recreation: All recreation expenditure should be excluded from the FBT reporting requirements, as is currently the case for meal entertainment expenditure and entertainment facility leasing expenses.

(f) Reportable Fringe Benefits Threshold: The threshold should be increased from $1,000 to $2,000.

(g) Interaction of GST and FBT and Financial Supplies: The provisions of Division 71 of the GST Act should be reviewed and overhauled.

(h) Reconciliation Difficulties: Difficulties in accounting for fringe benefits would be reduced if taxpayers could record the GST-exclusive value of benefits in the FBT return.

(i) Capping Thresholds: the capping of the provision of exempt benefits by certain employers (e.g., limiting the value of exempt benefits that can be provided to each employee by non-for-profit entities such as hospitals and public benevolent institutions) requires re-visiting, with the view to re-writing these provisions. The implementation of these capping provisions presents a major cost of compliance for affected non-for-profit employers, who generally do not have the resources to deal with such complexities. This has an undesirable flow-on effect of circumscribing the ability of a non-for-profit entity to offer salary packages to attract appropriately qualified professionals into employment in this sector.

(j) Road Tolls: The accounting for road toll fringe benefits is cumbersome and costly. It is suggested that amendment to Section 136(1) of the FBTAA 1986 be made to include within the definition of a ‘car expense’, ‘bridge and road tolls’.

(k) Minor and infrequent rule: The $100 threshold for minor and infrequent exempt benefits is too low. To allow real compliance savings this threshold should be increased to at least $200. This threshold should also be indexed each year.

The Committee should also look at reengineering the restrictive FBT rules on the provision of child care, thereby enabling more employers to provide child care benefits for employees

Recommendation 12

In the absence of changing the current FBT regime to shift the liability to the employee, the Committee should support a joint body submission dated 4 August 2004, sent to the then Assistant Treasurer and Minister for Taxation, the Hon Mal Brough MP, calling for the following legislative changes aimed at both simplification and reducing compliance costs.


The Institute of Chartered Accountants in Australia


4 August 2004.

The Hon Mal Brough MP
Assistant Treasurer and Minister for Revenue
Parliament House
Canberra ACT 2600

Dear Hon Mal Brough,

RE: Fringe Benefits Tax and Cost of Compliance Issues

This submission is presented on behalf of the professional bodies (in alphabetical order), The Institute of Chartered Accountants in Australia, Law Council of Australia, National Tax & Accountants Association Limited, National Institute of Accountants, Taxpayers Australia Inc and Taxation Institute of Australia.

The submission outlines the cost of compliance and other difficulties faced by employers as a consequence of the Fringe Benefits Tax (FBT) legislation. A common and consistent theme in feedback received from members of all the professional bodies is the compliance burden, which they regard as excessive and inappropriate that FBT places on business.

The Professional Bodies also see merit in the Government undertaking a review of the FBT Laws with the aim of rectifying the issues by amending the Legislation.

Below are some immediate areas where the professional bodies see the need for the Government to consider and implement urgent solutions. These are as follows:

SUMMARY OF RECOMMENDATIONS

1. Car Parking: An optional standard valuation for car parking benefits could be provided in the legislation.

2. Travel Costs for Employees working in one city and living in another: These should be exempt from FBT altogether as they are not remuneration related but a business cost of getting the right employees in the right place.

3. Optional 50/50 split for recreational expenditure: employers should have the option to adopt the 50/50 split method in respect of all recreation expenditure, as is the case for meal

entertainment and entertainment leasing facility benefits.

4. Reportable Benefits confined to Remuneration Benefits only: Only benefits that are part of a remuneration package or award should be reported on payment summaries. The excluded benefits would include the travel costs referred to in 2 above. In addition, the law should be amended to provide for an exception from the usual reporting rules where it is impossible to fairly allocate the value of a fringe benefit to individual employees. At a bare minimum, a short-term solution would be to provide clearer guidance as to an acceptable set of rules for the valuation and attribution of shared cars between employees.

As an alternative, or in addition to, the above recommendations the following are suggested:

- Where a car is used by more than one employee, the employer be given the option to calculate the statutory formula for the car separately for each employee based on the annualised kms for the period of use by each employee.

- The work related exemption for utilities and panel vans be extended to all cars.

Note that the above two recommendations are for fringe benefits tax generally and not just for reportable benefits.

5. Reportable Fringe Benefits and Recreation: All recreation expenditure should be excluded from the FBT reporting requirements, as is currently the case for meal entertainment expenditure and entertainment facility leasing expenses.

6. Reportable Fringe Benefits Threshold: The threshold should be increased from $1,000 to $2,000.

7. Interaction of GST and FBT and Financial Supplies: The provisions of Division 71 of the GST Act should be reviewed and overhauled.

8. Reconciliation Difficulties: Difficulties in accounting for fringe benefits would be reduced if taxpayers could record the GST-exclusive value of benefits in the FBT return.

9. Capping Thresholds: this area requires re-visiting with the view of re-writing these provisions.

10. Road Tolls: The accounting for road toll fringe benefits is cumbersome and costly. It is suggested that amendments to Section 136(1) of the FBTAA 1986 be made to include 'bridge and road tolls' within the definition of a 'car expense'.

11. Minor and infrequent rule: The $100 threshold for minor and infrequent exempt benefits is too low. To allow real compliance savings this threshold should be increased to at least $200. This threshold should also be indexed each year.

12. Election to group: Companies should be able to have the option to elect to group their FBT obligations and thus only lodge one FBT return.

GENERAL COMMENTS

By way of background, the FBT legislation was enacted in 1986 in order to overcome the perceived inadequacies of Section 26(e) of the Income Tax Assessment Act 1936 (ITAA 1936). This Section sought to subject to income tax the value of non-cash benefits received by employees as a consequence of their employment.

The fundamental difference between Section 26(e) of the ITAA 1936 and the FBT legislation was that employers are now liable to taxation in respect of benefits provided to employees.

Since 1986, numerous amendments have been made to the original FBT legislation. Most of these 'band aid' amendments were designed to rectify flaws in the original FBT legislation, widen the scope of the FBT legislation and simplify the application of the legislation or to reduce the costs of complying with the FBT legislation. These amendments and the sheer volume of the legislation and complex definitions, however, have lead to the FBT laws becoming inequitable, too complex and too costly to comply with.

Small and large business and tax practitioners continue to experience real problems in complying with the requirements imposed under the FBT legislation. The employer and not the employee is continually under pressure to get it right and is ultimately left exposed, in terms of penalties, for FBT record keeping errors and any fraud perpetrated by the employee.

Also, many of the provisions have failed to keep up with business change and result in employers being requested to make decisions using legislation that does not reflect modern practices, technology or the intention of other legislation.

The ATO on several occasions has resorted to applying administrative solutions to overcome legislative defects. However, this is not an ideal way to be addressing flaws and inflexibilities in the Law. An example of this is, the extension to the minor benefit exemption, as reported in the NTLG-FBT 15 November 2002 minutes, whereby the professional bodies contended that there were particular compliance difficulties for reporting purposes in these situations. The 'meal entertainment' component is not reportable yet the 'recreational entertainment' component, for example a band, would be reportable where the 'associated benefits' exceeded, in total, $100 per employee. The ATO acknowledge this concern and put in place an administrative solution by granting an increase to the threshold from $100 to $125 for some functions where the function includes the provision of a band or entertainment ('recreational entertainment' rather than 'meal entertainment').

SPECIFIC COMMENTS

1. Car Parking

Ideally the professional bodies would like to see 'on premise' car parking removed from the FBT coverage, as these benefits are difficult to determine, value and attribute to individuals or at the very least the rules need to be simplified.

Car parking is a classic case of the 80/20 rule where tax practitioners and taxpayers spend 80% of their time on something that adds 20% value at the end of the day. There is a real need to simplify this area in order to reduce the cost of compliance for businesses.

The cost of determining the lowest car parking fee at a commercial parking station within one kilometre of employer provided parking can be quite large, either in terms of time commitment from an employee undertaking the necessary investigation, or in paying an external consultant to provide the information. The same issue arises in determining whether or not there is a parking station within one kilometre that charges more than the threshold amount. It is also not uncommon for a commercial car park to give out inaccurate information in respect of its car parking rates.

Alternatively, in most cases an exemption applies and there is no FBT liability, so the benefit might well be made totally exempt.

The professional bodies recommend that an optional standard valuation for car parking be implemented to assist in resolving the existing issues that are faced by businesses.

2. Travel Costs for Employees

In today's economic climate, it is not unusual for an employee to reside in one capital city and to be required to move on a permanent basis (or for a 12 or 18 month project time period) to a different capital city. If their family wish to reside in the old location, it is also not unusual for that employee to travel to that capital city on Monday and return home on the Friday. This is a similar situation to politicians spending weekdays in Canberra and returning home for weekends.

In accordance with the information contained in Miscellaneous Taxation Ruling 2030, such employees would be considered to be living away from their usual place of residence and accordingly any accommodation provided to them near their current workplace would be exempt from Fringe Benefits Tax. However, the travel costs on the Monday and the Friday would not be exempt from Fringe Benefits Tax on the basis it was travel to and from work.

We consider with today's highly mobile workforce, it would be reasonable to treat these travel costs as also being exempt from FBT on the same basis as the accommodation costs would be exempt. Paying FBT on the mere cost of getting the right staff to be in the right place is bad enough but the cost of analysing the individual circumstances, for each such employee with varied arrangements, to determine the correct FBT treatment needs to be reduced by simplifying and modernising rules.

The professional bodies would be happy to work with Government to devise workable solutions.

3. Optional 50/50 split method for recreational expenditure

In relation to meal entertainment expenditure and entertainment facility leasing expenses, employers have the option to value this expenditure for FBT purposes using the 50/50 split method.

This method significantly reduces compliance costs for employers because it reduces the need to maintain detailed records to split the expenditure between employees, associates and non-employees (for example, clients and contractors).

Under the 50/50 split method, FBT is only payable on 50% of the employer's total expenditure on meal entertainment and entertainment facility leasing expenses.

The 50/50 split method is not available in relation to recreation expenditure that does not qualify as entertainment facility leasing expenses. The professional bodies submit that employers should have the option to adopt the 50/50 split method in respect of all recreation expenditure. Further, the professional bodies believe that the risk to Government revenue would be negligible, if any at all. In addition, we submit that this measure should be implemented without affecting the application of the minor benefits exemption under Section 58P of the FBTAA 1986.

4. Reportable Fringe Benefits confined to Remuneration Benefits only

The reporting provisions have resulted in increased compliance costs imposed on employers, particularly small businesses. The employer with several hundred motor vehicles used by different employees on different days and garaged at different locations each day is only one example of the administrative nightmare created by the law. The very essence of the design of FBT to impose one single liability on the employer in such a case is abrogated by this reporting legislation.

The legislation provides grounds for industrial disputes and disputes between employees. It has the potential to become fertile ground for litigation between employers and employees over the allocation of benefits.

The cost of tracking benefits to particular employees for reporting purposes can be burdensome. As this sort of information is not generally captured by an employer's accounting system, employers are effectively required to run another system that will maintain the information required. This is particularly an issue with (recreational) entertainment expenditure, as it can be difficult, for example, to know who attended a particular function.

Furthermore, the human resource cost of dealing with disgruntled staff, which may have lost government benefits as a result of benefits received as a condition of employment, impacts on the superannuation surcharge and medicare levy. For example, an employee receives a car fringe benefit as a condition of employment and once the benefit is included on his or her payment summary, the employee is ineligible to receive family allowance for the year. The employee becomes out of pocket by at least the amount of any lost benefit and has no recourse against their employer.

It is assumed that all fringe benefits confer a benefit on the employee and are a substitute for remuneration. The reality is that the bulk of fringe benefits tax is collected on benefits that confer no personal benefit on the employee. The professional bodies would have no trouble in accepting the taxing of benefits relating to an employee on a car benefit included in a salary sacrifice package. However, we see difficulties taxing lower and middle-income earners provided with tool of trade cars that are provided as part and parcel of their work activity.

Below are some examples, which demonstrate some of the practical difficulties that are currently experienced by tax practitioners and taxpayers:

Example 1

An employer has a car that is used by a salesperson for work. The first driver's annualised kilometres are calculated to be more than 15,000 up to the time of when he leaves his or her employment. A new driver is employed and his or her annualised kms for the use of the same car is calculated to be less than 15,000. At the end of the year the taxable value is calculated using the statutory formula method and allocated to the two employees' payment summaries, the result being that the first driver is disadvantaged because the first happened to clock up more than 15,000 annualised kms but the second driver did not use the car enough to bring the actual kms to above 15,000 kms. The first driver has no right against the employer and has to wait until he or she receives an assessment before being able to lodge an objection.

Example 2

A district nurse is required by her employer to take the car home because parking is not available at the employer's premises and the employee is required to be on call. Private use of the car is restricted to travel to and from work. The employee has a private vehicle and providing car parking for the employer's vehicle is an inconvenience. In this case, there is a fringe benefit borne and paid for by the employer. There is no personal benefit to the employee for using the employer's car. Yet the benefit must still be reported on the employee's payment summary and in turn this affects their liability to the medicare levy, (and/or) superannuation surcharge and the employee's entitlement to family allowance payments. In our view, the recording of the benefit on the employee's payment summary is both unfair and inequitable.

Example 3

A further example to demonstrate difficulties with allocating the amount of certain benefits to employees is where the employees of tax-exempt bodies (such as universities) are required to host visitors, for example, taking overseas visitors to 'Healesville Sanctuary' (which results in a expense payment benefit, residual benefit, or tax exempt body entertainment benefit). This isn't remuneration, nor is it (predominantly) meal entertainment, nor might it be particularly enjoyable,

especially after a number of visits. Yet this amount would ultimately end up on the payment summary for that employee.

Determining the allocation of shared cars creates an unnecessary high cost of compliance for businesses. The legislation refers to the need to consider any 'relevant matter' (Section 5F(3) and (4) of the FBTAA 1986) when determining the employee's share. Although this is sufficiently broad to allow an employer to consider a range of factors which impact on the use of the shared car, the broad nature of the provisions further adds to the cost of compliance, particularly where employees have a vested interest in understanding the determination of the apportionment of the taxable value and the reporting of this value on their payment summaries (as is the case due to reportable fringe benefits).

The current legislation creates the need to assess the various factors/matters which impact on the provision of the benefit, such as an attribution based on days used, kilometres driven, percentage of use, operating costs v statutory method and so on. These various permutations are necessary to ensure that there is an equitable allocation of the taxable value of the car. This becomes even more difficult where the use of the car changes between employees. For example, one employee uses the car primarily for business use and uses a log book, one uses it primarily for private use but does high kilometres and a third employee rarely uses the car at all. The varied use of the car and the combinations of the calculations of the car fringe benefit need to be considered before an assessment can be made as to how to value the car and attribute this value to each employee.

The professional bodies recommend that only benefits which are part of a remuneration package or award should be reported on payment summaries. This would thus avoid the inequitable recording of benefits such as in the examples above. The professional bodies also submit that there ought to be an exemption from these rules in such situations. Excluding non-remuneration benefits would achieve this most desirable outcome i.e. for examples 2 and 3 above.

The professional bodies further recommend that the law be amended to provide for an exception from the usual reporting rules where it is simply impossible to allocate fairly the value of a fringe benefit to individual employees. As is the case in example 1 above.

As an alternative to the above recommendations, the following are suggested as a means to solve the problems in each of the examples above:

- Where more than one employee uses a car, the employer be given the option to calculate the statutory formula for the car separately for each employee based on the annualised kilometres for the period of use by each employee.

- The benefit that employees obtain from the occasional use of a car to drive home when they use the car for employment is marginal. It is suggested that the work related exemption for utilities and panel vans be extended to all cars. If the Government is concerned about employees using this to obtain an inappropriate tax benefit by salary packaging the use of such cars, they could include provisions in the legislation that require the employer to have a well-regulated system of enforcing the no non-work related use of the cars.

At a bare minimum, and as a short-term solution, clearer guidance is required as to an acceptable set of rules for the valuation and attribution of shared cars between employees. This would assist in partly resolving some of the concerns outlined above.

It is also anomalous that a 1.9417 gross up factor is used on fringe benefits where the effective tax rate of employees and indeed the salary sacrifice required by the employees of the FBT

exempt and rebateable employers is less. This disadvantages employees who receive benefits, rather than being tax neutral.

5. Reportable Fringe Benefits and Recreation Expenditure

At present, recreation expenditure (except for entertainment facility leasing expenses) is subject to the FBT reporting requirements. 'Recreation' includes expenditure on any of the following:

- engaging an entertainer (eg, band, DJ, and comedian) for a social function;
- a game of golf or tennis;
- sightseeing tours; and
- tickets to a movie, theatre or sporting event (eg, AFL football match).

From a practical perspective, the requirement to trace every item of recreation expenditure to employees creates a compliance nightmare for employers.

This is especially the case where recreation expenditure involves an employer separately engaging an entertainer (eg, a band and/or comedian) for a social event, such as a gala dinner, award dinner or similar function.

To satisfy the reportable fringe benefits requirements in these circumstances, the employer would need to:

- determine the amount of recreation expenditure (eg, cost of the band and/or comedian);
- determine the identity of each person attending the social function; and
- allocate the total taxable value of the recreation expenditure to the employees.

The current legislation also leads to ridiculous situations, some of which were highlighted during the recent Rugby World Cup. An employee could be invited to attend the Rugby World Cup final in the company's corporate box and, whilst FBT would be payable on the benefit of the ticket, there would be no reportable fringe benefit on that employee's payment summary. However, if the company who leased the corporate box ran out of seats in that box, they could go out and purchase two tickets to exactly the same event. However, the recipients of those tickets, if they were employees, would have a reportable fringe benefit on their payment summary.

Other complications arise where there is a lack of information as to which employees attended, and whether an employee's associate also attended. The ATO has partly acknowledged this concern, by issuing an administrative concession to increase effectively the minor benefit exemption threshold to $125 to deal with incidental recreation in the above circumstances (refer to the NTLG - FBT minutes of meeting dated 22 February 2001).

However, in many cases, the cost of such a function per employee (including associates) would be greater than $125.

Having regard to the above compliance issues, the professional bodies strongly submit that all recreation expenditure should be excluded from the FBT reporting requirements, as is currently the case for meal entertainment expenditure and entertainment facility leasing expenses. Alternatively, to ensure that there is no abuse of the system, the exclusion could be limited to benefits provided in actually viewing a sporting event or participating in such an event (for example: a golf game, where the reportable issue arises with individual green fees).

6. Reportable Fringe Benefit Threshold too low

Under the reportable fringe benefits requirements, compliance costs have increased for employers, as they now have to record every benefit received by each employee to determine

employees who receive over $1,000 worth of benefits. The $1,000 limit is too low and should be higher to avoid the compliance costs of recording what are relatively small amounts.

For Example:

An employee may receive an occasional $100 (note that the $100 is only an illustrative amount) expense payment fringe benefit at the start of the year. As the year progresses, the expense payment fringe benefit is received more regularly and when all benefits are totalled, they exceed the $1,000 threshold.

The professional bodies recommend that the reportable fringe benefit threshold be increased to a greater amount of at least $2,000 to reduce the cost of complying with the reporting requirements.

7. Interaction of the GST & FBT and Financial Supplies

The GST/FBT interaction is leaving many tax practitioners and taxpayers open to major exposure because it is difficult to comply with. This is the case, for example, for input taxed suppliers i.e. financial institutions. This issue arises because providers of financial supplies have to establish whether a benefit is considered a remuneration benefit or not. This is required to determine whether FBT will apply. The ATO has issued some guidelines in GSTR Rulings GSTR 2000/22 and GSTR 2001/3 to assist with determining the treatment. This was required because of the existing inflexible and complicated FBT laws.

In order to establish whether something is subject to FBT, taxpayers and tax practitioners have to ask themselves whether the benefit falls within one of three broad classes: those that relate wholly to remuneration benefits; those that result partly in a remuneration benefit (with some FBT payable); and those that relate only to work benefits (where no FBT is payable on the supply of the benefit).

In general terms, remuneration benefits are provided as a reward for services, whereas work benefits are provided to meet the business needs of the employer.

In summary, acquisitions that relate ***wholly to remuneration benefits*** are not subject to Division 71 of the GST Act. For example, reimbursements of employees' private expenditure are remuneration benefits. This is because such benefits are purely of a private nature.

Acquisitions that result in benefits that are ***partly work benefits and partly remuneration benefits*** (some FBT payable) will be subject to Division 71 of the GST Act. For example, an asset such as a car is used partly for work purposes and also privately, or where the employer imposes restrictions on use (even where the benefit is essentially private), the benefit will be both a work and a remuneration benefit. This will also be the case where the FBT benefit value is reduced by the 'otherwise deductible rule' (because of the work activities).

Acquisitions that result ***only in work benefits*** where FBT is not payable on the supply of the benefit will not be subject to Division 71 of the GST Act. In many cases, this will be because the benefit arising is merely a by-product of normal enterprise activities. For example, Section 47(3) of the FBTAA 1986 provides that a residual benefit, provided to an employee, which consists of the use of property (other than a motor vehicle) that is ordinarily located on business premises, and is wholly or principally used directly in connection with business operations of the employer, is an exempt benefit. The private use of a work telephone by an employee is an exempt benefit under Section 47(3) of the FBTAA 1986. The use of the telephone merely results in a benefit to the employee as part of work activities.

Acquisitions that result only in work benefits where FBT is payable will be subject to Division 71 of the GST Act. For example, an employee is required to take a client out for a meal. Whilst paragraph 56 of GSTR 2001/3 lists entertainment as a remuneration benefit, we understand the

ATO's interpretation is that entertainment is an example of something that may be a remuneration benefit but that there will also be cases where entertainment is a work benefit according to the general definition of a work benefit in that ruling.

The professional bodies recommend that these rules be completely overhauled and simplified and a new set of rules be drafted. The professional bodies would be happy to work together with the ATO and Government to come up with some workable rules.

8. Reconciliation Difficulties

The requirement to report GST-inclusive values for FBT purposes, when accounting systems generally record the GST-exclusive values (because the GST component is coded to the GST account) can be very onerous. It is difficult to determine which values need to be grossed-up to their GST-inclusive values and which items did not include GST i.e. because they were GST-free or input taxed purchases. The time costs in identifying all this information is considerably high.

The professional bodies recommend that amounts be recorded as GST-exclusive in the FBT return.

9. Capping Thresholds

Fringe benefits that are exempt under Section 57A of the FBTAA 1986 are capped by the legislation. For public hospitals, non-profit hospitals and government employees performing duties in connection with such hospitals, the limit is $17,000 per employee, per year and for public benevolent institutions the threshold is $30,000.

The capping of benefits for certain employers is a difficult concept when it comes to completing the FBT return and determining any aggregate non-exempt amount or aggregate non-rebateable amount. Without professional assistance, the employers affected would find it difficult to complete these sections accurately, and obviously, this comes at a cost. These provisions present a major cost of compliance and not-for profits do not have the resources to deal with such complexities.

The professional bodies are of the view that this area requires re-visiting with the view of re-writing these provisions.

10. Road Tolls

At present the ATO's view and practice in relation to road tolls is that road tolls do not fall into the category of 'car expenses' under Section 53 of the FBTAA 1986 and that they are not included in the narrow definition of a 'car expense' under Section 136(1) of the FBTAA 1986.

The ATO is of the view that road tolls will either be an expense payment fringe benefit under Section 20 of the FBTAA 1986 (where the employee incurs an expense) or a residual fringe benefit under Section 45 of the FBTAA 1986 if the obligation to pay the road tolls is the employer's. However, there will be many factual matters that will ultimately determine the correct FBT outcome.

Where an expense or residual fringe benefit arises, an employee may lodge a declaration to show the extent to which road tolls paid or otherwise provided by an employer are for business use. An employer may, where the facts relevantly allow the same, prepare a 'business use only' declaration in accordance with Sections 20A and/or 47A of the FBTAA 1986.

Where road tolls are provided on an infrequent and irregular basis, the minor benefits exemption can be applied. Obviously, where an employee uses a car to travel predominantly for business purposes and is permitted to use an e-TAG or transponder to pay road tolls in relation to trips between home and work on a regular basis, the minor benefits exemption would not apply.

In accordance with the new FBT reporting requirements, fringe benefits need to be allocated to particular employees for the purposes of reporting benefits on employees' payment summaries, subject to some exclusion. If tolls paid on behalf of employees are to be included in this requirement where no exemption applies, accurate records will need to be kept indicating both whether tolling expenditure incurred on a journey was of a personal or business nature, and which employee was using the car. We, therefore, submit that simpler administrative arrangements are required if employers are expected to comply with these rules.

This varied treatment creates unnecessary extra work and the need to consider different section of the FBT laws to determine which provision should be applied for ultimately the same outcome.

It will be very difficult for employers to monitor vehicle use on an employee-by-employee basis, for the purposes of allocating benefits between employees and satisfying the new fringe benefits reporting requirements. Tolling expenditure is measured per account, rather than per employee or vehicle. For small business, two account options are available:

Option 1

When different employees use different vehicles, all of this usage will be recorded on the one account. How will the employer's breakdown this information down per employee for the FBT reporting requirements?

A solution could be to keep a logbook with each vehicle, recording who undertook and the purpose of, each tolled journey. If more than one employee is involved, apportioning of toll expense for FBT purposes may be required if there is any personal use of the vehicle. However, we submit that this method of recording by employees and the subsequent analysis by employers will be administratively burdensome.

Option 2

The second option for small business is to share one e-TAG or transponder amongst up to four registered vehicles of the same class that are attached to the Standard Toll Account. The same recording issues as above will exist. In addition, if one logbook is kept with the mobile e-TAG or transponder to record all journeys, employers will have the additional complexity of accurately recording trips taken in the other registered vehicles, which do not have the e-TAG or transponder with them for that journey.

A solution in this instance may involve having a logbook in each of the four registered vehicles, recording every journey. Once the toll account is received, the employer will need to cross-reference this with the logbooks and determine whether any private usage occurred. The relevant amounts for FBT will then be able to be calculated and allocated accurately between employees. Employers may need to be mindful of the additional fee incurred by registered vehicles that use toll-ways for example; CityLink in Melbourne without an e-TAG will incur such fees and need to incorporate these into any FBT calculations they perform. This would be a complex task to administer accurately and in turn a compliance nightmare.

If more than one employee uses the motor vehicle (eg pooled cars) and there is some private use, employers will need to decide how they are going to calculate the FBT allocation. Will apportioning between travellers be required, or allocated against a particular employee.

A further issue, for employers with mixed vehicle fleets, relates to the fact that vehicles exempt under Section 8(2) or 47(6) FBTAA 1986 are exempt from FBT, for example, where they are panel vans or utility trucks (either greater or less than 1 tonne carrying capacity). However, a fringe benefit can still arise from the employer paying or reimbursing the bridge or road toll and

FBT will be payable on any private use. This FBT treatment seems to be at variance with the original intention of the Act, that is, to exempt this type of vehicle from FBT in the first instance.

The professional bodies recommend an urgent review of the current FBT treatment of the payment by employers of bridge and road toll expenditure incurred by their employees. We suggest that the best solution would be to amend Section 136(1) of the FBTAA 1986 to include within the definition of a car expense, 'the payment of bridge and road tolls by employers'. We believe that the resulting exemption under Section 53 of the FTAA 1986 would be the most sensible approach.

Accordingly, these car expenses would be treated as exempt benefits under Section 53 of the FBTAA 1986 and, therefore, would be excluded from the reportable fringe benefits requirements. This would significantly reduce compliance costs for employers.

11. Minor and Infrequent rule

This rule as set out in Section 58P FBTAA 1986 allows for the exemption of fringe benefits, which are both minor and provided on an infrequent and irregular basis. The question of what is minor is set out in Subsection 58P(1)(e) of the FBTAA 1986. The question of what is infrequent and irregular is, however, much more subjective and can result in much time assessing the tests set out in subsection 58P(1)(f) of the FBTAA 1986. In addition, this causes much concern for employers and employees alike.

It is our view that the various tests set out in Subsection 58P(1)(f) of FBTAA1986 are highly subjective and create a compliance burden for employers when assessing whether the exemption applies. This has become more of an issue since the introduction of reportable fringe benefits, as employees now have a much greater interest in understanding the basis for the FBT treatment of particular benefits.

The professional bodies consider that the $100 threshold for minor and infrequent benefits is too low. It is recommended that the threshold be increased to at least $200. This amount should also be indexed each year to account for inflation. We note that no account for inflation has occurred since its introduction in 1986.

12. Election to group

At the present time there is no ability for companies that are a part of a group to elect to consolidate/group their FBT obligations.

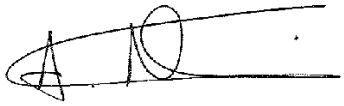
Other parts of the tax legislation allow for companies to group. For example: GST grouping and consolidations. In our view companies in a group should have the ability to group. Furthermore, their needs to be consistency in practice across all taxes to ensure compliance costs are kept to a minimum.

The professional bodies recommend that companies should be able to have the option to elect to group their FBT obligations and thus only lodge one FBT return. We, therefore, recommend that the legislation be amended to permit this.

CONCLUSION

The professional bodies look forward to working together with the ATO and Government to progress and resolve these recommendations. Should you require any further clarification on this matter, please do not hesitate to contact Ali Noroozi (on 9290 5623) or Maria Benardis (on 9290 5761) of the Institute of Chartered Accountants, the co-ordinating professional body.

Yours sincerely



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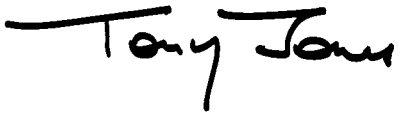

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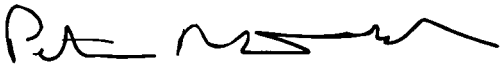

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