



10 August, 2012

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

Dear Mr Boyd

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

Please find enclosed a response from the Treasury to the questions on notice received from the House of Representatives Standing Committee on Economics on 1 August 2012 regarding the above Bill.

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

Yours sincerely

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Tax Analysis Division

HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON ECONOMICS

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

QUESTIONS ON NOTICE FROM SCOTT MORRISON MP

TO TREASURY

Reform of the living-away-from-home (LAFH) allowance and benefit rules

Financial impact: The reforms have the following fiscal impact over the forward estimates:

2011-12	2012-13	2013-14	2014-15	2015-16
-\$0.5m	\$204.5m	\$434.9m	\$590.6m	\$659.4m

Questions in relation to forward estimates

- 1 How much of the fiscal impact per year relates to LAFH allowances and benefits that will be provided to 457 visa holders?
 - A. Treasury estimates that around 80 per cent of the fiscal impact relates to LAFH allowances and benefits that will be provided to 457 visa holders in 2012-13, moving to around 60 per cent for 2014-15 onwards.

- 2 Of the amount that relates to 457 visa holders how much will be additional PAYG withholding revenue and how much will be additional FBT revenue? How was this composition determined?
 - A. The relative composition of revenue impacts is dependent on how individuals choose to respond to the policy. In estimating this composition, the scenarios considered by Treasury included: individuals being paid more cash salary by their employer instead of the fringe benefit; individuals moving completely out of the LAFH system and not receiving additional pay; and individuals staying within the system and incurring additional fringe benefits tax.

Given the uncertainty around how individuals choose to respond to the policy, there is a high degree of uncertainty about the respective contribution of different revenue components to the total fiscal impact.

3 How many 457 visa holders were the calculations based on for each year? What immigration data was relied upon? Was the most current data used? If immigration data was not used, what data was used to come up with the estimates?

A. Exact data on how many 457 visa holders are actually accessing LAFH allowances and benefits is not available, including from the Department of Immigration and Citizenship (DIAC). An estimate of around 50,000 was derived based on data provided by the ATO. DIAC data was looked at but due to LAFH allowance and benefit limitations could not be fully utilised.

4 If the revenue from 457 visa holders is expected to increase year on year, then given that the transitional provisions will not apply to the majority of them what is the basis of the increase?

A. The revenue from 457 visa holders is not expected to increase significantly year on year.

5 What percentage of the total number of 457 visa holders are receiving, or are assumed to be receiving either LAFH allowances or LAFH benefits?

A. See answer to question 3.

6 What family compositions were taken into account in relation to the calculations for 457 visa holders?

A. The costing was modelled on the notion of an average rate of LAFH allowances or benefits, which reflected a range of family compositions.

7 Were any assumptions made that employers would stop paying LAFH allowances or providing LAFH benefits? If so, what proportion and what was the basis for this?

How employers will choose to respond to the policy is highly uncertain. For the purpose of the modelling, it was assumed that around 50 per cent of employees will convert LAFH allowances and benefits into salary and wages.

8 Were any assumptions made that employers would compensate their employees by grossing up allowances for the additional PAYG tax payable?

A. Yes

9 What amounts were taken into account in relation to food allowances paid to employees? Was any recognition given to the fact that the majority of food allowances paid to 457 visa holders are based on the FBT exempt component of the reasonable food allowances published by the ATO each year?

A. The costing was based on data provided by the ATO which includes the food component, and consideration was also given to reasonable food allowances.

10 What amounts were taken into account in relation to accommodation allowances or accommodation costs for employees? How were these determined?

A. Assumptions in relation to accommodation amounts were made based on observed arrangements, informed by data provided by the ATO.

11 Did Treasury or ATO consult with the Department of Immigration and Citizenship on the impact of the changes on 457 visa holders? Did it seek or receive any data from the DIAC on which it based its assumptions? If so, what information was received and used?

A. Data was requested and received from DIAC on 457 visa holders, however DIAC only collects information on total remuneration and the LAFH allowance and benefit component is not able to be separately identified.

12 According to the Department of Immigration, on 1 June 2012, there were a total of 90,221 subclass 457 visa holders in Australia. The composition of these were as follows:

53,896 had no dependents

17,933 had one dependant (assumed to be a spouse)

8063 had two dependants (assumed to be a spouse and 1 child)

7633 had three dependants (assumed to be a spouse and 2 children)

2169 had four dependants (assumed to be a spouse and 3 children)

527 had five or more dependants (assumed to be a spouse and 4 or more children).

Assumptions:

All of these 457 visa holders are paid a LAFH allowance.

The food allowance is based on the ATO's exempt amounts for the relevant family structure.

An accommodation allowance of \$400 per week is paid for singles and \$500 per week is paid for families (2 or more dependants).

The employees' taxable income is between \$37,000 and \$80,000 – ie 34% marginal tax rate.

Scenario 1

Employees are fully compensated by their employers with grossed up allowances.

The additional tax revenue to the government under this scenario after factoring in the tax effect for the employer would be approximately \$1.175b per year.

The additional cost to employers under this scenario would be \$1.691b per year.

Scenario 2

Employees are not compensated by their employers and have to bare the PAYG cost themselves.

The additional tax revenue to the government under this scenario after factoring in the tax effect for the employer would be approximately \$1.103b per year.

The additional cost to employers under this scenario would be reduced by approximately \$1.27b per year.

Even if only 50% of the 457 visa holders received a LAFH allowance then the additional revenue would still be \$587.5m and \$551.5m under the respective scenarios per year.

However, it is more likely that the number of 457 visa holders receiving a LAFH allowance would be at least 80% if not more. It should also be noted that:

The accommodation allowances actually paid are likely to be substantially more than the amounts used in these calculations

A significant proportion of the allowances are likely to be taxed at the higher marginal tax rate of 38.5%

If benefits are provided through the FBT system then the tax revenue will be further increased due to the higher effective tax rate of 46.5%.

- 13 Based on these assumptions, does the Department agree that the revenue is likely to exceed their estimates? If not, why not? Please provide your assumptions and calculations used by Treasury and/or ATO to justify your estimates.

A. No, the Treasury modelling has been informed by data provided by the ATO.

- 14 Will the department provide the Committee with the modelling scenarios, assumptions and the figures generated from each of the scenarios they used to calculate the revenue savings in the forward estimates?

A. The costing was based on data provided by the ATO. The estimated data set was then ranged by the resident status of individuals, and the type of LAFH allowance or benefit – food or accommodation.

Employer and employee behavioral assumptions were incorporated to account for how individuals and employers will possibly react to the new system. This included some employees converting LAFH allowances and benefits into salary and wages, some employers paying extra remuneration, some people staying in the FBT system, and some alternative FBT concessions being accessed.

The net result of these changes was then computed.

- 15 What does the department anticipate the increased remuneration costs for an employer to be as a result of these changes? On what assumptions have these calculations been made? Can you set out where all those additional costs will occur?

A. Any increases in employment costs as a result of these changes will be different for each employer. Assumptions on increased costs of remuneration were made in line with the answer to question 8.

16 What would be the cost to the budget if the implementation of the measure was delayed until April 2013 based on the treasury's assumptions? What would be the cost to the budget be if the assumptions were changed to include the updated impact on 457 visa holders provided in the scenarios above?

A. Treasury does not have a costing for those scenarios.

17 What would be the cost to the budget if the implementation of the measure was transitioned over a two year period from July 2012?

A. There are no publically available estimates for this proposal. The two additional reforms to LAFH allowances and benefits announced in the 2012-13 Budget will not apply to arrangements entered into before Budget night until 1 July 2014.

18 If transitional provisions were introduced for 457 visa holders similar to those for resident Australians (assuming that the total number of 457 visa holders affected by the LAFHA remains constant) what would be the revenue implications? What would be the impact under a 2 year transitional period if the measure was fully compensated and if it was non-compensated for each year over the forward estimates?

A. Treasury does not have a costing for those scenarios.