Law Council
OF AUSTRALIA

Response to the Treasury Consultation Paper 'Fringe Benefits Tax Reform Living Away From Home Benefits'

To The Treasury

Submission by the Taxation Committee, Business Law Section,

Law Council of Australia

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Fiscal and economic considerations

- Under the proposed reforms, employers who currently compensate their employees for housing costs in circumstances where they are required to live away from home (**LAFH**) may incur additional costs relating to those employees. Where employers currently provide their employees with a living away from home allowance (**LAFHA**), employers may be obliged to gross up their employees' wages to ensure that the employees' net income position (i.e. after tax income) is maintained. This will be the case especially where there are legally binding employment agreements which commit the employer to providing these existing entitlements.

  Where businesses are unable to afford the increased costs to maintain this net income, this may lead to job/salary cuts resulting in a higher unemployment rate for Australia.

  Where employers are not contractually obliged to gross-up payments to employees for an increase in taxes imposed relating to housing, employees will bear the imposition of tax, which may impact on employment decisions for affected employees in terms of choice of employer, or choice of working in Australia at all

Inequity and discrimination

- The consultation paper indicates that the proposed reforms are designed to create a level playing field between an Australian resident and a temporary resident working in Australia.
- The proposed reforms do not achieve a level playing field between Australian residents and non-residents, as the proposed reforms seek to impose an obligation on non-residents to maintain a home in Australia without imposing a similar obligation (to maintain a home in Australia) on Australian residents.
- This inequitable treatment may also be a cause for concern regarding non-discrimination articles within Australia's relevant international tax conventions (discussed below).

Impact on community sector caps

- The consultation paper advises that the proposed reforms will not impact on employees of community sector organisations who are not currently using the extent of the fringe benefits tax (**FBT**) exemption cap afforded to them. Whilst the intention of this statement has some merit, there are practical implications which require further consideration.
- Under the proposed reforms, a benefit provided in the form of a LAFHA will no longer be regarded as a fringe benefit. Instead, LAFHAs will be subject to income tax in the hands of the employee at their marginal rate. Where a LAFHA is no longer subject to a tax concession, such as for certain temporary residents, the employee will not be able to utilise the concessional cap applicable to fringe benefits.
- Where currently provided as a fringe benefit, any living-away-from-home benefits would likely take up the majority of any concessional cap, if not all of it, particularly given the cost of living and rental prices in Australia.
- Accordingly, it is likely that the impact of the FBT concessional cap will be effectively diminished for community sector employers of temporary residents.

What transition arrangements would be appropriate?

- A main concern for employers is the timing between the announcement of the reforms and the date with which they are to have effect. In particular, the impact on pre-existing commitments, such as employment contracts and rental agreements.
- The Committee proposes that transitional arrangements should be implemented for all taxpayers so that arrangements in existence prior to 1 July 2012 (or date of enactment, whichever is earlier) are exempt from the proposed reforms for the year ended 30 June 2013. This would allow employers with the flexibility they need to assess living-away-from-home benefits without exposing either themselves or employees to tax obligations which were unforeseen at the time the arrangement was entered into.

Increased employer compliance and on-costs

- Significant administrative burden and costs are likely to be incurred by employers in adjusting their existing payroll systems to reflect the impact of the proposed reforms. Where an employee is provided with a LAFHA, the allowance will be required to be declared for payroll tax and WorkCover purposes, irrespective of whether the allowance is deductible. As such, the payroll tax liability and WorkCover premiums of employers will increase as a consequence of the proposed LAFHA changes. Furthermore, if the proposed changes take effect, employers will be required to pay superannuation on cash allowances that are currently not considered in employers' superannuation calculations.

Contract Issues/Lease agreements

- Employees who have residential lease agreements for a fixed number of years may no longer be able to afford the required lease payments due to accommodation allowances becoming assessable income under the pay-as-you-go withholding regime as a result of the proposed reforms. In addition, where the lease is in the employer's name, the employer will be required to fulfil the terms of the contract despite incurring extra taxes on LAFHA and/or LAFH benefits from 1 July 2012. Accordingly, post implementation of the LAFHA changes, employers will need to consider increasing the pre-tax remuneration of the relevant employee required to ensure that the employee is no worse off as a result of these proposed reforms.

Other potential discrimination concerns

The vast majority of Australia's international tax conventions contain an article regarding non-discrimination which are for the most part are consistent with Article 24 of the OECD Model Convention. Paragraph 1 of Article 24 provides:

> *"Nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith, which is other or more burdensome than the taxation and connected requirements to which nationals of that other State in the same circumstances, in particular with respect to residence, are or may be subjected"*[1]

OECD commentary on paragraph 1 of Article 24 provides that it:

[1] OECD, "Model Tax Convention on Income and on Capital (Condensed Version)", 22 July 2010, Article 24 Non Discrimination, para. 1, p. 35.

"Establishes the principle that for the purposes of taxation discrimination on the grounds of nationality is forbidden, and that, subject to reciprocity, the Nationals of a Contracting State may not be less favourably treated in the other Contracting State than nationals of the latter State in the same circumstances."[2]

- It is recognised that "in the same circumstances" may have particular regard to residency, which is a factor by which discrimination is allowed.
- The concern, even if the proposed reforms are not found to be in breach of the convention, is the apparent link between Nationality and residency unique to the concept of temporary residency, such that an Australian citizen will never be a temporary resident.

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[2] OECD, "Model Tax Convention on Income and on Capital (Condensed Version)", 22 July 2010, Commentary on Article 24 concerning non-discrimination, para. 5, p. 333.