



Submission to the  
Federal Treasurer  
Fringe benefits tax  
reforms: Living-away-  
from-home benefits

Manager  
Philanthropy and Exemptions Unit  
Personal and Retirement Income Division  
The Treasury  
Langton Crescent  
PARKES ACT 2600

3 February 2012

Our Ref: EB/AF/PT

Dear Sir/Madam

**FRINGE BENEFITS TAX REFORM  
LIVING-AWAY-FROM-HOME BENEFITS**

Please find attached our submission in response to the Federal Government's consultation paper entitled *Fringe Benefits Tax (FBT) Reform Living-away-from-home benefits*, inviting submissions regarding proposed reforms to certain living-away-from-home benefits concessions as announced by the Federal Treasurer on 29 November 2011 as part of the *2011-12 Mid-Year Economic and Fiscal Outlook*.

Please contact me on (02) 9322 7614 should you have any questions.

Yours sincerely



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Encl.

cc: Mr Lee Beaver – FBT Specialisation Manager, Law and Practice, Administration, Business and Personal Taxes, Centre of Expertise, Australian Taxation Office

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# Contents

Executive summary	1
1 Submission	7
2 Current FBT position	8
3 The Government's proposed reforms	10
3.1 Reasons for reform	10
3.2 Effect of proposed reform	10
3.3 Employees not affected by the reforms	12
4 Skills shortages in Australia	13
4.1 Australia's looming skills shortage	13
4.2 Importance of skilled migrants	13
4.3 Impact of reforms on skilled migrants	15
5 Fiscal and economic considerations	17
5.1 Impacts on economic growth	17
5.2 Skilled migrant contribution to revenue	18
5.3 Australian living standards	18
6 Inconsistency with other Government initiatives	20
6.1 National Resource Sector Employment Taskforce (2009)	20
6.2 Australia as a financial services centre	20
6.3 Positive credit reporting reforms	21
6.4 Establishing business in Australia	21
7 Inequity and discrimination concerns	22
7.1 Inequity between permanent and temporary residents	22
7.2 Potential discrimination concerns	23
8 Increased employer compliance and on-costs	24
8.1 PAYG withholding	24
8.2 Payroll tax, superannuation guarantee and WorkCover	24
9 Community sector FBT concessions cap	26
9.1 Summary of FBT concessions caps	26
9.2 Interaction between proposed reforms and concessional caps	26
10 Statutory and reasonable food amounts	28
10.1 Statutory food amount	28
10.2 Reasonable food amount	28

	10.3 Indexation	29
	10.4 Impact of reforms	29
11	Transitional arrangements	30
	11.1 Transitional issues	30
	11.2 Proposed transitional arrangement	30
	11.3 Community sector	30
12	Further clarity sought	31
	12.1 Maintaining a home	31
	12.2 Fly-in Fly-out (FIFO) arrangements	31
	12.3 Remote area housing	32
	12.4 Application to foreign-residents	32
	12.5 Other overseas employee concessions	32
	12.6 Living-away-from-home vs. travel benefits	33
13	Our proposed amendments	34
	13.1 Discussion of the Government's proposed reforms	34
	13.2 Explanation of our proposed amendments	35

# Executive summary

## Summary

FBT legislation provides for concessional taxation treatment of certain benefits to employees who are required to live away from their usual place of residence in order to perform the duties of their employment.

The Government has concluded that these tax concessions have been subject to growing exploitation, allowing people to claim significant amounts of tax-free income. In particular, the Government appears to be concerned by: 1) the application of living-away-from-home benefit concessions to temporary resident employees; and, 2) the ability (in some circumstances) for employees to access amounts of tax-free remuneration which exceed actual costs incurred.

Accordingly, the Government has announced proposed reforms which are intended to apply to both new and existing arrangements from 1 July 2012.

In essence, the reforms will require all employees to: 1) substantiate their living-away-from-home expenses; and, 2) for temporary residents to qualify, they must be living away from an Australian home which they maintain.

Furthermore, benefits paid as a living-away-from-home allowance (LAFHA) will no longer be considered a “fringe benefit” and will therefore be subject to income tax in the hands of the employee.

## Questions for consultation

The consultation paper provided a number of questions for consultation. We provide our responses as part of this submission below. We discuss these issues in further detail in the body of our submission and refer to the relevant section of the submission where appropriate.

### 1. Are there any unintended consequences from the proposed reforms?

#### **Skilled migrants and skills shortages**

It is well known that Australia faces looming skills shortages. This understanding is commonly held between industry, Government, media and economists alike, and was discussed extensively in Deloitte Australia’s recent paper, *Building the Lucky Country: Where is your next worker?*<sup>1</sup>. Similarly, it is also commonly held that skilled migration plays and will continue to play a vital role in ensuring Australia’s future economic growth amid skills shortages. Please refer to section 4 of this submission for further discussion.

Australia’s cost of living is relatively high on a global scale. There are also additional factors and costs that skilled migrants face, such as higher effective tax rates, the ability to receive fewer Government benefits, additional education costs and cultural familiarisation. Furthermore, many skilled migrants continue to maintain a home in their home country.

The proposed reforms will remove tax concessions currently available to temporary residents who are provided with living-away-from-home benefits, to the extent that they are living away from an overseas home. This means that these benefits will attract additional tax costs,

<sup>1</sup> Deloitte Touche Tohmatsu, *Building the Lucky Country: Where is your next worker?*, November 2011

which will either be incurred by the employee or employer, depending on how the benefit is provided.

It is not realistic to assume employees would choose to live away from home unless they are adequately compensated to cover any increased cost of living. Accordingly, employers will need to “gross-up” benefits to account for any additional taxes, resulting in higher costs.

Businesses are already compensating skilled migrants to the extent that their resources allow. Businesses relying on skilled migrants will therefore need to reduce profitability and growth potential or face failing to attract and retain new and existing talent.

In this regard, the proposed reforms are likely to have the following unintended consequences:

#### *Economic growth*

Economic growth is dependent not only on demand, but also on the ability for supply to meet demand. In the context of Australia’s looming skills shortages, the ability to access skilled workers is vital to promote economic growth.

While there are long-term domestic measures which can be implemented to address skills shortages, in the short- to medium-term, access to skilled migrants remains one of the most effective ways of increasing the supply of skilled labour.

Economic growth constraints hinder the ability of businesses to generate higher taxable income, resulting in less than optimal future corporate tax revenues.

#### *Inflationary pressures*

The inability for supply to meet demand results in pricing pressure on goods and services. Where the supply constraint is due to skills shortages, the demand for labour means further pricing pressure from an increase in the cost of labour.

In industries such as the resource sector, which accounts for almost half of Australia’s exports, the increased cost of labour resulting from skills shortages adds to unnecessary inflationary pressures, which may ultimately increase interest rates.

#### *Contribution to revenue*

Skilled migrants arriving in Australia boost the Federal Budget’s bottom line. This is a result of these individuals paying higher effective tax rates and receiving fewer Government benefits than average Australian residents.

To the extent that businesses cannot afford to attract and retain skilled migrants, there would expect to be a proportional impact on the Federal Budget’s bottom line. Furthermore, there will be a reduction in indirect and State tax revenues, such as from Goods and Services Tax (GST) and payroll tax.

Furthermore, the typical age of skilled migrants means that Australia has not had to subsidise their substantial education and healthcare costs, which have been subsidised by other countries prior to their arrival in Australia.

#### *Living standards*

Skilled migrants assist in increasing populations, particularly in remote areas with skills demands. An increase in population means there are more “users”, providing a greater potential for revenue and a greater opportunity for investment in infrastructure.

Accordingly, a reduction in migrant numbers has the potential to discourage investment in infrastructure, potentially reducing the living standards of all residents.

### ***Inconsistency with Government initiatives***

There are a number of initiatives which have been either undertaken or commissioned by the Government which have regard to Australia's looming skills shortages. Each of these initiatives have recommended the need for skilled migration. In particular, we make reference to recommendations made by the National Resource Sector Employment Taskforce, as well as the Australian Financial Centre Forum.

There are also other Government policies which will be hampered by the failure to attract skilled migrants. For the purpose of this submission, we specifically refer to the introduction of positive credit reporting, which Australia has been late to adopt. Accordingly, businesses will need to rely on experience obtained overseas to implement best practice.

This issue is also relevant for the purposes of establishing new business activities in Australia, where the expertise of skilled migrants is required.

We discuss in greater detail the importance of skilled migrants with regard to these initiatives at section 6 of this submission.

### ***Inequity and discrimination***

The proposed reforms require that a temporary resident is living away from a home in Australia (which they continue to maintain).

The consultation paper indicates that the proposed reforms are designed to create a level playing field between an Australian worker and a temporary resident working in Australia. Under the proposed reforms this will not be the case, as a permanent resident is not required to maintain an Australian home in order to obtain access the concessions.

We note this inequitable treatment may also be a cause for concern regarding non-discrimination articles within Australia's relevant international tax conventions.

### ***Community sector caps***

The consultation paper advises that the proposed reforms will not affect employees of the community sector organisations who do not use the full extent of the FBT exemption cap. While 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 tax rate.

Where a tax concession is no longer available (e.g. certain temporary residents), employees will no longer be able to utilise the concessional cap for LAFHAs as it is only applicable to fringe benefits.

Living-away-from-home benefits provided in the form of a fringe benefit, would likely utilise the majority of the concessional cap (if not all of it), particularly given the cost of living and rental prices in Australia.

Accordingly, it is likely that the FBT burden will increase for community sector employers of temporary residents.

## 2. What practical aspects of the proposed reforms need further consideration?

Further to the practical aspects arising from any unintended consequences above, we have considered the following practical aspects of the proposed reforms:

- *Substantiation requirements* – we do not propose any further consideration to the substantiation requirements of the proposed reforms at this time
- *Pay-as-you-go (PAYG) withholding* – where an employee is expected to incur deductible expenses, we seek confirmation that the PAYG withholding variation made by the ATO will automatically apply. Accordingly, employers will not be required to apply on behalf of each individual
- *Payroll systems* – where a PAYG withholding variation is not applicable, LAFHAs will be subject to PAYG withholding. Employers will be required to make changes to their payroll systems to ensure compliance with PAYG withholding rules. We do not propose any further consideration at this time. However, we wish to bring to the attention of Treasury the wider impact that the proposed reforms will have on employers
- *Employment tax obligations* – in addition to compliance with PAYG withholding, the proposed reforms will also impact other employment tax obligations, which we discuss further at question 3
- *Pre-existing commitments* – we believe that pre-existing arrangements, such as employment contracts and rental agreements will hinder the flexibility required by employers to restructure how living-away-from-home benefits are provided. Please refer to section 12 of this submission where we discuss this issue in the context of transitional arrangements.

## 3. Are there any interactions with other areas of the tax law that need to be addressed?

### *Interaction with other employer obligations*

Living-away-from-home benefits are currently only subject to other employer obligations such as State payroll tax and WorkCover where it is taxable for fringe benefit tax purposes (including a LAFHA).

However, as a LAFHA will no longer be a fringe benefit, payroll tax and WorkCover obligations will arise irrespective of whether a concession applies. Furthermore, a superannuation guarantee obligation will also arise.

We summarise the treatment of living-away-from-home benefits for other employer obligations under the proposed reforms.

	Fringe benefit (Non-taxable)	Fringe benefit (Taxable)	LAFHA (Deductible)	LAFHA (Non-deductible)
Payroll Tax	No	Yes	Yes	Yes
Superannuation Guarantee	No	No	Yes	Yes
WorkCover	No	Yes	Yes	Yes



### ***Interaction with FBT legislation and principles***

In addition to employment tax obligations, we seek further clarity from Treasury with respect to the proposed reforms and their interactions with other areas of tax laws, including:

- The meaning of “maintaining a home” for the purposes of applying the proposed reforms to temporary residents
- The impact of proposed reforms on FIFO arrangements and clarity regarding existing limitations
- The application of concessions under the proposed reforms to foreign-residents living away from home
- The impact of the proposed reforms on other concessions available to overseas employees under FBT legislation (and the apparent inconsistencies that result) and
- The distinction between an employee who is living-away-from-home and one who is travelling for business.

Please refer to section 12 of this submission in this regard.

#### **4. As the statutory food amount is intended to reflect the ordinary costs incurred by an Australian in 2011, what should the statutory food amount be updated to?**

We propose that Treasury uses data collated by the Australian Bureau of Statistics (ABS) to determine the statutory food amount, such as weekly expenditure on food and non-alcoholic beverages in Australian capital cities.

We also propose that Treasury determines the statutory food amount with respect to the lower quartile. This would be so as not to disadvantage employees from households who incur less than the average.

#### **5. Should the statutory food amount be indexed annually to ensure it remains up to date?**

We propose that the statutory food amount is indexed annually going forward to ensure it remains current and reflective of actual weekly expenditure.

#### **6. What transitional arrangements would be appropriate for the community sector?**

A main concern for employers is the timing between the announcement of the reforms and the date on which they are to have effect, in particular, as regards pre-existing commitments, such as employment contracts and rental agreements, and the impact they will have on project costing and businesses generally.

We propose 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 ending 30 June 2013. We further propose that for community sector employers, these transitional arrangements may apply beyond the year ending 30 June 2013.

This would allow employers 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.

To facilitate and encourage employers and their employees to vary their existing arrangements, we propose that a FBT exemption is made available for lease break costs.

Please refer to section 12 of this submission for our full discussion on transitional arrangements.

### **Alternative amendments**

We propose that tax concessions be available for all employees who are required to live away from their usual place of residence, irrespective of whether they are: 1) permanent or temporary residents; or, 2) living away from a home in Australia or overseas.

Please refer to section 13 of this submission for a more detailed discussion in this regard.

# 1 Submission

We refer to the Federal Government's (the "Government") consultation paper entitled *Fringe Benefits Tax (FBT) Reform Living-away-from-home benefits*, inviting submissions from professional and business groups regarding proposed reforms to certain living-away-from-home benefits concessions as announced by the Federal Treasurer on 29 November 2011 as part of the *2011-12 Mid-Year Economic and Fiscal Outlook*.

We respond to the questions for consultation as sought in the Government's consultation paper. Our submission also seeks further clarification regarding the implementation and depth of the reforms and, where appropriate, proposes alternative reforms.

We outline in the following sections our analysis and responses to the proposed reforms as well as our suggested alternative reforms which have been constructed based on our analysis.

## 2 Current FBT position

The *Fringe Benefits Tax Assessment Act 1986* (FBTAA) provides for concessional taxation treatment of certain benefits provided either by way of an allowance or an expense payment, property or residual fringe benefit (whichever is relevant) to employees who are required to live away from their usual place of residence in order to perform the duties of their employment.

The relevant concessions for the purpose of this submission are as follows:

1. Living-away-from-home allowance
2. Exempt accommodation expense payment benefit
3. Exempt residual benefits – living-away-from-home accommodation and
4. Reduction of taxable value of living-away-from-home food fringe benefits.

### 2.1 Living-away-from-home allowance (LAFHA)

The FBT treatment of a LAFHA is determined pursuant to Division 7 of the FBTAA.

Where an allowance is paid to an employee in respect of living-away-from-home expenses it will generally be taxable in the hands of the employee for income tax purposes unless it is regarded as a LAFHA as determined under Division 7 of the FBTAA.

Section 30 of the FBTAA defines a LAFHA as an allowance paid to an employee that is in the nature of compensation for additional expenses incurred, and other disadvantages suffered, by reason that the employee is required to live away from his or her usual place of residence in order to perform the duties of their employment. Additional expenses do not include expenses for which the employee would be entitled to an income tax deduction.

The taxable value of a LAFHA is determined pursuant to section 31 of the FBTAA. The taxable value is the amount of the LAFHA reduced by the ‘exempt accommodation component’ and ‘exempt food component’, whichever is applicable. These terms are defined in subsection 136(1) of the FBTAA as follows:

- ‘Exempt accommodation component’ is so much of the allowance that is in the nature of compensation for additional expenses on accommodation that the employee could reasonably be expected to incur and
- ‘Exempt food component’ is so much of the allowance that is reasonable compensation for additional expenses on food (i.e. in addition to the cost of food and drink expected to have been ordinarily incurred had the employee continued to reside at their usual place of residence – ‘home food costs’).

For the purposes of consistently applying home food costs, a ‘statutory food amount’ was legislated in subsection 136(1) to be \$42 (for persons aged 12 and over) and \$21 (for persons less than 12 years of age). Only the amount of the food component portion of the allowance that exceeds (or is designed to be paid in addition to) the statutory food amount is treated as an exempt food component.

### 2.2 Exempt accommodation expense payment benefit

Section 21 of the FBTAA provides that an expense payment benefit in respect of expenditure incurred by an employee on accommodation because the employee was required to live away from his or her usual place of residence in order to perform the duties of their employment is exempt from FBT.

## 2.3 Exempt residual benefits – living-away-from-home accommodation

Subsection 47(5) of the FBTA provides that a residual benefit in respect of residential accommodation granted to an employee who is required to live away from his or her usual place of residence in order to perform the duties of their employment is exempt from FBT.

## 2.4 Reduction of taxable value of living-away-from-home food fringe benefits

Section 63 of the FBTA provides for the taxable value of living-away-from-home food fringe benefits to be reduced in cases where an employee is required to live away from their usual place of residence in order to perform the duties of their employment.

A living-away-from-home food fringe benefit can be provided by an employer to an employee as an expense payment fringe benefit or property fringe benefit.

# 3 The Government's proposed reforms

## 3.1 Reasons for reform

In principle, employees should pay for their housing and food costs out of income that has already been taxed. The tax system currently assists people who are living away from home with their accommodation and food expenses.

The Government has found and concluded that these tax concessions have been subject to growing exploitation, allowing people to claim significant amounts of tax-free income. In particular, the Government appears to be concerned by temporary resident employees who are living away from a home outside Australia who they regard as having "an advantage" in receiving tax-free income over Australian workers.

Furthermore, the Government is concerned that the concessions currently allow some employees to access large amounts of tax-free remuneration as an allowances that is well in excess of actual costs incurred by the employee. This is outside the scope of the original policy intent and Treasury has determined that this represents a significant and growing cost to Government revenue.

## 3.2 Effect of proposed reform

The Government proposes to apply its reforms as announced from 1 July 2012. These reforms will apply to both new and existing arrangements from this date.

In essence, the availability of living-away-from-home benefits will be reformed so that tax concessions are only available provided the following conditions are met:

- *Temporary residents* – employees will be required to maintain a home for their own use in Australia (which they are living away from for work) to access the concession, and in those cases the expenses will need to be substantiated or
- *All other employees* – employees will be required to substantiate their living-away-from-home expenses.

We address the effect of these reforms further with reference to the background and intent as provided in the Government's consultation paper.

### 3.2.1 Income tax treatment

An allowance paid to an employee as compensation for being required to live away from their usual place of residence will no longer be a fringe benefit. Instead, the allowance will form part of the employee's assessable income, which is consistent with other employment allowances.

Employees who are permanent residents will be able to claim an income tax deduction for the expenses incurred for accommodation and food while living away from home, provided they can substantiate those expenses.

Temporary resident employees, who maintain a home for their use in Australia which they are required to live away from to perform their work, will also be able to claim a deduction

(provided they can substantiate those expenses). An income tax deduction is therefore not available to temporary resident employees who do not maintain a home for their use in Australia and any LAFHA will be subject to income tax in the hands of the employee.

The Government has indicated that substantiation will not be required for food expenses up to an amount considered by the Commissioner to be reasonable. It is intended that the Australian Taxation Office (ATO) will publish administrative guidance to determine a reasonable food component. If employees choose to claim deductions for amounts in excess of the reasonable amount, the full amount must be substantiated.

### 3.2.2 FBT treatment

Division 7 of the FBTAA will be amended to remove a LAFHA from being treated as a fringe benefit.

#### 3.2.2.1 Accommodation

Where an employer either reimburses an employee for accommodation expenses incurred or provides accommodation directly while they are required to live away from home, the exemptions under section 21 and subsection 47(5) of the FBTAA respectively will continue to apply for permanent residents.

However, consistent with the income tax deductibility of a LAFHA provided to a temporary resident, an exemption will only apply to temporary residents where they are required to live away from a home they maintain in Australia.

Employers will be required to substantiate the expenses of the employee in order for the exemption to apply. Employers will be required to obtain documentary evidence from employees to substantiate the expenses incurred on accommodation. This evidence could include lease agreements, mortgage documents and receipts for accommodation.

#### 3.2.2.2 Food

The reduction in taxable value for living-away-from-home food fringe benefits in section 63 of the FBTAA will continue to be available for permanent residents and for temporary residents who maintain a home for their use in Australia, which they are required to live away from to perform the duties of their employment.

The reduction will only be available to the extent the employee substantiates their expenses. Similar to the substantiation requirements for claiming an income tax deduction for the food component of a LAFHA, substantiation will not be required for food expenses for an amount considered by the Commissioner to be reasonable. The ATO will publish administrative guidance to determine a reasonable food component. If employers choose to reimburse amounts in excess of the reasonable amount, the full amount must be substantiated in order to reduce the taxable value of the benefits.

The taxable value of living-away-from-home food benefits is currently reduced by the amount of the food component which exceeds the statutory food amount. The Government has indicated that the statutory food amount will be reviewed as part of these reforms.

### 3.2.3 Temporary residents

The Government has indicated that the term 'temporary resident' will have the same meaning as used for income tax purposes. The *Income Tax Assessment Act 1997* (ITAA 1997) defines temporary resident in subsection 995-1(1) as a person who:

- Holds a temporary visa granted under the *Migration Act 1958*
- Is not an Australian resident within the meaning of the *Social Security Act 1991* and

- Whose spouse is not an Australian resident within the meaning of the *Social Security Act 1991*.

As explained in the Government's consultation paper, a temporary resident will be considered to be maintaining a home in Australia for their own use when that home is available for their personal use and enjoyment at all times, even though they are living away from it for their work.

To qualify as maintaining a home for their own use in Australia, the temporary resident employee may either own or rent a unit of accommodation. The unit of accommodation must be available for their use at any time and cannot be rented out or sub-let while they are living away from the accommodation.

'Unit of accommodation' is defined in subsection 136(1) of the FBTAA to include:

- A house, flat or home unit
- Accommodation in a house, flat or home unit
- Accommodation in a hotel, hostel, motel or guesthouse
- Accommodation in a bunkhouse or any living quarters
- Accommodation in a ship, vessel or floating structure and
- A caravan or other mobile home.

We understand temporary resident employees who work in remote areas on a fly-in fly-out basis and maintain a home in Australia for their use at all times will qualify for the living away from home concessions.

The Government has indicated that temporary resident employees will be required to provide documentary evidence to their employers that they are maintaining a home in Australia for their own use. The documents must show that the accommodation is available for the employee's use at the time for which the living-away-from-home benefits are being provided.

### 3.3 Employees not affected by the reforms

The Government has indicated that the following classes of taxpayer should not be affected by the reforms:

- Permanent residents receiving living-away-from-home benefits that can be substantiated
- Employees operating under fly-in fly-out arrangements within Australia and
- Employees of community sector organisations who are not currently using all of their FBT exemptions cap.

Furthermore, the Government has indicated that the following should not be affected by the reforms:

- Employees receiving travel allowances who have to travel from their usual place of work for short periods
- Employees receiving FBT remote area concessions and
- Employees receiving FBT education expense concessions for their children when they are living away from home for work.



# 4 Skills shortages in Australia

## 4.1 Australia's looming skills shortage

It has been and continues to be well publicised that Australia faces a looming skills shortage, which is of great significance for Australian's economic growth.

Research conducted by the Department of Education, Employment and Workplace Relations ('DEEWR') found that despite softened labour market conditions in the second half of the 2010-11 year, the proportion of surveyed vacancies in shortage increased from 53 per cent in 2009-10 to 63 per cent in 2010-11.<sup>2</sup>

In particular, the DEEWR survey found skills shortages in a wide range of essential sectors of either great social or economic importance, including building, architectural and construction, engineering, resources (includes mining), education, health (including nursing), social and welfare (including child care), automotive, telecommunications and foods trades.<sup>3</sup>

In addition to current conditions, there are further factors which must be considered that will affect labour shortages in the future. In particular, the expected number of skilled Australian graduates and the retirement of mature-age workers. Both of these factors were referenced in Deloitte's *Building the Lucky Country: Where is your next worker?* publication. Among these references, it provided that the pace of retirement will ramp up over the next few years, whereas the number of students exiting education is projected to remain stagnant through to the early 2020s<sup>4</sup>.

In particular, over the next five years it is projected that fewer than 125 people will be exiting education for every 100 retiring. This would be the highest ratio of job market retirements to new entries in Australia's history<sup>5</sup>. It is expected that the number of graduates will increase from 2023 (the number of births in Australia increased by 20% between 2001 and 2009<sup>6</sup>). However, the ratio of working age Australian's to those aged 65 and older will fall from 5 to 1 in 2010 to 2.9 to 1 in 2050<sup>7</sup>, resulting in significant reliance on mature-age workers set to retire.

## 4.2 Importance of skilled migrants

In light of Australia's looming skills shortages and factors referred to above, skilled migration plays and will continue to play a vital role in ensuring Australia's future economic growth.

Immigration Minister Chris Bowen noted the importance of immigration with respect to Australia's future economic growth:

*"Without immigration, it is projected that Australia's labour force growth will almost cease within the next decade and actually start going backwards from*

<sup>2</sup> Australian Government, Department of Education, Employment and Workplace Relations, *Skills Shortages Australia*, June 2011, p.9, <http://www.deewr.gov.au/Employment/LMI/SkillShortages/Documents/NationalSkillShortageReportJun.pdf> (herein referred to as "DEEWR Skills Shortages Australia")

<sup>3</sup> DEEWR Skills Shortages Australia, p.10

<sup>4</sup> Deloitte Touche Tohmatsu, *Building the Lucky Country: Where is your next worker?*, November 2011, p. 6

<sup>5</sup> Deloitte Access Economics estimates, 2011

<sup>6</sup> Australian Bureau of Statistics, *Births, Australia*, Cat. No. 3301.0, 2009

<sup>7</sup> Deloitte Access Economics, *Demographic Model*, 2011

*2036. This demographic change, of course, poses significant challenges for Australia's economic growth, long-term fiscal outlook, living standards and funding increased costs associated with an ageing population.*<sup>8</sup>

In addition to the ability for skilled migrants to be used to fill short-term skills gaps, they can also be utilised to develop and train local workers and implement best practice based on their global experience.

Any reforms which place constraints on access to skilled migrants would potentially disadvantage businesses and negatively affect Australia's economy.

#### 4.2.1 Resources sector

The National Resources Sector Employment Taskforce (NRSET) was established by the current Government in late 2009 to examine ways to meet the skills needs of future major resources projects. Even with reference to current unemployment, the NRSET found:

*"There are emerging shortages at present – mainly engineers and other professional staff with more than five year experience. The domestic supply of mining engineers and geoscientists will not be sufficient to meet demand over the next five years with a shortfall of around 1,700 and 3,000 respectively... While there are currently significant numbers of unemployed tradespeople... the resources sector could be 36,000 tradespeople short by 2015."*<sup>9</sup>

Deloitte Access Economics made a similar conclusion with respect to the resource sector in Queensland, finding:

*"Current labour market settings will fail to meet the expectations and requirements of the resource sector... [there are] a number of specific skill sets that will be in short supply unless there is increased private and public sector action to train, attract and retain new workers for Queensland... Action is needed in the short rather than medium term to deliver solutions to expand the available labour force. If this does not occur, a lack of skilled labour is likely to be a major impediment to the expansion of Queensland's resources sector."*<sup>10</sup>

The NRSET found that there are large numbers of people with relevant qualifications currently working in other occupations; however, to the extent that resource sector skills shortages are recruited from other sectors, there will likely be skills shortages in those industries<sup>11</sup>.

Conversely, the NRSET found that:

*"Each additional job in the resources sector may lead to a further one to three jobs in other industries, with the employment effect tending to be higher in regional centres where the resources sector is a major employer and there are readily available job seekers."*<sup>12</sup>

It is evident that domestic measures alone will not be sufficient in meeting the skills shortages in the resources sector. In fact, they will likely lead to further skills shortages in similar industries in an effort to meet the resources sector's labour demands. Skilled

<sup>8</sup> Chris Bowen, Minister for Immigration and Citizenship, *Australia's migration program as part of Australia's future – Address to the Law Council of Australia – 5<sup>th</sup> Annual Immigration Law Conference* 11 March 2011, <http://www.minister.immi.gov.au/media/cb/2011/cb160145.htm>

<sup>9</sup> Australian Government, National Resources Sector Employment Taskforce, *Resourcing the Future*, July 2010, p. 3 (herein referred to as "Resourcing the Future")

<sup>10</sup> Deloitte Access Economics, *Queensland Resources Council Queensland Resource Sector State Growth Outlook Study*, November 2011, p.5

<sup>11</sup> *Resourcing the Future*, p. 3

<sup>12</sup> *Resourcing the Future*, p. 1

migrants provide the resources sector with a means to fill skills gaps while at the same time relieving pressure on similar industries and even providing an opportunity for growth.

#### 4.2.2 Health sector

As part of an assessment of health workforce sustainability it was found that Australia has a high level of dependence on internationally recruited health professionals relative to other OECD countries<sup>13</sup>.

Australia's nursing workforce is heavily affected by worldwide nurse shortages. Additionally, there is a need for greater general practice healthcare workers in regional and remote areas.

In early 2010, the Government asked Skills Australia, an independent Board of industry, economics and education experts to develop a new Skill Occupation List (SOL)<sup>14</sup> for migration purposes to identify occupations in demand to assist in meeting the skills needs of Australia. The 2011 SOL included 192 occupations, which included the following occupations in the health sector, to name a few:

- General, cardiothoracic, paediatric and neurosurgeons
- Medical practitioners
- Registered nurses
- Nursing clinical director and
- Hospital and retail pharmacists.

Given the importance of healthcare and the difficulty in attracting health workforces in the context of world skills shortages, it is particularly important that concessions are not removed which assist in attracting healthcare workers to Australia.

### 4.3 Impact of reforms on skilled migrants

Notwithstanding the plethora of positive aspects working in Australia has to offer, Australia's cost of living is relatively high on a global scale. In an analysis undertaken by the Organisation for Economic Co-operation and Development (OECD) of monthly comparative price levels (i.e. the price of the same representative basket of consumer goods and services) between OECD countries, Australia was ranked as the 3<sup>rd</sup> most expensive OECD country.<sup>15</sup>

In addition to Australia's cost of living, there are other factors and costs that skilled migrants (who are typically temporary residents) face. Examples include the inability of certain temporary residents to receive Medicare benefits (depending on the migrant's previous country of residence) and the cost of education (e.g. education fees for temporary resident children in NSW public schools currently vary between \$4,500 and 5,500<sup>16</sup>). Furthermore, in many cases, temporary residents continue to maintain a home in their home country.

<sup>13</sup> Australian Healthcare and Hospitals Association, James M. Buchan, Lucio Naccarella, Peter M. Brooks, *Is health workforce sustainability in Australia and New Zealand a realistic policy goal*, 2011, Australian Health Review 35(2) 152-155 <http://dx.doi.org/10.1071/AH10897>

<sup>14</sup> Skills Australia, *Providing advice to the Australian Government about the 2011 Skilled Occupation List*, June 2011, [http://www.skillsaustralia.gov.au/PDFs\\_RTFS/SOL/FactSheetExplanatorySummary.pdf](http://www.skillsaustralia.gov.au/PDFs_RTFS/SOL/FactSheetExplanatorySummary.pdf)

<sup>15</sup> OECD, *Monthly Comparative Price Levels*, November 2011, <http://stats.oecd.org/Index.aspx?DataSetCode=CPL>, accessed 9 January 2012

<sup>16</sup> NSW Government, NSW Department of Education and Communities (Schools), *Temporary Residents Program Fees and Payment*, 9 June 2011 (Originally published 15 February 2007)

In addition, temporary migrants who wish to withdraw their superannuation as part of the Departing Australia Superannuation Payment (DASP), face an additional tax burden as a withholding tax rate of 35% is applied to the superannuation benefits in addition to a 15% contributions tax (i.e. an effective tax rate of 44.75%).

There are also non-financial considerations which are faced by skilled migrants, such as familiarisation with a new culture and language and the time taken to establish one's affairs (e.g. setting up bank accounts, insurance and professional membership). It is not to say that these conditions do not exist for any person looking to work overseas or even interstate, but in light of Australia's skills shortage, they are factors which need to be considered in attracting talent where it is needed.

It is not realistic to assume employees would choose to live away from home unless they are remunerated or otherwise adequately compensated to cover any increase in the cost of living. Providing tax concessions which are limited to additional costs will mean that these costs may be incurred by the employer with no additional tax cost.

From our experience, tax concessions such as living-away-from-home benefits have been a crucial factor in attracting talent, in effect getting the employee "over the line". Without an incentive, or at the very least a method to reduce the financial burden of employees who are living away from home, there is a significant risk that a substantial number of skilled migrants will choose to work in other countries, in particular countries with similar tax concessions designed to attract talent, such as nearby Asia-Pacific English-speaking countries either with a lower cost of living or lower effective tax rate (e.g. Hong Kong, Singapore or New Zealand).

The removal of tax concessions would mean that businesses would need to effectively "gross-up" an employee's remuneration to ensure the same net tax position, resulting in a higher cost to business. Businesses are already compensating talent to the extent that their resources allow and will simply not be able to meet these demands, failing to attract new talent or retain existing skilled migrants.

## 5 Fiscal and economic considerations

Based upon our analysis, in particular in section 4.2 of this submission regarding the need for attracting and retaining skilled migrants and the impact the proposed reforms may have, we note the following factors which we envisage will ultimately affect revenue and the Government's estimated savings.

In the Treasurer's media release, it is estimated that the reforms would result in about a \$683.3 million saving over the forward estimates. Neither the media release, nor the consultation paper makes reference to the basis by which estimated savings were calculated.

Many employers of existing temporary residents provided with living-away-from-home benefits will not be able to afford the additional FBT cost or, in the case where the employee is receiving a cash allowance, the additional grossed-up payment which will be required to maintain the employee's net income position (i.e. after-tax income).

The vast majority of skilled migrants are attracted to a position based upon a guaranteed net income position. If businesses are unable to afford the increased costs to maintain this net income, given the considerations previously discussed regarding attracting skilled migrants, businesses may fail to retain existing employees who will in turn depart Australia.

This would result in no living-away-from-home benefits being provided to these individuals and subsequently there would be no increase in Government revenue. Furthermore, there would be less revenue from indirect taxes such as GST (as a result of reduced consumer spending), as well as less revenue for State Governments from State taxes such as payroll tax (from a reduction in wages paid).

Employers who are able to afford the increased costs will be entitled to an equivalent tax deduction which will reduce any tax savings from FBT and PAYG withholding revenues.

Community sector employers, such as the health sector, who has little choice but to source workers from overseas, will be required to incur additional tax costs resulting from the proposed reforms. Additional tax costs will be a drain on the health sector's resources and will take away from funds required to provide services. Alternatively, further funds will be required, such as from Government, to subsidise these costs.

### 5.1 Impacts on economic growth

Businesses invest in infrastructure in return for potential profit. The prices which businesses charge are determined in accordance with their necessary return. Population increases (e.g. due to increases in migrant numbers) create more "users" providing greater potential for revenue and a greater opportunity for investment in infrastructure.

In a study commissioned by the Queensland Resources Council, Deloitte Access Economics found:

*“if the labour supply is not able to adjust sufficiently to supply enough appropriately qualified staff that are willing to work in the resources sector, the number of projects that are able to proceed as per their preferred timetable will fall. At the same time companies operating outside the resources sector*

*requiring staff with similar skills will also be likely to have to cut back on expansion plans.”<sup>17</sup>*

While this finding refers to Queensland, it is also applicable within the resources sector in WA, as well as other businesses Australia wide. Skills shortages will mean businesses will fail to take advantage of existing opportunities, which is of particular importance in the resource sector.

With particular reference to the resources boom, skills shortages put pressure on supply, meaning that businesses are not able to compete with demand, putting inflationary pressure on prices. Furthermore, there will be pricing pressure resulting from: 1) an increase in the cost of labour due to additional tax costs to bring in these workers; and, 2) an increase in the cost of labour due to competition with industries which rely on similar skilled labour.

Inflation would likely result in a hike in interest rates, which will be felt by all debtors, such as mortgage holders. In terms of Australia’s ability to take advantage of the resources boom, the benefits of high commodity prices, rather than allowing potential to grow and develop infrastructure is lost by higher interest rates and borrowing costs.

In addition to inflationary pressures, economic growth constraints hinder the ability of business to generate higher taxable income, resulting in less-than-optimal future corporate tax revenues.

## 5.2 Skilled migrant contribution to revenue

As noted in Deloitte’s *Building the Lucky Country: Where is your next worker?* paper, the 168,000 skilled immigrants who arrived in Australia in 2009-10 boosted the Federal Budget’s bottom line by around \$880 million in the first year after arrival<sup>18</sup>. This is brought about by skilled migrants typically paying higher rates of income tax while receiving fewer Government benefits than an average Australian resident.

An example of additional Government revenue is the tax generated by temporary migrants who wish to withdraw their superannuation as a DASP. These taxpayers face an additional tax burden through a withholding tax rate of 35%, which is applied to the superannuation benefits in addition to a 15% contributions tax (i.e. an effective tax rate of 44.75%).

The age of migrants means that Australia is typically is not required to subsidise their education and healthcare prior to them contributing to the Australian economy and workforce as other countries have incurred these costs. Accordingly, Australia is spending relatively less.

As above, to the extent that many businesses cannot afford to attract and retain, new and existing temporary resident workers, we would expect there to be a proportional impact on the Federal Budget’s bottom line.

## 5.3 Australian living standards

We referred above to investment in business infrastructure, but this notion is equally applicable to other privately funded community infrastructure. As the population increases due to an increased birth rate or migrant numbers etc., there are more “users”, providing a greater potential for revenue and a greater opportunity for investment in infrastructure.

<sup>17</sup> Deloitte Access Economics, *Queensland Resources Council Queensland Resource Sector State Growth Outlook Study*, November 2011, p.36

<sup>18</sup> Australian Government, Department of Immigration and Citizenship, *Migrant Economic Outcomes and Contributions*, April 2011, p. 11, [http://www.immi.gov.au/media/publications/research/\\_pdf/outcomes-contributions-apr11.pdf](http://www.immi.gov.au/media/publications/research/_pdf/outcomes-contributions-apr11.pdf)

The same argument is applicable for Government-funded public infrastructure. As mentioned above, migrants pay above average taxes and, accordingly, provide sufficient contribution towards Government funding.

In the medium-to-long-term then, maintaining and/or increasing temporary migrant numbers can expect to encourage a greater investment in infrastructure, which may be utilised by and raise the living standards of all residents.



## 6 Inconsistency with other Government initiatives

### 6.1 National Resource Sector Employment Taskforce (2009)

Following the NRSET Report, the National Resource Sector Workforce Strategy (NRSWS) in March 2011 highlighted seven key area of workforce development, to be overseen by the NRSWS Steering Committee. This report specifically includes meeting temporary skills shortages with temporary migration.

As previously discussed in section 4.3 of our submission above, living-away-from-home tax concessions allow Australia, which is among the highest cost of living countries in the world, to retain and attract skilled migrants in sectors which are experiencing skills shortages.

The NRSET Report found, unsurprisingly, that “labour demand is driven by demand for resources”<sup>19</sup>. The relevance of the resource sector is due to its size and importance to the Australian economy, contributing 48 per cent of Australia’s exports<sup>20</sup> and 8 per cent of our Gross Domestic Product (GDP)<sup>21</sup>. Accordingly, any constraints which may result in an inability to meet labour demand have the potential to limit growth in an industry which is of significant importance to Australia’s economy.

### 6.2 Australia as a financial services centre

The Australian Financial Centre Forum (AFCF) was established on 26 September 2008 to further the Australian Government’s initiative to position Australia as the leading financial services centre in the region. The focus of the AFCF was to ensure that Australia’s policy setting allowed the financial sector to take advantage of the business opportunities available.

On 17 November 2009, the AFCF released its final report, noting that:

*“It is thus crucial that domestic policies do not inhibit companies that have the capacity, skills and comparative advantage from expanding into offshore markets and transacting with offshore counterparties; and also that domestic policies do not inhibit offshore international financial services companies from competing domestically or from using that financial centre as a regional base.”*<sup>22</sup>

The report also commented on a growing body of surveys and academic studies undertaken to determine the key factors which determine where financial services companies establish themselves. In this regard the AFCF commented that:

*“...one feature which most frequently comes at or near the top of the list in terms of importance is human capital. Indeed, in a world of increasingly mobile financial capital, and where such factors as the rule of law, adequate*

<sup>19</sup> Resourcing the Future, p. 18

<sup>20</sup> Australian Bureau of Statistics, 8418.0 – Mining Statistics Newsletter, 2009 to 2010, 10 June 2010

<sup>21</sup> Australian Bureau of Statistics, 5368.0.55.006 – Characteristics of Australian Exporters, 2009-10, 30 March 2011

<sup>22</sup> Australian Financial Centre Forum, Australia as a Financial Centre, November 2009, p.8



*technology and reasonable market liquidity are becoming more common, the importance of human capital is, if anything, increasing.*<sup>23</sup>

The report found that skilled migration played an important role in complementing the Australian workforce by relieving skills “gaps”, not only allowing business to expand but also to transfer and enhance the skills of existing local employees.

As previously discussed, the proposed reforms mean that Australia is less attractive to skilled migrants, many of whom will inevitably take up alternative employment opportunities.

The impact of a reduction in Australia’s competitiveness to attract talent from abroad would be twofold. Not only would companies wishing to establish a financial base in Australia be faced with greater and more costly restraints to attract skilled migrants, but the relative attractiveness of various other Asia-Pacific countries would mean that these countries would be able to attract greater skilled human capital resources.

In an environment where sufficient human capital is crucial, Treasury should have regard to the impact of these proposed reforms with respect to making Australia less attractive as a financial base.

### 6.3 Positive credit reporting reforms

The Australian Government is on the cusp of introducing positive (comprehensive) credit reporting reforms. Australia is one of the few countries to still be operating in a negative credit reporting regime. The consequence is that for affected companies to adopt best practice under a positive credit reporting regime, it is essential these companies attract personnel with relevant positive credit reporting experience. Due to the existence of positive credit reporting around the world, it is advantageous for personnel to be sourced from overseas not only to implement best practice but also to up-skill local employees, which would reduce reliance on overseas skilled migrants in the future.

In an environment where the Federal Government is encouraging competition within the credit market, in particular with respect to the “Big Four” banks, any constraints which hinder the competitiveness of smaller credit providers is inconsistent with current policy.

### 6.4 Establishing business in Australia

The establishment of new business operations in Australia helps to strengthen the economy, promote competition, create employment opportunities and contribute to the Federal Budget through taxation.

Businesses wanting to establish operations in Australia will often rely on management in other foreign operations with specific knowledge of the business and relevant markets to oversee the setup and initial growth phase of the operations. These businesses provide employment opportunities for Australians and the skilled migrants brought in assist to up-skill local employees.

The removal of tax concessions for temporary residents would increase the overall cost involved with establishing new business operations. As these businesses are not already in existence, the decision to establish the operations in Australia is discretionary and therefore is a factor which would discourage potential new investment in Australia.

<sup>23</sup> Australian Financial Centre Forum, *Australia as a Financial Centre*, November 2009, p.9

# 7 Inequity and discrimination concerns

## 7.1 Inequity between permanent and temporary residents

In addition to eliminating the exploitation of living-away-from-home tax concessions and the resulting estimated savings, the proposed reforms have been introduced on the basis that they will establish equity between temporary and permanent residents working in Australia. The foreword to the consultation paper by the Assistant Treasurer and Minister for Financial Services and Superannuation states that:

*“The changes will ensure a level playing field exists between hiring an Australian worker or a temporary resident worker living at home in Australia, in the same place, doing the same job.”<sup>24</sup>*

Under the proposed reforms this is not exactly the case. For example, an Australian permanent resident is not required to continue to maintain a home in Australia in order to be eligible for the proposed tax concessions.

The distinction between eligibility for permanent and temporary residents is such that the original intention of “additional expenditure” differs between a permanent and temporary resident.

A temporary resident must continue to incur the costs for at least one residence in Australia out of income which has already been taxed, whereas a permanent resident, where they either do not maintain a residence or otherwise receive rental income to recover the cost of maintaining their residence, will not incur any cost for accommodation out of taxed income.

Furthermore, even though it is not the basis of the statement referred to above, we examine the inequity created by the proposed reforms between permanent and temporary residents living away from an overseas home.

An Australian citizen (or even a spouse of an Australian citizen) who has been working overseas and intends to return overseas on completion of an Australian assignment, under the proposed reforms would be afforded with tax concessions on the basis that they would be living away from their usual place of residence and would not be regarded as temporary residents.

The same cannot be said for a non-Australian citizen (or an individual who is not the spouse of an Australian citizen) who experiences the exact same circumstances. They would not receive any tax concessions on the basis that they would most likely be regarded as a temporary resident and would therefore not be considered living away from a home they maintain in Australia.

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<sup>24</sup> Australian Government, the Treasury, *Fringe Benefits Tax (FBT) Reform Living-away-from-home benefits*, November 2011, p. vii

## 7.2 Potential discrimination concerns

The vast majority of Australia's international tax conventions contain articles regarding non-discrimination which are for the most part 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”*<sup>25</sup>

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

*“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.”*<sup>26</sup>

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 to Treasury, 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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<sup>25</sup> OECD, *Model Tax Convention on Income and on Capital (Condensed Version)*, 22 July 2010, Article 24 Non Discrimination, para. 1, p. 35.

<sup>26</sup> 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.

# 8 Increased employer compliance and on-costs

## 8.1 PAYG withholding

It is the intention of the proposed reforms that a LAFHA will no longer be assessable for FBT purposes and will instead revert to being assessed under the income tax regime.

Section 12-35 of Schedule 1 of the *Tax Administration Act 1985* (TAA1953) provides that:

*“An entity must withhold an amount from salary, wages, commissions, bonuses or allowances it pays to an individual as an employee.”*

We understand that under the proposed reforms, the ATO will make a PAYG withholding variation to exempt employers from PAYG withholding obligations where it is expected that the allowance is to be expended and allowable as a deduction.

As part of this submission, we seek further clarification as to the level of substantiation required by employers in order to apply the ATO’s withholding variation.

Furthermore, if employers are required to obtain substantiation from employees, we seek clarification as to whether Treasury has considered if the allowance would more appropriately be in the nature of a reimbursement, as per the criteria in *Taxation Ruling TR 92/15 Income tax and fringe benefits tax: the difference between an allowance and a reimbursement* (TR 92/15). We note this would impact PAYG withholding for non-deductible LAFHA payments, as well as other employment tax obligations, such as superannuation guarantee (SG). We discuss the impact on these obligations further below.

We would also like to bring to the attention of Treasury the administrative burden and costs likely to be incurred by employers to adjust their existing payroll systems to reflect the impact of the proposed reforms.

## 8.2 Payroll tax, superannuation guarantee and WorkCover

To the extent that living-away-from-home benefits are taxable for FBT purposes, they will be considered taxable wages or remuneration for both payroll tax and WorkCover purposes in each relevant State or Territory. As a fringe benefit, no SG obligation will arise irrespective of whether the benefit is taxable or not.

Alternatively, where employees are provided with a LAFHA, the allowance will be captured for State payroll tax and WorkCover purposes, as well as result in an SG obligation, irrespective of whether the allowance is deductible.

Accordingly, in addition to the increased cost to businesses arising from other employment tax obligations, we also wish to bring to the attention of Treasury, the inconsistent application of other employment tax obligations resulting from the proposed reforms, which we summarise in the following table.

	Fringe benefit (Non-taxable)	Fringe benefit (Taxable)	LAFHA (Deductible)	LAFHA (Non- deductible)
Payroll Tax	No	Yes	Yes	Yes
Superannuation Guarantee	No	No	Yes	Yes
WorkCover	No	Yes	Yes	Yes

# 9 Community sector FBT concessions cap

## 9.1 Summary of FBT concessions caps

FBT legislation provides concessions for certain community sector and non-profit organisations. Concessions available are in the form of either an exemption or a rebate. Entitlement to either concession is limited to a concessional cap, applied on a per employee basis. The concessional cap is determined with reference to the aggregate grossed-up taxable value of fringe benefits provided to each employee.

We provide the following list of concessional organisations, together with the type of concession and applicable concessional cap.

Organisation type	Exemption/Rebate	Concessional cap
Public benevolent institutions (excl. hospitals)	Exemption	\$30,000
Health promotion charities	Exemption	\$30,000
Public and non-profit hospitals	Exemption	\$17,000
Public ambulance services	Exemption	\$17,000
Certain religious, educational, scientific or public educational institutions	Rebate	\$30,000
Trade unions and employer associations	Rebate	\$30,000
Certain non-profit organisations	Rebate	\$30,000

## 9.2 Interaction between proposed reforms and concessional caps

The consultation paper advises that employees of community sector organisations who are not currently using the full extent of their FBT exemption cap will not be affected by the reforms.

While the intention of this statement has some merit and may be correct in theory, there are practical implications which require further consideration.

### 9.2.1 LAFHA will no longer be a “fringe benefit”

The proposed reforms provide that a LAFHA will no longer be regarded as a fringe benefit. Accordingly, a LAFHA will not be subject to FBT. Therefore, both employees and employers will lose the benefit of FBT concessions altogether.

Instead, any LAFHA paid will be taxed in the hands of the employee at their marginal rate.

To avoid this less-effective tax treatment, we would expect to see employers provide living-away-from-home benefits in the nature of fringe benefits (i.e. expense payment, property or residual benefits) rather than in the form of a cash allowance.

In practice, while it is relatively straightforward to provide accommodation by way of a fringe benefit (e.g. to reimburse actual expenditure), the same cannot be said for food costs,

for which an allowance provides significant administrative advantages. Accordingly, additional food costs are likely to continue to be compensated for as an allowance and to be ineligible for concessional treatment as part of the concessional cap.

Consideration should also be given to the additional administrative burden on concessional organisations and their employees in altering the way these organisations provide living-away-from-home benefits.

### 9.2.2 Living-away-from-home benefits will likely exceed concessional caps

The statement made in the consultation paper, which finds that employees who do not currently use the full extent of their concessional cap will not be affected, is misleading.

In reality, the value of living-away-from-home benefits provided to employees, given the level of rental expenses in Australia, would take up the majority of any concessional cap (if not all of it). For example, an employee living in Sydney paying rent of \$250 per week (which is very conservative), would pay \$13,000 over a 12-month period. In this instance, due to accommodation alone, the employee has already used \$24,299.60 of a \$30,000 cap and is well in excess of a \$17,000 cap.

Accordingly, it is likely that the FBT burden on community sector employees will increase where living-away-from-home benefits (other than as a taxable allowance) are provided to non-exempt temporary residents.

# 10 Statutory and reasonable food amounts

## 10.1 Statutory food amount

The Explanatory Memorandum to the *Fringe Benefits Tax Assessment Bill 1986*, which introduced LAFHAs to FBT legislation, described the statutory food amount as the amount an employee could reasonably be expected to have incurred on food at his or her home.

The consultation paper provides that the statutory food amount is intended to reflect the ordinary costs incurred by an Australian in 2011.

Notwithstanding that under the proposed reforms, a permanent resident can be living away from a home outside of Australia, an essential and perhaps primary intention of the concession is to promote domestic mobility. Therefore, we agree that the statutory food amount should have regard to costs ordinarily incurred in Australia.

We recommend that Treasury uses statistical data provided by the ABS to determine the statutory food amount. ABS data provides that the average weekly expenditure on food and non-alcoholic beverages in Australian capital cities during the quarter ended June 2011 was \$230.87<sup>27</sup>. In our opinion, this is an appropriate data source, particularly as capital cities represent a significant portion of the population and would represent, on average, a lower cost of goods and services than in less populated and remote areas. Accordingly, on the assumption that employees have come from a lower cost area, this would mean that the statutory food amount would not disadvantage employees living away from home.

However, for the purposes of determining the statutory food amount it would be inappropriate to apply an average on the basis that employees from households who incur less than the average \$230.87 per week would be disadvantaged. In this regard, we recommend that Treasury determines the statutory food amount with respect to the lower quartile.

In any event, the current statutory food amount of \$42 does not appear to reflect what an Australian typically spends on food per week and we welcome the proposed reforms in relation to this matter.

## 10.2 Reasonable food amount

We agree with the proposal that the Commissioner continues to determine reasonable food amounts to ease the administrative burden on employers and/or employees.

We agree with the current method by which the Commissioner determines reasonable food amounts and note employees who incur food costs in excess of the amount determined by the Commissioner may continue to be entitled to a tax concession provided the costs can be substantiated.

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<sup>27</sup> Australian Bureau of Statistics, *6470.0 Information Paper: Introduction of the 16<sup>th</sup> Series Australian Consumer Price Index, 2011*, 22 September 2011



## 10.3 Indexation

We agree with the notion presented in the consultation paper that the statutory food amount should be indexed annually going forward to ensure it remains up to date.

Furthermore, we agree that the reasonable food amounts as determined by the Commissioner should continue to be indexed or otherwise determined as to remain up to date.

## 10.4 Impact of reforms

As mentioned above, we welcome proposed changes which aim to adjust the statutory food amount to reflect the purpose for which it was intended. However, the notion that permanent residents receiving living-away-from-home benefits (which can be substantiated) will not be affected by the reforms appears to be misleading. This is on the basis that an anticipated increase in the statutory food amount to reflect current weekly costs will reduce the exempt food component (or tax deduction) available.

# 11 Transitional arrangements

The proposed reforms were announced on 29 November 2011 with an intended effective date from 1 July 2012.

## 11.1 Transitional issues

One of the main concerns that employers have raised is the lack of time between the announcement of the reforms and the date on which they are to have effect, particularly in relation to pre-existing commitments, such as existing employment contracts and rental agreements.

Existing and upcoming projects would have been costed based upon the current treatment of living-away-from-home benefits and, therefore, a change in these costs will affect the profitability or even viability of these projects.

Given the likely additional cost to employers (for employees affected by the reforms), many employers may seek to reduce their potential exposure by changing the way they provide living-away-from-home benefits. For example, employers may encourage employees to enter into more affordable housing or simply cease to provide assistance.

In practice, however, the ability of employers to implement these changes or modify existing arrangements depends upon many other factors, such as obligations under employment contracts and fixed-term rental agreements under which either the employer or employee is bound.

## 11.2 Proposed transitional arrangement

We propose that transitional arrangements should be implemented so that any arrangements which are in existence prior to 1 July 2012 (or the date of enactment, whichever is earlier), are exempt from the proposed reforms for the year ending 30 June 2013.

These transitional arrangements would provide employers with the flexibility they need to assess employee benefits without exposing either themselves, or the employee, to tax obligations which were unforeseen at the time the arrangement was entered into. They would also minimise any potential impact on projects which have already been costed.

We argue it would not be appropriate to only apply transitional treatment to arrangements existing as at 29 November 2011. This is on the basis that even at the date of this submission, the proposed reforms had not been introduced into Parliament and Treasury is yet to receive guidance on appropriate transitional arrangements as part of this (and other) submissions. Accordingly, between 29 November 2011 and 1 July 2012 (or date of enactment), decisions cannot be made by either employers or their employees with any certainty.

Furthermore, to facilitate and encourage both employers and employees to vary existing arrangements, we propose that a FBT exemption is available for employers who reimburse or otherwise compensate employees for lease break costs incurred.

## 11.3 Community sector

We understand that, in particular, Treasury is concerned about the impact the proposed reforms may have on the community sector. We believe our proposed transitional arrangements would assist in reducing any unintended additional costs to the community sector. We further propose that for community sector employers, these transitional arrangements should apply beyond the year ending 30 June 2013 for arrangements in existence prior to 1 July 2012 or the date of enactment (whichever is earlier).

# 12 Further clarity sought

In addition to those items already discussed above, there are a number of issues which require further clarity.

## 12.1 Maintaining a home

It is our understanding that the proposed reforms are intended to allow a tax concession for temporary residents who are living away from their overseas home, being their usual place of residence, provided they maintain a home for their own use in Australia.

In this regard, we seek confirmation that a temporary resident's Australian home which they maintain is not required to be their usual place of residence in order to be entitled to tax concessions.

We note this understanding is also relevant for our discussion regarding fly-in fly-out arrangements at section 12.2 below.

## 12.2 Fly-in Fly-out (FIFO) arrangements

The consultation paper comments that employees operating under FIFO arrangements within Australia will not be affected by the proposed reforms.

### 12.2.1 FIFO travel

Subsection 47(7) of the FBTAA aims to exempt from FBT any travel between the employee's usual place of employment and usual place of residence where a FIFO arrangement is considered reasonable. While its application will not change due to the proposed reforms, we wish to bring to Treasury's attention, the application of section 47(7) for temporary residents in the context of the proposed reforms.

A temporary resident living in Australia, away from their usual place of residence (overseas home), who is employed under a FIFO arrangement, would not receive any concessions on the basis that they are not living away from a home they maintain in Australia, nor are they travelling between their usual place of employment and usual place of residence.

For example, under the proposed reforms, a citizen from the United Kingdom (UK) living in Perth as a temporary resident, who is living away from their usual place of residence in the UK, would not be eligible to receive living-away-from-home benefit concessions with respect to their Perth home. The temporary resident is required to work in a remote area of Western Australia (WA) under a FIFO arrangement. However, as the temporary resident's usual place of residence is not their Perth home, the travel between Perth and the temporary resident's usual place of employment will not satisfy the exemption under subsection 47(7).

### 12.2.2 FIFO accommodation

We seek confirmation that accommodation provided to a temporary resident under a FIFO arrangement (which is near their usual place of employment) will continue to be eligible for a tax concession under the proposed reforms, provided that employee continues to maintain a home in Australia.

This is notwithstanding that travel to and from that accommodation will not be exempt pursuant to subsection 47(7) of the FBTAA as mentioned above.

For example, under the proposed reforms, a citizen from the United Kingdom (UK) living in Perth as a temporary resident, who is living away from their usual place of residence in the UK, would not be eligible to receive living-away-from-home benefit concessions with respect to their Perth home. The temporary resident is required to work under a FIFO arrangement where they are provided with accommodation near their usual place of employment. As the temporary resident is living away from their home in Perth which they maintain, we would expect that the accommodation near the employee's usual place of employment would be eligible for tax concessions under the proposed reforms.

## 12.3 Remote area housing

The remote area housing concessions in section 58ZC of the FBTA aims to exempt any housing benefit in a remote area for which the circumstances are reasonable. However, in accordance with section 25 of the FBTA and the definition of "housing right" in section 136(1), the housing must be the employee's usual place of residence.

Accordingly, for temporary residents living away from their usual place of residence (being their overseas home), the exemption pursuant to section 58ZC of the FBTA will not apply.

Currently, this is not a concern as temporary residents who are living away from their usual place of residence are entitled to living-away-from-home tax concessions. However, under the proposed reforms, temporary residents will not be eligible for either concession unless they live away from a home they maintain in Australia.

We seek confirmation as to our interpretation of the exemption pursuant to section 58ZC of the FBTA and propose a review of its application to housing, which is not an employee's usual place of residence, so that it may be applied to attract temporary residents to remote areas where workers are required.

## 12.4 Application to foreign-residents

We note that neither the proposed reforms, nor the consultation paper, provide commentary regarding foreign-residents who may be living away from home in order to perform short-term services in Australia.

We recognise that treaty income tax exemptions apply to certain employees. However, for those who are not exempt, we seek clarification as to the application of the proposed changes.

We would expect that based on the proposed reforms as discussed in the consultation paper, foreign-resident workers who are not treaty exempt would not be subject to the conditions applicable to temporary residents and would continue to be eligible to receive living-away-from-home benefit concessions.

While we believe that the concession should apply to foreign-residents in this regard, we seek confirmation as to how the concessions are intended to apply to non-resident employees.

## 12.5 Other overseas employee concessions

The consultation paper comments that employees receiving FBT education expenses concessions for their children when living away from home for work will not be affected by the proposed reforms.

In this regard we seek confirmation regarding the continued application of these and other concessions currently available to overseas employees. As discussed in sections 12.1 and

12.2 above, the requirement for temporary residents to maintain a home in Australia does not appear to require the Australian home to be their usual place of residence. We summarise the application of the following concessions on this basis and seek confirmation accordingly regarding:

- *Overseas employment holiday transport* (section 61A of the FBTAA) and *Education of children of overseas employees* (section 65A of the FBTAA)  
Under sections 61A and 65A, there will be no requirement for a temporary resident employee to maintain a home in Australia as required under the proposed reforms
- *Connection of utilities* (section 58D of the FBTAA)  
The concession under section 58D will allow an exemption for the connection or re-connection of certain utilities required because the employee is required to live away from their usual place of residence.

For temporary residents who are living away from their usual place of residence and who also maintain a home in Australia from which they are living away from, the concession will apply only to the residence for which they are required to maintain. A concession will not apply to the home for which a tax concession is available for living-away-from-home benefits

- *Leasing of household goods* (section 58E of the FBTAA)  
For temporary residents who are living away from their usual place of residence and who also maintain a home in Australia from which they are living away from, the concession will apply only to the residence for which an exemption is allowed. The concession will not apply to the home they are required to maintain.
- *Relocation transport* (sections 58F and 61B of the FBTAA)  
The concession under section 58F allows an exemption for relocation transport required because the employee is required to live away from their usual place of residence. We note, however, that where a temporary resident is living away from a home they maintain, it will not be their usual place of residence and therefore the exemption will not apply to transport between these homes, which is inconsistent with the application of living-away-from-home concessions for temporary residents.

We note that the proposed reforms appear to result in the inconsistent application of these concessions.

## 12.6 Living-away-from-home vs. travel benefits

Given Treasury's proposed living-away-from-home reforms and the interaction between living-away-from-home and travel benefits, we suggest Treasury review and clarify the distinction between where an employee is travelling on business and when they are living away from home.

This distinction remains a significant area of confusion for employers, as well as a significant area of risk. In particular, the difference between "reasonable" allowances for travel and living-away-from-home purposes has the potential to result in a significant tax liability.

We suggest Treasury have specific regard to the 21-day rule, which the ATO has determined should apply in circumstances where a distinction is not clear.

# 13 Our proposed amendments

In light of our analysis and observations above, we propose our amendments which we believe would adequately address the Government's concerns.

## 13.1 Discussion of the Government's proposed reforms

Treasury's consultation paper provides a history of living-away-from-home benefits, citing the Explanatory Memorandum from the introduction of living-away-from-home tax concessions in 1945. Clause 6 of the Explanatory Memorandum of the *Income Tax Assessment Bill 1945* provided:

*“Various wage-fixing authorities have granted away-from-home allowances to employees whose places of employment are located away from their usual place of abode. The allowance is paid to compensate the employee for additional expenditure he is obligated to incur in providing board and accommodation for himself at his place of employment while, at the same time, maintaining his home elsewhere.”*

The consultation paper and the Government's proposed treatment of living-away-from-home benefits provided to temporary residents suggests that living-away-from-home concessions were specifically intended to assist with Australian domestic mobility. It is clear that living-away-from-home concessions were initially introduced in recognition of a legitimate scenario which would disadvantage workers required to live away from their usual place of residence as part of their employment. While the Explanatory Memorandum has reference to an allowance provided in a specific scenario, we argue that it was not intended to be limited, but rather applied as a principle.

Given the global nature of the current labour market, which is in complete contrast to the labour market in 1945, we do not believe it is in the interests of Australian businesses to concentrate the application of living-away-from-home tax concessions to local mobility. Furthermore, similar living-away-from-home concessions apply in other countries, including the United States of America, the United Kingdom, Canada, Japan and the Netherlands. Concessions available in each of these countries do not require the employee to be living away from a home in the local country.

In 1995, the then Australian Labor Party Government attempted to reform living-away-from-home treatment by addressing certain uncertainties that remain today, including time limits a person could be regarded living away from home and to redefine the “exempt accommodation component”, including a limit to accommodation. The consultation paper admits that the then Government decided not to proceed with these reforms due to concerns raised by industry groups.

We argue that the proposed abolition of living-away-from-home benefits to temporary residents (except to the extent that temporary residents are living-away-from-home from an Australian residence) would cause similar, if not the same, industry concerns to those raised by the failed introduction of proposed changes in 1995.

The consultation paper proposes that employees from overseas have a greater advantage as they are all living away from their homes. We believe that this statement is misguided as the purpose of living-away-from-home tax concessions is not to disadvantage employees for

additional costs incurred because they are required to live away from their usual place of residence for the purpose of work.

Additional costs which are by no means minor would not be incurred by the employer unless the business had the need to do so, whether the employee is sourced locally or from overseas. The tax concession itself is neutral and does not discriminate as to whether a business chooses to source workers from overseas rather than Australia. We do not believe reforms should be implemented which disadvantage Australian businesses that genuinely need to source workers from overseas, particularly in light of Australia's skills shortage.

We accept that under existing law, that there are scenarios whereby employees may misuse tax concessions to bring about a financial gain and welcome any reform which aims to arrest this misuse, as well as to provide clarity to the application of the law. However, in this regard, we suggest a tightening of laws consistently applied to permanent residents and temporary residents alike.

## 13.2 Explanation of our proposed amendments

Given the uncertainty surrounding the current treatment of living-away-from-home benefits, we propose that amendments are made to the current treatment of living-away-from-home benefits which we believe would assist taxpayers in determining the correct tax treatment. This would also reduce the unintended misuse of these concessions.

### 13.2.1 Maximum time limit

Despite its failed introduction in 1995, the introduction of a time limit for which an employee is eligible to receive living-away-from-home concessions would continue to encourage short-term skilled migration where it is needed, while removing any longer-term cost to revenue.

The introduction of time limits would further align LAFH benefit tax concessions in Australia with those available in other countries, as well as to provide much greater certainty for employers, particularly with respect to the extension of assignments.

### 13.2.2 Substantiation of costs

The consultation paper made note of Treasury's concern regarding the erosion of PAYG withholding revenue resulting from the re-characterisation of salary and wages (i.e. salary sacrifice arrangements).

We propose the introduction of substantiation requirements similar to those in Treasury's proposed reforms.

Substantiation requirements would ensure that there is no incentive for employees to salary sacrifice living costs in excess of costs actually incurred.

### 13.2.3 Reasonable test for accommodation

Tax concessions should continue to be available for all employees who are required to live away from their usual place of residence, irrespective of whether they are permanent or temporary residents or where their usual place of residence is located.

We propose that a "reasonable test" similar to that currently applicable to the accommodation component of a LAFHA should also be introduced for accommodation, where it is provided as a fringe benefit.

A "reasonable test" would allow a tax concession only where the accommodation provided is reasonable given the employee's circumstances and would deny employees from being provided with tax-free accommodation in excess of that which they could ordinarily afford.

### 13.2.4 Review of the statutory food component

We do not propose any alternative amendments to those in the Government's proposed reforms. This would enable the statutory food amount to be designed to reflect food costs already incurred at home.

Furthermore, we agree that to ease administrative burden, the ATO should set reasonable food amounts for which no substantiation would be required.

Please refer to section 10 of this submission for our discussion on statutory food and reasonable amounts.



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