1987

THE PARLIAMENT OF THE COMMONWEALTH

OF AUSTRALIA

HOUSE OF REPRESENTATIVES

TAXATION LAWS AMENDMENT (FRINGE BENEFITS AND SUBSTANTIATION) BILL 1987

EXPLANATORY MEMORANDUM
PART A

(Circulated by authority of the Treasurer, the Hon. P.J. Keating, M.P.)

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FORWARD

Part A of this memorandum contains explanations that provide a broad guide to the Bill that has been introduced to give effect to announced changes of a concessional nature to the fringe benefits tax and income tax laws that were announced on 26 August 1986 and 29 October 1986.

Part B of the memorandum, to be issued shortly, will contain a clause by clause explanation of the Bill.

GENERAL OUTLINE

This Bill will amend :-

. the Fringe Benefits Tax Assessment Act 1986 -

.. to modify the rules that require - where the cost basis of valuing car benefits is chosen - substantiation of business use by log book records, and petrol and oil expenses by documentary evidence (proposal announced on 29 October 1986);

.. to exempt from tax the following benefits:

- the private use of unregistered motor vehicles used principally for business purposes (29 October 1986 announcement);

- the use of the employer's business equipment on a non-working day or away from the employer's business premises (29 October 1986 announcement);

- benefits provided to employees of a government body who are employed in a public hospital (29 October 1986 announcement);

- benefits in respect of travel costs incurred in attending job interviews (proposal announced on 26 August 1986);

- benefits in respect of specified relocation costs (26 August 1986 and 29 October 1986 announcements);

- motor vehicle parking benefits (29 October 1986 announcement);

- newspapers and periodicals used for business purposes (29 October 1986 announcement);

- compensation for work-related injuries (26 August 1986 announcement);

- medical services provided in work site medical facilities that are operated principally for the treatment of work-related injuries (26 August 1986 announcement);

- benefits in respect of travel costs incurred in travelling from a prescribed developing country to obtain medical treatment (26 August 1986 announcement);

- occupational health and counselling benefits (29 October 1986 announcement);

- benefits provided for immediate relief in times of emergency (29 October 1986 announcement);

- benefits of small value which are infrequently provided and/or difficult to record and value (29 October 1986 announcement);

- long service awards granted in recognition of 15 or more years service provided the value of the award does not exceed a specified ceiling which varies according to length of service (29 October 1986 announcement);

- safety awards provided the value of the award does not exceed $200 (29 October 1986 announcement);

- accommodation and food provided to trainees engaged under the Australian Traineeship System (29 October 1986 announcement);

- accommodation and food provided for live-in domestic employees in religious houses (29 October 1986 announcement);

- accommodation and food provided for live-in help employed to care for elderly or disadvantaged persons (29 October 1986 announcement);

- food provided in the home to non-live-in domestic employees (29 October 1986 announcement);

.. to increase the annual exemption per employee for in-house fringe benefits to $500 (29 October 1986 announcement);

.. to extend the concessional valuation rules applying to in-house fringe benefits to purchases of an employer's products through independently owned retail outlets (29 October 1986 announcement);

.. to increase the existing 40% discount on remote area housing (including home ownership and residential fuel assistance) to 50% (29 October 1986 announcement);

.. to replace the statutory formula for valuing remote area housing by a statutory value of $60 per week per unit of accommodation or $15 per week for single person's quarters, those values to be increased annually in line with movements in the rent component of the CPI (29 October 1986 announcement);

.. to permit employers to use either the statutory value or market value for each unit of remote area accommodation and to alter the method of valuation each year (29 October 1986 announcement);

.. to provide that a 50% discount is to apply to remote area housing benefits provided as rent reimbursements or actual payments of rent incurred by the employee as well as to any assistance provided for the cost of residential fuel for that accommodation (29 October 1986 announcement);

.. to liberalise the rules under which a 50% discount is applied to remote area holiday travel (29 October 1986 announcement);

.. to apply, in respect of employees posted overseas, a 50% discount concession to the cost of holiday travel subject to a maximum discount equal to 50% of the cost of travel for one return holiday per year to the employee's home country (29 October 1986 announcement);

.. to exempt education costs met by employers for children of employees posted overseas for the period of the employee's overseas service (29 October 1986 announcement);

.. to reduce the taxable value of fringe benefits provided to employees located overseas for periods of between 3 and 12 months by the percentage of the employee's salary or wage income that is exempt from income tax (26 August 1986 announcement);

.. to modify the rules for calculating the reduction in taxable value of a benefit that is used for business purposes to:

- ensure that the reduction is equal to the additional deduction that would have been allowable to the employee had he or she paid for the benefit (variation of 29 October 1986 announcement);

- remove, with effect from the 1987-88 year of tax, the existing exclusion for expenses that would otherwise be subject to the income tax negative gearing rules (consequence of the abolition of the income tax negative gearing rules);

.. to provide that employers will no longer be required to obtain declarations from employees in a number of specified circumstances (29 October 1986 announcement);

.. to provide that appropriate petty cash entries rather than receipts will now be acceptable proof of business expenses that are not capable of being readily evidenced by receipts (29 October 1986 announcement);

.. to permit employers to value a housing benefit on the basis of the current market value of the accommodation as an alternative to the indexed market value (29 October 1986 announcement);

.. to exclude from the operating cost of a car the cost of any crash repairs that are met by an insurance company or by the person legally responsible for the damage (29 October 1986 announcement);

.. to treat reimbursements of car expenses on a cents per kilometre basis for holiday travel outside remote areas as fringe benefits rather than assessable income of the employee (proposal announced on 18 November 1986);

.. to make minor drafting corrections.

. the Income Tax Assessment Act 1936-

.. to ensure that an employee is not entitled to an income tax deduction for a contribution to a fringe benefit to the extent that the contribution is, in effect, a payment for the private element of the benefit (29 October 1986 announcement);

.. to exclude from the rules that require substantiation of certain expenses, claims within the limits of allowances paid to employees for fares and other transport costs

where the allowances are payable pursuant to an award and are not higher in amount than was payable pursuant to the award as at 29 October 1986 (29 October 1986 announcement).

FINANCIAL IMPACT

The effect on revenue of these measures, together with the revised log book rules relating to income tax deductions for car expenses that were enacted earlier this year, are estimated to reduce the full year revenue yield of the fringe benefits tax and income tax substantiation rules by $75m.

MAIN FEATURES

The main features of the Bill are as follows -

Fringe Benefits Tax

Substantiation requirements: car rules

(Clauses 5 to 8, 12, 17, 27, 29, 42, 45, 58 to 60)

Under the present law, employers providing car benefits to employees or associates, etc., have a choice of two methods to calculate the taxable value of each car benefit. Under the first, which applies unless an election is made to adopt the second method, the taxable value is a percentage of the original cost of the car, which varies according to the total number of kilometres travelled in the year of tax. Under the second, the taxable value of the car fringe benefit is the total operating cost of the car for the relevant year, reduced in the proportion of private kilometres to total kilometres travelled.

If the operating costs method of valuation is adopted, a log book to establish the number of business and private kilometres travelled is required. Under either method, any contribution by the employee for the use of the car, or in payment of car operating expenses, is deducted in calculating the final taxable value of the car fringe benefit. For operating expenses to be taken into account for this purpose, documentary evidence - usually in the form of a receipt - of the expenditure having been paid by the employee must be provided to the employer.

The requirements for supporting documents are being changed by provisions in the Bill.

Firstly, the documentary evidence rules relating to expenses paid by the employee are being revised so that, where the recipient of a car fringe benefit incurs fuel or oil expenses for the car, it will no longer be necessary to provide the employer with receipts to verify that expenditure provided that a declaration of the expenditure is provided in an approved form. In relation to expense

payment fringe benefits, a similar form of declaration may be used instead of receipts to evidence car fuel and oil expenses incurred by an employee on his or her own car which are paid for or reimbursed by an employer.

Secondly, amended log book requirements will mean that it will no longer be necessary to record details of business trips throughout the whole year of tax. Instead, the percentage of business use of a car can be established by making log book entries in a continuous twelve week log book period. Provided the actual percentage of business use does not vary substantially (i.e., by more than 10 percentage points) from that established by reference to the log book records, that established percentage continues to be the basis for calculating the taxable value of the fringe benefits relating to the particular car or a car that replaces it. The revised log book rules will apply as follows.

The first year

- For the first year in which a car is used to provide fringe benefits, a log book recording business journeys will need to be kept for a minimum continuous period of 12 weeks at any time in the year. The transitional year of tax that ended on 31 March 1987 is a "first year" for that purpose. Details of the odometer reading at the start and end of the 12 week period must also be recorded.

- On the basis of the 12 weeks' log book records, the employer is entitled to nominate a business percentage for the car for the year which is a reasonable estimate having regard to the business percentage established during the log book period and any variations in other parts of the year that would affect the full year's business use, e.g., holidays and seasonal fluctuations. The nominated percentage of business use must not be greater than the percentage established in the log book period.

The preceding rules apply in a case where the car is used throughout the whole year of tax in providing fringe benefits. The operation of the rules in circumstances where the car is first used to provide fringe benefits part way through the year of tax (e.g., where the car is purchased to expand the employer's fleet) is discussed later in these notes.

Subsequent years

The business percentage nominated by the employer in the log book year of tax will be treated as the business percentage for subsequent years provided there has not been a substantial reduction in the proportion of business use.

- For this purpose a substantial reduction is more than 10 percentage points, e.g., if the nominated business percentage is 70%, that percentage can continue to be used in subsequent years provided the business percentage during a subsequent year, based on a reasonable estimate, does not fall below 60%.

- In any subsequent year in which the nominated percentage is being used to calculate the taxable value, it will be necessary that a record of total kilometres travelled in the year be maintained. For this purpose odometer readings at the beginning and end of the year must be recorded.

- If the car ceases to be used for providing fringe benefits during a subsequent year, the taxable value of the fringe benefit will be determined by applying the nominated business percentage to car operating costs relevant to the period up until that time. In these cases the odometer readings required will be those at the start of the year and at the time the car ceases to be used for providing fringe benefits.

- To prevent exploitation of rules that are designed for high business use cars, the 10 percentage points margin will not apply on the same basis for cars which have a business usage of 5000 or fewer kilometres per annum. For these, log books need not be kept in any subsequent year where there has been a reduction in business use that does not exceed 10 percentage points. However, the taxable values of car fringe benefits in these years are to be based on a reasonable estimate of the actual percentage of business use in the year rather than the prior year's nominated percentage.

Substantial falls in business use

If in a year subsequent to a nominated business percentage being adopted by an employer there is a substantial fall in business use of the car (i.e., by more than 10 percentage points), the following rules will apply. (Whether or not a substantial fall has occurred is to be on the basis of a reasonable estimate of the actual percentage of business use during the year.)

- The employer must adopt the lower actual business percentage for the purposes of determining the taxable value of the car fringe benefit for that year.

- Alternatively, the employer may calculate the value under the statutory formula method mentioned earlier.

- If in the year following the substantial fall in business use the employer wishes to adopt the operating cost method of calculating the taxable value of the car fringe benefit, it will be necessary to establish a new nominated business percentage by ensuring that log books are maintained for a continuous 12 week period.

Increase in business use

If an employer wishes to increase the nominated business percentage in any year, that may be done by ensuring that a log book is maintained for a further minimum continuous period of 12 weeks.

Replacement cars

If a car for which log books have been maintained and a nominated business percentage established is replaced, the nominated business percentage may continue to be used for the replacement car provided there is not a substantial fall in the proportion of business use.

Car first used during a year of tax to provide fringe benefits

The following rules apply where an employer commences to use a car to provide fringe benefits to an employee or associate, etc. The rules vary according to whether or not that use commences in the last 12 weeks in the year of tax.

- Where the car is first used to provide fringe benefits in the last 12 weeks, log books need not be kept for that year. The taxable value of the fringe benefit is to be calculated on the basis of a reasonable estimate of the percentage of business use during the period. Log book records must, however, be kept in the following year of tax on the basis of which the employer will be entitled to nominate the business percentage for that next year which, provided there is no substantial reduction in business use, will also apply for subsequent years of tax.

- Where the car is first used to provide fringe benefits more than 12 weeks before the end of the year, the normal rules apply. That is, log book records must thereafter be kept for a minimum 12 week period. On the basis of those records and any variation in the business use during the period to the end of the year of tax the employer is entitled to nominate a business percentage which, provided there is no substantial reduction in business use, will apply for subsequent years of tax.

Inaccurate car fringe benefit calculations

Provisions contained in the Bill will enable the Commissioner of Taxation to increase the taxable value of car fringe benefits where they are found to be inaccurate.

- Where the employer nominates an inaccurate business percentage in the year in which log books are maintained, the Commissioner will be entitled to adjust the nominated percentage. Where this percentage has been used as the nominated percentage for subsequent years of tax, the taxable values of car fringe benefits for those years will similarly be adjusted to reflect the correct nominated percentage. That corrected percentage will form the basis for calculating the taxable value of car fringe benefits for subsequent years provided the actual business use is not substantially less (i.e., by more than 10 percentage points).

- Where the nominated business percentage has been accurately determined in the log book year but is used in a subsequent year in which there has, in fact, been a substantial reduction in business use (i.e., by more than 10 percentage points), the Commissioner will be entitled to adjust the taxable value in that subsequent year to reflect the true business percentage.

- If any adjusted taxable value based on the corrected business percentage is more than what it would have been if calculated under the alternative statutory formula, the taxable value will be the lesser amount.

The normal penalty rules will apply to inaccurate claims.

Switching from one method of calculation to another

Under the present law, an employer is generally prohibited from switching from one method of calculating the taxable value of a car fringe benefit to another in respect of the same car, i.e., if the operating cost method is chosen in one year, the employer cannot change to the statutory formula method in a subsequent year, and vice versa. Provisions in the Bill remove that restriction so that an employer may move from one basis of calculation to another year by year. Where an employer takes advantage of that option by switching from the statutory formula basis to the operating cost method, it will be necessary to ensure that log book records are kept for a minimum continuous period of 12 weeks to establish the nominated business percentage. This will be the case whether or not the operating cost (log book) method has been used previously to calculate the taxable value of car fringe benefits in relation to the car.

Retention of log books and odometer records

The existing law requires employers to retain 'statutory evidentiary documents' - which includes log books and odometer records - for the 'retention period'. That period is, broadly, six years from the date of assessment of the employer's fringe benefits taxable amount. If at the end of that six year period there is an objection or request for amendment relevant to the document that has not been finally disposed of - including where the matter has gone on review or appeal - the six year retention period is extended until the matter has been resolved.

In recognition that car log books and odometer records from a log book year may continue to be evidentiary documents for the purpose of calculating the taxable value of car fringe benefits in subsequent years as long as there is not a substantial fall in the business percentage of the particular car or of replacement cars, provisions in the Bill extend the six year retention period from the original date of assessment of a year of tax in which the taxable value of a car fringe benefit is based on those records.

Revised log book rules to establish the business percentage of fringe benefits other than cars

Under the present law, the taxable value of a loan fringe benefit, expense payment fringe benefit, property fringe benefit or residual fringe benefit is reduced to the extent to which the interest on the loan, or the cost of the benefit, would have otherwise been allowable as an income tax deduction of the employee had he or she borne the relevant expense. If the benefit relates to the employee's own car, e.g., a reimbursement of expenses of operating the employee's own car or a loan to purchase the car, the employer needs to obtain from the employee evidence to substantiate the extent to which the car was used for business purposes. That evidence is in the form of a declaration of the period of ownership or lease of the car during the year, the total kilometres travelled and the total business kilometres travelled. If the declaration also states that a car log book was maintained during the year and a copy given to the employer, the deductible percentage in relation to the relevant fringe benefit will be the proportion of the declared business kilometres over total kilometres.

If log books have not been maintained, the deductible percentage is determined by reference to the details shown in the declaration but may not exceed 33 1/3%. Alternatively, the deductible percentage will be 33 1/3% if the employee declares that the average weekly business kilometres travelled in the car exceeded 96.

The log book rules for determining the deductible percentage for the purposes of calculating the taxable value of a fringe benefit (loan, expense payment, etc.) relating to an employee's car are being revised in line with the revised log book rules for determining the taxable value of car fringe benefits. That is, it will no longer be necessary for the employee to record details of business trips throughout the whole year of tax. Instead, the percentage of business use of a car can be established by making log book entries in a continuous twelve week log book period. Provided the actual percentage of business use does not vary substantially (i.e., by more than 10 percentage points) from that established by reference to the log book records, that established percentage continues to be the basis for calculating the taxable value of the fringe benefits relating to the particular car or a car that replaces it. The revised log book rules will apply in a parallel way to those outlined above in relation to car fringe benefits.

Exemption of certain fringe benefits

The Bill provides that the following kinds of benefits that would otherwise be taxable fringe benefits will be exempt from fringe benefits tax:

. Unregistered motor vehicles
(Clauses 4, 28, 60)

The private use by an employee of an employer-provided motor vehicle which is unregistered throughout the whole year of tax and used principally for business purposes will be exempt from fringe benefits tax.

. Use of employer's equipment
(Clause 28)

Under an existing exemption, benefits consisting of the use on working days of staff amenities or business equipment located on the employer's business premises are exempt from fringe benefits tax. That exemption will be extended to include use of such amenities or equipment on non-working days. The exemption will also be extended to an employee's use of the employer's business equipment (not including motor vehicles) away from the business premises provided the equipment is normally located on the business premises (e.g., where an employee borrows a typewriter to use at weekends).

. Public hospital employees
(Clause 32)

Under an existing exemption, benefits provided to employees of public benevolent institutions are exempt from fringe benefits tax. That exemption applies to employees of public hospitals. The Bill ensures that benefits provided to employees who work in a public hospital but are

technically employed by a Commonwealth, State or Territory Health authority will also be exempt from fringe benefits tax.

. Employment interviews
(Clauses 34, 39, 55)

Benefits which meet travel costs incurred by a current or future employee for the purpose of attending a job interview or selection test will be exempt from fringe benefits tax.

. Relocation costs
(Clauses 10, 34, 39, 47, 48, 50, 51, 53, 55)

Where an employee moves from one locality to another in the course of employment or in order to commence employment, a range of relocation costs may be met by the employer. The Bill provides that benefits provided in respect of the following relocation costs are to be exempt from fringe benefits tax:

- the travel costs of the employee and his or her family resulting from relocation;

- the costs of removal of furniture and personal effects including the costs of packing, insuring, transporting and storing such items;

- the costs of temporary accommodation provided at the former locality during the period of 21 days prior to the day on which the employee commences work at the new locality;

- the costs of temporary accommodation provided at the new locality where the temporary accommodation is required while the employee is searching for suitable long-term accommodation. Where the employee sells his or her home at the former locality within 6 months of commencing work at the new locality and is attempting to purchase a home at the new locality, the maximum period of exemption will be 12 months. In other cases, the maximum period of exemption will be 6 months;

- the costs of leasing furniture and other household goods for use in temporary accommodation;

- the cost of meals provided to the employee (or family member) while staying in temporary accommodation in a hotel, motel, hostel or guesthouse to the extent that the value of the meal exceeds $2 ($1 if the recipient is under 12);

- advances to employees for the purpose of paying deposits associated with temporary accommodation (e.g., bond moneys or deposits required for the connection of services such as electricity or gas) provided the advance is repayable within 1 year;

- costs incurred in the sale of the employee's home at the former locality and the purchase of a home at the new locality (e.g., stamp duties, legal fees and agents' commissions); and

- the cost of reconnecting a telephone, electricity or gas service to temporary accommodation at the new locality or to a home purchased at the new locality.

. Motor vehicle parking benefits
(Clause 34)

Benefits provided in respect of motor vehicle parking facilities will be exempt from fringe benefits tax. The exemption applies whether or not the parking facilities are provided on the employer's premises.

. Newspapers and periodicals
(Clause 34)

Newspapers or periodicals provided to employees for use for business purposes are to be exempt from fringe benefits tax.

. Compensation for work-related injuries
(Clauses 34, 48)

Medical treatment and other benefits provided in respect of a work-related injury for which compensation benefits are payable under a workers' compensation law will be exempt from fringe benefits tax. For employees not covered by a workers' compensation law, benefits provided in respect of a work-related injury will be exempt if the injury would have been compensable under an Australian workers' compensation law if it had applied to the employee's employment. Where an employer pays premiums under a workers' compensation insurance policy, any benefit constituted by the insurance cover under that policy will also be exempt from fringe benefits tax.

. Work site medical facilities
(Clauses 34, 48)

The provision of medical services or other health-care benefits will be exempt from fringe benefits tax where they are provided through a facility such as a first aid post or medical clinic located at the employer's premises (or at a site where employees of the employer

perform duties of their employment) and the facility is principally for the treatment of work-related injuries and illnesses. This exemption complements the proposed exemption of benefits in respect of work-related injuries by exempting the incidental use of such facilities for the treatment of injuries of the employee (or a family member) that are not related to the employee's employment.

. Travel from prescribed developing countries for medical treatment
(Clause 34)

Benefits in respect of travel costs incurred by an employee working in a prescribed developing country will be exempt from fringe benefits tax where the travel is for the purpose of obtaining medical treatment.

To qualify for exemption, the travel must be from the work locality to either the nearest place at which medical treatment suitable for the patient can be provided or the place at which such treatment can be obtained at least cost.

The exemption will extend to the travel costs of a family member who lives with the employee at the overseas employment place and requires medical treatment. Where the employee (or family member) receiving the medical treatment requires an escort, the exemption will also apply to the travel costs of the escort.

. Occupational health and counselling
(Clauses 34, 39, 48 55)

The following occupational health and counselling benefits are to be exempt from fringe benefits tax:

- pre-employment medical tests;
- hearing, eye and medical screening of employees where there is a perceived risk of injury or disease from the work environment of those employees (e.g., lung tests for asbestos workers);
- the provision of preventative health care where there is a perceived risk of injury or disease from the work environment (e.g., hepatitis vaccinations for dental staff);
- work-related counselling services provided to employees (e.g., individual or group counselling related to safe work practices, stress management, drugs, alcohol or pre-retirement planning); and
- migrant language training.

. Benefits provided in emergencies
(Clauses 34, 48)

Benefits such as emergency food, clothing and shelter provided by employers for the immediate relief of employees and their families in times of emergency (e.g., on the occurence of fires, floods, accidents, etc.) are to be exempt from fringe benefits tax.

. Minor benefits
(Clauses 34, 48)

The Bill introduces an exemption for benefits which are of small value and infrequently provided and/or difficult to record and value. The proposed exemption would apply, for example, to benefits which arise where an employer pays taxi fares for an employee on an infrequent and irregular basis where the employee is unexpectedly required to work late.

. Long service awards
(Clauses 34, 48)

Long service awards granted in recognition of 15 years or more service will be exempt from fringe benefits tax provided the taxable value of the award does not exceed a specified maximum value which varies according to the length of service. Where the period of service being recognised by the award is 15 years, the specified maximum value is $500. If the first long service award received by an employee recognises a period of service greater than 15 years, the maximum value increases by $50 for each additional year (e.g., the maximum value for a first award recognising 20 years service is $750). Where the value of an award exceeds the relevant maximum value, no part of the award is exempt.

. Safety awards
(Clauses 34, 48)

Where an award genuinely related to occupational safety achievements is granted to an employee and its taxable value does not exceed $200, the award will be exempt from fringe benefits tax. Where more than one award is granted to an employee during a fringe benefits tax year, they will be exempt provided their aggregate value does not exceed $200. If the aggregate value exceeds $200, none of the awards will be exempt.

. Australian traineeship scheme
(Clause 34)

Accommodation and food provided by employers to trainees engaged under the Australian Traineeship System are to be exempt from fringe benefits tax.

- Benefits provided in religious houses (Clauses 34, 48)

Accommodation and food provided to a live-in domestic employee of a religious institution or a religious practitioner (e.g., a minister of religion) at a place of residence of one or more religious practitioners will be exempt from fringe benefits tax. For example, accommodation and meals provided to a housekeeper in a presbytery are to be exempt.

- Live-in help for elderly and disadvantaged persons (Clauses 33, 34, 48)

Accommodation and food provided to live-in help employed to care for elderly (60 years or over) or disadvantaged persons will be exempt from fringe benefits tax. Disadvantaged persons are those who are intellectually, psychiatrically or physically handicapped or in necessitous circumstances.

The existing exemption for accommodation provided to employees of government bodies, religious institutions or non-profit companies who live with and care for disadvantaged people will be extended to include meals and to similar care of elderly people.

- Food for domestic employees (Clauses 34, 48)

The Bill makes it clear that food provided in the home to non-live-in domestic employees are exempt from fringe benefits tax. An example would be a baby sitter caring for children in their home who shares lunch with the children.

<u>In-house fringe benefits</u>
(Clauses 15, 17, 40, 48)

Under the existing law, concessional valuation rules apply to 'in-house' fringe benefits. Broadly, these are airline transport fringe benefits, property fringe benefits or residual fringe benefits attributable to goods or services, etc., of a kind supplied to the public in the ordinary course of the employer's business. The concessional valuation rules take two forms. First, the taxable value of the particular goods or services, etc, are determined in accordance with special valuation rules. For example, if a retail store sells goods to staff at a discount, the goods are valued at their cost to the retailer so that a taxable value will not arise unless the goods are sold below cost. Secondly, the first $200 of the aggregate of the taxable values of in-house fringe benefits provided to an employee in a year of tax is exempt from fringe benefits tax. The exemption is proportionally reduced to $150 for the transitional year of tax.

The Bill will increase the $200 annual exemption to $500 ($375 for the transitional year).

The Bill will also extend the range of fringe benefits that qualify for the in-house concessional valuation rules. At present, property and residual fringe benefits only qualify as in-house fringe benefits where the goods or services, etc., are provided to the employee (or an associate) by the employer or an associate of the employer. Under the proposed amendments, property and residual fringe benefits provided by a third party by arrangement with the employer (or associate) will also qualify where the goods, etc., were purchased by the third party arranger from the employer (or associate) in the ordinary course of business.

A further category of fringe benefits will also now qualify for the in-house concessions. The new category will, broadly, comprise expense payment fringe benefits where the employee receives a reimbursement of expenditure incurred in respect of the purchase of goods, etc., of a kind supplied to the public in the ordinary course of the employer's business. For example, where an employee of a petroleum company purchases the company's brand of petrol from an independently owned retail outlet at the usual retail price and the employee subsequently receives a reimbursement of a percentage of that retail price from the employer, that reimbursement will qualify as an in-house expense payment fringe benefit.

The proposed valuation rules for in-house expense payment fringe benefits are consistent with the existing valuation rules for in-house property and residual fringe benefits. In addition, in-house expense payment fringe benefits will be eligible for the $500 annual exemption that is to apply to other in-house fringe benefits.

The effect of the amendments will be that irrespective of whether a staff discount is provided directly as a property or residual fringe benefit or indirectly as an expense payment fringe benefit, the taxable value will be the same.

Remote area housing
(Clauses 20, 21, 35, 36, 48, 52, 53)

Under the existing law, where an employer chooses to value remote area housing fringe benefits on a market rental basis, the market rental value of the accommodation is discounted by 40%. The employer may, however, elect to value remote area housing fringe benefits using a statutory formula instead of a market rental basis. Once made, the election applies to all units of accommodation and is irrevocable.

The amendments proposed by the Bill will:

- increase the existing 40% discount for remote area housing fringe benefits to 50%;

- replace the statutory formula with an annual statutory value (after taking into account the 50% discount) of $60 per week per unit of accommodation or $15 per week for single person's quarters. These values include any electricity and residential fuel supplied or paid for by the employer. For years following the transitional year of tax, the statutory values are to be increased in line with movements in the rent sub-group of the national Consumer Price Index; and

- permit the employer to choose in each year, for each unit of accommodation, either the statutory value or market rental basis.

In addition, the present 40% discount available for housing assistance provided by way of a low-interest loan, reimbursement of housing loan interest or the sale of a house below market value is to be increased to 50%. Similarly, the 40% discount which currently applies where a fringe benefit in respect of residential fuel is provided in connection with a housing assistance arrangement is to be increased to 50%.

A new discount of 50% is also to apply where a housing benefit is provided as a rent reimbursement or actual payment of rent incurred by the employee. The new 50% discount will extend to the value of residential fuel provided in connection with the rental accommodation.

Remote area holiday travel
(Clauses 37, 38, 54)

Under the existing law, the taxable value of a fringe benefit related to remote area holiday travel is reduced by 50% provided the employee travels either to his or her place of engagement or to the capital city of the State or Territory where the work place is located.

The amendments being made by the Bill will mean that travel to a destination other than the place of engagement or the capital city of the State or Territory in which the work place is located will now qualify for the concession. However, the reduction in the taxable value of fringe benefits related to such travel is not to exceed 50% of the usual cost of travel to the capital city of the State in which the work place is located. For this purpose, the usual cost of travel will generally be the return economy air fare for an air service ordinarily used from the work location to the State capital city.

The amendments proposed by the Bill will also:

- provide that the holiday travel concession is to apply in relation to employees located in the Northern Territory and Christmas Island as though the relevant State capital were Adelaide and Perth respectively;

- remove the existing requirement that holiday travel by an employee's spouse and children must be undertaken while the employee is on recreation leave in order to qualify for the concession; and

- provide that, where the holiday assistance takes the form of a reimbursement of expenses incurred by the employee, those expenses may now be evidenced by a declaration from the employee rather than by actual receipts, etc.

Employees posted overseas
(Clauses 39, 42, 48, 55)

Benefits provided in accordance with an award or industry custom to employees posted overseas in respect of holiday travel and education costs are to be given concessional treatment. These concessions will apply in relation to both Australian employees posted overseas and overseas residents posted to Australia.

Under the holiday travel concession, the taxable value of a fringe benefit in respect of holiday travel by the employee is to be reduced by 50%. The concession applies irrespective of the actual destination. However, the total reduction in the taxable value of holiday travel fringe benefits provided in a fringe benefits tax year is not to exceed 50% of the cost of return travel for one holiday to the employee's home country. In a case where the travel is not to the home country, the limit on reduction in taxable value is calculated by reference to the cost of economy air travel to the home country.

The holiday travel concession also applies where holiday travel fringe benefits are given to the employee's family whether or not they live with the employee at the overseas post.

Fringe benefits in respect of the education costs of the employee's children will be exempt from fringe benefits tax for the period of overseas service . If the overseas service commences or ceases during a school term, the education costs for the whole term will be exempt.

Fringe benefits provided in respect of overseas employment
(Clauses 42, 47, 48)

Under the existing fringe benefits tax law, fringe benefits are subject to the fringe benefits tax where the benefits are provided in respect of employment activity that gives rise to salary or wages that is assessable to income tax in Australia. This is the case irrespective of whether the salary or wages is assessable in full or in part.

Sections 23AF and 23AG of the Income Tax Assessment Act provide that, in specified circumstances, Australian residents employed overseas for periods of between 3 and 12 months are subject to Australian income tax on their foreign source income only on a pro-rata basis. For example, if an employee is located overseas on an approved project for 6 months and the employee's income is not taxed in the country where the work place is located, section 23AF provides that one-half of his or her income from that overseas employment is exempt income.

The amendments proposed by the Bill will ensure that fringe benefits provided to an Australian employee working overseas for a period between 3 and 12 months is taxed in a comparable manner to the employee's salary. That is, where the employee's salary from overseas employment is taxed on a pro-rata basis, fringe benefits provided to the employee in respect of that overseas employment will be taxed on the same pro-rata basis.

Reduction in taxable value provisions: expenditure otherwise deductible to employee
(Clauses 12, 17, 24, 25, 27, 29, 48, 49, 65, 66)

Under the existing law the taxable value of a loan, airline transport, board, property or residual fringe benefit is reduced by the amount of any employee contribution for the benefit. The taxable value of the benefit after deducting the employee contribution (i.e., the net value of the benefit) is then reduced by the extent to which any expenditure that would otherwise have been incurred by the employee in obtaining the relevant benefit would have been deductible for income tax purposes.

That rule can have inappropriate results in circumstances where the contribution made by an employee for a fringe benefit is intended to cover the private component of the benefit.

This can be illustrated by the following example. Assume:

- accounts for a telephone installed in an employee's home are billed direct to the employer;

- under an arrangement between the employer and the employee, it is anticipated that business use of the telephone will be 40% and, based on that assumption, the employee is required to contribute 60% of the amount payable by the employer under each telephone account;

- the amount payable by the employer for a particular telephone account is $500 and the employee contributes $300 (i.e., 60%); and

- the employee's actual business use of the telephone is 40%.

Under the present law, it could be argued that the employee would be entitled to an income tax deduction of $120 (i.e., 40% of $300). At the same time, the taxable value of the fringe benefit (a residual fringe benefit) would be calculated as follows:

Gross value of benefit	$500
Less: employee contribution	300
Net value of benefit	200
Less: notional deduction (40% of $200)	80
Taxable value	$120

The effect of such an application of the present law is that the business component of the expense ($200) operates to reduce the taxable income of the employee by $80 and the taxable value of the fringe benefit by $120. However, under the arrangement between the employer and the employee it was intended that the business component of the account be met wholly by the portion of the account met by the employer and that the private component of the account be met wholly by the portion of the account met by the employee.

To overcome such anomalies, it was announced on 29 October 1986 that the law would be amended to provide that the taxable value of a fringe benefit would be calculated by first applying the otherwise deductible rule and then reducing the taxable value by the amount of the employee contribution. Complementing this proposal, it was also announced that the income tax law would be amended to ensure that an income tax deduction would not be allowable to the employee in respect of the amount of the contribution.

While these proposals would produce an appropriate result in cases where the employee's contribution is solely for the private element of the benefit, they could produce an inequitable result in the event that the contribution is not related to the private component. For example, assume that an employee of an oil company purchases, say, $2,000 worth of petrol from the company under a standard staff discount of, say, 10% and uses the car 90% for business

purposes. In such a case, the adoption of the announced proposal would deny the employee any deduction for his or her expenditure of $1,800 on fuel, despite the fact that it was incurred 90% for business purposes and was not intended as a contribution for the private element.

Against this background, the Bill will introduce a variation of the announced proposal which will not produce inequitable results where the employee contribution is not related to the private component of the benefit.

The modified proposal is to amend both the income tax law and the fringe benefits tax law to ensure that, in all cases, the rules for calculating the income tax deduction allowable to the employee and the taxable value of the fringe benefit reflect the intention of the parties to the arrangement under which the employee makes the contribution.

The proposed amendment to the income tax law will ensure that the employee is not entitled to an income tax deduction for a contribution to a fringe benefit to the extent that the contribution is, in effect, a payment for the private element of the benefit.

The complementary amendments being made to the fringe benefits tax legislation will amend the otherwise deductible rules to ensure that the taxable value of a fringe benefit is reduced by the amount of the additional deduction that would be allowable to the employee if he or she had incurred and paid additional expenditure equal to the net value of the benefit.

This involves three steps. First, it is necessary to determine the deduction (the 'gross deduction') that would be allowable to the employee if he or she had incurred expenditure to obtain the benefit equal to the gross value of the benefit (i.e., the taxable value before deducting the employee contribution). Secondly, the deduction (the 'recipient's deduction') allowable to the employee in respect of his or her contribution for the benefit is determined. This is determined by looking to the arrangements surrounding the provision of the benefit, e.g., the extent to which the amount borne by the employer was intended to cover the business component. Finally, the recipient's deduction is subtracted from the gross deduction to arrive at the amount of the additional deduction (the 'notional deduction').

To illustrate the operation of the revised rules, the effect of the amendments in the telephone example above will be that the employee will not be entitled to a deduction for any part of the $300 contribution (the contribution is, in effect, a payment for the private component of the benefit). However, the business component

of the benefit will operate to reduce the taxable value of the residual fringe benefit which will be calculated as follows:

Gross value of benefit	$500
Less: employee contribution	300
Net value of benefit	200
Less: notional deduction (40% of $500)	200
Taxable value	$ 0

In the second example, the employee would continue to be entitled to a deduction for 90% of his or her actual expenditure while the taxable value of the benefit after reduction for the amount paid by the employee for the petrol will similarly qualify for a 90% business use reduction.

The revised otherwise deductible rules outlined above (and the corresponding income tax deduction rules for employees) are also being extended on a comparable basis to expense payment fringe benefits.

Expenditure of a kind subject to "negative gearing" rules

The Bill also proposes to amend the otherwise deductible rules to remove an existing provision which denies a reduction in taxable value where any expenditure to obtain the benefit would otherwise be subject to the income tax 'negative gearing' rules. That exclusion will not now apply in relation to the fringe benefits tax year commencing on 1 April 1987 or subsequent years.

Declarations
(Clauses 12, 28, 48)

Under the existing law, the taxable value of certain fringe benefits may be reduced under either the otherwise deductible rules or the living-away-from-home concessions provided the employer obtains a declaration from the employee setting out information required to support the reduction.

The Bill provides that employee declarations will not now be needed for loan benefits and living-away-from-home benefits in specified circumstances.

For loans, the requirement to obtain a declaration for the purposes of the otherwise deductible rule is to be dispensed with where:

- the loan is used solely to enable the employee to acquire shares in the employer's company and the shares are owned by the employee throughout the period of the year that the loan is outstanding; or

- the loan consists of the provision of credit by the employer in respect of a sale to the employee of goods or services that are used exclusively in the employee's employment (e.g., where an employer sells a uniform to an employee on interest-free credit terms).

In these circumstances it is clear from the nature of the benefit that the otherwise deductible rule applies.

Living-away-from-home declarations will not now be needed for 'fly-in fly-out' arrangements (e.g., where employees live for periods on offshore oil rigs). This means that accommodation provided at the work site under a fly-in fly-out arrangement will now be eligible for the existing living-away-from-home exemption without the need for a declaration.

Undocumentable expenses
(Clause 17)

Under the existing law, where an employee incurs a business expense which is reimbursed by the employer, the taxable value of the expense payment fringe benefit is reduced under the 'otherwise deductible' rule provided the employer obtains appropriate documentary evidence of the expense from the employee.

The amendments proposed by the Bill will enable business expenses incurred by an employee that by their nature are not readily documentable (e.g., train fares) to be verified by appropriate petty cash entries rather than receipts.

Market value of housing fringe benefits
(Clauses 18, 19)

Under the existing rules for valuing housing fringe benefits, the market value of the right to occupy accommodation is determined in the year when the accommodation is first used to provide a housing fringe benefit and is then generally indexed annually for the next 9 years in accordance with movements in the rent sub-group of the relevant Consumer Price Index.

The Bill will amend the rules for valuing housing fringe benefits to enable an employer to use the current market value of the accommodation in any year where the CPI adjusted figure exceeds the current market value.

Crash repairs
(Clause 6)

Under the existing law an employer may elect to use the operating cost method to value car fringe benefits. For this purpose, the operating cost of the car includes expenses incurred in respect of repairs to the car.

The Bill will amend the law to exclude from the operating cost of the car any repair expenses that are met by the employer's insurer or by the person legally responsible for the damage to the car.

Holiday car expenses
(Clause 14)

Under the existing law, a reimbursement of an employee of car expenses on a cents per kilometre basis is exempt from fringe benefits tax except where the reimbursement is in respect of remote area holiday transport. A complementary provision of the income tax law ensures that such exempt payments are treated as assessable income of the employee.

The Bill proposes to amend the law so that all cents per kilometre reimbursements of car expenses in respect of holiday travel are subject to fringe benefits tax and, correspondingly, not treated as assessable income of the employee. This means that employees in non-remote areas who receive holiday transport assistance by way of a cents per kilometre reimbursement of car expenses will be treated in a similar manner to employees in remote areas in receipt of such assistance - although the 50% discount on taxable value available for remote area benefits will not apply.

Application of amendments

The changes to the fringe benefits tax legislation outlined in these notes will apply for the transitional year of tax that ended on 31 March 1987 and to subsequent years (i.e., from the commencement of the tax). In addition, a number of minor drafting corrections are proposed by the Bill. These drafting amendments will not apply in any case where a benefit was provided to an employee before the date on which the Bill is introduced into the House of Representatives if the application of the amendment would increase the liability of the employer to fringe benefits tax in respect of that benefit.

Income tax

Substantiation requirements: transport allowances
(Clauses 67 to 73)

Under the present law it is a requirement for deduction that documentary evidence be maintained to substantiate relevant employment-related expenses, and car and travel expense claims. This requirement is subject to a number of specific exclusions (e.g., claims within the limits of reasonable domestic travel allowances).

The amendments proposed by the Bill provide that claims within the limits of certain transport allowances are also to be excluded from the substantiation

requirements. Under the new exclusion, substantiation will not apply to claims within the limits of allowances paid to employees for fares, car expenses and other transport costs incurred in the course of performing their employment duties where the allowances are payable pursuant to an award and are not higher in amount than was payable pursuant to the award as at 29 October 1986. Claims which exceed the amount of the allowance will remain subject to the substantiation requirements.

Where the amount of an allowance increases after 29 October 1986 the exclusion from substantiation will cease to apply. This will mean, for example, that if the award is varied at any time after 29 October 1986 to increase the amount of the allowance, the full amount of claims in respect of the allowances payable at the higher rate will be subject to the substantiation requirements. Similarly, if the award as it was in place on 29 October 1986 contained clauses which provided for future variations determined by reference to matters external to the award (e.g., changes in the C.P.I.), increased allowances payable as a consequence of such variations will not qualify for the exclusion from substantiation. However, as a transitional arrangement, the substantiation exclusion will apply where an allowance was increased after 29 October 1986 pursuant to an application to vary the award that was made on or before that date.

The new exclusion from the substantiation requirements is to apply with effect from the income year commencing on 1 July 1986, i.e., the date of commencement of operation of the substantiation rules.