Australian Government

The Treasury

November 2013

Mr Jason McNamara
Executive Director
Office of Best Practice Regulation
Department of Prime Minister and Cabinet
John Gorton Building
King Edward Terrace
PARKES ACT 2600

Jason

Dear Mr McNamara

POST-IMPLEMENTATION REVIEW –FRINGE BENEFITS TAX – REFORM OF THE CAR FRINGE BENEFIT RULES

I am writing to the Office of Best Practice Regulation (OBPR) regarding a post-implementation review (PIR) for the proposal to reform the statutory formula method for determining the taxable value of car fringe benefits.

This measure was announced by the previous Government in the 2011-12 Budget to implement a recommendation of the Australia's Future Tax System Review (the AFTS Review) and to continue the then Government's process of tax reform started in May 2010 with the release of the *Stronger, Fairer, Simpler* package of reforms.

Although this measure was primarily revenue in nature and, therefore, did not require a regulation impact statement (RIS), an exemption was provided by the then Prime Minister as part of the broader package of reforms from the AFTS Review. As a result, the OBPR agreed that a short form PIR was sufficient for this measure (attached).

The Treasury understand that this letter fulfils the Australian Government Best Practice Regulations for a PIR and, as such, will be published on the OBPR website.

Yours sincerely

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Attachment

POST-IMPLEMENTATION REVIEW –FRINGE BENEFITS TAX – 2011-12 REFORM OF THE CAR FRINGE BENEFIT RULES TO CREATE A SINGLE STATUTORY RATE

Problem

This measure improves the effectiveness, sustainability and integrity of the taxation of car fringe benefits by replacing the sliding scale of statutory rates used to calculate the taxable value of car fringe benefits with a single statutory rate.

Since the introduction of the fringe benefits tax system in 1986, there have been two methods for determining the taxable value of car fringe benefits – the operating cost method and the statutory formula method.

Under the operating cost method, the taxable value of the car fringe benefit is based on the cost of owning and operating the car, reduced by the portion relating to business use. The statutory formula method, on the other hand, determines the taxable value based on the cost of the car multiplied by a statutory rate. The statutory rate was, prior to the 2011 reforms, a sliding scale based on the number of kilometres travelled by the car for a year.

Inherent in the sliding scale was the assumption that as the distance travelled increased, the business use of the vehicle increased. However, this assumption pre-dated the advent of salary sacrifice arrangements and no longer reflected vehicle usage. The AFTS Review found that the sliding scale was creating an incentive for individuals to travel additional kilometres to reduce the taxable value of the car. This may result in a favourable tax outcome for employees who choose to take part of their remuneration as a car fringe benefit.

Objectives

The Government's objective of this reform was to improve the effectiveness, sustainability and integrity of the taxation of car fringe benefits. This is achieved by removing the unintended incentive for people to drive their vehicles further to increase their tax concession by replacing the sliding scale of rates with a single statutory rate. The single statutory rate provides a better reflection of the value of the fringe benefit to the employee.

Impact analysis

The measure applies a single statutory rate of 0.20 to car fringe benefits valued under the statutory formula method, regardless of the distance travelled during the FBT year for arrangements entered into after 7:30pm AEST on 10 May 2011. Changes for new contracts are phased in over four years (see table below); however, an employer may choose to move to the single rate immediately.

Distance travelled during the FBT year (1 April – 31 March)	Existing contracts	New contracts entered into after 7:30pm (AEST) on 10 May 2011			
		From 10 May 2011	From 1 April 2012	From 1 April 2013	From 1 April 2014
0 – 15,000 km	0.26	0.20	0.20	0.20	0.20
15,000 – 25,000 km	0.20	0.20	0.20	0.20	0.20
25,000 – 40,000 km	0.11	0.14	0.17	0.20	0.20
More than 40,000 km	0.07	0.10	0.13	0.17	0.20

The measure was introduced to Parliament in Tax Laws Amendment (2011 Measures No. 5) Bill 2011 on 2 June 2011. As part of the Senate debate on the Bill, a resolution was agreed to require the Senate Economics References Committee to conduct a review of the changes 12 months after their commencement. The Committee issued their report *Review of changes to car fringe benefits arrangements* in February 2013.

The Committee found that the analysis of the impacts was limited by the transitional implementation of the measure. However, submissions received provided the Committee with an indication of the effects once fully implemented.

The Committee noted that the move to a flat statutory rate affected taxpayers differently depending on the number of kilometres travelled. Taxpayers in the 0 - 15,000 kilometre bracket actually benefited immediately from the measure as the FBT payable is reduced under the new statutory rate. Taxpayers in the 15,000 - 25,000 kilometre bracket were unaffected by the change, but may benefit from simpler compliance. While taxpayers travelling more than 25,000 kilometres would be worse off from the changes, the impact was minimised by the phase-in period of four years.

One submission indicated that taxpayers would benefit from the measure once fully implemented with the calculation of FBT liability simplified with a single statutory rate. Another submission indicated that the measure addressed their concerns of maintaining compliance ease for car fringe benefits. The Committee concluded that the measure reduced complexity and had economic efficiency benefits that would be achieved once fully implemented.

Therefore, while this measure has not yet been fully implemented, it is concluded from the information available that the measure has low impact on business and the not-for-profit sector. However, it should be stressed that this conclusion is based on limited information and, therefore, lacks certainty.

Consultation

This measure implements a recommendation made by the AFTS Review which found that:

> 'The existing statutory formula for valuing car fringe benefits applies a reduced taxable value the further a vehicle is driven. At the margin, this may encourage individuals to travel unnecessary kilometres.'

Extensive consultation was undertaken as part of the Review, including discussions with salary sacrifice providers, charitable organisations and industry groups.

To address this, the Review recommended that the sliding scale of rates should be replaced with a single statutory rate applying regardless of the kilometres travelled.

The Senate Economics Committee conducted a review into the changes to car fringe benefits and received four submissions to the review. Consultation on the measure was undertaken as part of the Committee's review.

Again, it is concluded that the measure has low impact on businesses and the not-for-profit sector.

Conclusion

It is concluded that this measure meets its objectives and has a low impact on businesses and the not-for-profit sector.