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General Manager
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Dear Treasury

Tax and Superannuation Laws Amendment (2015 Measures No. #) Bill 2015: Limiting fringe benefits tax concessions on salary packaged entertainment benefits

Governance Institute of Australia is the only independent professional association with a sole focus on whole-of-organisation governance. Our education, support and networking opportunities for directors, company secretaries, governance advisers and risk managers are second to none.

Our members are all involved in governance, risk management and corporate administration. Furthermore, many of our members serve as officers of not-for-profit (NFP) organisations, or work for, or are involved with NFP organisations and charities, many of which are companies limited by guarantee and some of which are entitled to tax concessions. As a result, they are also involved in the governance of charities and compliance with the Australian Charities and Not-for-profits Commission (ACNC) regulations.

Governance Institute of Australia (Governance Institute) is itself a charity operating in the legal form of a company limited by guarantee, established to promote and advance the efficient governance, management and administration of commerce, industry and public affairs and the development of secretaryship of organisations through education and the dissemination of information. Our members therefore possess extensive knowledge of administration, governance and regulatory frameworks in the NFP and charity sector to support our comments in this submission.

While Governance Institute applies fringe benefits tax (FBT) concessions, our use of them is minimal. Indeed, in the interest of transparency, we can declare that we paid fringe benefits tax at the effective rate of 51.3% on the total cost of our entertainment expense in the FBT year ended 31 March 2015. Governance Institute paid a total of $10,146 in fringe benefits tax. In addition, its employees paid $26,789 in fringe benefits tax on their fringe benefits.

Our comments therefore do not stem from any desire to ‘protect’ the concessions for our use, but derive from our extensive knowledge of the NFP sector, its regulatory framework and how that regulatory framework has been developed in order to support the aims of the sector. We have been significant contributors to the development of the regulatory framework for the NFP sector over many years and have deep expertise in relation to the public policy underpinning that framework. Our comments stem from this authority.

General comments

Our members agree with the view that the NFP sector is well overdue for tax reform[1]. However, as always, the public good should guide the public policy position — public good outcomes should be the basis on which reform proceeds. However, Governance Institute is strongly of the view that overarching tax reform for the NFP sector is preferable, rather than the piecemeal approach evident in the exposure draft of the Tax and Superannuation Laws Amendment (2015 Measures No. #) Bill 2015.

Any reform to tax affecting the NFP sector needs to take account of the impact of proposed reform across the sector. Governance Institute is of the view that this bill does not take account of this larger impact, but is targeting one aspect of tax reform in isolation.

Moreover, we are deeply concerned that the proposed legislative reform takes a 'one-size-fits-all' approach by considering fringe benefit tax (FBT) concessions in the NFP sector within a narrow context, rather than fully explaining that these tax concessions were introduced at different times to fulfil different policy objectives.

Governance Institute strongly supports appropriate tax concessions for the sector that effectively assist the sector to fulfil its role. We are not opposed to either simplification or change to the public policy concerning tax concessions, but **recommend strongly** that any reform must be made on the basis of:

- supporting the sector to achieve its outcomes, which are of benefit socially and economically to society
- not hindering the sector to achieve its outcomes, with a commensurate decline in benefit to society
- making the policy and procedures attached to the policy more equitable and efficient.

However, the Tax and Superannuation Laws Amendment (2015 Measures No. #) Bill 2015 has been introduced to address particular and limited instances of abuse of the FBT concessions, without consideration for how the application of the proposed reform will affect the majority of the NFP sector.

Moreover, we have strong concerns that the bill is unlikely to address the very abuse the government contends has generated the need for legislative reform.

The bill introduces a single grossed-up cap of $5,000 for salary packaged meal entertainment and entertainment facility leasing expense benefits for employees of employers able to access a general FBT exemption or rebate. We note that the proposed reform does not take account of the fact that hospital employees, such as doctors and nurses, may work in multiple hospitals — these employees were singled out in the *Re:think — Tax discussion paper* issued in March 2015.[2] Therefore, employees with more than one employer can continue to receive benefits with multiple caps.

Despite the bill not addressing the abuse the government was keen to stop, it will have a punitive effect on the entire NFP sector — the consequences for the sector as a whole have not

[1] Senator Arthur Sinodinos, 'Integrity restored to Australia's taxation system', Media Release, No. 8, 14 December 2013

[2] Maher, S, in 'Budget 2015: Coalition tackles fringe benefits tax loophole', *The Australian*, 7 May 2015 states that: 'Two years ago Treasury warned about the "illegitimate" use of a fringe benefits tax exemption for entertainment and meals by hospital employees'.

been considered, given that the bill seeks to target particular instances of abuse of the concessions without consideration for the impact of the proposed reform across the sector.

We strongly recommend that before the bill proceeds, the government should conduct targeted consultation with the NFP sector in relation to not just this proposed reform but also in order to canvass overarching tax reform proposals, based on an informed and holistic view of the impacts and outcomes on the sector. This would include consideration of FBT concessions. Stakeholder roundtables will assist in securing all views to ensure that any unintended consequences have been considered and avoided.

Governance Institute opposes the bill, as no such consultation with the NFP sector has been undertaken and the consequences for the NFP sector as a whole have not been considered. We also oppose the bill because it is unlikely to address the very abuse the government contends has generated the need for legislative reform, while causing significant negative impact on the entire NFP sector.

Background to FBT concessions in the NFP sector

It is worth revisiting the public policy rationale for introducing the FBT concessions in relation to the NFP sector.

The explanatory memorandum quotes from the Productivity Commission report on the NFP sector[3] as follows:

> The meal entertainment exemption for public and NFP hospitals was originally introduced because of the difficulty of accounting for the provision of meals to hospital employees when most hospitals had a subsidised staff canteen. However, in recent years it appears that the use of these concessions has grown much wider than the original intent. The salary packaging providers are actively promoting the use of meal entertainment cards for dining and holidays – domestic and overseas …

However, this is not a full explanation of why FBT concessions were introduced for the NFP sector and it is not correct to suggest that this is the only rationale for their existence.

FBT concessions were introduced as NFP organisations could not afford to recruit and retain employees at the same level as for-profit or government organisations.[4] NFP organisations were offered the tax concession as a means of attracting a competent labour force and to alleviate to some degree the wage disparity between commercial, 'market-based' remuneration and the wages offered in the NFP sector. This wage disparity has only continued to grow, thus any benefit that can assist in limiting the disparity must still be offered. This issue has not abated. The Productivity Commission report also noted that:

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[3] Productivity Commission, *Contribution of the Not-for-profit Sector*, January 2010, http://www.pc.gov.au/inquiries/completed/not-for-profit

[4] The Hon Frydenberg, J, MP, Opinion piece, 'Fairness extends even to charity', *The Australian*, 7 May 2015, states: 'The public policy rationale is that these concessions enable the not-for-profit sector to attract high-quality staff without having to match the high salaries that may be offered in the private -sector.' Department of Treasury, *Re:think — Tax discussion paper,* states that*:* 'A range of NFP entities are exempt from paying tax on fringe benefits provided to employees up to a monetary limit per employee (either $17,000 or $30,000 for certain NFPs, excluding the temporary increase associated with the Temporary Budget Repair Levy) or are entitled to a rebate. By utilising salary sacrificing arrangements, the cost of labour to these NFPs is reduced. This lower cost could be used by the NFP to offer employees a higher salary, providing them with an advantage in hiring and retaining staff.'

> For NFPs, less than full cost funding of many services has resulted in substantial wage gaps for NFP staff. The challenges in retaining staff threaten the sustainability and quality of services.[5]

The rationale of attracting people with the right skills to work for NFP organisations continues to justify the FBT concession. The focus on good governance in the NFP sector further emphasises the need to attract suitably skilled employees.

Impact of proposed bill on NFP sector

The provision of salary packaging is a fundamental employee benefit offered across the NFP sector.

Exempt benefits are an accepted component of salary packaging arrangements across the NFP sector, and the possible 'capping' of such benefits will cause economic hardship to employees, many of whom are acknowledged as receiving relatively poor remuneration for their work. For example, the retention of FBT concessions for NFP disability organisations will be critical to the success of the National Disability Insurance Scheme (NDIS). The bulk of people who work in the disability sector (along with aged care, child care and welfare services) are staff with few or no formal qualifications. They are responsible for providing personal care and support to the most vulnerable in Australia, and generally the work is hard and poorly remunerated.

Those working in the disability sector see salary packaging as a key component of their recruitment, remuneration and retention incentives, because the direct financial benefits are highly valued. At a time when more staff will be required as the demand for services grows with the introduction of NDIS, Governance Institute shares the deep concern of those in the disability sector that the loss of the added benefits associated with salary packaging will place acute pressure on a sector which already struggles to recruit and retain employees.

Furthermore, it will have a significant impact on the capacity of NFP organisations to recruit and retain staff across the entire sector, as those working in particular support roles such as business services, HR, finance and legal services will no longer be able to utilise the FBT concessions to seek to achieve some parity with for-profit and government salaries.

Based on feedback from our members working in the NFP sector, it is clear that participation rates in these benefits have been steadily increasing over the last few years, and the average expenditure on these benefits has also been rising.

Yet the bill is predicated on an assumption that only those receiving higher wages are in receipt of such benefits. There is no analysis provided in the explanatory memorandum of the effect of the proposed changes on those receiving lower wages, which is likely to be the majority of employees in the NFP sector. We stress again that, without consultation with the NFP sector, the assumptions underpinning the bill are questionable, as they have not been informed by knowledge of practice within the sector.

Furthermore, the bill provides that the benefit will be reportable. This will have significant impact on those on lower salaries, as follows:

- when an employee's income tax return is lodged it will include the grossed-up cap on the Payment Summary
- as a result, this amount will be included in the calculation of HELP Debt Repayment Levies, some child support arrangements, and potentially Family Tax Benefit A & B.

This will mean that staff on low salaries will be negatively affected twice.

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[5] xxiv

Conclusion

Governance Institute strongly supports the important and intrinsic role that the NFP sector plays in Australian society. Our members are of the opinion that FBT concessions for the NFP sector are integral to the continuation of the provision of these substantial social and economic benefits. In particular the FBT exemptions/rebates that facilitate salary packaging will continue to be crucial in the attraction and retention of staff and any reduction would add to the increasing workforce pressures and related wage negotiations.

The Productivity Commission Research Report: Contribution of the Not-for-Profit Sector sets out its social impact compellingly:

> Community (not-for-profit) organisations play an important role in combating social exclusion and enhancing the economic, social, cultural and environmental wellbeing of society.[6]
>
> Many do not operate in the market (or economic) sector, and only a relatively small number (around 20 000), mainly in the human services area, rely heavily on government as their main source of funding. NFPs deliver services to their members, to their clients or to the community more broadly, such as welfare, education, sports, arts, worship, culture and emergency services. Some NFPs build or maintain community endowments such as biodiversity, cultural heritage and artistic creations. Some engage in educative, advocacy and political activities, while for others the focus is on activities that create fellowship. Many offer their participants opportunities to build a sense of self worth and for connection and influence that form an important part of the foundations of an active civil society.[7]

Any changes to FBT concessions would affect the sector's capacity to serve the community in future years, given the negative impacts the bill will have on recruitment, remuneration and retention incentives. Governance Institute is of the belief that it is short-sighted to remove FBT concessions to the NFP sector in order to penalise those few that might have misused the system to their advantage. Moreover, it is not clear that the 'one-size-fits-all' approach set out in the bill will address the abuses that have raised concern. Where there are loopholes in the current tax arrangements that are being abused, those loopholes should be addressed rather than removing tax concessions for the NFP sector as a whole.

For the reasons set out in this submission, Governance Institute opposes the bill.

We recommend that alternatives be considered, rather than restricting access to the FBT concessions by all employees, with commensurate impact on recruitment such as:

- the threshold is applied on an annual basis to individuals, irrespective of the number of employers
- apply indexation to the threshold limits (whatever the threshold limits are) — the 'real value' of the concessions has been eroded over the years as no indexing has occurred
- introduce a rebate which can be claimed on the tax return of those on lower incomes.

Another alternative that could be considered is to revise the grossed-up annual limit to $13,000, which would reduce the negative impact on those on lower salaries in the NFP sector.

We further recommend that stakeholder consultation in the form of roundtables take place before the bill proceeds. Any proposals arising from that consultation should be released as

[6] Ibid, p iv

[7], Ibid, p xxv

consultation papers, to provide the opportunity for the sector to consider how each proposal would be implemented.

Yours sincerely

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