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Commissioners Jonathan Coppel and Paul Lindwall  
Remote Area Tax Concessions and Payments Study  
Productivity Commission  
GPO Box 1428  
Canberra City ACT 2601

**DEPARTMENT OF DEFENCE: RESPONSES TO THE PRODUCTIVITY  
COMMISSION'S DRAFT REPORT ON REMOTE AREA TAX CONCESSIONS AND  
PAYMENTS**

Defence thanks the Productivity Commission for the opportunity to comment on the draft report on Remote Area Tax Concessions and Payments released in August 2019.

Defence has a constant and strong presence in remote and regional Australia. Having a strong, ongoing military presence in these regions is critical if Defence is to meet the needs as expressed in the 2016 Defence White Paper and provide for the national security of Australia and its national interests.<sup>1</sup> Any changes to tax law should be weighed against a range of direct and indirect consequences, in this case consideration should be given to maintaining operational capability and the ability for Defence to defend Australia and its national interests. This should include consideration of:

- The financial impact to the Department from increased Fringe Benefits Tax (FBT) payable.
- The financial impact to personnel arising from increased Reportable Fringe Benefits Amount (RFBA) and decreased transfer payments.

Defence provides below a response on the expected impact to Defence and Defence personnel as a result of draft recommendations 5.1, 8.1, 8.2 and 8.3 made by the Productivity Commission.

The impact assessment is based on the current list of remote locations. We note the Productivity Commission has recommended reviewing the locations eligible for the concessions and payments. Further consultation would be welcome should such locations change.

There are three different classes of personnel considered: 1) "ADF members" comprise members of the Navy, Army and RAAF; 2) "APS employees" are Australian Public Service employees of the Department of Defence; and 3) "ASD officials" are employees of the Australian Signals Directorate (ASD).

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<sup>1</sup> See: Commonwealth of Australia, '2016 Defence White Paper' <https://www.defence.gov.au/whitepaper/Docs/2016-Defence-White-Paper.pdf>; Defence Portfolio, 'Portfolio Budget Statements 2019-20' [https://www.defence.gov.au/Budget/19-20/2019-20\\_Defence\\_PBS\\_00\\_Complete.pdf](https://www.defence.gov.au/Budget/19-20/2019-20_Defence_PBS_00_Complete.pdf)

## **Responses and Comments to Draft Recommendations made by the Productivity Commission**

In summary, legislating the current draft recommendations would have a significant impact on Defence personnel. The result would be decreased net cash in hand to personnel due to increased RFBA and decreased transfer payments (such as Family Tax Benefit payments), and removal of the Zone Tax Offset and Overseas Forces Tax Offset. It is anticipated that this would reduce the ability for Defence and ASD to attract and retain personnel capability in critical remote and rural regions within Australia.

Furthermore, legislating the current draft recommendations would be expected to result in an increased FBT cost to Defence and ASD. To the extent this is not supplemented, this would be anticipated to result in reduced capability for Defence and ASD to deliver upon their outcomes.

### **DRAFT RECOMMENDATION 5.1 ABOLISH ZONE AND OVERSEAS FORCES TAX OFFSETS**

The Australian Government should abolish the zone tax offset and the overseas forces tax offset.

Defence does not support this draft recommendation. While the Zone Tax Offset and Overseas Forces Tax Offset are currently of limited monetary value, any adjustment to benefits for ADF personnel should only be considered within a holistic review of tax concessions provided to ADF members in remote areas and on Foreign Service.

The Zone and Overseas Forces Tax Offsets are important to Defence because they compensate Defence personnel for the additional costs and hardship experienced in remote locations and uncongenial overseas service.

Removal of the Zone Tax Offset would affect a significant number of Defence personnel. In the 2019 financial year 22,114 Defence personnel resided in Zone Tax Offset eligible locations. 10,428 personnel would have been eligible for the full tax offset, and those not eligible for the full amount may have been eligible for a partial tax offset.

The 1993 Conditions of Service Framework set by Cabinet recognised that the Overseas Forces Tax Offset was an appropriate mechanism for providing a tax offset for uncongenial service overseas where the service does not satisfy the definition of 'warlike service', which attracts the full tax exemption under section 23AD of the *Income Tax Assessment Act 1936*.

The removal of the Overseas Forces Tax Offset does not appear to be in line with the decisions under the 1993 Conditions of Service Framework.

While the current number of ADF members receiving the Overseas Forces Tax Offset is less than 50 personnel per year it is noted that eligibility to the Overseas Forces Tax Offset only arises where the individual is not eligible for an income tax exemption under sections 23AG or 23AD of the *Income Tax Assessment Act 1936*. Accordingly, any adjustment to tax exemptions made under section 23AG or 23AD of the *Income Tax Assessment Act 1936* may significantly increase the number of personnel that would be eligible for the Overseas Forces Tax Offset.



There would be no direct cost to Defence or ASD as a result of these proposed changes to the Zone Tax Offset or the Overseas Forces Tax Offset as the transfer payment is made by the Australian Taxation Office. However any reduction in ability to attract and retain personnel in remote locations as a result of the loss of these offsets may result in higher costs to Defence and ASD to compensate personnel.

Minor increases in administration costs are expected to arise for Defence or ASD should recommendation 5.1 be implemented.

DRAFT	RECOMMENDATION	8.1	TIGHTEN	TAX	TREATMENT	OF
<b>EMPLOYER-PROVIDED HOUSING</b>						

The Australian Government should amend the *Fringe Benefits Tax Assessment Act 1986* (Cth) to change the tax treatment of employer-provided housing. Specifically, it should:

- revert the exemption for employer-provided housing (section 58ZC) to a 50 per cent concession (as it was prior to 2000)
- remove the provision that enables employers to claim the concession because it is 'customary' to provide housing (section 58ZC(2)(d)(iii))
- remove the provision that extends the concession to additional areas for 'certain regional employers' (section 140(1A)).

Defence does not support this draft recommendation. The increased RFBA impact for personnel and increased FBT payable for Defence may make it difficult for Defence to attract and retain ADF personnel to remote locations.

The ability to provide housing for ADF members who are posted to remote locations is key to fulfilling the capability requirements of Defence. ADF members are directed to reside and work in remote locations where the supply of appropriate housing may be limited and costs are higher. The intervention of Defence to increase the affordability of remote area housing is essential to attracting and retaining ADF members to remote areas and maintaining a mobile work force.

APS employees and ASD officials may also be provided with housing, particularly when posted or living away from home.

This recommendation, if implemented, is anticipated to result in an increased RFBA to APS employees and ASD officials. No RFBA impact is anticipated for ADF members to the extent that there are no changes to the RFBA exclusions in the *Fringe Benefits Tax Assessment Regulations 2018*. The imposition of an FBT cost to employers and RFBA to employees will result in much higher costs to support personnel in remote locations.

However, to the extent the *Fringe Benefits Tax Assessment Regulations 2018* exclusion is amended, an RFBA impact may arise for ADF members. This would be a significant change to current policy with serious financial consequences for ADF members and to the ability of Defence to attract and retain personnel in remote areas. Due to the broad implications of such a change it is strongly recommended that this exclusion not be removed.

Recommendation 8.1, if agreed, is anticipated to result in an increased FBT cost to Defence and ASD for posting personnel to remote locations.



Increased administration costs are expected for Defence and ASD primarily as a result of valuations required for remote area properties, as well as updating processes and communicating with affected personnel.

<b>DRAFT RECOMMENDATION</b>	<b>8.2</b>	<b>REMOVE CONCESSION FOR</b>
<b>EMPLOYEE-SOURCED HOUSING</b>		

The Australian Government should amend the *Fringe Benefits Tax Assessment Act 1986* (Cth) to remove the 50 per cent concession on employee-sourced housing (section 60).

Defence does not support this draft recommendation. The increased RFBA impact for personnel and increased FBT payable for Defence may make it difficult for Defence to attract and retain ADF personnel to remote locations.

Defence Home Ownership Assistance Scheme (DHOAS) loan subsidies assist current and former ADF members to achieve home ownership. This is provided in order to improve ADF recruitment and retention.

Personnel may receive an RFBA on the taxable value of their DHOAS loan subsidies received. Implementation of recommendation 8.2 would result in increased RFBA for both current and former serving ADF members who receive DHOAS loan subsidies for homes purchased in a remote location. This would undermine the aims of DHOAS loans of improving ADF recruitment and retention.

It is noted that eligibility for DHOAS loan subsidies arises due to ADF service, therefore APS employees and ASD officials would not be affected.

Recommendation 8.2 would result in additional FBT costs to Defence in respect of DHOAS loan subsidies.

Increased administration costs are expected for Defence and ASD from recommendation 8.2 as a result of updating processes and communicating with affected personnel.

<b>DRAFT RECOMMENDATION</b>	<b>8.3</b>	<b>TIGHTEN TAX TREATMENT OF OTHER</b>
<b>GOODS AND SERVICES</b>		

The Australian Government should amend the *Fringe Benefits Tax Assessment Act 1986* (Cth) to change the tax treatment of residential fuel, meals for primary production employees, and holiday transport provided by employers in remote areas. Specifically, it should:

- limit access to the residential fuel concession for use in conjunction with employer-provided housing (section 59(1)) to instances where there is an operational requirement for the employer to provide residential fuel
- remove the residential fuel concession for use in conjunction with employee-sourced housing (section 59(2) and (3))
- limit access to the exemption that currently applies to meals for primary production employees (section 58ZD) to instances where there is an operational requirement for the employer to provide these meals
- remove the definition limiting the exemption to meals 'ready for consumption', as it leads to ambiguity and difficulty in implementation
- remove the holiday transport concession (section 60A and section 61).

Defence does not support this draft recommendation. The increased RFBA impact for personnel and increased FBT payable for Defence may increase the difficulty for Defence and ASD to attract and retain personnel to remote locations.

Defence personnel posted to remote locations are geographically disconnected from their usual family and social support networks. Provision of transport, including for reunion with their families and access to health care and facilities in urban centres is important to the wellbeing of Defence's workforce and is key to attracting and retaining personnel to remote areas.

Subsection 5E(3)(j) of the Fringe Benefits Tax Assessment Act 1986 currently provides an RFBA exclusion for all personnel (ADF, APS, and ASD) where travel is to a major population centre. If this RFBA exclusion remains, the impact of increased RFBA for Defence personnel will be limited to travel outside of major population centres.

Draft recommendation 8.3, if agreed, is anticipated to result in an increased FBT payable for Defence and ASD.

Further, higher administration costs are expected for Defence and ASD from updating processes.

Defence thanks the Productivity Commission for the opportunity to be involved in this consultation process. We would welcome the opportunity to further discuss our comments on the draft recommendations.

Yours sincerely

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