

FBT audits on the rise

The ATO is stepping up fringe benefits tax (FBT) audit and compliance activities. What are your FBT obligations?

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The ATO has continued to ramp up its FBT compliance and audit activities. For employers, this is a clear warning to review your FBT obligations sooner rather than later. The level of FBT compliance activity we are seeing is unprecedented. In the lead-up to the end of the 2011 FBT year, employers need to be aware of the current and planned ATO activities.

FBT is often faced with neglect – this is due to real or perceived complexity, priority of tax issues and a long-held belief that FBT audits do not exist. This article reviews the key findings released by the ATO and key focus areas. In light of this unprecedented ATO activity, we highlight some areas for consideration in planning the 2011 FBT return preparation.

KEY ATO FINDINGS

The initial findings from the ATO's early risk work found that 70 per cent of taxpayers were non compliant. The ATO was strongly encouraged by these results and undertook a pilot project focused on employers who have lapsed in their FBT lodgements. The aim was to establish the extent to which employers were continuing to employ staff and provide benefits but were no longer lodging a FBT return. The ATO described this as dropping-out of the FBT system. The results from the pilot established that more than 50 per cent of employers contacted had continued to provide benefits and had an obligation to lodge. Given the low level of compliance, the ATO expanded the compliance focus in this area.

In the next phase, following the pilot, 330 employers were contacted directly or through their tax agent. More extensive questioning was employed including specific questions on cars and employee contributions. From this, it was found that 228 employers (69 per cent) agreed that they had an obligation to lodge and made an undertaking to do so. A further 11 per cent confirmed that

they did not have an obligation to lodge a FBT return. The remaining 20 per cent were uncontactable and the ATO will pursue them.

Among other things, these results proved a decline in compliance was due to a major failure by employers to report car fringe benefits.

LIVING AWAY FROM HOME

The ATO has made it clear that the living-away-from-home allowance (LAFHA) will be a significant focus, and there is an intention to pursue a number of cases.

Businesses often struggle with maintaining a consistently compliant process for LAFHA. The rules are difficult to understand or, where there is a perceived understanding of the rules, businesses are often confronted with challenges in the practical application. Commercially-driven objectives can get in the way of the law.

There seems to be a view within the ATO that there is widespread abuse of the living-away-from-home concession treatment. With the ongoing requirement to disclose gross LAFHAs on the FBT return form, this provides good visibility to the ATO on the extent of the perceived problem.

Therefore, it is advisable to review your policies against the practical application. Often the watching brief on LAFHAs is unclear and the responsibility or accountability falls between the human resources, payroll and tax groups. It is important to allocate the responsibility and ensure the appropriate level of support is provided to ensure compliance.

CARS AND FBT: DRIVEN TO NON-COMPLIANCE

Cars have been at the centre of the compliance activities. The focus on cars has broadly been on luxury cars, cars with high business use, logbooks and exempt vehicles (or a combination of the aforementioned). Particular areas where non-compliance has

been detected include:

- > Luxury cars with a high business use percentage
- > Cars garaged at home
- > Record-keeping requirements (eg odometer readings, log books, purchase documentation, calculation of cost price, maintenance and running cost records)
- > Determination of the business use percentage
- > Basic errors in calculating the liability
- > Employee declarations to substantiate employee paid costs
- > Correctly complying with the GST and income tax obligations associated with employee contributions
- > Incorrect application of the luxury car threshold in determining the deemed interest and depreciation for the operating cost method.

Data matching against state road authority records, questionnaires and compliance verification have been the key methods undertaken in the focus on cars.

HIGH FAILURE RATE

The ATO has had a strong focus on employee contributions for a number of years and more recently the net has widened significantly. Based on the earlier work undertaken by the ATO it was clear that employers struggle with the back-office compliance duties required by the contribution method. These struggles brought audit success for the ATO and once again, the ATO was encouraged to broaden its focus.

The ATO focus is to determine whether the income tax and GST obligations have been correctly fulfilled. Simple data matching between the FBT return and the income tax return provides the ATO with verification targets. As acknowledged by the ATO, in many cases the correct amount of income tax has been paid. However, due to the employer inadvertently not using the correct

label, the employer has been selected for further follow-up.

MINOR BENEFITS

With an increased threshold of \$300 per head per employee (extended to associates as well), employers have had a keen interest on the practical application versus the technical greyness. So has the ATO.

The ATO is reviewing a large entity's FBT treatment of corporate box facility hire, together with the meal entertainment provided at the same time. It appears that the entity has claimed the minor benefit exemption separately in respect of both the corporate box hire and the related food and drink cost.

The ATO considers that while the per head

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cost is less than \$300 per head for each benefit category, the benefits are associated and therefore the minor benefit exemption may not apply.

Most would agree that the practical application of the minor benefits exemption remains nothing short of an FBT mystery, shrouded in uncertainty and clouded by the lack of commercial guidance for businesses.

While at an individual employee level the amounts involved are small, across all employees (and their spouse and family if applicable) of an organisation and over a period of time, the dollars involved usually become significant. This fact is not lost on the ATO. We watch developments with interest.

FBT YEAR-END MATTERS

With the FBT year-end fast approaching some serious planning and preparation prior to 31 March is required. Here are some suggestions:

- > To fail to plan is to plan to fail...the nature of FBT is a myriad of data sources, internal and external, requiring tenacity and the ability to ask the right questions. This is quickly followed by valuation challenges. Therefore, understand what your likely valuation choices will be – depending on the data that is available, you might not have to make a choice
- > Prepare a high level project plan including timeline – plan for contingencies
- > Identify the people who are required to be responsible and ensure you get their buy-in and agreement to the process by allocating specific responsibilities to them (preferably in writing!)
- > While it will vary from business to business, logically the people involved would include representatives from finance, tax, payroll, purchasing, human resources, sales and

marketing, sponsorships and events, facilities management and fleet management. By involving these people, this should go some way to reducing what may be the biggest key FBT risk: It's not what's in the FBT return that's the problem, it's what's not in the return that's the problem"

- > Really focus on the key benefits and big-ticket benefit items in your business – get those right and you're a long way down the track
- > Will the review/sign-off be done internally or externally? Either way, check the relevant people are available, understand their expectations and communicate your own expectations
- > What were the tricky issues in last year's return/s? An issue can

be technical, logistical, accounting or systems-based or just plain in the too-hard, deal-with-it-next-year basket

> Are there any carried forward items from last year's FBT return that need to be considered for this year's FBT. These may include deposits paid for events held in the 2011 FBT year, employee contributions rolled forward from the 2010 FBT year or prepaid corporate box hire straddling two FBT years

> Finally, are there any new benefits?

If real concerns exist at the end of the initial planning phase, whether they be lack of appropriate resourcing or prior year technical treatment issues, escalate your concerns and don't try to go it alone. FBT is an issue for the business and needs to be managed appropriately.

CONCLUSION

Have a think about the benefits provided in your organisation and consider the potential risk, not just from the ATO focus areas but more importantly from internal challenges if you believe the compliance is questionable.

Based on the findings, it appears that the ATO is identifying a high rate of non-compliance in a number of areas. The focus on FBT will continue. What will be of interest and probably concern for employers is the future strategies the ATO will employ in relation to cars, LAFHA, car parking, entertainment, minor benefits and other benefits. The ATO has experienced enough upside to further develop compliance strategies throughout 2011. ☺

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