

A Suggestion for Fringe Benefit Tax Changes for Public Transport Tickets

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This document proposes creating a general exemption to FBT for seasonal public transport tickets to replace several specific exemptions which exist in the current FBT legislation.

The Hon Chris Bowen MP (Assistant Treasurer) has already forwarded an early draft of this proposal to the Review Panel for consideration. This document expands on the problem which prompted the proposal, discusses alternate solutions and provides some vague economic arguments to promote the proposed legislative change.

Table 1: Proposed Replacement for Paragraphs 1 and 1A of Fringe Benefits Tax Act of 1986 Clause 47

(1) "Where:

- a) in respect of the employment of a current employee, the employer, or an associate of the employer, provides a residual benefit to the employee that consists of free access to use public transport for a period of time;
- b) the employee uses the free access to travel between places at which the employee performs duties of that employment;

the benefit is an exempt benefit."

1 Quotes

The committee recommends that the Australian Government review the current FBT concessions . . . extending incentives to other modes of transport.

- Transport Recommendation 8,
Senate Inquiry into Sustainable Cities, 2005
Chapter 5, Paragraph 79.

Overseas experience has shown major benefits from Federal assistance to public transport.

- Professor Graham Currie
Institute of Transport Studies
Monash University

Microsoft has a worldwide goal to reduce its carbon emission intensity by 30% by 2012 (on 2007 levels) and to help our customers, partners and staff reduce their environmental impacts. A significant portion (about 10%) of our local carbon footprint is from staff commuting in private vehicles. We are seeking ways to encourage alternative commute methods - particularly greater use of public transport - that would result in lower carbon impacts, improved productivity and higher quality of life for our employees. Tax incentives are an important factor that could stimulate greater take-up of public transport by our staff.

- Sarah Hatcher,
Environment & Sustainability Director,
Microsoft

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2 Background

I run a small company with employees going to several different sites and I've noticed an incongruity in the Australian tax legislation which is penalising public transport over private transport.

- If I pay for an employee to take a taxi to a client's office in the CBD every morning and afternoon, there's no question that that is a valid business expense.
- I could also choose to pay for train tickets back and forth each day. In Sydney at least, this would be more expensive than paying for a weekly travel pass.
- But, if I pay for the worker's travel pass, **it is regarded as a fringe benefit**, since they could also use it for personal use and there is tax to pay for it – or at least the need to consider FBT implications.

Obviously, this is a problem since the most cost-effective option (and the most economically efficient for all parties) suffers not only a tax burden, but also a special reporting burden.

The problem is particularly acute in Brisbane, where almost all public transport tickets are for a period of time rather than a particular distance or journey.

3 Proposed Amendment

Currently, Part III (Fringe Benefits), Division 12 (Residual Fringe Benefits), Section 47 paragraphs 1 and 1A grant a fringe benefit exemption to a few small classes of employees¹:

- Railway workers, bus drivers and the like who will obviously end up making free use of the public transport network.
- Employees of companies doing work which is related to public transport; for example, workers who test-drive new diesel train engines.

¹The full text is quoted on page 12.

- Police workers, who have the right to catch any method of transport in order to police crime on-board.

Teachers are not mentioned explicitly as having an FBT exemption even though they have the right to travel on school buses from home to work for free. This is perhaps because of the challenges involved in placing a monetary value of travelling in a crowded bus surrounded by schoolchildren early in the morning!

Paragraphs 1 and 1A of Section 47 cover less than two pages, and so are not particularly convoluted by the standards of tax legislation worldwide. But I propose that the two clauses be deleted, and replaced by the much simpler text on page 1.

This amended paragraph covers the existing conditions, is simpler to understand and also solves the problem of employees using public transport within the work-day which I outlined in section 2:

- Railway workers, bus drivers and police workers most certainly perform duties in several locations, so their free access to public transport is still exempt.
- Employees who travel between customer sites and who hold a seasonal ticket to do so are exempt from FBT.

But is the resulting legislation too broad? Could we solve the problem any other way? Is it going to be expensive? I have attempted to discuss this in sections 4 to 8.

4 Implications – what would this legislation change do?

The effect of the legislative amendment on page 1 would be to encourage employers to supply seasonal tickets to their staff because it would be cheaper to do so than it is at the moment.

Staff could have a quarterly or yearly universal public transport pass bundled in as part of their salary (for example) as long as they could demonstrate that as part of their job they sometimes had to leave their normal place of work and go somewhere else.

This is not a very difficult requirement to meet. I suspect there will be employers who would even game the system by occasionally requiring fixed-location workers (who otherwise would not have travel needs) to leave the office and go somewhere a few times per year.

So the *real* effect of this legislation is that salary sacrificing seasonal public transport tickets would be on a level playing field with the salary sacrificing of cars.

This implements recommendation 5.8 of the Senate Committee Inquiry into Sustainable Cities (2005), which suggested extending tax concessions to encourage public transport use.

Worldwide, legislation of this sort is not usual. When I was working in Zürich (Switzerland), employer contributions towards the cost of an annual public transport pass were quite common and were deductible. There are also many examples of USA-based companies providing these kinds of passes and receiving full deductions for doing so, which is all the more remarkable for the lack of public transport in most parts of the USA!

5 What the Assistant Treasurer Said

The Hon Chris Bowen MP (Assistant Treasurer and Minister for Competition Policy and Consumer Affairs) responded to the issues outlined in section 2. He concisely described the goals of the FBT system:

It places employees with access to fringe benefits on a more even footing with whose remuneration consists entirely of salary or wages... The FBT system also facilitates including fringe benefits in an employee's income for means testing benefits such as family tax benefit... While I appreciate that there would be compliance benefits from exempting public transport passes from FBT, this should be balanced against the need to provide equitable outcomes for employees.

Summarising, if seasonal public transport tickets were to be made FBT-exempt we need to make sure that:

1. Employees should have a measure of equity in their access to such an exemption.

Principle	How it is met
Equitable access	Almost all employees would be eligible.
Higher-income hiding	Natural ceiling
Preferential support for lower incomes	Public transport used more by lower incomes

Table 2: Assessing the proposed amendment against the FBT exemption principles

2. Higher-income individuals and families should not be able to use seasonal public transport tickets as a way to hide income.
3. Lower-income individuals and families need to be given more access to government support rather than less.

I think the proposed legislation meets these criteria, and have summarised them in table 2 on page 7.

- The exemption would be open to all employees and employers, which would be an improvement over the current system in which a few occupations have access to exemptions. The criterion for accessing the exemption (that the employee has to travel between different places as part of their employment) is not a hard one to meet, and would apply to almost all workers.
- The exemption is not a particularly effective tax avoidance tool, since no-one can make use of more than one universal annual travel pass per year.
- According to the NSW Council on Social Services² and many other studies, public transport is used more by lower-income individuals. Opening up a tax exemption on public transport tickets is therefore progressive and disproportionately benefits the poor, unlike almost all other kinds of fringe benefits exemption.

²NSW Council on Social Services 2006, Who uses Public Transport: Quantifying Low Income Public Transport Use in Greater Metropolitan Sydney

6 Alternate Solutions – Why They Won't Work

The Hon Mr Bowen made several suggestions on avoiding the FBT liability on time-based public transport tickets under the current legislation.

... the FBT system allows employers to seek declarations from employees that the travel pass has not been used privately. . . Alternatively, employers could require that all public transport passes be kept on the business premises and only issued for business related travel (to be returned after travel has been completed).

I was extremely flattered to receive a considered response from the Hon Mr Bowen and feel extremely guilty about now explaining why neither of these solutions is economically efficient nor desirable.

A flow chart working through all possibilities is in figure 1 on page 9.

Briefly, if employees need to declare that they will not use an employer-supplied travel pass for private use, then this is rewarding people who do not normally use public transport and causes a kind of double payment event to occur for those that do.

On the other option, many cities' public transport ticketing systems explicitly state that long-term passes are non-transferable and cannot be "handed out" to employees in the same way that keys to car from a car pool can be handed out.

7 Financing

If the FBT amendment I proposed in on page 1 is enacted:

- **Employers** would be more likely to buy an expensive multi-region pass to save on administrative costs. This would still be cheaper (for the employer) than compensating an employee with a higher salary to pay for their own commuting.

Both the employer and employee stand to benefit from this.

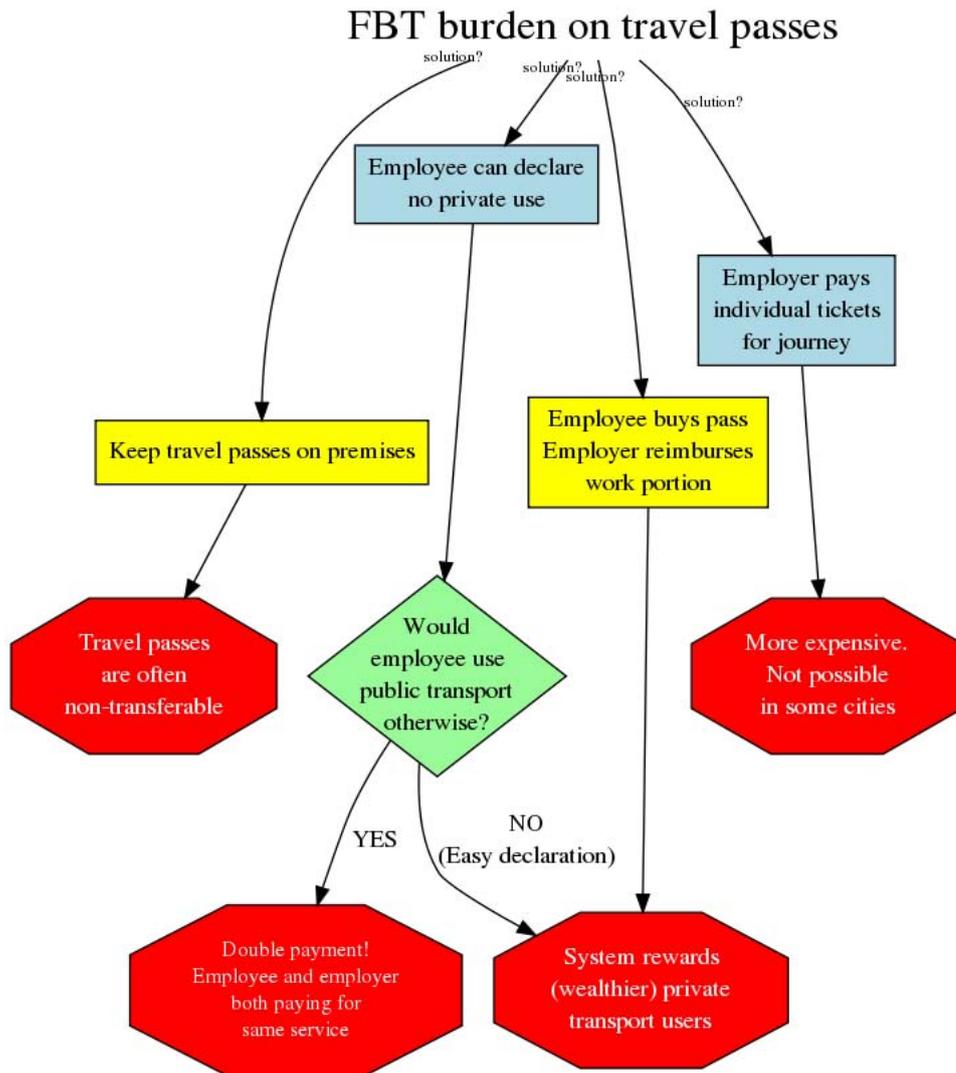


Figure 1: Flow chart of problems with maintaining the current legislation

- The relevant **state governments** would benefit from the more expensive ticket sales (and the lower costs associated with lower volumes of sales).
- Under the proposed FBT legislation employers would be opting to send extra money to support their local state-based public transport infrastructure directly while reducing their federal taxes. The amount of this directed support is very simple to measure – for example, by auditing high value ticket sales.

The **federal government** can compensate for the resulting loss of tax revenue in the remittances given by the federal government to the states.

8 Further Economic Arguments

Odlyzko and Levinson wrote³:

(Outside of peak periods) charging fares still discourages demand, but as there are no added marginal costs with the extra passenger, this reduces total welfare. Many transit systems in the early 21st century are in this situation... In response, many agencies sell “season passes”... Season tickets in Zürich increased bus passenger trips by 4.5 per cent, while in other Swiss cities, the increase was as large as 16 percent (FitzRoy & Smith 1999).

Encouraging the use of long-term public transport tickets is likely to be a net economic gain. Employees who benefit from the public transport FBT exemption would grow used to the idea of catching public transport at off-peak times (after all, they are being encouraged to do that by their employer, and it is a no-cost journey on their own time). This will improve utilisation of off-peak public transport, reduce greenhouse gas emissions and reduce car ownership and fossil fuel dependency⁴.

³**Too expensive to meter: The influence of transaction costs in transportation and communication**, David Levinson and Andrew Odlyzko. *Phil. Trans. Royal Soc. A*, vol. 366, no. 1872, 2008, pp. 2033-2046.

⁴**Pre-commitment and usage: season tickets, cars and travel**, Axhausen, K., Simma, A. & Golob, T. *European Research in Regional Science* 11, pp 101-110, 2001.

Interestingly, individuals (i.e. employees) regularly show preferences towards flat-rate charging, across a range of consumer goods and services, even when it is demonstrably cheaper to use usage-based charging⁵. So there is even scope for a seasonal travel pass to be more expensive (even after tax concessions have been considered) than point-to-point ticketing and yet still be the preferred choice. This would substantially increase the value of public transport ticketing income to the states, well above the value of the tax exemption offered federally.

9 Conclusion

Widening an exemption from a Fringe Benefits Tax liability is always going to be controversial and fraught with the possibility of abuse.

But this proposal to exempt all time-based public transport tickets from FBT is unlikely to have any of the fall-out problems of other kinds of exemptions.

This proposal is supported by representatives from small business, large business, academia, economists and taxation lawyers.

- It does not look as though it will be expensive to implement or fund.
- It is not politically difficult to implement (such as dropping FBT exemptions for private transport would be likely to be).
- It is more likely to be used effectively by lower income earners than higher income earners.
- It is not going to occupy an army of tax lawyers attempting to find loop-holes, since the criteria for eligibility are extremely simple.
- There are economic, social and environment benefits from implementing this proposal.

⁵For example, timed local telephone calls to landlines have never been popular in Australia; capped mobile phone services are more popular, and so on.

10 Current FBT Legislation for Public Transport Benefits

Part III (Fringe Benefits), Division 12 (Residual Fringe Benefits), Section 47 paragraphs 1 and 1A.

47 Exempt residual benefits

(1) Where:

- (a) in respect of the employment of a current employee, the employer, or an associate of the employer, provides a residual benefit to the employee that consists of transport of the employee, otherwise than in an aircraft:
 - (i) between:
 - (A) the place of residence of the employee; and
 - (B) the place of employment of the employee or any other place from which or at which the employee performs duties of that employment;or
 - (ii) in a case where the place referred to in sub-subparagraph (i) (B) is in a metropolitan area -- on a regular and scheduled service over a route wholly within that metropolitan area;
- (b) where the provider is the employer -- the employer carries on a business of providing transport to members of the public;
- (c) where the provider is an associate of the employer -- the employer and the associate each carries on a business of providing transport to members of the public;
- (d) the transport referred to in paragraph (a) is provided in the same, or substantially the same, circumstances as transport provided to members of the public in the ordinary course of carrying on a business of providing transport to members of the public; and
- (e) the employee is employed in the business of providing transport to members of the public;

the benefit is an exempt benefit.

(1A) Where:

- (a) a person is an employee of a government body; and
- (b) the person's duties of employment are performed in a police service; and

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- (c) the person is provided with a residual benefit consisting of the provision of travel on public transport; and
- (d) the benefit is provided for the purpose of travel between:
 - (i) the person's place of residence; and
 - (ii) the person's primary place of employment;

the benefit is an exempt benefit.

11 About the author

This document is a submission to the Australian Future Tax System.

It was written by Mr Gregory David Baker.

Mr Baker is an Australian citizen, on the electoral role at: