THE TAX INSTITUTE

22 August 2017

Ms Kim Hall
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By email: kim.hall@ato.gov.au

Dear Ms Hall,

Draft Taxation Ruling TR 2017/D6 – Income tax and fringe benefits tax: when are deductions allowed for employees' travel expenses?

The Tax Institute welcomes the opportunity to make a submission to the Australian Taxation Office in relation to the *Draft Taxation Ruling TR 2017/D6 – Income tax and fringe benefits tax: when are deductions allowed for employees' travel expenses?*
(**Draft Ruling**).

Summary

In the main, we are concerned that the decision in *John Holland Group Pty Ltd v Commissioner of Taxation [2015] FCAFC 82* (**John Holland**) has been misunderstood which has caused the ATO to overreach in their interpretation of *John Holland* and consequently how they intend to apply the case to travel expenditure. Our submission below addresses our main concerns in detail in relation to the Draft Ruling.

Discussion

1. General

The Draft Ruling is a solid start to providing guidance in this area. However, there is much more material that could be included. For example, the common scenario of persons who commute interstate weekly on a regular basis should be included in the Draft Ruling. Also, given the modern workplace is changing and is no longer just an office, for office workers who have flexible work arrangements, information regarding how travel between various workplaces, such as home, a café or the beach, should be considered.

The Draft Ruling focuses on whether an employee is under the 'direction and control' of their employer and are getting paid during the course of their travel to determine whether the cost of the travel is deductible. This seems to be derived from a statement from Logan J in the *John Holland*[1] case. Both Pagone J (who delivered the lead judgment) and Edmonds J (who agreed with Pagone J's conclusion and reasons but approached the issue from a different perspective) also referred to the fact that the employees were paid while travelling from Perth to Geraldton, but in terms of direction and control, simply noted that factually, employees were subject to the directives and policies of John Holland. However, these factors were not the principle on which the case was decided. The principle, consistent with *Lunney v Commissioner of Taxation of the Commonwealth of Australia and Hayley v Commissioner of Taxation* (1958) 100 CLR 478 (**Lunney**), was that **the employees were required to travel as part of their employment** and as such they were travelling **on** work.

Paragraphs 10 and 11 set out the numerous rulings which have been withdrawn pending the finalisation of the Draft Ruling. In this regard, the only available guidance on the issue of travel expenses is the Draft Ruling. In particular, the withdrawal of *Miscellaneous Taxation Ruling MT 2030 Fringe Benefits Tax: Living-away-from-home allowance benefits* has resulted in the withdrawal of the 21-day guideline[2] for when an allowance will be treated as a travel allowance rather than a living-away-from-home allowance. In the interests of practicality, we suggest the ATO consider implementing a 'safe harbour' of a period such as 50 days so that if the travel is for under 50 days, this will be acceptable to the ATO as deductible business travel, and if the travel is for 50 days or more then all relevant factors need to be considered. This latter point should be emphasised so that any such new threshold is not interpreted to mean that travel for longer periods can never be treated as deductible business travel (as was previously occurring in relation to the 21-day rule). We suggest the ATO consider including this guideline in a Practical Compliance Guideline (**PCG**).

2. Specific comments on the Draft Ruling

Please find below our specific comments on the Draft Ruling:

- Paragraph 26 – In our view, this is an overreach and misunderstanding of the decision in *John Holland*. In fact, the very example Edmonds J provided at [35] of a solicitor travelling from Sydney to Melbourne to conduct litigation does not suggest or even imply the solicitor is being paid while travelling. There is no justification in the law to determine the deductibility of a transport expense based on whether the travel can be characterised as an 'income-producing activity' for which the employee is being paid. Rather, whether the travel expense is deductible should be determined based on whether the travel is an essential part of the employee's duties. The ATO should clarify this. Otherwise, anomalous situations may arise with different results occurring depending on whether the travel occurs during normal working hours (such as on a weekday) or whether the travel occurs outside of normal working hours (such as a weekend).

[1] Per Logan J in *John Holland* at para 48 "*Once it was concluded, as it had to be on the evidence, that both "workforce" and "staff" employees* ***were on paid duty under the control and direction of the appellant*** *on and from their arrival at Perth Airport and during the flight from there to Geraldton the outcome of the case was dictated by Lunney v Commissioner of Taxation; Hayley v Commissioner of Taxation (1957–1958) 100 CLR 478."*

[2] Refer to paragraph 41 of former MT 2030

- Paragraph 27 – In our view, in reference to wage-earning employees, the paragraph should be revised to say 'this factor is generally satisfied'. Reference should be made to the general concepts applying to the deductibility of expenses. Example 16 should be revised for the above.

- Paragraph 30 – While it may be relevant to consider whether the employee is 'subject to the employer's direction and control' during the period of travel, this is not determinative and not the basis for the decision in *John Holland*. As stated above, we consider the better test to be whether the travel was essential to the carrying out of the employee's duties and was required or necessitated by that employment.

- Paragraphs 32 & 33– It seems what is being stated here in relation to 'contrivance' is really just a general principle and is unnecessary. It may have the unintended effect of stopping employers from making specific arrangements to pay employees for certain travel the employee needs to undertake. While we do not consider it is necessary to include any comment on contrivance, at the very least, the second sentence in paragraph 32 and the whole of paragraph 33 should be deleted.

- Paragraph 37 – the use of the word 'contrived' in this paragraph is unnecessary. The second sentence of the paragraph should be deleted.

- Paragraph 40 – in our view, the bullet point 'a requirement to work away from home for an extended period' better belongs in the category 'Co-existing work locations travel' rather than the 'Special demands travel' category.

- Paragraph 73 – we suggest that a time period be included in a PCG as a guideline or 'safe harbour' to help an employer have some certainty about the treatment of particular employees just as spending time working away from home and is therefore accepted as travelling for work where the travel is less than 50 days.

- Paragraphs 79 and 80 – In our view, the relevance of the nature of the accommodation should be focused on whether the accommodation is temporary or permanent (ie hotel vs renting), rather than the standard of the accommodation (ie a hut and caravan vs accommodation with amenities such as an equipped kitchen).

- We refer to Examples 12 and 13 which discuss when lease costs (Example 12) and purchase costs (Example 13) are deductible. These two paragraphs appear to be mainly about whether the costs are disproportionate to the cost of suitable commercial accommodation. There does not appear to be any support provided for this contention and we submit that the conclusion in Example 13 regarding part of the costs being on capital account is not justified. Further, these examples do not really give any context to the comments in paragraph 56 regarding additional property expenses.

- Paragraph 83 – In our view, it is more likely that a person who is accompanied by their family would have relocated or is living away from home, rather than just be travelling for work.

3. The Examples

Please find below our specific comments on the examples in the Draft Ruling:

- Example 3 –Example 3 notes that the employee is being paid for the travel time (paragraph 112), but the cost of the travel is not deductible (paragraphs 114 and 115). The reason for this seems to be that Bill is 'not subject to his employer's direction, control and code of conduct when he undertakes the travel' (paragraph 112). This seems to be an unfair and incorrect extrapolation of the principle in the *John Holland* case. While there is a statement in the *John Holland* case at paragraph 63 that the employee Mr Chan was advised:

  > '…that his employer's code of conduct and other policies applied to him, and to the other employees, whilst travelling between Perth domestic airport and the project site. Misbehaviour on flights "paid for by the company" could result in disciplinary action against him or other employees.'

  This was simply a statement of fact.

  Logan J added the following comment in his judgement:

  > *'Once it was concluded, as it had to be on the evidence, that both "workforce" and "staff" employees* ***were on paid duty under the control and direction of the appellant*** *on and from their arrival at Perth Airport and during the flight from there to Geraldton the outcome of the case was dictated by Lunney v Commissioner of Taxation; Hayley v Commissioner of Taxation (1957–1958) 100 CLR 478.'*

  However, these statements seem to have been extrapolated by the ATO to mean more than the context of the *John Holland* case suggests.

  In our view, Example 3 is contradictory to Edmonds J's statement at paragraph 35 of *John Holland* and the principle in *Commissioner of Taxation v Day* 2008) 236 CLR 163, being the determination of what it is that is productive of assessable income, and that no narrow approach should be taken to this question.

  We submit that 'direction and control 'by the employer during the period of travel should not be considered a necessary element for the travel to be treated as work-related travel. This would also produce some anomalous results if applied more broadly. Further, we suggest that whether this test is met would be very difficult to determine in the vast majority of cases. What is relevant is whether the travel is an essential part of the employee's duties and was required or necessitated by that employment.

  The example concludes that the accommodation, meal and incidental expenses are 'otherwise deductible' to the employer (paragraph 119, but that the travel expenses are not (paragraph 114). In our view, these conclusions are contradictory.

- Example 4 – paragraph 122 states that Brian is obliged to respond to work phone calls or texts while he is in transit. In our view, the vast majority of 'fly-in fly-out' (**FIFO**) workers would not be required to do this. This seems to be trying to unduly restrict the principle in

the *John Holland* case to say that an employee needs to be being paid and undertaking work duties while they are travelling for the travel expenses to be deductible to the employer. There is no authority at law for this view.

Further, we consider it unreasonable to include any reference to a requirement for the employee to respond to work phone calls or texts while travelling, since for much of the time this would not be possible and in our experience, whilst many employees may actually do this, it would be extremely unlikely for the employer to impose such a requirement.

- Example 6 – again, in this example it is stated that Duy is required to respond to any work calls or texts he receives while travelling between Rockhampton and Brisbane. Similar to Example 4, we are unclear where this requirement to answer work calls or texts while travelling is derived from and consider it to be unreasonable and has no basis at law. The point is also made that Duy receives a salary, which we presume means there is an inference that Duy is effectively being paid whilst travelling. In our view, this point is unnecessary, given the comments above re the overemphasis on the relevance of being paid.

- Example 9 – at paragraph 164, the statement is made that 'While they are travelling, the employees will be paid and will be under the direction of their employer and subject to the employer's code of conduct'. As stated above, the emphasis should be placed on whether the travel is an essential part of carrying out employment duties (ie that the employee is required to travel) rather than whether the employee is being paid while they are traveling. Paragraph 164 should be removed altogether.
  Further, we recommend this example be extended to include an employee who lives in the city where the conference is being held – to draw out that the accommodation and meals for that employee are also otherwise deductible for the employer.

- Examples 15 and 16 – in Example 15, the employee is working at another location for a period of 2 months and can go home every weekend. In this case, all travel and accommodation expenses are considered to be deductible. In Example 16, the employee is away for four months and will also be able to travel home every weekend, though in this case the meal and incidental expenses will not be deductible and the employee is considered to be 'living away from home'. Examples 15 and 16 seem inconsistent. It also seems inconsistent to suggest that travel to and from a LAFH destination is deductible.

- Example 17 –In this example, the employees come to Australia from overseas. It seems to be being suggested that on this basis, both the travel and accommodation expenses are non-deductible, even though the facts are not significantly different from examples 15 and 16. Clearly this is an inappropriate basis for differentiation. It is also inconsistent with the experience of Tax Institute members that private rulings have been obtained which provide that the travel and accommodation expenses are deductible to the employer in similar instances to the facts in this example.

- Examples 15-17 all deal with examples of extended business travel and for all practical intents and purposes are essentially similar, yet somehow, the examples suggest different outcomes should arise. In our view, insufficient weight is given in these examples to the

following factors which are clearly relevant to determining the deductibility of travel costs (transport and accommodation) in situations similar to those set out in the examples:

- The employees are required to travel by their employers;
- Their permanent job location and permanent home does not change;
- They are working away from home for relatively short periods of time;
- They are required to live close to the project site;
- Their accommodation is arranged by their employer and they have little choice in this respect; and
- They are not accompanied by family.

- Based on relevant case law, in particular recent cases such as *John Holland* and *Day*, in our view, employees should clearly be entitled to deductions for transport and accommodation costs in these circumstances. The comments in paragraph 243 suggesting otherwise are a misguided application of the relevant principles. We also note that the above factors are remarkably similar to those listed in Example 3 as justifying deductibility of accommodation costs in that example.

If you would like to discuss any of the above, please contact either myself or Tax Counsel, Stephanie Caredes, on 02 8223 0059.

Yours sincerely

Prof Robert Deutsch
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