

Submission

By



To The

Inland Revenue Department

On The

**Tax-free Relocation Payments & Overtime
Meal Allowances Paper**

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**TAX-FREE RELOCATION PAYMENTS AND OVERTIME MEAL ALLOWANCES
SUBMISSION BY BUSINESS NEW ZEALAND¹
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1. INTRODUCTION

1.1 Business New Zealand welcomes the opportunity to comment on the *tax-free relocation payments and overtime meal allowances* issues paper (referred to as 'the paper'), released by the Inland Revenue Department (IRD). Recent formal interpretations by IRD on relocation expenses seemed to run contrary to the given views of how most businesses have usually treated them. Therefore, the introduction of an issues paper is a necessary step to ensure policy changes are made that revert IRD's formal policy stance back to one that is generally agreed upon by the business community.

2. SUMMARY OF RECOMMENDATIONS

2.1 Business New Zealand makes the following **recommendations** with regard to the tax-free relocation payments and overtime meal allowances paper, namely that:

(a) ***The criteria for determining a distance requirement, before a move could be considered a qualifying relocation, is solely left to employers to decide (p.3);***

Notwithstanding the recommendation above, if IRD's ongoing preferred position is to import an existing scheme, then:

(b) ***The second best option for determining a distance requirement before a move could be considered a qualifying relocation is based on the current United Kingdom approach of a reasonableness test (p.4);***

(c) ***Costs associated with the re-direction of physical mail be included as part of the eligible expenditure list (p.4);***

(d) ***The Commissioner takes a pragmatic and open-minded view of deciding what should be included on the eligible expense list. (p.4);***

(e) ***The decision not to place a cap on the amount of eligible relocation expenses is supported (p.4);***

(f) ***While the threshold amount of \$20 would be deemed sufficient at this present time, the amount should be revised upwards on a fairly regular basis to take into account any inflationary impacts (p.5);***

(g) ***Terms such as normal and ordinary within the definition of overtime are appropriately used as set out by existing employment relations definitions (p.6);***

¹ Background information on Business New Zealand is attached in the appendix.

- (h) ***That the definition of overtime is amended to read “beyond the persons ordinary hours of work as set out in the employment agreement” (p.6); and***
- (i) ***Any tax credit that arise in relation to the deduction of PAYE from past relocation payments should be given to the employer (p.7).***

3. BACKGROUND

- 3.1 The release of this paper provides the first crucial steps towards formally acknowledging the tax treatment of relocation payments and overtime meal allowances that the majority of the business community have thought to already exist for some years. The exposure draft issued by IRD in October 2006 contained interpretations that were in most cases the opposite of how many businesses had treated relocation costs on a day-to-day basis, and therefore created a fair degree of uncertainty and concern.
- 3.2 Business New Zealand welcomes the release of this paper, along with the thrust of changes we would expect to be included in the May 2008 Tax Bill. We would also like to take the opportunity to acknowledge IRD for the constructive way in which they have canvassed the views of the broader business community in preparation of the paper – a level of consultation that we have come to expect from the department over recent years.
- 3.3 While the paper has set out a range of specific questions relating to relocation costs and meal allowances, Business New Zealand would like to take the opportunity to discuss the issues in a more general sense, with recommendations included throughout.

4. RELOCATION PAYMENTS – WHO WILL QUALIFY?

- 4.1 The paper outlines four steps which need to be considered to ensure a robust qualifying process for relocation payments, which are as follows:

When Does Employee Relocation Occur?

- 4.2 The paper outlines three determinants for a relocation to take place:

- Taking up a new job with a new employer; or
- Taking up new duties at a new location with the existing employer; or
- Continuing the current job, but at a new location.

In addition, the relocation of the employee's home base must also occur to carry out the job.

- 4.3 However, as the paper points out, *“if an employee could have commuted to a new job from an existing home base there would be a clear monetary private benefit involved when the employer pays for the relocation costs, and, in principle, this should be taxable”*. Therefore, the paper investigates whether there is the need for some distance requirement before a move could be considered a ‘qualifying relocation’.

- 4.4 The paper provides three possibilities for determining this. The first is the USA example which provides for a specific minimum distance test. However, we agree with the views expressed in the paper that while this would be the most certain, it would also be the most inflexible when taking into account travel time. Considering around 1/3 of New Zealanders live in the Auckland region, combined with ongoing traffic congestion problems, any measure by distance would simply be unrealistic compared with the time it took for an employee to get from their place of residence to their workplace. Therefore, time may be a more reliable measure.
- 4.5 The second option is based on the UK model where an employee's existing home must be outside a reasonable daily travelling distance of the new workplace. As the paper notes, *"in terms of the reasonableness aspect, we note that the reasonable daily travelling distance is not defined in the United Kingdom's legislation. Instead, taxpayers are expected to apply common sense and take account of local conditions. The usual time taken to travel given distance is an indication of whether that distance is reasonable"*.
- 4.6 The third option involves simply leaving it to employers to decide whether there has been a home base relocation that they wish to pay for. While the paper acknowledges that employers will be reluctant to pay for relocations that are not related to work, there could be instances where a salary recharacterisation could be achieved by relocating locally to coincide with taking up a new job.
- 4.7 Obviously, it is not possible to determine the extent of people effectively 'gaming' the third option of recharacterising their salaries by relocating to coincide with a new job. However, Business New Zealand believes these occurrences would be very rare, and we would doubt whether there would be any real adverse effect on the tax revenue base. Also, eliminating this option because of legislating for the small minority rather than the majority does not take into account the additional compliance costs that would be placed on all employers compared with the option leaving employers to decide. Lastly, as pointed out in the paper, there is a natural motivation for employers who will almost always be reluctant to pay for relocations that are not related to work.
- 4.8 Therefore, Business New Zealand prefers the option of leaving employers to decide whether there has been a home base relocation that they wish to pay for.

Recommendation: That the criteria for determining a distance requirement before a move could be considered a qualifying relocation is solely left to employers to decide.

- 4.9 Notwithstanding our recommendation above, Business New Zealand's second best option is the present UK approach that is based on a reasonableness test. Also, we would strongly object to any specific minimum distance test being applied that currently occurs with the USA approach.

Recommendation: That the second best option for determining a distance requirement before a move could be considered a qualifying relocation is based on the current United Kingdom approach of a reasonableness test.

Listing Eligible Expenses

4.10 Paragraph 3.15 of the paper outlines a list of eligible expenditure involved with relocation of employees. Overall, we believe the list is a good starting point, as it typically picks up many of the standard expenses most employees would encounter. However, we would certainly not want the present list condensed or shortened in any way from what it currently includes, and we would expect IRD to take an open-minded approach regarding any additions to the list.

4.11 One possible addition to the list are the costs associated with redirection of physical mail. New Zealand Post had previously provided this service free of charge for a certain time period. However, they have recently changed their policy and now charge for any re-direction. As an employee may need two re-directions for mail (the first being at a transit place such as a motel, while the second at their end place of residence), we recommend that this should be added to the list.

Recommendation: That costs associated with the re-direction of physical mail be included as part of the eligible expenditure list.

4.12 We would also like to note our support for the decision to not include the list in the Act, but rather as a determination issued by the Commissioner of IRD. As the paper points out, it provides a much easier way in which the list could be added to over time, which may occur sometime in the near future given technological change and ongoing changes to the sociology changes of families. However, we would expect the Commissioner to take a pragmatic and open-minded view of the determination process.

Recommendation: That the Commissioner takes a pragmatic and open-minded view of deciding what should be included on the eligible expense list.

4.13 Lastly, we support moves by IRD not to place any limits on the amount of eligible relocation expenses, as is the case in the UK. The paper rightly points out that it would not adequately recognise variations in areas such as family size or distance travelled for the relocation.

Recommendation: That the decision not to place a cap on the amount of eligible relocation expenses is supported.

Expenditure has to be Incurred

4.14 Business New Zealand agrees that the exemption should only apply to actual expenditure incurred. We have previously stipulated this viewpoint to Ministers and IRD, as there would be a potential disconnect between the expenses incurred and the amount claimed.

Time Limit for Incurring Expenditure

- 4.15 Overall, Business New Zealand agrees with the stipulations regarding time limits for incurring expenditure, particularly the proviso if an employee moves on a temporary basis for a period of time, then moves to their final place of residence.

5. OVERTIME MEAL ALLOWANCES

- 5.1 Overall, Business New Zealand agrees with the approach taken by IRD to exempt overtime meal allowances, given these payments have not generally been considered taxable in the past. However, there are a few issues that we would like to comment on regarding the particulars of any proposed legislation in this area.

Monetary Limitations

- 5.2 The paper discusses the possibility of having to provide cost of verification only if the allowance is above a certain amount, as is the case in Australia. The threshold amount provided in the paper is \$20, which is similar to that in Australia.
- 5.3 For practical purposes, we agree that a threshold above which verification is required sufficiently takes into account the compliance issues associated with smaller purchases. We believe the amount of \$20 is currently adequate, although we would expect this to be updated on a fairly regular basis to take into account inflation.

Recommendation: That while the threshold amount of \$20 would be deemed sufficient at this present time, the amount should be revised on a fairly regular basis to take into account any inflationary impacts.

Defining Overtime

- 5.4 The paper outlines a possible definition of overtime, which is defined as:

Overtime, for a person, means time worked for an employer-

- (a) Beyond the person's normal hours of work as set out in the employment agreement; and
- (b) On a day, -
 - i) Beyond a minimum requirement of eight hours; or
 - ii) For which the person is eligible to be paid under the employment agreement at a rate that is at least 1.5 times their rate of pay for normal hours.

- 5.5 Business New Zealand has two fundamental problems with the definition. Firstly, there appears to be some confusion in terms of the existing relationship between the words 'normal' and 'ordinary' as applied to remuneration issues. Also, we believe the definition is too restrictive, and

does not take into account the broad working arrangements typically found in the private sector.

- 5.6 Regarding our first point, there seems to be confusion between the use of the words 'normal' and ordinary throughout the definition. In employment relations issues, 'normal' is typically defined as the hours of the day and/or the days of the week an employee are obliged to be at work. Payments for work outside these hours worked are regarded as penal payments (e.g. weekends). In comparison, 'ordinary' typically refers to hours or days of work in which an employee would receive their standard rate of pay. Hours extended to these would be paid as overtime. Therefore, the definition needs to ensure that the words normal and ordinary are used appropriately.

Recommendation: Terms such as normal and ordinary within the definition of overtime are appropriately used as set out by existing employment relations definitions.

- 5.7 The second issue relates to the very narrow view of overtime as defined in part (b) of the proposed definition. Essentially, the requirement of at least eight hours work and a rate of pay of 1.5 times the employees' rate of pay during overtime does not take into account a wide array of arrangements in the private sector that have been agreed upon in employment contracts.
- 5.8 For instance, a person may work part-time, encompassing 3 hours per day from 3-6pm five days a week. In addition, the rate of pay for overtime may have been agreed upon at 1.2 times their rate of pay for ordinary hours. Under the proposed definition of overtime, the employee in question would fail part (b) of the definition. Overall, part (b) assumes that all employees work by a standard model of employment, rather than the various requirements of the market, i.e. the imposition of 1.5 may have far reaching consequences, and is not required in a review of this nature.

Recommendation: That the definition of overtime is amended to just read "beyond the persons' ordinary hours of work as set out in the employment agreement".

6. RETROSPECTIVE APPLICATION

- 6.1 The paper outlines that the two legislative changes will have retrospective effect, so their coverage includes the past four years. One of the questions that arises concerns who should receive any tax credits in relation to the deduction of PAYE from past relocation payments.
- 6.2 As the paper points out, these credits would normally go to the employee if the original payment is considered to have been part of the employee's income. However, when in relation to a relocation payment, an employer has deducted PAYE and has grossed up the payment to reflect the tax liability, there is certainly enough grounds for giving the tax credit to the employer instead.

- 6.3 Because the employee in this instance has been fully reimbursed for the relocation costs, while the tax has been borne by the employer, Business New Zealand believes the employer rather than the employee should receive the tax credit. Also, the grounds for an employer receiving the credit are backed by this approach being administratively simpler as it would avoid adjustments where relevant to employee's liabilities such as student loans and child support.

Recommendation: That any tax credit that arise in relation to the deduction of PAYE from past relocation payments should be given to the employer.

APPENDIX

7. About Business New Zealand

- 7.1 Encompassing four regional business organisations (Employers' & Manufacturers' Association (Northern), Employers' & Manufacturers' Association (Central), Canterbury Employers' Chamber of Commerce, and the Otago-Southland Employers' Association), Business New Zealand is New Zealand's largest business advocacy body. Together with its 70-member Affiliated Industries Group (AIG), which comprises most of New Zealand's national industry associations, Business New Zealand is able to tap into the views of over 76,000 employers and businesses, ranging from the smallest to the largest and reflecting the make-up of the New Zealand economy.
- 7.2 In addition to advocacy on behalf of enterprise, Business New Zealand contributes to Governmental and tripartite working parties and international bodies including the ILO, the International Organisation of Employers and the Business and Industry Advisory Council to the OECD.
- 7.3 Business New Zealand's key goal is the implementation of policies that would see New Zealand retain a first world national income and regain a place in the top ten of the OECD (a high comparative OECD growth ranking is the most robust indicator of a country's ability to deliver quality health, education, superannuation and other social services). It is widely acknowledged that consistent, sustainable growth well in excess of 4% per capita per year would be required to achieve this goal in the medium term.