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Our ref KPMGsubFBTissues paper

5 May 2025

Dear David

Fringe Benefit Tax - Options for Change

KPMG is pleased to make a submission on the issues paper. We provide our responses to the specific questions below. Please note that we have attempted to answer most, but not all, of the questions asked.

As a general comment, we welcome the focus on reducing the complexity and compliance burden that is associated with the Fringe Benefit Tax ("FBT") rules.

In particular, we endorse the proposed approach in paragraph 2.4 that "close enough is good enough" rather than requiring absolute precision in the application of the FBT rules, with some caveats (discussed in our detailed submissions).

We recommend that this approach should be used more widely in the development of tax policy but also in the practical application of the rules by Inland Revenue. In relation to the latter, we note that a key test will be how the proposals (if implemented) will be interpreted and applied by Inland Revenue's customer compliance specialists tasked with enforcing compliance.

It is critical that the intended flexibility (for example, in relation to the "incidental private use" test for motor vehicles and "not in substitution for remuneration" test for minor unclassified benefits) is reflected in Inland Revenue's practical application of any new rules. Otherwise, any compliance cost savings, in our view, will be significantly reduced. We recommend there is clear operational guidance accompanying any legislative changes to ensure the policy intent of the FBT changes is preserved.

And while we support the overall objective of reducing FBT compliance costs, it needs to be acknowledged that there could be challenging trade-offs for employers if simplification results in significant additional tax costs. In some cases, including for smaller employers who may be less able to absorb additional FBT costs, this trade-off may not make commercial sense. There needs to be reflection of this in the overall package of proposals.

Q6.1 Should the value of a motor vehicle be determined by reference to external calculations undertaken by remuneration consultants or built up by Inland Revenue from external resources (such as the AA)?

It is not clear to us what this question is getting at. Is the "value" the value of the (taxable) benefit? If so, based on our reading of the issues paper, it appears the proposed approach for calculating the taxable value of a motor vehicle, for FBT purposes, is a hybrid of both approaches. That is, the proposal in paragraph 7.38 to calculate the percentage of cost based on fuel type appears to be based on use of external (i.e. modified AA) data sets on running costs, while the proposed categories of use in table 4 appear to be based on an adaptation of remuneration consultants' methodology for determining the "perk value" of a motor vehicle.

Q6.2 How often should these rates be set (annually or a certain number of years)?

Paragraphs 6.21 and 7.35 proposes moving to a four-year re-calculation period for calculating the motor vehicle rates using external running cost data. This seems reasonable to reduce compliance costs.

Q6.3 Should FBT be calculated based on the limitation on private use of the vehicle?

Basing the FBT liability on limitations on private use (which we assume is a reference to the proposed category approach in table 4), rather than requiring employees and employers to count private use days, should reduce compliance costs. Paragraphs 6.26 and 6.27 indicate that an employer would need to determine the limitations on private use to determine the taxable value of the benefit only once, unless there is a material change in private use. The suggestion is that once the classification is made, for a vehicle, the FBT liability would remain static for the term of use. Paragraph 6.27 also notes that there may need to be restrictions on the use of a particular category (in table 4) when there is a lack of controls to police private use.

While we support an approach that allows employers to classify vehicles at the outset to reduce their compliance costs, it is not clear what is expected in terms of policies around private use and, importantly, whether/how those will need to be enforced by the employer. For example, will having a policy (which presumably would be a form of control) around private use of a company vehicle, that is communicated to the employee, be sufficient for the categorisation exercise? What obligations will there be on the employer, if any, to monitor compliance with that policy (testing of the control)? The compliance cost saving, if any, will depend on these factors. So, there needs to be clear guidance on expectations to ensure this approach is feasible.

Q6.4 Do employers see the ability to categorise a vehicle at the time of acquisition of the vehicle as workable?

We consider that the ability to effectively categorise a vehicle will depend on the factors discussed in the response to Q6.3 above, namely the obligation/expectation on employers not only to have a private use policy but also monitor compliance with that policy.

Q7.1 What should the weight limit be for the purposes of determining if a motor vehicle is subject to FBT?

We consider that it makes sense to link the weight limit to the driver licence standard rather than an arbitrary threshold of 4,500 kg.

Q7.2 Notwithstanding that most of these types of vehicles are likely to fall out of FBT naturally, is it appropriate to remove them via exemption?

We see merit in a specific exemption for emergency vehicles to provide certainty. The proposed exemption criteria in paragraph 7.15 seems reasonable.

Q7.3 Is the suggested exemption suitable, and does it capture all vehicles used for those services?

We propose that vehicles owned or operated by the New Zealand Defence Force is included in this exemption, as well as vehicles owned by suppliers and contractors to the emergency services organisations. These suppliers and contractors are essential to the provision of emergency services to the New Zealand public and, like the emergency services, are on-call 24/7 to provide support. The vehicles operated by these suppliers and contractors are fitted with flashing warning lights and other equipment like the vehicles operated by emergency services themselves.

Q7.4 Would the removal of the ability to use tax value as a cost base option have any negative consequences?

It is not clear to us that the removal of the tax value option will result in significant compliance cost savings. It could disadvantage taxpayers with older vehicle fleets which could disproportionately impact smaller businesses that may not update their vehicles as regularly. We therefore do not recommend removing this valuation option. If the proposal proceeds, transitional rules should be considered.

Q7.5 Should the FBT regime move to a more hybrid approach based on the availability for private use but also considering the permitted private use of the vehicle?

We agree that the current availability-based test for calculating the fringe benefit value potentially overstates the taxable value of the benefit. However, it is not clear to us that the proposed category-based approach has enough flexibility to capture different private use scenarios and, as a result, could lead to significant over-taxation, particularly when combined with the proposed increase (as suggested in to paragraph 7.38) to motor vehicle rates based on fuel type.

While compliance cost reduction is important, this should not come at the expense of significantly higher FBT liabilities, particularly for smaller employers.

Q7.6 Should there be an option for taxpayers to use actual costs to determine the private running of a vehicle?

We believe that actual running costs should be available as an option as there will be trade-offs for some employers. That is, it should not be assumed that the trade-off will be in favour of compliance cost reduction if this results in significantly higher FBT costs.

Q7.7 Should any option to use actual costs be restricted to a certain group of taxpayers or available more widely?

We do not believe any option should be limited to a particular group of taxpayers. However, if a limitation is proposed, for example for fiscal reasons, this could be based on the size of the employer (i.e. limited to smaller employers) or the number of motor vehicles provided (e.g. less than 5 vehicles). This is on the basis that the compliance cost savings may not justify the increased FBT cost where only a limited number of motor vehicles are involved.

Q7.8 Do submitters prefer a more exact calculation or a "close enough is good enough" approach to the calculation of motor vehicle benefits bearing in mind the latter approach could result in under- and over-taxation?

While we support the "close enough is good enough approach", as a general concept, we do have concerns that the proposed category approach to classifying vehicle use (and therefore FBT liabilities) could result in significant inaccuracy in some cases. (This is discussed more fully as part of the responses to some of the questions in Chapter 8.) Particularly, if the operationalisation of the rules by Inland Revenue results in most vehicle use being fully taxable (i.e. treated as Category One vehicles). And while larger employers may be able to better deal with 'unders-and-overs' created by the proposed category approach, this may not be the case with smaller employers.

Q8.1 Do you think a scaled rate of FBT would bring the impact of FBT closer to actual use than is currently the case? (We note that responses to Q8.2 to Q8.17 are also included as part of this response.)

We consider the proposed category-based approach would bring the impact of FBT closer to actual use in certain circumstances, namely where the only allowed private use component is home to work travel (to a single workplace).

Our concern is that any permitted private use that is not of an incidental nature outside of those strict parameters would result in the vehicle being fully subject to FBT as a Category One vehicle.

This is a change from the application of the work-related vehicle exemption, for example, where the exemption is based on whether the legislative criteria is met on a given day. This allows a greater degree of flexibility – for example, if employees are allowed to use the vehicle during the weekend (but all other private use is prohibited), FBT can be paid on the 2 days where the vehicle is available for private use. (We note that Inland Revenue's FBT guide supports this approach.)

While we acknowledge the rationale for limiting the number of categories, we do wonder to what extent Category Two, as currently defined in the issues paper, will be applicable in practice. In our experience, the work-related vehicle example above is not uncommon. Such employers could see a significant (300%) increase in their FBT liability, compared to the status quo. We do not believe that the correct policy outcome, under a close enough is good enough approach, is for these vehicles to be fully taxed as "perk vehicles".

While we recognise that there will be inevitably be some 'unders and overs', for some taxpayers with large existing vehicle fleets, the additional FBT costs may outweigh any compliance cost

savings. As the aim of the proposal is not to raise additional revenue, this may support retaining the work-related vehicle exemption in some form, as an alternative, or modifying the new category-based approach to allow a hybrid model. That is, similar to how the work-related vehicle exemption applies to 'qualifying days', a motor vehicle that is otherwise a Category Two vehicle could be treated as a Category One vehicle for calculating FBT on those days where there is private use outside of home to work travel that is not incidental. While this would result in greater compliance costs, we consider this is justified to deal with situations which are simply not able to be dealt with appropriately under the three categories being proposed.

We support ignoring incidental private travel when calculating FBT. The suggested criteria in paragraph 8.23 for determining whether private use is incidental should be (a) legislated and (b) their practical application clarified in detailed operational guidance. The latter is needed to give certainty around how Inland Revenue will practically enforce the new rules, as what is meant by "ad hoc" or "irregular", use of "short duration" and "limited purpose" are inherently subjective concepts. There is also a suggestion that employer permission should be sought (we refer the example in paragraph 8.21). It should be clarified whether this is intended to be a qualifying factor.

While we support additional integrity measures for vehicles provided to shareholder employees (with a shareholding of greater than 25%), the proposed $80,000 cost threshold for application of Category Two and Three could be a blunt instrument. For example, if the cost threshold is exceeded because the motor vehicle needs to be customised for the needs of the business. If a threshold is proposed as a limiting factor, there should be the ability for Inland Revenue to provide exemptions from this requirement in appropriate circumstances (similar to the discretion from the branding requirement).

Specifically in respect of the branding requirements, we are supportive of the ability for employers to obtain an exemption from this requirement. For example, some organisations such as defence contractors, who provide services to the New Zealand Defence Force and the emergency services do not brand their vehicles due to understandable and real safety concerns for their staff. An exemption from branding would therefore be appropriate in these cases.

We also recommend that detailed operational guidance is provided on the expected record keeping requirements to support the classification of vehicles, if this is reviewed or audited by Inland Revenue.

Q9.1 Are the three factors a sensible test for whether a benefit is provided "in substitution for remuneration"? Would any other factors be more appropriate? Q9.2 Would it be feasible to apply this test? Q9.3 Are there any unclassified benefits that would not receive the correct treatment under this test?

We consider that the three factors listed in paragraph 9.21 are an appropriate base for determining whether a benefit is provided in lieu of/in substitution for cash remuneration. We question whether an employee's "expectation" of receiving a benefit (when there is no clear legal entitlement as part of an employment agreement) should be a factor as this may be difficult for

employers to judge. As far as possible, the criteria for the remuneration test should be based on objective criteria within the control of the employer.

Q9.4 Would a per benefit test help to reduce compliance costs? Q9.5 Is $200 the right cap? Should it be higher/lower? Q9.6 Are there any unclassified benefits which are not in substitution for remuneration that would not receive the correct treatment under a $200 per benefit cap?

We support replacing the current de minimis exemption for unclassified benefits with a $200 per benefit test. We consider this would result in considerable compliance cost savings for employers from having to track minor benefits, particularly those employers ineligible due to the current $22,500 per employer cap.

We acknowledge the concern around connected benefits being split to circumvent the cap and can see the rationale for an anti-avoidance rule to prevent this. The examples in Table 6 are useful illustrations of what is intended to be caught by the rule and should be included as part of operational guidance on the new de minimis rule.

Q9.7 Would a list excluding non-remunerative unclassified benefits help to reduce compliance costs? Q9.8 Are there any other benefits that should be included on the list? Q9.9 Which option would be more effective at reducing compliance costs and strengthening the link to remuneration; option one or option two?

While both options have their merits, on balance, our preference is for the $200 per benefit cap, rather than an exhaustive list of non-taxable non-remunerative unclassified benefits. We note that the latter would give certainty as any listed benefit (without having to determine whether provided in substitution for employment) would be exempt. However, it would still require employers to track benefits provided against the list (regardless of the benefit value) to ensure that the exemption criteria are met increasing compliance costs relative to the benefit cap option. There would also be administrative burden on Inland Revenue in keeping the list up to date and relevant.

Q9.10 Do submitters who operate such schemes see any issues with the proposed treatment?

We support the introduction of specific rules for points accrual reward schemes and their treatment for FBT purposes. Specifically, the benefit should be considered provided at the time the points are accrued, with the value being the amount paid by the employer for the points in the scheme.

Some might argue that these benefits should then be evaluated under the main test (either option one or option two) to determine if they should be exempt from FBT, similar to other unclassified benefits. This is because, in practice, these schemes are often used in place of other unclassified benefits, such as open or closed loop stored value cards (e.g., Prezzy cards and Woolworths vouchers). Like these other unclassified benefits, employees are awarded points to reward and encourage desirable behaviours. Employees are not entitled to receive them, nor do they expect

to be awarded them. They are given on an ad-hoc basis and not awarded "frequently and regularly." While the potential receipt of reward points might be detailed on an intranet page, including how the points reward scheme works, this is no different from the potential receipt of Prezzy cards, which is also usually detailed on the intranet.

Therefore, some would argue that it might not be correct that points accrued under a reward scheme are inherently remunerative, especially given that applying the proposed remuneration test to them would likely not conclude they are in substitution for remuneration.

Furthermore, it could be seen as inconsistent to suggest that points awarded under a points accrual scheme are inherently remunerative, while open and closed loop stored value cards are not, given that they are provided under the same circumstances, with the same frequency, to reward and encourage similar employee behaviours. A points accrual reward scheme could simply be seen as a more formal method of providing these types of benefits to employees. This preference for a formal scheme is particularly evident among larger employers, who prefer structured processes over informal methods, such as purchasing $10k worth of Prezzy cards and distributing them without records or a formal process.

We would also expect that if points accrual reward schemes are not evaluated under the main test to determine their exemption from FBT, similar to other unclassified benefits, employers will likely discontinue these schemes. Instead, they will revert to using open or closed loop stored value cards (or similar alternatives), which are likely to be exempt from FBT under the proposed main test.

Q9.11 Is the on-premises exemption still necessary under these two options?

We see no reason for removing the on-premises exemption under either option. As noted in paragraph 9.41, it may be a useful safeguard against minor and non-remunerative items being brought to tax as unclassified benefits.

In addition, the on-premises exemption is critical to the application of FBT to car parks. If this exemption were to be removed, unless specifically legislated for, car parks would become subject to FBT going against Inland Revenue's longstanding position on car parks.

Q10.1 What are submitters thoughts on moving the entertainment deduction limitation within the FBT regime? Q10.2 Are there any concerns submitters see with this approach? Q10.3 Are taxpayers comfortable with the trade-off between potentially paying more tax in respect of the adjustment and the reduction in compliance costs?

While we acknowledge the compliance costs concerns around the current treatment of entertainment expenditure, we do not consider that proposal to mandate such expenditure to be included as a non-attributable benefit in the FBT return is appropriate.

As noted in paragraph 10.29, bringing all entertainment expenditure into the FBT regime would mean that those businesses (and non-businesses) that otherwise are not required to file FBT returns would need to establish new tax compliance processes (unless the relevant expenditure

falls with one of the proposed "de minimis" options outlined in paragraph 10.25). This may result in a net increase in compliance costs. It would also create a cash tax cost for those organisations that are income tax exempt or in losses, relative to the status quo, which seems unfair as the proposal is not intended to raise additional revenue.

Our recommendation therefore is for this proposal to be optional.

Q11.3 Are there any issues with the proposed treatment for open loop cards in deeming these to be subject to FBT rather than PAYE?

We support subjecting open loop cards to FBT rather than PAYE due to the impracticality of applying PAYE to these benefits. In our experience, many employers purchase open loop cards in bulk, such as $10k worth at a time, and distribute them to business units to provide to employees over the course of a year or another period. Tracking the recipient of each card is impractical, if not impossible. Consequently, many employers, particularly larger ones, will simply remit FBT on the total purchase amount (e.g., the full $10k) rather than at the time the cards are given to employees.

Subjecting open loop cards to PAYE, in our view, creates significant challenges in achieving accurate and timely tax remittance. Employers would be forced to track the recipient of each card and communicate this information to their payroll team for processing, resulting in a compliance-heavy process. Additionally, payroll processes inherently carry risks, especially with manual adjustments, which would be required for the receipt of an open loop card.

Q11.4 Is the proposed treatment of global insurance plans workable for employers or is there a better way to apportion these?

We support treating the payment of premiums under a global insurance scheme as a pooled benefit due to practical reasons. Global organisations typically recharge the cost of these insurance schemes to each subsidiary. It is practical and straightforward for the FBT payer to take this cost and apply FBT at the pooled rate. Apportioning the cost by the number of employees is challenging, as the number of employees could vary over the period, making the calculation unclear. Pooling the benefit would also reduce the compliance costs associated with paying FBT on this benefit, which is a key aim of the proposed changes.

Q11.5 Do submitters see any issues with the proposed deeming of certain reimbursements to be subject to FBT rather than PAYE?

Similar to the concerns above, we do not support deeming reimbursements to be subject to FBT, where an employer would not otherwise have an FBT obligation. This seems to be creating new compliance costs. We also note that the change outlined in section 11.23 was to align the tax outcomes between FBT and income tax, depending on which regime applies, not to subject the relevant expenditure/reimbursement/benefit to a single regime.

Instead, we propose that employers be given the option to treat certain reimbursements as subject to FBT rather than PAYE. This would provide flexibility, allowing employers to choose the

treatment that minimises compliance costs and administrative burden for their specific circumstances.

Additionally, section CX 19 currently exempts a fringe benefit from FBT if it would have been exempt under certain PAYE rules. We suggest creating a similar rule that exempts reimbursement payments from PAYE if they would have been exempt under the FBT rules.

Q11.6 If the entertainment proposals in Chapter 10 do not proceed how could a better boundary rule be enacted to make it clear which benefits are subject to the entertainment deduction limitation or FBT?

As noted in paragraph 11.25, the current rule for determining whether the entertainment or FBT rules apply is unintuitive. One suggestion is to simplify the rule by focusing on whether the benefit was provided in the course of the employee's duties, rather than on whether the employee has the choice of where and when to enjoy the entertainment.

For example, a restaurant voucher used by an employee is clearly not provided in the course of their employment duties. Instead, it serves as a strictly private benefit, likely intended to reward the employee for desirable behaviours. Similarly, an all-expenses-paid trip that is not linked to any work responsibilities would fall under the same category, meaning that FBT should be payable. However, if the primary purpose of the travel is to meet with clients, any entertainment will be in the course of performance of their employment duties. In this case, the private benefit received by the employee from any entertainment activity is secondary to the primary objective of hosting clients. Thus, the entertainment rules should apply. We would also query whether the deduction limitation should apply at all as the benefit is clearly not remunerative.

Applying this approach should yield outcomes similar to the current rule but would be simpler for employers to understand and implement in practice

Q12.1 Do submitters see any issues in providing more detailed FBT information when they file their returns? Q12.2 Would the ability to electronically file returns via software increase the use of software to assist in FBT compliance?

We support more detailed information being provided on the types of benefit categories (and sub-categories) as part of the FBT return process, to improve the information available to Inland Revenue and policy makers when considering future policy changes/improvements in relation to the FBT regime.

Taxpayers may be encouraged to transition from using Excel spreadsheets to specialised software for completing their FBT calculations as a result of the requirement to provide additional information to Inland Revenue. Additionally, we would expect that the ability to electronically file returns would increase the use of software, which in turn is likely to enhance accuracy and compliance.

Q12.3 Do submitters see any value in being able to file their first three quarters based on 25% of the prior year's FBT liability? Q12.4 Do submitters see any issues with doing this?

We support the proposal as a compliance cost reduction measure.

Q12.5 Do submitters have other practical ideas which would make FBT return preparation easier?

We recommend that employers, by election, be allowed to form a FBT group, similar to GST and consolidated income tax groups.

Currently, organisations with several subsidiaries all of whom are employers must prepare and file multiple FBT returns. Many of these organisations would find it easier and preferable to simply prepare and file one FBT return encompassing employees across the entire group.

This would significantly reduce compliance costs.

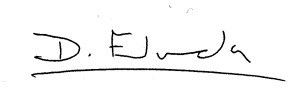
Q12.6 Do submitters see any issue with the proposed declaration in the income tax return of the taxpayer [that FBT obligations in relation to motor vehicles has been complied with]?

While we acknowledge the purpose of the income tax return declaration, it is not clear what taxpayers would be declaring in relation to their FBT and what the consequences would be if a declaration is incorrectly made. This should be made clear.

Further information

Please do not hesitate to contact us if you would like to discuss our submission in greater detail.

Yours sincerely



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