

## Manawatu District Council

### Deloitte FBT Review – 2022



Summary of findings

Confidential – Tax Advice Document

## Executive summary

We have carried out a review of Fringe Benefit Tax (“FBT”) compliance for Manawatu District Council (“MDC”) in accordance with our agreed scope. The scope and limitations of our advice are set out in **Appendix A** of this report.

Overall, we consider MDC has a low risk profile in relation to its FBT compliance. Our review highlighted several areas of medium to low-risk areas which do not require urgent attention but should be addressed.

We make the following key recommendations:

- MDC creates a FBT manual containing a summary of the technical and procedural knowledge currently held, which can be utilised by current and future staff members.
- The FBT declaration form for motor vehicles available for private use is amended to distinguish between situations where the business travel exemption will apply, and situations where the vehicle is unavailable for private use.
- MDC monitors unclassified benefits on a per employee basis where possible, in order to ensure that the de minimis threshold is not breached.
- MDC ensures that any SUV’s purchased as a dedicated vehicle have their back seats bolted down or removed in order to be able to apply the work-related vehicle exemption and the FBT workpapers clearly state which vehicles have these modifications.
- MDC reviews Health Support benefit payments which have been paid via staff reimbursement to determine the extent of historic PAYE underpayments. Depending on the level, these corrections may be able to be made in the next payroll filing.
- Direct payments made in respect of the provision of eye wear and noise cancelling headphones should be included in the unclassified benefits calculations as these are not eligible for the FBT health and safety exemption.
- MDC considers amending its policy which currently provides for reimbursements to employees for health support benefits to allow a direct charge facility only or the provision of vouchers if staff are to retain the ability to select a provider. This would mean the payments would be not be subject to PAYE and the FBT Health and Safety exemption may apply.
- The unclassified benefits calculations should also be updated to include the waiver of library fees that are not eligible for the on-premises exemption given the benefit is enjoyed offsite.

Your sincerely



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**(as trustee for the Deloitte Trading Trust)**



## Overview

Our Report uses a heat map to represent a high-level overview of the FBT risks and opportunities in your business and is intended to allow you to better understand, measure performance and identify areas for further action or consideration.

Our findings are presented in the following manner:

- An **overall traffic light risk and impact analysis**, which categorises major issues and FBT topics based on the risk and impact to MDC utilising a high, medium and low scale.
- **Discussions** which focus in more detail on specific issues and topics within each category of the overall traffic light analysis. The topics have been included in the section with the highest risk or impact rating.

The traffic light analysis is undertaken based on the risk and impact associated with each issue or topic:

- **Risk** – the extent to which the issue could result in an exposure for the organisation. For example, whether non-compliance in this area is likely to result in a tax penalty or reassessment, or a complete change from current treatment.
- **Impact** – the extent to which the issue affects the organisation. This includes both historical and potential future impacts. Please note that impact is not simply restricted to the financial impact of the issue but includes potential risk rating impact from an Inland Revenue perspective.













In each case our methodology contemplates three possible risk and impact outcome classifications: low, medium and high:

- **Low (Consider)** – indicates a topic where MDC is satisfying its FBT obligations and no immediate action may be required. These topics should continue to be monitored if factual or situational changes occur within the organisation that could change the FBT obligation and the risk and impact classification.
- **Medium (Review)** – indicates action may be required but this is likely to depend on additional facts, business strategy, attitude to risk, regulatory developments, or similar matters that management will need to consider.
- **High (Mitigate)** – the strongest categorisation and suggests more immediate remedial action is required. This category represents areas we recommend immediate change is made for best practice and to ensure MDC can meet all the requirements of the FBT regime.
- **Opportunities** – Indicates areas that may create an FBT opportunity in the future.





## Traffic Light Risk and Impact Analysis

### 1. Issues

No.	Description	Risk	Impact
1.1	Motor Vehicle Declaration & Exempt Days		
1.2	Unclassified Benefit Tracking		
1.3	Work related vehicle exemption		
1.4	On premises exemption		
1.5	FBT Manual		
1.6	Health Support Benefits – reimbursements subject to PAYE / not eligible for health and safety exemption		

## 1. Review findings - issues

Subject	Risk	Impact	Explanation and Comments
<b>1.1 – Motor Vehicle Declaration &amp; Exempt Days</b>			<p>We understand that employees who have been allocated a vehicle which is available for their private use are required to fill out a FBT declaration form each quarter. Question 2 of the declaration form asks employees to specify dates on which the employee is away from home over night on work related activity in order to determine FBT exempt days.</p> <p>The business travel exemption can be applied in the following situation:</p> <ul style="list-style-type: none"><li>- The employee is absent from home with the vehicle for at least 24 hours; and</li><li>- The employee is required to use a vehicle in the performance of their duties; and</li><li>- The employee is required to be regularly absent from home in the performance of their duties.</li></ul> <p>Where employees are away with a vehicle on a business trip for less than 24 hours (i.e. they leave on Wednesday at 12pm and return Thursday morning at 10am), the business travel exemption will not apply, meaning that the vehicle is treated as being still available for private use on both days. However, if instead an employee left at Wednesday at 9am and returned on Thursday at 10am, the business travel exemption will apply such that the vehicle is not available for use on either of these days for the purposes of the FBT calculation.</p> <p>In contrast, where employees are away without their vehicle on a work-related trip e.g. they leave the vehicle in the airport carpark while away, the vehicle will only be unavailable for private use (and therefore exempt from FBT) on the <u>full days</u> that the employee is away from the vehicle (i.e. departure on Wednesday and return on Thursday means that there are no exempt days. Departure on Wednesday and return on Friday means that Thursday is an exempt day). This is because on the days on which the employee travels to and from the airport in the vehicle, the vehicle is technically available for private use before/after the airport trip, and will be subject to FBT.</p> <p><b>Recommendation</b></p> <p>We recommend that the FBT declaration form is amended to split Question 2 into two separate sections:</p>

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Subject	Risk	Impact	Explanation and Comments
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1. Employee is away from home over night on work-related activity with the vehicle. The employee should specify their departure and arrival times so that it can be determined by the Finance team whether they were absent for more than 24 hours to determine whether the business travel exemption applies.
2. Employee is away from home over night on work-related activity without the vehicle. Again, the employee should specify their departure and arrival times so that the days where the vehicle was fully unavailable for private use can be determined.

**1.2 –  
Unclassified  
Benefits  
Tracking**



We understand that MDC currently assesses whether it needs to return FBT on unclassified benefits to employees by reference to the annual \$22,500 de-minimis threshold.

We note that there is also a quarterly per employee threshold as part of this rule. For employers paying FBT on a quarterly basis, no FBT will be payable provided that:

- The total taxable value of unclassified benefits provided in the quarter to each employee does not exceed \$300, and
- The total taxable value in the last four quarters, including the current quarter, of all unclassified benefits provided does not exceed \$22,500.

If the \$300 per employee per quarter de minimis threshold is exceeded, FBT must be returned on all unclassified benefits provided to that employee in that quarter.

If the total unclassified benefits for all employees for the current and previous three quarters exceeds \$22,500, FBT must be returned on all unclassified benefits.

MDC's tracking schedule shows that MDC was under the annual \$22,500 threshold for the FBT year ended 31 March 2022. We note that during our review we identified some amounts in the unclassified benefits calculation that were subject to FBT and do not need to be included in the total. These included morning teas or lunches provided on premises to employees, or at a specified time and place (meaning that the employees cannot choose when they enjoy the benefit provided).

However, we also identified two additional types of benefit that should be included in this calculation:

- Health support benefits paid directly to suppliers which are not eligible for the health and safety FBT exemption such as the provision of eyewear (see 1.6 for more detail).

Subject	Risk	Impact	Explanation and Comments
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- Waiver of library fees for services enjoyed offsite such as DVD and reserve charges, lost book and late fees (see 1.3 for more detail).

### Recommendation

We recommend that where benefits are provided to individual employees (i.e. gift cards, or health support benefits where the health and safety exemption does not apply (see 2.2 for more detail)), a record of this is kept to ensure that MDC does not breach the \$300 per employee per quarter limit. We note that we understand from discussions with Debbie Fulton that the risk of the per employee per quarter limit being breached is low, as MDC provides limited benefits of this nature to employees.

In addition, contributions to eyewear and the waiver of library charges where the benefit is able to be enjoyed offsite should be included in the unclassified benefits calculation.

### 1.3 – Work related vehicle exemption



We understand that MDC has a number of dedicated vehicles assigned to specific employees which are treated as not subject to FBT, on the basis that the work-related vehicle exemption applies to these vehicles.

A work-related vehicle can be exempt from FBT, even where that vehicle is taken home, if it is a vehicle:

- That is not designed to mainly carry passengers e.g. utes, utility vans or a vehicle that has had qualifying modification, such as bolting down the back seats);
- That prominently and permanently displays on its exterior the employer’s identification or branding;
- Where there is a condition of employment that requires the employee to store the vehicle at home for business purposes, which may include circumstances such as:
  - o The vehicle is being used to carry tools or other work-related equipment;
  - o The employee is required to be on call;
  - o As part of their job the employee is based from home, travels between multiple work sites in a day and habitually performs some part of their job at home (e.g. a requirement to complete paperwork at home in the evening); or
  - o The vehicle is required to be stored at home for security purposes.
- Private use of the vehicle is prohibited except for travel between work and home and incidental private travel during business use;
- A letter or company policy prohibiting private use is issued to employees or there is a clause in their employment contract prohibiting private use; and

Subject	Risk	Impact	Explanation and Comments
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- Recorded checks to ensure that policy is adhered to are carried out.

We understand that all of the dedicated vehicles to which the work-related vehicle exemption has been applied are either utes, or SUV's with cargo barriers and the rear seats either bolted down or partially removed. In addition, sign-writing and private use prohibitions are in place.

**Recommendation**

The FBT return workpapers should be updated to note that the dedicated vehicle SUV's have cargo barriers and rear seats are bolted down (i.e. they are able to be classified as work related vehicles provided the other criteria are met).

We understand that the E-roads report is reviewed quarterly when the FBT return is prepared to ensure that there has been no private use of the dedicated vehicles by employees. In the event of a review, Inland Revenue would expect MDC to be able to provide evidence that it polices the policy, and therefore we recommend that the FBT return workpapers are updated to show how the E-roads reporting functionality is used to check compliance. Evidence should also be retained (ideally in the FBT workpapers) of any follow-up action taken as a result of any infractions identified.

**1.4 – On premises exemption**



MDC provides employees with free access to council facilities including the pool, gym and library.

As MDC owns the land and buildings where these facilities are located, the FBT on-premises exemption will apply such that the benefits provided are not subject to FBT. This exclusion of these benefits from the calculation is therefore correct.

In order for the exemption to apply, the benefit needs to be “used or consumed” on premises. This means that any waived library charges such as DVD and reserve charges, lost book and late fees should be included in the unclassified benefits calculation as these benefits are not technically used on the library premises.

**1.5 – FBT Manual**



MDC currently has limited documentation in place outlining their FBT policies and procedures.

**Recommendation**

We recommend that a FBT manual is created containing a summary of the technical and procedural knowledge held by MDC which can be made available to all staff members who handle FBT both currently and in the future. We recommend that the manual also includes details on the

Subject	Risk	Impact	Explanation and Comments
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process involved as well as the underlying reasoning for the following transactions:

1. Motor vehicles
  - o Work-related vehicle exemption requirements
  - o Business travel exemption requirements
  - o How to determine exempt days
  - o How e-roads data is used and the process to check and review this information
  - o Modifications required to ensure that SUVs are able to be classified as work related vehicles
2. Unclassified benefits
  - o What is an unclassified benefit?
  - o Entertainment vs. FBT so that the unclassified benefits tracker contains the correct information
  - o How the de-minimis threshold
  - o Use of the on-premises exemption by MDC including its application to the pool and gym and its non-application to library charges
3. FBT vs. Payroll distinction and the impact of structuring benefits are reimbursements rather than direct payments
4. FBT return preparation and review process (including attribution vs. single rate method and when each is appropriate)
5. Treatment of GST on fringe benefits

We are happy to assist with preparing a skeleton template or reviewing a draft manual for you if required.

**1.6 – Health Support Benefits**



We understand that MDC currently provides the following health support benefits to employees:

- Eyecare: MDC will make a contribution towards the cost of eye care for employees, up to \$65 once every two years. The \$65 can be used for either an eye examination or eyewear. Employees can choose to use either MDC’s preferred provider (in which case the provider will invoice MDC directly), or another provider (in which case the employee will pay for the services themselves and then claim a reimbursement).
- Health Checks: MDC will make a contribution towards an employee’s health check with a GP, up to \$100 once every two years. Employees can choose to use either MDC’s preferred provider (in which case the provider will invoice MDC directly), or another provider (in which case the employee will pay for the services themselves and then claim a reimbursement).
- Noise cancelling headphones: MDC will make a contribution towards the cost of noise cancelling headphones, up to \$100 once every three years. The employee will pay for the headphones themselves and then claim a reimbursement.

Subject	Risk	Impact	Explanation and Comments
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Where employees are reimbursed by MDC for expenditure which the employee incurs, the reimbursing payment is subject to the PAYE rules rather than the FBT regime. As there is no health and safety exemption in the PAYE rules, structuring these payments as a reimbursement means that these payments are required to be grossed up for PAYE payable as well as Kiwisaver and student loan repayments etc as applicable to the relevant employee.

In addition, some of the direct Health Support Benefit payments made will be subject to FBT. This is because the FBT health and safety exemption can only be used for benefits which are “aimed at managing risks to health and safety in the workplace as provided under the Health and Safety at Work Act 2015”.

While eye and health checks provided by MDC would qualify for this exemption, Inland Revenue’s historic position is that the provision of eye wear (i.e. the contribution to the glasses themselves rather than the eye testing) is not generally considered as qualifying under this exemption. This was on the basis that Inland Revenue Officials considered that research had not shown an increased risk of eyesight deterioration as result of the use of screens and monitors. In addition, officials considered that payments for glasses were primarily of a private and domestic nature and not an expense which a self-employed person would be able to claim a deduction for. This is contrasted with the use of corrective lenses in safety goggles which are used for work related purposes only.

For noise cancelling headphones a similar analysis applies in that there would need be a specific noise and safety related risk requiring ear protection for headphones to fall within the Health and Safety exemption (for example working on a factory floor).

We note that there has not been any published Inland Revenue guidance on the impact the significantly broader and more stringent health and safety legislation enacted in 2015. This means that the while the breadth of the health and safety exemption is unclear, we are not aware of taxpayers successfully applying the exemption for these types of benefits in the event of Inland Revenue challenge.

**Recommendation**

We recommend that MDC reviews Health Support benefit payments which have been paid via staff reimbursement to determine the extent of historic PAYE underpayments. Depending on the level, these corrections may be able to be made in the next payroll filing.

Going forward, we understand that MDC intends to change the Health Supports Benefit policy in relation to noise cancelling headphones so that reimbursements do not occur. MDC will instead provide a voucher or Prezzy card up to the value of the allowed benefit to cover an

Subject	Risk	Impact	Explanation and Comments
			<p>expense with a staff selected provider. The provision of a voucher means the benefit will fall under the FBT regime, rather than PAYE.</p> <p>We understand that it is not practical to apply a similar approach to the provision of eyewear. As a result, any reimbursement payments for the provision of eyewear will need to be processed via payroll (and grossed up for the relevant Kiwisaver and student loan deductions etc).</p> <p>In addition, direct payments made in respect of the provision of eye wear and noise cancelling headphones should be included in the unclassified benefits calculations.</p> <p>However, there may potentially be scope for MDC to argue that the increased obligations and expectations on employers regarding management and prevention of health and safety risks means that the applicability of the health and safety exemption has broadened to include benefits aimed at reducing a larger number of risks, such as the provision of eyewear and noise-cancelling headphones (where the benefit structure is not via reimbursement).</p> <p>As we have not seen this approach applied successfully in practice, taking this approach comes with a risk of challenge from Inland Revenue in the event of a review or audit. In order to rely on this exemption, MDC would need to be comfortable that there is a specific health and safety risk to specific employees or categories of employees that is addressed by the provision of eyewear and headphones.</p>

## Appendix A: Our approach

Our scope uses a risk-based approach focusing on MDC's existing FBT systems and the technical treatment of FBT. Our prudential review is designed to test the technical and human / process elements of your FBT systems. We prioritise these areas as we find that Inland Revenue generally takes a risk assessment approach of these areas before deciding whether to proceed with a full audit.

After receiving the completed FBT questionnaire and undertaking our initial review of the information provided, we met with Debbie Fulton and Kathryn McDonald to clarify some queries and obtain further information and a clearer understanding of MDC's treatment of technical areas of FBT. This has enabled us to close out our review and to assist in gaining an overview of MDC's FBT systems and processes.

*We note that this FBT review was undertaken to an agreed scope. Our review is focused on the documentation provided and the completed questionnaire as well as the answers to our questions provided by Debbie Fulton. We accepted any explanations supplied at face value with limited verification. It is not intended that the review be comprehensive in nature, and we are not providing assurance on any aspect of any of MDC's FBT systems or procedures.*

### Agreed scope of our review:

- Review of the completed questionnaires;
- Interviews with the relevant team or individual(s) who prepare / review the FBT returns to discuss and clarify the treatment of technical areas of FBT;
- Review a sample of the FBT returns and supporting calculations;
- Review of any existing FBT policies and procedures;
- Running through the FBT return process with the relevant staff for the balance date tax period to identify any issues and potential efficiencies;
- Review of all non-cash benefits provided to employees; and
- Consideration of relevant issues / opportunities for each entity.



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