MINERALS COUNCIL OF AUSTRALIA

SUBMISSION ON THE TAX TREATMENT OF NATIVE TITLE BENEFITS SECTION OF THE TAX AMENDMENT BILL 2012

DECEMBER 2012

SUPPORTED BY:

- Chamber Minerals and Energy Western Australia
- South Australia Chamber of Minerals and Energy
- Minerals Council of Australia (Victorian Office)
- Minerals Council of Australia (Northern Territory Office)
- Tasmanian Minerals Council

SUBMISSION 9

MINERALS COUNCIL OF AUSTRALIA – SUBMISSION ON THE TAX TREATMENT OF NATIVE TITLE BENEFITS SECTION OF THE TAX AMENDMENT BILL 2012

Introduction

The Minerals Council of Australia (MCA) has advocated strongly about the opportunity for, and the importance of, native title benefits provided by industry being used to facilitate greater economic development and wealth creation for current and future generations of Indigenous people. We believe that using such an approach will establish vibrant, diversified and sustainable regional communities, particularly in areas where there is limited mainstream economic opportunity.

The Tax Amendment Bill 2012 (the Bill) proposes that native title benefits, provided under the *Native Title Act 1993* or under an agreement made under an Australian law to the extent that the payment or benefit relates to native title, will not be subject to income tax (including capital gains tax). It is understood that other key elements of the bill include:

- enabling monies to maintain the non-assessable non-exempt (NANE) status whether paid to an individual, community or trust; and
- making provision for retrospective consideration to payment assessments made from 2008.

Many of the concerns outlined in this submission were highlighted in our earlier submission on the exposure draft materials which aimed to provide clarity on the proposed tax/treatment of native title benefits in August 2012. It was disappointing that very few of our concerns appear to have been acknowledged and addressed in the preparation of the Bill.

While we agree with the Government's underlying policy objectives we are concerned about the unintended adverse consequences should be Bill be implemented. Specifically we are concerned that it may be counterproductive to achieving our shared objectives and may undermine decades of progress in relations between Indigenous Australians and the minerals industry, founded in a mutual desire for sustainable intergenerational benefit for Indigenous communities from mining operations on traditional communal lands.

As we have said throughout the course of successive Governments' consideration of native title and Aboriginal land rights legislation, we are committed to working with Government to ensure that the taxation treatment of payments from agreement, in all of their complex forms, from agreements contribute to and do not detract from the objective of intergenerational benefit through the facilitation of social and economic development within and for those Indigenous communities.

The MCA recommends that a better approach to what is being proposed in the Bill is one which:

- broadens the range of agreements between proponents and Indigenous groups that are eligible preferential tax treatment;
- links preferential tax treatment to a vehicle (for example an Indigenous Community Development Corporation) and purposes that deliver specific community and economic development outcomes for current and future generations of Indigenous Australians not only for the narrower class of native title claimants and holders.

The MCA's proposed approach would broaden the class of agreements and other transactions that the tax concession could apply to but narrow the purpose for which funds that receive the tax concession can be used to those directed at genuine community benefit. Funds could still be used for direct personal gain outside of activities aligned to the Closing the Gap objectives however these purposes would receive normal tax and social security treatment in the hands of recipients.

The MCA approach would result in:

- tax-exempt status for benefits used for charitable or genuine community and economic development outcomes, including interest earned on funds, that are accumulated for future generations and in turn utilised for those purposes.
- tax-reduced/effective treatment of benefits that are used for specific purposes which are already recognised and obtain special treatment within the existing taxation framework, such as pensions and superannuation funds.
- benefits used for other purposes including benefits provided to individuals for purposes outside of specific measures associated with capacity building and the Closing the Gap objectives taxed as income;
- embedding good governance and capacity building to support effective decision making while reducing administration requirements for government; and
- should not result in a significant revenue cost to Treasury and overtime will represent a net revenue to Treasury.

Discussion

The MCA specific concerns are that the Bill:

1. does not adequately address the range of agreements that are being made with native title parties;
2. does not support the range of measures in agreements which support non-native title parties, i.e. other Aboriginal people who are resident in a region but cannot demonstrate the required connection under law;
3. proceeds on the basis that benefits under native title agreements are exclusively compensatory in nature in the sense that they address extinguishment, impairment and/or suspension of native title; and
4. does not provide incentive for good governance, community and intergenerational benefit regarding management and distribution of benefits.

<u>Types of agreements</u>

The Government's focus on the tax treatment of financial and non-monetary benefits (i.e. benefits) made pursuant to agreements under the NTA (or relevant State or territory legislation) which relates to an act affecting native title or native title compensation covers only a narrow range of the sorts of agreements that are made.

The MCA agrees with the Government's stated views that native title agreements provide a valuable opportunity to establish and continue a sound relationship between Indigenous people and industry, and that native title agreement-making is an ongoing feature of economic and social relations in Australia.[1] These views are particularly important to our members as the development of mining projects involves significant investment and a long term presence in areas where resources are located. Further, these areas are in many instances, remote and regional areas where there are often a high percentage of Indigenous people in the local population.

[1] *Leading practice agreements: maximizing outcomes from native title benefits*, Discussion Paper, July 2010, The Hon. J. Macklin MP, Minister for Housing, Community Services and Indigenous Affairs and The Hon. R. McClelland MP, Attorney-General, p.4.

Agreements are negotiated with Indigenous groups, usually (but not exclusively) on the basis of a group's native title claim or determined native title. However agreements commonly also make provision to provide benefits where native title:

- may ultimately be found not to exist because a group has not been able to establish connection sufficient to establish native title; and
- has been determined to be extinguished by subsequent dealings in land.[2]

Agreements may not end up being native title related depending on the outcome of a group's native title claim or alternatively, may not be native title related from the outset if there is no native title claim.

In addition, an agreement may not be made under an Act of the Commonwealth a State or territory such as an Indigenous Land Use Agreement (ILUA) or an agreement under the "right to negotiate" provisions. Agreements may involve ancillary ILUAs but can themselves be detailed commercial documents that are not made under any legislation.

Thus the Government's proposals do not provide clarification on the tax status of payments made under all types of agreements that are being made with Indigenous groups. For those agreements, substantial effort and cost will be required in seeking ATO determination and advice on the appropriate tax treatment.

The Government's proposals also encourage a narrow approach to agreement making focussing strictly on the legal effect of third party land use on native title rights and interests. This narrow approach is contrary to the Government's objectives in developing the proposed amendments. The MCA notes that in commencing consultation in 2010 the Assistant Treasurer said that "the Government is committed to ensuring a more flexible, less legalistic approach to native title that delivers practical outcomes for Indigenous Australians. The tax system can play a valuable role in this area by ensuring that it supports the resolution of claims and the management of benefits under native title agreements".[3]

The MCA recommends broadening the range of agreements between proponents and Indigenous groups that could receive preferential tax treatment.

<u>The characterisation of payments as compensatory</u>

The Government's proposed amendments proceed on the basis that benefits under agreements are made only to address extinguishment, impairment or suspension of native title and thus are fundamentally compensatory in nature. Proponents however, make agreements to address a range of issues that are relevant to their relationship with groups, not just the legal effect of their titles and activities on native title.

The benefits provided to groups under agreements can be quite substantial and, while they are provided in satisfaction of any compensation liability, compensation is an unascertained sub-set of the total payment. Further

[2] In relation to this point note existing provisions for statutory revival of native title extinguished by dealings in land especially in s. 47B of the NTA which enables native title to be recognized even long years after a determination declaring its extinguishment, if the land reverts to Unallocated Crown Land. The point here is that there is a driver under the NTA itself for a business with a long term presence in an area to include in its agreement any land that a group asserts a traditional connection to, even if native title is currently extinguished, because of the possibility of a subsequent revival of those rights and interests. The MCA notes that the Commonwealth is seeking to extend this statutory revival regime in its current proposals to amend the NTA.

[3] See the Assistant Treasurer's Foreword and the Overview in *Native Title, Indigenous Economic Development and Tax*, Consultation Paper, May 2010, Department of Treasury.

compensation is often a small portion of the total benefits which may also include benefits directed to land access, community development and measures aimed at improving indigenous employment and business development outcomes. There is unlikely to be an agreed spilt between benefits provided by way of native title compensation and additional benefits.

Importantly, negotiations are greatly assisted by avoiding disputation over the percentage of benefits that are to be attributable as compensation, given the complexity of the issues in assessing how native title has been affected or will be affected and the lack of case law as a guide on quantifying compensation. Moreover, in the case of an agreement with a native title claim group, if native title is ultimately determined not to exist then benefits under the agreement can no longer be considered compensatory.

The MCA understands it is the Government's intention to provide non-assessable non-exempt (NANE) treatment to the full range of compensation and benefit sharing arrangements provided under any eligible agreement. However, as mentioned above, the Government's proposals potentially encourage a narrow legalistic focus on native title compensation in agreement negotiations rather than an approach that prioritises addressing the long term relationship between proponents and Indigenous groups.

Governance and distribution of native title benefits

In its discussion paper *Leading practice agreements: maximising outcomes from native title*[4] the Government stated its own objectives as being *inter alia*, that benefits received under agreements be adequately preserved and deployed for the benefit of both current and future generations.

Similarly MCA members are concerned to ensure that:

- benefits provided under agreements are managed and distributed for the benefit of the group, with limited capacity for individual benefit unless it is tied to ends such as relief of poverty, health, education and genuine community development outcomes ; and
- intergenerational benefit is secured through accumulation of an adequate portion of the benefits in properly managed tax effective funds.

Where benefits are made to individuals outside of these objectives, the MCA considers that benefits should be subject to the ordinary tax and social security treatment in the hands of the recipient.

The Government's proposal to characterise native title benefits as fundamentally compensatory in nature and apply a NANE classification to the payments even in the hands of individuals risks subverting its own policy objectives, as it removes any incentives to ensuring benefits that do qualify are managed and applied to maximise current and intergenerational benefit to the group.

There could also be significant pressure exerted by groups (especially those with determined native title) to modify the controls on management and distribution on benefits that apply under existing agreements on the basis of the tax reforms incentivising individual use of funds rather than acts which would accumulate funds and therefore attract taxation on both interest earned as well as distributions to parties not acknowledged in the initial agreement, including future generations.

[4] Leading practice agreements: maximizing outcomes from native title benefits (see above).

It is a concern that since the tabling of the Bill there have been early indications that it will be more difficult to incentivise the allocation of native title funds for community benefit and that there will be a greater demand for individual payments and the establishment of personal/family trusts. The driver being that there is no longer a financial advantage to having funds placed in a Charitable Trust. This is counter to the outcomes that Government is trying to deliver in Closing the Gap and additional measures should be adopted to prevent this early indicator becoming a reality should the legislation be passed.

The taxation treatment of benefits provided to groups where either no native title exists from the outset or where no native title is ultimately found to exist is not clarified by the proposed amendments, yet such agreements clearly promote the Government's policy objectives in promoting a sound relationship between Indigenous communities and industry, which is also what the MCA and its members seek to achieve.

The Government's objectives would be promoted if taxation advantages attached, not to the benefits, but to the entities (including charitable and discretionary trusts which appear to have been excluded from the proposals) and the purposes to which those entities can apply the benefits. The preferential tax treatment would be linked to purposes that deliver specific community and economic development outcomes for current and future generations of Indigenous Australians not the narrower class of native title claimants and holders. In summary this approach would result in:

- Tax-exempt status for benefits used for charitable or genuine community and economic development outcomes, including the accumulation for future generations of funds for those.
- Tax-reduced/effective for benefits that are used for specific purposes which are already recognised and obtain special treatment within the existing taxation framework, such as pensions and superannuation funds.
- Taxed as income for benefits used for other purposes including benefits provided to individuals for purposes outside of specific measures associated with capacity building and the Closing the Gap objectives.

The MCA considers it is important that the entities meet certain standards in relation to the management and distribution of benefits, including limitations on the transfers to individuals untied to health, education or other relief of poverty or capacity building purposes (i.e. minimum management standards). This would mean that:

- clarity would be provided for the full range of community agreements that exploration and mining proponents are providing benefits under;
- agreements with Indigenous communities that addressed disadvantage in those communities would be encouraged; and
- good governance arrangements in relation to those benefits could be secured, reducing the administration burden on government.

The capacity of those entities to hold benefits in perpetuity and to accumulate funds (while maintaining their preferential tax treatment) in order to address intergenerational benefit should also be confirmed.

This proposal would mean that where an entity does not meet minimum management standards and apply the benefits for the purposes that attract the preferential tax treatment, the preferential tax treatment would be lost. The MCA's proposal however, is that where benefits are subject to minimum management standards and the benefits are applied for the purposes that attract the preferential tax treatment then, whether they are compensation or not, they will attract the preferential tax treatment.

Charitable trusts are currently the most appropriate vehicle to secure intergenerational benefit. However, charitable trusts have limited purposes that do not permit community and economic development measures and there is some

doubt as to the extent they permit the accumulation of funds for intergenerational benefit. . In an attempt to overcome this restriction some parties have also included discretionary trusts in tandem arrangement with charitable trusts to enable a wider set of purposes to be addressed. Discretionary trusts of course do not enjoy the same tax advantages that charitable trusts do. [5]

The MCA together with the National Native Title Council has developed the concept of an Indigenous Community Development Corporation (ICDC), an alternative trust vehicle with related governance requirements and preferential tax treatment. Further detail on the ICDC is provided below (in Box A).

BOX A.

INDIGENOUS COMMUNITY DEVELOPMENT CORPORATION (ICDC)

The ICDC concept is intended as a special purpose vehicle for managing native title and other payments negotiated by traditional owners and Indigenous Groups to maximise economic and social benefits, reduce administration and provide preferential tax treatment to maximise the value of those funds. The ICDC will provide an effective single holding place for funds negotiated through native title and other agreements that can accumulate over time to deliver a substantial service or facility for Indigenous people, their communities and future generations.

Unlike models under current tax legislation, the ICDC will have the capacity to provide incentives for Indigenous peoples to not only fund community development activities to alleviate social disadvantage, but also economic development activities enabling individuals and families to participate in the mainstream economy. The ICDC would also support the accumulation of funds for the benefit of future generations.

An ICDC can be entered into on a voluntary basis and can be delivered at a scale ranging from small local funds to large regional funds that could be state based in some cases. The ICDC will be underpinned by strong governance and management processes through a model constitution that includes a set of minimum key principles, supported by a mechanism for registration, capturing and sharing information and delivering governance training. The ICDC Compliance with the governance requirements will establish the minimum criteria for the preferential tax treatment.

Limitations on individual benefit

The MCA is aware that limitations on individual benefit may be seen as discriminatory on the basis that non-Indigenous Australians can enjoy individual benefits derived from their proprietary rights and interests. Native title is a *sui generic* – or unique – communal title that belongs to the current and future community of native title holders. Accordingly, measures need to be in place to ensure that benefits derived from native title agreements are applied for the benefit of the current and future community of native title holders. The equity or non-discrimination point is addressed in that native title holders can also acquire conventional property rights and interests. Communally held benefits derived from native title can and should be directed to wealth generation, education and other measures to lift the capacity of individuals in the group to participate in main stream economic life.

While the unique, communal nature of native title is the substantive answer to the need to ensure that funds are applied primarily for community benefit, the minerals industry has learned lessons from the past. One of the lessons

[5] The MCA wishes to note that industry best practice is to include limitations on the capacity of discretionary trusts to transfer benefits to individuals that are not tied to capacity building purposes.

learnt over the last 20 years has been the divisive effect in Indigenous communities of native title benefits being paid directly to individuals. The best known example is the practice of mining companies operating in the Goldfields region of Western Australia during the 1990s of making substantial payments to registered applicants in order to secure grants of tenure, which resulted in multiple overlapping native title claims being made. Where a few individuals can secure control over benefits by virtue of a privileged position in the group, it has a divisive effect on the whole community.

Transitional Measures

As already discussed, it can be expected that some proponents who previously invested native title payments into Charitable Trusts may want to be revisit these decisions given the previous tax incentives for some individuals and communities which will no longer be relevant if the Bill is adopted. This will result in a movement of funds between charitable trusts and personal/family trusts. The Government will need to give serious consideration as to whether enabling or transitional arrangements will need to be put in place or whether existing arrangements will be expected to be retained and the resultant tax implications.

Financial Impact

It is noted that the financial impact of the Bill has been rounded to zero in each of the income years for 2012 -13 to 2015 -16. . The MCA believes the Government has significantly under estimated the revenue impact of the proposed measure. The under estimate may be based on a lack of information about the size and structure of existing and likely future agreements with native title claim groups. Although many of the agreements in question are confidential, the MCA has been provided with information from its members to the effect that:

- In the Pilbara region of Western Australia alone, it is likely that more than $200 million in payments is already being made **each year** pursuant to native title related agreements. The number of persons who benefit is quite small and is likely to number in total to no more than a few thousand people. Some of the major agreements benefit no more than a 100-300 people. Anecdotal evidence suggests that the quantum of payments is likely to increase significantly in coming years and the revenue stream will last for decades.
- The mechanisms used to receive the payments vary but current common practice is to use one or more charitable trusts and one or more (generally non-exempt) discretionary trusts or corporations.

The flow of such large amounts of money is a relatively recent phenomenon, and consequently it is possible that Treasury does not have any reliable information about them upon which to base its estimates.

If the Bill becomes law, it is inevitable that the beneficiaries of the agreements will seek to characterise all or most of the payments in question as compensation and therefore exempt from income tax. There will also be pressure to move payments away from charitable trusts (or other entities that have tax exempt status due to community benefit) into structures that allow for immediate distribution of funds to individuals or enterprises.

As a consequence, a significant proportion of agreement funds that would otherwise be taxable, will become tax exempt. Based on the information provided, that would involve tens of millions of dollars per annum in revenue foregone. Subject to confidentiality restrictions more information if necessary can be made available from MCA member companies.

By contrast, under the MCA's proposal, the role of charitable trusts would be effectively augmented by or transitioned to the ICDC model but any discretionary trust income for the benefit of individuals would remain taxable.

Further, it is our view that given the retrospectivity of the application of the Bill to 2008, and the number and size of the native title agreements that have been generated since 2008 and subsequent distributions, Government can expect to be required to:

- refund overpaid tax payments to individuals and organisations that have received native title payments since 2008. We are of the view that this could be quite substantial;
- establish a clear and transparent process that calculates refunds payable and processes for individuals and organisations to make their claims; and,
- allocate the necessary resources for the Australian Taxation Office and courts to consider the existing ambiguities between what payments are compensation and other benefits derived from ancillary agreements that are not directly related to the main compensation/benefit sharing agreement driven by the Native Title Act 1993.

Conclusion

The MCA recommends that a better approach to the Government's current proposals would be one that:

- broadens the range of agreements between proponents and Indigenous groups that could receive preferential tax treatment; and,
- links preferential tax treatment to a vehicle (for example an ICDC) and purposes that deliver specific community and economic development outcomes for current and future generations of Indigenous Australians not the narrower class of native title claimants and holders. The MCA approach would result in:
    - tax-exempt status for benefits used for charitable or genuine community and economic development outcomes, including funds that are accumulated for future generations and in turn utilised for those purposes.
    - tax-reduced/effective for benefits that are used for specific purposes which are already recognised and obtain special treatment within the existing taxation framework, such as pensions and superannuation funds.
    - benefits used for other purposes including benefits provided to individuals for purposes outside of specific measures associated with capacity building and the Closing the Gap objectives taxed as income; and
    - good governance and capacity building being embedded in agreements to support effective decision making while reducing administration requirements for government.

The MCA is concerned that the Bill describing how tax treatments will be applied to native title benefits has not given adequate consideration to how good governance, community and economic development, accumulation, wealth creation and intergenerational benefits would be encouraged. It is also of concern that the impacts of the Bill have not been fully understood and appropriate management strategies put into place. It is also our view that the budget impacts have been significantly under represented.

The impacts of this proposed taxation amendment require an integrated Government response which is currently not apparent, but which is critical to manage and mitigate the impacts whilst being able to achieve stated Government policy.

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The MCA requests further engagement between the Government and native title and industry groups to address the issues raised in this submission. Should you wish to discuss any of the issues outlined in this paper in further detail,

Yours sincerely,

Melanie Stutsel
Director – Health, Safety, Environment and Community Policy