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Issues in the Bills

Company directors and the superannuation guarantee

2.1 At the hearing, the Australian Institute of Company Directors (AICD) outlined its concerns with the provisions. The key issues are discussed below.

Restricting scope to phoenixing

Background

2.2 Currently, the Tax Laws Amendment (2012 Measures No. 2) Bill 2012 and the Pay As You Go Withholding Non-compliance Tax Bill 2012 extend the existing penalty provisions of the PAYG Withholding Tax to the Super Guarantee, and strengthen the defense provisions for both. Director penalties were introduced in 1993 as a trade-off to removing the Australian Taxation Office (ATO) as a preferred creditor.[1]

2.3 The amendments do not distinguish between whether a company director is engaged in phoenixing or not. Broadly, a general liability is to be imposed on directors where the company involved fails to notify the ATO if it does not pay its employees' super in full.

2.4 The Tax Laws Amendment (2011 Measures No. 8) Bill 2011 and the Pay As You Go Withholding Non-compliance Tax Bill 2011 aimed to prevent directors from escaping their superannuation obligations. They worked the same way as the current Bills and in the previous inquiry industry

1 Ms Kate Preston, Treasury, *Committee Hansard,* Canberra, 4 June 2012, p. 3.

expressed concern that they would affect 'all directors of all companies throughout Australia – over two million, in fact.'[2] In its 2011 advisory report, the committee noted that the Bills did not add to existing requirements, but instead applied a more effective penalty regime. However, given industry concerns, the committee recommended that the Government investigate whether it was possible to amend the Bills to better target phoenix activity.[3] Following further consultations, the Government did not amend the Bills in this regard.

2.5 Industry reiterated its preference for targeting phoenix operators in this inquiry. The Institute stated:

> ...the problem with this bill is it is not confined to fraudulent phoenix operators. By failing to define fraudulent phoenix activity, it instead targets all of Australia's 2.2 million directors including those who volunteer their time to work for charities and community organisations. Following submissions to this committee last year, it recommended the government investigate whether it was possible to amend the bills to better target phoenix activity. Yet the government has made virtually no attempt to target phoenix activity in revising the bill. We strongly recommend this bill not be passed until a definition of fraudulent phoenix activity is inserted and until it is amended so that the measures only apply when fraudulent phoenix activity is suspected.[4]

2.6 The Institute accepted that company directors should be responsible and accountable for the payment of their employees' superannuation. However, it did not accept that directors should be liable for it.[5]

Analysis

2.7 The committee notes that, in order for a company director to be subject to these provisions, there would need to be an ongoing period of non-compliance. The superannuation guarantee operates on a quarterly basis. If a company does not pay any superannuation during a January to March

2 Professor Bob Baxt AO, AICD, House of Representatives Standing Committee on Economics, *Advisory report on the Tax Laws Amendment (2011 Measures No. 8) Bill 2011 and the Pay As You Go Withholding Non-compliance Tax Bill 2011,* November 2011, p. 26.

3 House of Representatives Standing Committee on Economics, *Advisory report on the Tax Laws Amendment (2011 Measures No. 8) Bill 2011 and the Pay As You Go Withholding Non-compliance Tax Bill 2011,* November 2011, p. 27.

4 Mr John Colvin, AICD, *Committee Hansard,* Canberra, 4 June 2012, p. 2.

5 Mr John Colvin, AICD, *Committee Hansard,* Canberra, 4 June 2012, p. 11.

quarter, then this raises a superannuation guarantee shortfall. The company would be required to report this shortfall to the ATO by 28 May. If the shortfall is not reported by then the directors will be liable for director penalties for this amount from this date.[6]

2.8 Further, as Treasury advised the committee, the act of not reporting a shortfall is a key requirement for a director penalty:

> The aspect of the measure that does not allow a company to remit a penalty by liquidating or going into administration if a debt is three months old is targeting people who are trying to avoid detection, because those provisions only have application if the debt is unreported. The bill was never intended only to apply to phoenix operators; it could not, because it builds on existing law. It was intended to protect workers' entitlements and it does that.[7]

2.9 In other words, there must be an extended period of non-compliance for a director to be liable, not just in terms of not paying super, but also in terms of not communicating this fact to the ATO. The former may be restricted by a company's cash flow, but the latter only requires correspondence.

2.10 Witnesses at the hearing discussed how these provisions might operate in different sized companies. In larger companies, as the Institute stated, the directors would be less involved in the day to day running of the company and they would not have direct knowledge of whether super had been correctly paid. One effect of the provisions would be to push more superannuation-related information up to boards.[8] Treasury also noted that larger companies tend to have strong systems covering salaries and employee benefits. The real difference will occur in more closely held entities.[9]

Conclusion

2.11 The committee accepts that company directors have a large number of obligations and that this potentially adds to them. However, extended and consistent non-compliance is required before personal liability applies. Not only must super be unpaid, but the company must omit the simple step of reporting it to the ATO. This compares with the position of sole

6 Explanatory Memorandum, Tax Laws Amendment (2012 Measures No. 2) Bill 2012; Pay As You Go Withholding Non-compliance Tax Bill 2012; Income Tax (Managed Investment Trust Withholding Tax) Amendment Bill 2012, p. 16.

7 Ms Kate Preston, Treasury, *Committee Hansard,* Canberra, 4 June 2012, p. 4.

8 Mr John Colvin, AICD, *Committee Hansard,* Canberra, 4 June 2012, pp. 9-10.

9 Ms Kate Preston, Treasury, *Committee Hansard,* Canberra, 4 June 2012, p. 4.

traders who are already personally liable for non-payment of superannuation.[10]

2.12 The Committee questions whether it is practical to limit the Bills to cases where pheonixing is suspected, as requested by industry. Since pheonixing happens after the fact, it would place an unreasonable expection on the ATO to identify possible future breaches. It could be argued that it would add a layer of unfairness and considerable room for error. These amendments only apply where a company has consistently not met its obligations and failed to notify the ATO of this for several months and provides strengthened defence provisions for directors. The committee has come to the view that no amendments are required.

New directors

Background

2.13 Sections 269-15 and 269-20 of the *Taxation Administration Act 1953* provide that directors must cause a company to comply with an 'obligation' and that they are liable to pay a penalty 'at the end of the due day'. Someone who becomes a director after the due day adopts this obligation 14 days after they become a director.

2.14 The Bills extend this 14-day period for new directors to 30 days. This is a key difference from the package of Bills last year. It recognises that new company directors will have extra obligations in that they must turn their minds to the company's superannuation affairs, in addition to its tax affairs.[11] Importantly, this extension applies both to directors' tax and super obligations.

2.15 Despite accommodating the interests of directors, the Institute argued at the hearing that making a director liable for something that occurred before they were appointed was inherently unfair:

> No person in Australia in any occupation should commence a new job or a new position only to find that within 30 days they become personally liable for a breach that occurred before they commenced work in the role, which involve acts which they, by definition, cannot have taken part in and cannot be held culpable for. We are of the view that applying automatic liability on new

10 Mr Adam Craig, Treasury, *Committee Hansard,* Canberra, 4 June 2012, p. 6.

11 Explanatory Memorandum, Tax Laws Amendment (2012 Measures No. 2) Bill 2012; Pay As You Go Withholding Non-compliance Tax Bill 2012; Income Tax (Managed Investment Trust Withholding Tax) Amendment Bill 2012, pp. 14-15.

> directors for acts of the company which occurred before they were a director is particularly offensive to the rule of law. We recommend that a penalty regime not apply to directors unless they were a director at the time of the company's original breach and had some level of culpability in relation to the company's offence when it is confined to phoenix activity.[12]

Analysis

2.16 At first glance, there may be a question mark about making someone liable for something that they did not do, or did not omit to do. However, it is important to also ask the counterfactual question: 'What would happen if new directors were not made personally liable?' Treasury responded that unscrupulous operators could use a new director defence as a loophole against liability:

> That is already a characteristic of some phoenix operators. They will appoint a spouse or someone. In fact the ATO will point to instances where people have basically gone through the phone book and picked out names and listed those people as directors. Yes, if there were no penalty against new directors then that is exactly what could happen. You could just cycle through directors.[13]

2.17 In other words, allowing a new director to avoid liability for the superannuation guarantee charge simply because they are new would provide the sort of loophole that phoenix operators are adept at exploiting. What is important is that there must be some balance between the interests of new directors and employees' rights to their superannuation. The mechanism in the Bill to achieve this balance is extending the period of grace for new directors from 14 to 30 days.

Conclusion

2.18 It is appropriate to make new directors liable for the superannuation guarantee charge of a company where the super liability arose before they became a director. There are three reasons for this. Firstly, if they were not liable in some way, this would be an easily exploitable loophole for phoenix operators. Secondly, directors will have a longer, 30-day period of grace to ensure that either the super and tax affairs of a company are in

12 Mr John Colvin, AICD, *Committee Hansard*, Canberra, 4 June 2012, p. 2.

13 Mr Adam Craig, Treasury, *Committee Hansard*, Canberra, 4 June 2012, p. 11.

order, or advise the ATO of the liability, which would in practice lead to the ATO and the entity agreeing on a payment arrangement.

2.19 Finally, the position of a director of a company is different to that of an ordinary individual. A company is a legal device created to facilitate commerce through protecting investors with limited liability. In order to achieve this, directors must have high standards of ethics, skills and leadership. The committee fully supports legislation that requires these standards of directors when they join a company in relation to its employees' superannuation.

Not-for-profit organisations

Background

2.20 At the hearing, the Institute noted that not-for-profit organisations incorporated under the *Corporations Act 2001* would be affected by the provisions and that this would be very onerous on organisations that are run by volunteers.

> ... 11,700 companies limited by guarantee are in operation at the moment. I assume many of those would be charities, like the one I was on, for example, and that directors per this legislation—because it refers to Companies Act directors—would be picked up in that area...
>
> These guys are volunteers: would some of them have the capacity to sit down and work out all the problems they need to do? Would company directors have done a company directors course to work all this out? The answer is it would be a hard ask for these people.[14]

Analysis

2.21 The committee analysed this issue in its report last year. In particular, Treasury provided the committee with evidence that most not-for-profit organisations do not come under the *Corporations Act 2001*:

> Clubs and associations are commonly incorporated under the incorporated associations legislation in the various states and territories. As clubs, sporting associations and not-for-profits are generally not run as companies under the *Corporations Act 2001*,

14 Mr John Colvin, AICD, *Committee Hansard*, Canberra, 4 June 2012, p. 12.

> the director penalty provisions and proposed changes will not alter their status, obligations or potential implications.[15]

2.22 This is confirmed by data published by the Australian Bureau of Statistics. In June 2007, there were 41,008 not-for-profit organisations in Australia.[16] According to the Institute's figures, up to approximately one quarter of these are companies limited by guarantee.

2.23 Further, it is well known that the compliance obligations for corporations under national law are more onerous than for state or territory-based associations. An example is the website advice given by the Queensland Council of Social Service:

> Generally speaking, the regime for incorporated associations under the Queensland Associations Incorporation Act is simpler and more straightforward than the regime for companies under the Commonwealth Corporations Act.
>
> Queensland's Associations Incorporation Act was specifically designed to provide a simple and inexpensive means of incorporating not-for-profit groups. It is likely that, with help from resources that explain the Associations Incorporation Act (ideally supported by a good operations manual), most people would be able to assist in the running of an effective association without specialist skills or training.
>
> In contrast, the Corporations Act is a much more complex, lengthy piece of legislation that governs both for-profit companies, as well as not-for-profit companies limited by guarantee.[17]

2.24 Therefore, it is reasonable to expect that the more volunteer-driven community groups would be incorporated under simpler state or territory legislation. Groups incorporated under the *Corporations Act 2001* would be used to a higher level of compliance and those incorporating under it have fair notice of the higher compliance costs involved.

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15 Treasury, *Submission 17,* p. 1, from the House of Representatives Standing Committee on Economics, Inquiry into the Tax Laws Amendment (2011 Measures No. 8) Bill 2011 and the Pay As You Go Withholding Non-compliance Tax Bill 2011.

16 Australian Bureau of Statistics, Not-for-profit Organisations, Australia, 2006-07 (Re-issue), Cat. No. 8106, 'Overview,' <http://www.abs.gov.au/ausstats/abs@.nsf/ Products/8106.0~2006-07+(Re-Issue)~Main+Features~Overview?OpenDocument>, viewed 7 June 2012.

17 Queensland Council of Social Service, 'Incorporated association or a company limited by guarantee,' <http://www.communitydoor.org.au/incorporated-association-or-a-company-limited-by-guarantee>, viewed 7 June 2012.

Conclusion

2.25 The committee reiterates the comments that it made on this issue in its report on the 2011 phoenixing measures. It is concerned that there is significant confusion about the status and responsibility of directors and office holders in the voluntary and not-for-profit sectors, most of whom are governed by the less onerous requirements of state and territory associations legislation. Based on evidence to the committee and publicly available statistics, there is no reason to believe that the Bills have any negative implications for the sector.

Disputing an estimate

Background

2.26 The Bills apply the current estimates system to any unpaid superannuation guarantee amounts. The estimates system is designed to allow the ATO to take prompt action to recover amounts so that non-compliant entities do not escape their liabilities.

2.27 Under Division 268 of the *Taxation Administration Act 1953*, the Commissioner may estimate an unpaid and overdue amount of a liability. The Commissioner must estimate what is reasonable based on all relevant information and must give the taxpayer written notice of the estimate. A taxpayer can have an estimate reduced or revoked through information within an affidavit or statutory declaration provided to the Commissioner, within seven days, or longer if the Commissioner agrees to an extension. If the amount is not paid within seven days of the notice, then the general interest charge will apply to any remaining liability, dated from when the original liability arose.

2.28 At the hearing, the Institute expressed concern about how the estimates system would translate to the superannuation guarantee charge in practice, in particular that the seven day period may not be sufficient to collect the required information:

> My concern remains with this, essentially, around the whole estimates procedure and the capacity to issue an estimate. It may be that a particular former employee feels that the super obligations were not met and has a chat to the ATO, and the ATO issues an estimate. The estimate may be wrong. The employee's knowledge may be imperfect. There is not a lot of detail around

> the whole estimate procedure. I guess that is a concern. Once you kick off that estimate, it all rolls on...[18]
>
> If it is some years down the track, it is a question of assembling the information. Seven days is tight, it really is. People might have moved on and you do not have their latest address. I have certainly been involved in that. I know it is difficult, and seven days is just extraordinarily tight.[19]

Analysis

2.29 At the hearing, Treasury made two responses to this criticism. Firstly, it stated that the seven day period for estimates has applied to tax matters generally and that it has operated satisfactorily in a field more complex than superannuation:

> I would also like to say that it has been said that the estimates regime for pay-as-you-go withholding has been seven days since it has been in existence. I do not see what is more difficult about working out a superannuation guarantee obligation which is simply known—if you look at how much salary and wages have been paid, it is nine per cent. With pay-as-you-go withholding you have got marginal tax rates that differ from the level of salary paid to the employee. I think it would be harder to work out your pay-as-you-go withholding obligations. It has been seven days all along and it seems to be working.[20]

2.30 Treasury also suggested that, if a company is communicating and cooperating with the ATO, it would have the option of extending the seven day period for the taxpayer to provide the affidavit to the ATO. In fact, one of the key purposes of the director penalty regime is to encourage directors 'to enter into a conversation with the ATO.'[21]

2.31 The Institute made its own counter-arguments. In relation to Treasury's first point, it stated that although calculating a superannuation entitlement was simple, the question in many superannuation disputes was whether an individual was an employee or contractor.[22] Treasury responded that

18 Mr Shayne Carter, AICD, *Committee Hansard,* Canberra, 4 June 2012, pp. 6-7.

19 Mr Shayne Carter, AICD, *Committee Hansard,* Canberra, 4 June 2012, p. 8.

20 Mr Adam Craig, Treasury, *Committee Hansard,* Canberra, 4 June 2012, p. 8.

21 Ms Kate Preston, Treasury, *Committee Hansard,* Canberra, 4 June 2012, pp. 8, 11.

22 Mr Shayne Carter, AICD, *Committee Hansard,* Canberra, 4 June 2012, p. 8.

directors were protected in this instance by the reasonable care and reasonably arguable defence.[23]

2.32 In relation to Treasury's second point, the Institute queried whether a taxpayer could or should rely on the goodwill of the Commissioner.[24] However, the Institute did not provide evidence to the committee that the ATO does not apply its discretion appropriately when considering whether to extend the seven day period for estimates. Rather, the committee is of the view that effective administration in agencies often depends on officials exercising their judgement. The committee also notes that the current ATO practice statement on enforcement measures for collecting liabilities requires ATO staff to cooperate with compliant taxpayers. Clause 26 states:

> The Commissioner will make an estimate and issue a notice in circumstances where there is reason to suspect that there is a liability to withhold and remit and where:
>
> - there is difficulty in establishing that liability expeditiously
> - there is reason to suspect that the debtor has reported less than the total amount of withholdings in a period
> - there is a history of a failure to notify liabilities as required by the law or a history of late payment and there is no reason or evidence to believe that a liability has not been incurred
> - attempts to establish debts are met with a lack of cooperation - for example, phone calls are not returned, or there is a refusal to provide details of amounts withheld when requested, or there are continuing delays or excuses for not making details available
> - the debtor refuses access to, or cooperation with, field officers
> - the debtor continually breaks appointments or refuses to meet with tax officers
> - the debtor claims that no amounts have been withheld but there is evidence to suggest that amounts have, in fact, been withheld...[25]

2.33 Clause 29 requires ATO staff to consider extensions of the seven day period when this will assist in determining the correct liability amount:

> The Commissioner only seeks to recover an amount equivalent to the underlying liability...Accordingly, in the interests of

23 Mr Adam Craig, Treasury, *Committee Hansard,* Canberra, 4 June 2012, p. 8.

24 Mr Shayne Carter, AICD, *Committee Hansard,* Canberra, 4 June 2012, p. 8.

25 ATO, 'Practice Statement Law Administration PS LA 2011/18', 14 April 2011, <http://law.ato.gov.au/atolaw/view.htm?locid='PSR/PS201118/NAT/ATO'&PiT=99991231235958#P22>, viewed 8 June 2012.

> ascertaining the correct amount of the liability, the Commissioner will consider a request to extend the time for lodgment of the statutory declaration where the debtor can satisfy the Commissioner that it cannot be completed or lodged within the required time.[26]

Conclusion

2.34 The estimate process is designed to allow the ATO to quickly recover liabilities where there is evidence that monies are at risk through non-compliance. It has been working effectively to date and the committee sees no additional risk in extending it to the superannuation guarantee charge. This is especially so, given ATO practice of cooperating with compliant taxpayers.

Consolidation and TOFA

2.35 The taxation of financial arrangements (TOFA) provides an overarching framework in relation to the taxation of financial arrangements. The emphasis of the arrangements is on economic considerations, rather than the prior tax law emphasis on legal form. The previous approach led to inconsistencies and layers of complexity.[27]

2.36 TOFA was introduced to reduce the influence of tax considerations on how financial arrangements are structured, emphasising other factors, such as risk, when making financing decisions.

2.37 Division 230 rules covering the tax treatment of gains and losses on financial arrangements were introduced in 2009, to apply generally from 1 July 2010. Taxpayers had the option to elect to 'ungrandfather' their existing financial arrangements, which involved bringing their existing financial arrangements into the new TOFA regime.

2.38 Taxpayers were required to elect to ungrandfather their financial arrangements on, or before, their first income tax return was due under

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26 ATO, 'Practice Statement Law Administration PS LA 2011/18', 14 April 2011, <http://law.ato.gov.au/atolaw/view.htm?locid='PSR/PS201118/NAT/ATO'&PiT=99991231235958#P22>, viewed 8 June 2012.

27 Australian Tax Office website, *Guide to the taxation of financial arrangements (TOFA) rules*, <http://www.ato.gov.au/businesses/content.aspx?doc=/content/00194622.htm&pc=001/003/109/001/002&mnu=0&mfp=&st=&cy= >, viewed 6 June 2012.

the Division 230 rules. The option to ungrandfather was intended as a compliance mechanism to enable taxpayers to apply a single set of rules.

2.39 At the time tax payers had to make a judgement about whether to ungrandfather their existing arrangements, taking into consideration how the adjustment arrangement under TOFA might affect them, in contrast to the ongoing administrative demands of separately assessing some arrangements that were subject to Division 230 and the prior financial arrangements that would have different requirements.

2.40 A number of submitters raised concerns about Schedule 2 of the Tax Laws Amendment (2012 Measures No. 2) Bill 2012.[28] The main issue considered during the inquiry was the retrospective application of the proposed provisions.

Retrospectivity

Background

2.41 The amendments proposed in Schedule 2 are to ensure that the tax treatment of the financial arrangements is consistent with the TOFA tax timing rules. This involves recognising gains and losses from financial arrangements on an accruals rather than realisation basis. These changes are intended to have retrospective effect from the commencement of the TOFA (Division 230) rules on 1 July 2010.

2.42 The Tax Institute acknowledged the logic of the amendments on a 'go-forward' basis,[29] but objected to the retrospective element of Schedules 2 and 3 of the Bill. It expressed concern that the retrospective application of some of the measures in Schedules 2 and 3 would be detrimental to certain taxpayers, and stated:

> ...while the circumstances for some parts of the legislation before us have been justified in terms of retrospective change and there are some minor elements, it is certainly not the case for the vast majority of the measures in this bill. It appears that the government has taken the opportunity to go far beyond those small measures where retrospective application is appropriate.

28 The Tax Institute, *Submission 3*; Greenwoods & Freehills, *Submission 5*; and Deloitte Tax Services, *Submission 7*.

29 Mr Andrew Hirst, The Tax Institute, *Committee Hansard*, Canberra, 4 June 2012, p. 18.

> As I have discussed, the outcome will be the cause of significant commercial detriment for a large number of taxpayers.[30]

2.43 In evidence to the committee, the Tax Institute outlined what the proposed changes in Schedule 2 involved and how they could affect certain groups, stating:

> The issue really arises in relation to financial arrangements where you have a consolidated group...
>
> The announcement was made on 25 November 2011 and, in essence, it operates to effectively deem A Co. to have received an amount equal to the accounting value of that swap at the time when B Co. joined the group. So, in essence, it says, 'You're treated as effectively having received $100,' which means that if A Co. then closes out of that swap the next day and pays $100, A Co. will no longer get a deduction in relation to that.[31]

2.44 In particular, submitters expressed concern about the impact on groups who had chosen to ungrandfather their financial arrangements when they moved under the TOFA rules. The Tax Institute argued that:

> ...we are in a situation where if a taxpayer has made this compliance ungrandfathering election (1) they are in a worse position than taxpayers who are not subject to TOFA, because they still get the deduction, (2) they are in a worse position than taxpayers who are subject to TOFA but did not make this compliance ungrandfathering election, because they would still get the deduction because these provisions would not apply to their historic arrangements and (3) they are in a worse position than the other class of taxpayers who have been granted this further exception under the provisions.[32]

2.45 Certain classes of taxpayers, such as those who had received Australian Taxation Office (ATO) rulings would not be affected by the retrospective application of this schedule.

Analysis

2.46 At the public hearing on 4 June 2012, the committee and witnesses discussed the merits and drawbacks of retrospective legislation, generally, and specifically in relation to Schedule 2.

30 Mr Robert Jeremenko, The Tax Institute, *Committee Hansard*, Canberra, 4 June 2012, p. 16.

31 Mr Andrew Hirst, The Tax Institute, *Committee Hansard*, Canberra, 4 June 2012, p. 16.

32 Mr Andrew Hirst, The Tax Institute, *Committee Hansard*, Canberra, 4 June 2012, p. 17.

2.47 Treasury indicated that when the TOFA regime was introduced, the Government foreshadowed that 'as we identify unidentified issues or the law does not achieve its original policy intention, further refinements through retrospective legislation, might be necessary.'[33]

2.48 In relation to the effect of the Schedule 2 changes on particular taxpayers, Treasury clarified that:

> ...there could be assessable income and allowable deductions with respect to a liability. Normally people think about liability as only deductions. When it is related to an out-of-the-money swap, the market value can move in a positive direction, which gives you an assessable income, or it can move in a negative direction, which gives you an allowable deduction. So there could be gains and losses associated with a particular liability. I think Mr Hirst is talking about a deduction in relation to a liability. That is only true if, in the period that we are talking about, the market moved against this particular derivative. If the market moved for this derivative in the same period, you could have unrealised gains.[34]

2.49 Treasury noted that the ungrandfathering election was required to be made early in a taxpayer's move to the TOFA regime, to prevent taxpayers making a decision in hindsight as to which choice would provide a tax advantage.

2.50 Treasury indicated that the Schedule 2 measures were restoring the original intent of the TOFA rules, stating:

> ...in relation to the vast majority of TOFA taxpayers which have made the [ungrandfathering] election to match their tax with accounting—that is what we call the fair-value taxpayer, financial report taxpayer or foreign currency retranslation taxpayers—what is in schedule 2 was the original policy intention. So there was no policy shift with respect to those taxpayers, and that was clearly spelt out in the EM and in the following consultations. In one of the consultations, with the banking industry, we actually said at the consultation that making this transitional election could potentially wipe out your permanent differences between tax and accounting. Therefore it is a purely technical amendment for those taxpayers.[35]

33 Ms Nan Wang, Treasury, *Committee Hansard*, Canberra, 4 June 2012, p. 17.

34 Ms Nan Wang, Treasury, *Committee Hansard*, Canberra, 4 June 2012, p. 17.

35 Ms Nan Wang, Treasury, *Committee Hansard*, Canberra, 4 June 2012, p. 19.

Conclusion

2.51 When the TOFA regime was introduced, the Government foreshadowed that retrospective changes to the law were possible to ensure that the TOFA regime achieves its policy intent.

2.52 The committee's view is that groups who chose to ungrandfather their financial arrangements will not be unfairly disadvantaged by the provisions in Schedule 2 of the Tax Laws Amendment (2012 Measures No. 2) Bill 2012. The decision for a group to ungrandfather its financial arrangements when moving into the TOFA regime in 2010 was never intended to be based on what would provide the taxpayer with a greater tax advantage. It was designed to simplify compliance.

2.53 The provisions in Schedule 2 restore the original policy intention for the interaction of consolidated groups and the TOFA rules in relation to the treatment of financial assets.

Consolidation

Retrospectivity

Background

2.54 Consolidation arrangements commenced in 2002. The consolidation regime allows the head company of a consolidated group to lodge tax returns on behalf of all the entities in the group. It was introduced to reduce tax compliance costs. However, deficiencies in the consolidation regime were identified in the years following its introduction. One area identified for improvement was in how the cost of an asset is recognised when acquired by a company.

2.55 Legislative changes in 2010 broadened the scope of the residual tax cost setting rule and introduced the rights to future income rule. This enabled consolidated groups to claim tax deductions in relation to these rules, effective from 2002.

2.56 The changes had a significant negative impact on revenue, which the Tax Laws Amendment (2012 Measures No. 2) Bill 2012 seeks to address. Treasury explained to the committee that:

> ...[problems] started to emerge towards the end of 2010 when the tax office brought to our attention that significant claims were

> coming in. Early in 2011 the Board of Taxation raised concerns directly with the government that it thought that some activity that was happening was undesirable. That is what led the government to undertake the review and see if it could establish the concerns being raised.[36]

2.57 Schedule 3 of the Bill proposes to modify the consolidating tax cost setting and rights to future income rules so that the tax outcomes for consolidated groups are more consistent with the tax outcomes for non-consolidated groups when acquiring assets.

2.58 How the changes will affect consolidated groups will depend on when the asset was acquired. Schedule 3 proposes three distinct categories: pre-rules (prior to the announcement of the changes on 12 May 2010); interim rules (between 12 May 2010 and 30 March 2011); and prospective rules (after 30 March 2011).

2.59 The pre-rules are to restore the original tax cost setting rules that operated prior to the 2010 amendments. The rules will apply to acquisitions prior to 12 May 2010 (when Parliament passed the 2010 amendments). Schedule 3 also modifies the rules to:

- limit deductions for rights to future income to unbilled income assets;
- ensure that a deduction is allowed for the reset tax costs for consumable stores; and
- treat certain assets as goodwill.[37]

2.60 The interim rules restore the current 2010 residual tax setting and rights to future income rules and modifies the rules to:

- treat certain assets as goodwill;
- ensure that no value is attributed to certain contractual rights to future income; and
- ensure that the reset tax costs for consumable stores are deductible.[38]

2.61 The rules will apply broadly to the period between 12 May 2010 and 30 March 2011. These rules are designed to 'protect taxpayers who acted

36 Mr Anthony Regan, Treasury, *Committee Hansard*, Canberra, 4 June 2012, p. 25.

37 Explanatory Memorandum, Tax Laws Amendment (2012 Measures No. 2) Bill 2012; Pay As You Go Withholding Non-compliance Tax Bill 2012; Income Tax (Managed Investment Trust Withholding Tax) Amendment Bill 2012, p. 105.

38 Explanatory Memorandum, Tax Laws Amendment (2012 Measures No. 2) Bill 2012; Pay As You Go Withholding Non-compliance Tax Bill 2012; Income Tax (Managed Investment Trust Withholding Tax) Amendment Bill 2012, p. 105.

on the basis of the current law before the Board of Taxation review was announced.'[39]

2.62 The prospective rules will apply generally after 30 March 2011, when the Government announced that it had asked the Board of Taxation to examine the rights to future income rules and the residual tax cost setting rules.

2.63 In evidence to the committee, Treasury explained the reason for the changes and how the different rules would apply:

> One of the issues that the Board of Taxation raised and was concerned about was that the 2010 amendments did bring in a specific deduction that was available only for consolidated groups. The board emphasised that, in its view, consolidated groups should only get deductions that are available for all other taxpayers. So, under both the pre rules and the interim rules, there still is a specific deduction that is available only for consolidated groups; but under the prospective rules that has been removed, so you revert to deductions that are available for other taxpayers.[40]

2.64 Submitters opposed the retrospective application of certain amendments contained in Schedule 3.[41] In evidence to the committee, the Tax Institute commented that:

> ...part of the proposed amendments in schedule 3 are quite appropriate in clarifying that certain items such as customer relationships would constitute goodwill and there would be no deduction in respect of those types of assets. Where I think it is not appropriate is going back some 10 or 12 years and denying deductions that taxpayers would have thought, or did think, were available given the combined effect of the December press release through to the amending law in 2010.[42]

2.65 Treasury noted that in a recent speech the Assistant Treasurer covered the issue of retrospectivity in tax law, stating:

> One of the things [the Assistant Treasurer] said was that beneficial retrospective tax changes that go too far carry with it the risk that

39 Explanatory Memorandum, Tax Laws Amendment (2012 Measures No. 2) Bill 2012; Pay As You Go Withholding Non-compliance Tax Bill 2012; Income Tax (Managed Investment Trust Withholding Tax) Amendment Bill 2012, p. 103.

40 Mr Anthony Regan, Treasury, *Committee Hansard*, Canberra, 4 June 2012, p. 22.

41 The Tax Institute, *Submission 3*; TPG Telecom, *Submission 4*; Greenwoods & Freehills, *Submission 6*; Deloitte Tax Services, *Submission 7*; and Ernst & Young, *Submission 8*.

42 Mr Peter Murray, The Tax Institute, *Committee Hansard*, Canberra, 4 June 2012, p. 20.

> the government will need to subsequently introduce adverse retrospective tax changes. The consolidation measures are a good example of this. The key reason why the amendments announced in 2011 needed to be retrospective was that the beneficial 2010 amendments were also retrospective to 2002.[43]

2.66 Treasury maintained that the pre-rules and interims rules in Schedule 3 must be retrospective, as they are 'taking away the unexpected and unintended retrospective benefits of the 2010 changes to law and is necessary to protect a very significant amount of revenue that is otherwise at risk.'[44] Treasury estimate the revenue risk to be in the order of $6 billion, based on claims from around 60 large consolidated groups.

Analysis

2.67 At the public hearing participants acknowledged that the 2010 changes had significant revenue impact that had not been anticipated by the Government or industry, with the nature of certain claims not envisaged in 2010.[45]

2.68 In discussion with the committee, Treasury advised that the retrospective nature of the pre-rules was necessary to address the significant impact on revenue. Treasury stated:

> ...the primary reason for introducing the pre-rules...is to protect the significant amount of revenue that would otherwise be at risk because people are able to take advantage of the retrospective changes that were made in 2010 in an unexpected way. We are talking about revenue in the order of $6 billion, so it is very significant.[46]

2.69 The Tax Institute argued that the interim rules in Schedule 3 go beyond protecting taxpayers and have 'taken away deductions in respect of customer contracts.'[47]

2.70 However, Treasury maintained that the modifications are 'largely consistent with recommendations that were made by the Board of Taxation to clarify those rules for that period.'[48]

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43 Mr Anthony Regan, Treasury, *Committee Hansard*, Canberra, 4 June 2012, p. 28.
44 Mr Anthony Regan, Treasury, *Committee Hansard*, Canberra, 4 June 2012, p. 25.
45 Discussed in *Committee Hansard*, Canberra, 4 June 2012, p. 21.
46 Mr Anthony Regan, Treasury, *Committee Hansard*, Canberra, 4 June 2012, p. 21
47 Mr Peter Murray, The Tax Institute, *Committee Hansard*, Canberra, 4 June 2012, p. 21.
48 Mr Anthony Regan, Treasury, *Committee Hansard*, Canberra, 4 June 2012, p. 21.

2.71 The Tax Institute expressed concern about the date from which the prospective rules will apply. It proposed that a more appropriate date for the prospective rules to take effect was 25 November 2011, when the intended changes were announced. It argued that, although from 30 March 2011 it was known that the Board of Taxation was investigating these matters, the resulting prospective changes were not known.[49]

2.72 Treasury indicated that the prospective rules apply 'from the date that the government said it would review the operation of the rules.' Treasury also noted that the modifications are 'to a large degree' consistent with some of the Board of Taxation recommendations, with refinements made when developing the proposed changes.[50]

2.73 Treasury acknowledged that some of the changes in the Bill go beyond what was contemplated in 2010. The prospective rules propose 'fundamental changes' to address the problems that emerged following the 2010 amendments. Treasury stated:

> One of the key problems from the 2010 amendments is that, with this consolidation tax costing process, some taxpayers revisited the assets that they were identifying for consolidation purposes. They started in particular to identify a range of intangible type assets, which are not generally recognised under the tax system. The difficulty with that is that, where such assets are not recognised under the tax system, they get allocated a cost. Taxpayers reasonably seek to find a way to deduct that cost. Under the prospective changes a key change is that under consolidation you only recognise assets are those that are ordinarily seen by the tax system and therefore there will be a way to deal with them. That is where they differ.[51]

2.74 Consolidated groups that have already made a claim and received a tax refund, or have an ATO ruling, will generally be protected from the retrospective changes in the pre-rules and interim rules. Treasury confirmed at the hearing that taxpayers who 'have received money from the ATO...will essentially be protected from the changes, except in a very unusual circumstance.' [52]

49 Mr Peter Murray, The Tax Institute, *Committee Hansard*, Canberra, 4 June 2012, p. 21.
50 Mr Anthony Regan, Treasury, *Committee Hansard*, Canberra, 4 June 2012, p. 21.
51 Mr Anthony Regan, Treasury, *Committee Hansard*, Canberra, 4 June 2012, p. 24.
52 Mr Anthony Regan, Treasury, *Committee Hansard*, Canberra, 4 June 2012, p. 26.

2.75 The retrospective changes are to address the $6 billion revenue risk. No significant revenue impact is expected for the prospective changes. Treasury stated that:

> ...under consolidation you go through an exercise of resetting the tax costs of assets. To do that you work out the allocable cost amount. In the basic case, the allocable cost amount is the cost of buying a joining entity's shares plus the value of the joining entity's liabilities...The amount that is allocated is not changing. Certainly the assets which it gets allocated to is changing, but the amount that is being allocated is not changing, so the view is that there is not going to be a significant revenue impact as a result of that.[53]

Conclusion

2.76 The amendments in 2010 were intended to clarify the reset tax costs of certain assets and tax outcomes for rights to future income assets. However, they provided a windfall through tax deductions for some consolidated groups. These deductions were not available to non-consolidated groups. It was not the intention of the Bills to introduce inconsistency in tax treatment.

2.77 The 2010 changes were retrospective to the 2002 commencement of the consolidation regime, as they were thought to give effect to the original policy intent. Once implemented it became clear that the changes went beyond what had been foreshadowed and had significant negative revenue implications. The nature of claims for tax deductions subsequently made by consolidated groups had not been anticipated by the Government or industry.

2.78 Schedule 3 of the Tax Laws Amendment (2010 Measures No. 2) Bill 2012 will clarify the arrangements in relation to the tax cost setting and rights to future incomes rules.

2.79 The three categories of rules (pre, interim and prospective) provide a measured application of the changes to take into account what taxpayers could reasonably have known or expected the rules to be at the relevant time. There are protections for groups who have already received tax refunds or ATO rulings.

2.80 These changes are necessary to address the $6 billion revenue risk, clarify these arrangements and provide greater certainty for consolidated groups.

53 Mr Anthony Regan, Treasury, *Committee Hansard*, Canberra, 4 June 2012, p. 25.

The retrospective application of the pre-rules and interim rules are appropriate to counteract effects of the 2010 changes, which were also retrospective. Schedule 3 will restore the policy intent of consolidation and clarify future arrangements.

Managed investment trust final withholding tax

2.81 The Income Tax (Managed Investment Trust Withholding Tax) Amendment Bill 2012 increases the managed investment trust (MIT) final withholding tax on foreign investors from 7.5 per cent to 15 per cent. The tax will apply on fund payments made in relation to income years that commence on or after 1 July 2012. Over the forward estimates this measure is estimated to have a gain to revenue of $260 million.[54]

Grandfathering

Background

2.82 Industry has questioned both the substance of the Bill as well as the manner of its introduction. Industry and investors argue that they were taken by surprise, particularly given that recent government policy has seen a lowering of the tax rate since 2008.

2.83 Several MIT bodies have criticised the move to double the tax rate without clear price signalling. Infrastructure Partnerships Australia (IPA) argued:

> The 7.5 per cent rate was an incentive to attract investment into Australia, and protection must now be given to investors who, in good faith, relied on the expectation of that reduced rate going forward over the term of their investment.[55]

2.84 Industry groups broadly oppose the measure outright. However, if the tax increase is to proceed, they have suggested several measures the most prominent being the proposed grandfathering of the 7.5 per cent rate for investments made on the expectation that this rate would continue.[56]

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54 Explanatory Memorandum, Tax Laws Amendment (2012 Measures No. 2) Bill 2012; Pay As You Go Withholding Non-compliance Tax Bill 2012; Income Tax (Managed Investment Trust Withholding Tax) Amendment Bill 2012, p. 133.

55 Infrastructure Partnerships (IPA), *Submission 10*, p. 3.

56 Mr Martin Codina, Financial Services Council (FSC), *Committee Hansard*, Canberra, 4 June 2012, p. 34.

Analysis

2.85 At the hearing, participants discussed the recommendation presented by industry groups that the current 7.5 per cent tax rate be grandfathered for investments made on the assumption that this rate would continue. This rate has been applied to distributions to foreign investors since the 2010-11 income year. However, Treasury responded by noting the complexity and impractical nature of such a move:

> Who are you effectively giving that grandfathering to and why? That becomes quite an interesting and complex question. Are you looking at just people who have invested since 1 July 2010 or are you looking more broadly than that? Are you looking at assets that came into existence after that time or at all assets? Those are some of the sorts of questions that would need to be considered.[57]

Conclusion

2.86 Creating grandfathering arrangements for investors at the 7.5 per cent tax rate is likely to be unwieldy in its implementation. It would also leave a difficult precedent that individuals and business should expect to get grandfathered rates on changes made to other kinds of tax rates in the future.

Investor confidence

Background

2.87 Industry warned that the unexpected increase in the withholding tax rate has the potential to damage foreign investor confidence and Australia's reputation as a secure and stable investment destination. AMP in their submission argued:

> The suddenness of the announcement without consultation or discussion with industry created unease within the international investment community as to whether further changes could arise that would fundamentally change the nature of investment in Australia.[58]

2.88 Testimony was given at the hearing that the proposed tax increase has already resulted in capital flight by foreign investors and will significantly decrease the incentive for foreign capital investments in Australia in the

57 Mr Anthony McDonald, Treasury, *Committee Hansard*, Canberra, 4 June 2012, p. 35.

58 AMP, *Submission 13*, p. 1.

future. For this reason both the Property Council of Australia (PCA) and the Financial Services Council (FSA) questioned the accuracy of the assumed revenue flows from the increase as they predict reduced foreign investment.[59]

Analysis

2.89 Treasury responded that the potential for reputational damage to Australia as a safe investment destination must be seen in the broader context of the Australian economy. The Government has prioritised fiscal consolidation in the context of reduced revenue in order to improve budget sustainability.

> In the course of doing that, the government has reached the view that that 7½ per cent rate for managed investment trusts for non-residents was something that was not consistent with that broader sustainability in achieving the medium-term fiscal strategy, which...is a very important part of our AAA credit rating.[60]

2.90 Treasury argue that given these circumstances:

> By setting out a clear path for a sustainable medium-term fiscal strategy, my proposition would be that that would enhance, rather than reduce, foreign investors' confidence in the policy framework in Australia.[61]

2.91 Furthermore, prior to the measures announced in the 2008-09 budget, the MIT withholding tax was at the company tax baseline of 30 per cent. This is because investments made through MITs are in equity and taxes are paid on income comparable to the company tax paid on profits. The MIT withholding tax is not comparable to taxes paid on interest earned from 'debt' investments. Treasury pointed out that the 15 per cent rate is still concessional when compared to the company tax rate of 30 per cent.[62]

Conclusion

2.92 The increase to the MIT withholding tax to 15 per cent maintains the original policy intent of the promise to lower the withholding tax. It maintains a concessional rate to attract investors when compared to the

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59 Mr Verwer, Property Council of Australia (PCA), *Committee Hansard,* Canberra, 4 June 2012, p. 30.

60 Mr Anthony McDonald, Treasury, *Committee Hansard,* Canberra, 4 June 2012, p. 30.

61 Mr Anthony McDonald, Treasury, *Committee Hansard,* Canberra, 4 June 2012, p. 31.

62 Mr Anthony McDonald, Treasury, *Committee Hansard,* Canberra, 4 June 2012, p. 39.

company tax rate of 30 per cent, while balancing this with the need to create and maintain budget sustainability.

Revenue forward estimates

Background

2.93 At the hearing, industry groups queried the method used by Treasury to determine the expected gain to revenue of $260 million over the forward estimates. They argued that the increase in the tax rate would lead to capital flight and a decrease to potential revenue.[63]

Analysis

2.94 Treasury explained that the approach used to calculate the effect of this budget measure was the same 'adopted by successive governments and set out in relation to the Charter of Budget Honesty'.[64] This approach takes into account the immediate 'first-round' implications of the policy but not potential 'second-round' flow on effects. These are not straightforward to predict and need to take into account effects across the economy rather than just those immediate to the industry. To constitute a meaningful analysis one would also need to model the effect on the economy of alternative savings in the budget if the cuts were not made in this sector.[65]

2.95 In general Treasury has found that while there may be implications of 'second-round' effects to an individual sector, these tend to balance out through the economy as a whole.[66]

2.96 While it was recognised that the impact of the tax increase may make some investments less attractive to some investors and negatively affect some MITs, Treasury stated that movement by investors will not necessarily result in a reduction of capital in the economy overall:

> ...if we are looking at financial flows there would be a greater reduction in the flows that occur through managed investment trusts but what we are interested in is what happens to the aggregate base and that is a different thing.[67]

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63 Mr Peter Verwer, PCA, *Committee Hansard,* Canberra, 4 June 2012, p. 30.

64 Mr Anthony McDonald, Treasury, *Committee Hansard,* Canberra, 4 June 2012, p. 31.

65 Mr Anthony McDonald, Treasury, *Committee Hansard,* Canberra, 4 June 2012, p. 31.

66 Mr Anthony McDonald, Treasury, *Committee Hansard,* Canberra, 4 June 2012, p. 40.

67 Mr Anthony McDonald, Treasury, *Committee Hansard,* Canberra, 4 June 2012, p. 40.

2.97 Treasury also argued that tax revenue gives benefits to all Australians through government spending:

> GDP does not necessarily directly relate to the wellbeing of Australians. It relates closely but not perfectly. One of the things we do think about is, 'How does that increase production and benefit the Australian economy as a whole?' One of the important ways in which that is done is through an appropriate sharing in the proceeds and the profits from those ventures through the tax system.[68]

Conclusion

2.98 Treasury have calculated the expected revenue from this measure through the forward estimates using the accepted approach adopted by previous governments and set out in the Charter of Budget Honesty.

2.99 While the Committee recognises that the increase to the tax rate has the potential to make certain other investment opportunities more attractive to some investors, concessions to support any one industry has to be balanced with ensuring that the wider Australian population also benefits by obtaining a fare share through the tax system. This measure does this by providing an increase that is still concessional and well below the previous 30 per cent rate.

Effective tax rate

Background

2.100 Finally, some stakeholders are concerned that the MIT Withholding tax as a final withholding tax does not allow investors to make deductions or allowances for their outgoings. The issue is that the final nature of the tax means that some investors' Australian tax will be higher than before the MIT final withholding tax was introduced in 2008.[69] While the headline tax rate puts us in the middle of like nations, industry is concerned that the effective tax rate, particularly in light of the tax's final nature, is actually much higher when compared with other effective tax rates around the globe.

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68 Mr Anthony McDonald, Treasury, *Committee Hansard,* Canberra, 4 June 2012, p. 40.

69 Ernst and Young, *Submission 14,* p. 1.

Analysis

2.101 Treasury pointed out that, as recently as 2007, the FSC supported a final withholding tax, even at a rate of 15 per cent, because it relieves foreign investors of the burden of lodging a tax return.[70] Treasury also noted that 'in many cases, the tax that is paid in Australia is able to be credited in the other country.'[71] This means that it is difficult to do a meaningful comparison of effective tax rates around the world as the tax laws within the investor's home jurisdiction must also be taken into account.

2.102 Treasury reiterated that the headline tax rate at 15 per cent is 'broadly in line with other advanced economies' and 'somewhat lower than other rates in the region.'[72]

Conclusion

2.103 Stakeholders have been supportive of having a final withholding tax at a 15 per cent rate in the past. While it is understandable that industry would prefer to keep the tax rate as low as possible, the final nature of the tax was specifically sought by them to provide a simpler tax system for foreign investors. Australia will remain competitive in the region and with like countries around the world at the increased tax rate of 15 per cent.

Passenger Movement Charge Amendment Bill 2012

Background

2.104 The Passenger Movement Charge Amendment Bill 2012 (the Bill) will increase the Passenger Movement Charge (PMC) from $47 to $55 per person from 1 July 2012 and enable automatic indexation, based on the Consumer Price Index, from 1 July 2013.[73] Over the forward estimates the measure will deliver an additional $610 million.[74]

2.105 The Committee heard from a range of industry bodies about the difficulties currently faced by the tourism sector. These included global economic instability, the high Australian dollar and high fuel costs. It was

70 Mr Anthony McDonald, Treasury, *Committee Hansard,* Canberra, 4 June 2012, p. 34.

71 Mr Anthony McDonald, Treasury, *Committee Hansard,* Canberra, 4 June 2012, p. 32.

72 Mr Anthony McDonald, Treasury, *Committee Hansard,* Canberra, 4 June 2012, p. 31.

73 Explanatory Memorandum, Passenger Movement Charge Amendment Bill 2012, p. 5.

74 Australian Government, *Budget Measures: Budget Paper No 2: 2012-13*, Commonwealth of Australia, Canberra, 2012, p. 11.

posited that the Government was over-collecting on the PMC for consolidated revenue and not sufficiently supporting the needs of the tourism industry. Industry witnesses did not support the $8 increase to the PMC nor its indexation.[75] The Australian Airport Association told the Committee:

> If nothing else, we beg that the indexation be removed. If you look at the past budgeted amounts for the passenger movement charge versus what has come in, it is quite cyclical; it goes up and down. Let us not lock ourselves into indexation. Let us see how the tourism industry goes. We are struggling in regional areas in particular.[76]

2.106 The Government has allocated $61 million of the monies raised by the PMC to the Asia Marketing Fund.[77] This initiative will further the Government's 2020 Tourism strategy. In addition, the Government will continue to support a range of initiatives which underpin and promote the visitor economy, including $40 million over four years to the T-QUAL Grants project, infrastructure upgrades, rolling out the NBN which will improve the industry's digital capabilities, and funding national cultural and natural heritage attractions.[78]

Analysis

2.107 The Committee was presented with a range of impacts associated with increasing the PMC, and its indexation. These included:

- decreasing Australia's competitiveness in the global tourism market;[79]
- the PMC being a poorly designed 'tourism tax';[80]
- the PMC over-collects from the tourism sector for general consolidated revenue without sufficient monies being returned to passenger

75 Ms Caroline Wilkie, Australian Airport Association, *Committee Hansard*, 4 June 2012, p. 44.

76 Ms Caroline Wilkie, Australian Airport Association, *Committee Hansard,* 4 June 2012, p. 44.

77 Australian Government, *Budget Measures: Budget Paper No 2: 2012-13*, Commonwealth of Australia, Canberra, 2012, p. 11.

78 Tourism Australia, *2020 Tourism: Overview*, <http://www.tourism.australia.com/en-au/documents/Corporate%20-%20Research/Tourism_2020_overview.pdf>, viewed 6 June 2012; Department of Resources, Energy and Tourism, *T-QUAL Grants – Tourism Quality Projects: Fact Sheet*, Commonwealth of Australia, Canberra, 2012, p. 1.

79 Ms Juliana Payne, National Tourism Alliance, *Committee Hansard*, 4 June 2012, p. 43.

80 Accommodation Association of Australia, *Submission 19*, p. 5; Tourism and Transport Forum, *Submission 20*, p. 4.

facilitation or border agencies such as customs and border protection, quarantine and immigration;[81]

- further disadvantaging a sector that is struggling in Australia's 'two-speed' economy, particularly in regional areas;[82] and
- being a particular disincentive for the short-haul market from Asia and New Zealand.[83]

2.108 The global financial crisis has resulted in a $150 billion write-down in government revenue since the 2008-09 budget.[84] However, the Government has taken measures to ensure Australia retains its AAA credit rating, while meeting its policy priorities. Despite this difficult fiscal backdrop the Government has remained committed to the Tourism 2020 initiative.[85] Tourism 2020 is a whole-of-government and industry strategy which will grow tourism in Australia. Its six key areas are:

- grow demand from Asia;
- build competitive digital capability;
- encourage investment and implement regulatory reform agenda;
- ensure tourism transport environment supports growth;
- increase supply of labour, skills and indigenous participation; and
- build industry resilience, productivity and quality.[86]

2.109 The proposed Asia Marketing Fund will directly contribute to realising the Tourism 2020 strategy. In addition the Government will continue to assist the tourism sector both directly, by funding projects like T-QUAL, and indirectly, by funding infrastructure upgrades to roads, public transport

81 Ms Caroline Wilkie, Australian Airport Association, *Committee Hansard*, 4 June 2012, p. 43; Mr John King, Australian Tourism Export Council, *Committee Hansard*, 4 June 2012, p. 46; Tourism and Transport Forum, *Submission 20*, p. 1; Melbourne Airport, *Submission 16*, p. 2, 9.

82 Mr John Lee, Tourism and Transport Forum, *Committee Hansard*, 4 June 2012, p. 44; Cairns Airport, *Submission 15*, p. 1.

83 Mr John Lee, Tourism and Transport Forum, *Committee Hansard*, 4 June 2012, p. 45; Qantas, *Submission 22*, p. 2.

84 Mr Tony McDonald, Treasury, *Committee Hansard*, Canberra, 4 June 2012, p. 30.

85 Tourism Australia, *Tourism 2020*, < http://www.tourism.australia.com/en-au/default_6111.aspx>, viewed 5 June 2012.

86 Tourism Australia, *Tourism 2020*, <http://www.tourism.australia.com/en-au/default_6111.aspx>, viewed 5 June 2012.

and the NBN.[87] It will also continue to fund Australia's world class cultural institutions and national parks.

2.110 As discussed in chapter one, the Sustainable Tourism Cooperative Research Centre modelled the impact of a 20 per cent rise in the PMC ($9.40 in current terms) on 'tourism output' and the economy more broadly.[88] It was postulated that 'contrary to conventional wisdom' increasing the PMC would increase the gross national income by $49 million but decrease tourism output by $7 million.[89]

2.111 It is acknowledged by the committee that the tourism sector is experiencing difficult economic times. The high Australian dollar, fuel prices and global instability have all impacted on the industry. Recent, data from Tourism Australia contained some positive news for the tourism sector:

- There were 5.9 million visitor arrivals for year ending March 2012, an increase of 1.0 per cent relative to the previous year.
- There were 1.6 million visitor arrivals to Australia during the three months to March 2012, an increase of 4.1 per cent relative to the same period of the previous year.
- There were 544,200 visitor arrivals during March 2012, an increase of 8.6 per cent relative to the same month of the previous year.[90]

Conclusion

2.112 The PMC has not been increased since 2008 and an $8 increase to the PMC is considered a small amount in the context of international travel. The Government remains committed to supporting and growing the tourism sector in Australia. Ten per cent of the additional revenue raised as a result of the increase will be dedicated to the Asia Marketing Fund on an ongoing basis. More generally, it will support the operations of Customs and Border Security and continue to invest in other Government priorities

87 Australian Government, *Budget and Additional Estimate Statements 2012-13: Department of Resources, Energy and Tourism*, Commonwealth of Australia, Canberra, 2012, pp. 49-57. Department of Resources, Energy and Tourism, *T-QUAL Grants – Tourism Quality Projects: Fact Sheet*, Commonwealth of Australia, Canberra, 2012, p. 1.

88 P Forsyth et al, *The Impacts of the Passenger Movement Charge on Tourism Output and the Economy*, 15 March 2011, Sustainable Tourism CRC – The Centre for Economics and Policy, Queensland, pp. 1-49.

89 P Forsyth et al, *The Impacts of the Passenger Movement Charge on Tourism Output and the Economy*, 15 March 2011, Sustainable Tourism CRC – The Centre for Economics and Policy, Queensland, p. 18.

90 Tourism Australia, *Visitor Arrivals Data*, <http://www.tourism.australia.com/en-au/research/5236_6469.aspx>, viewed 5 June 2012.

including upgrading infrastructure and supporting public institutions. It is the Committee's recommendation that the Passenger Movement Charge Amendment Bill 2012 be passed by the House unamended.

Overall conclusion

2.113 The Bills make a number of significant improvements to the tax laws. Schedule 1 of the Tax Laws Amendment (2012 Measures No. 2) Bill 2012 and the Pay As You Go Withholding Non-compliance Tax Bill 2012 seek to make directors personally liable for the superannuation guarantee charge of their company. This will prevent unscrupulous directors from phoenixing their businesses to avoid their super responsibilities. This practice has cost Australian employees hundreds of millions of dollars in lost superannuation and the committee commends both the intent and the operation of the Bills in this regard.

2.114 Last year, the committee inquired into a package of Bills in similar terms. The committee recommended that the Government should investigate whether additional defences for directors should be inserted in the Bills. This has occurred. If passed, the legislation will give new directors 30 days, up from the current 14 days, to conduct due diligence before adopting a company's pre-existing obligations. Directors will also not be liable for a director penalty where they took reasonable care in a matter and applied the super legislation in a reasonable way.

2.115 The committee also recommended that the Government should investigate whether the provisions should only apply if an individual has been engaged in phoenixing. The Bills do not have this feature and industry argued that they should be amended along these lines. Ultimately, the committee has come to the view that such a change is not warranted because the provisions will only apply when a company has not only failed to pay a super amount, but that it has failed to notify the ATO of this two months after the event. The high level of non-compliance required to trigger the provisions will protect directors and companies who do the right thing.

2.116 Schedule 2 of the main Bill is designed to ensure that the tax treatment of financial arrangements is consistent with the TOFA tax timing rules. The provisions are to be retrospective from the commencement of other TOFA amendments on 1 July 2010 and this retrospectivity was the key issue in the inquiry. Stakeholders expressed concern that taxpayers who had chosen to adopt the new TOFA rules (rather than elect to keep prior arrangements) would be disadvantaged. However, the committee did not accept this because the measures restore the original policy intent and the Government had previously flagged that retrospectivity will be necessary with TOFA to restore the policy intent from time to time.

2.117 Schedule 3 aims to protect a $6 billion revenue risk that has arisen as a result of retrospective amendments in 2010 in relation to consolidation rules. These changes allowed consolidated groups to claim deductions back to 2002 in relation to the residual tax cost setting rule and the rights to future income rule. In 2011, revenue problems with the 2010 changes became apparent and the Board of Taxation conducted an inquiry into the matter. The Bill largely reflects the Board's report. Groups that have already received a refund or have an ATO ruling will generally be protected from the retrospective changes. Given the transparency of the process and the amount of revenue at stake, the committee again agrees that retrospective legislation is appropriate.

2.118 The Income Tax (Managed Investment Trust Withholding Tax) Amendment Bill 2012 and Schedule 4 of the main Bill increase the tax rate on managed investment trusts for foreign investors from 7.5 per cent to 15 per cent. This is a partial reversal of the recent decreases on this tax rate from 30 per cent a few years ago. The committee is mindful that, as equity investments, the correct comparative rate is the company tax rate, currently set at 30 per cent. Although the industry sector was concerned about how the change would affect it, the committee supports the provisions because of the wider macroeconomic importance of Australia having a sound fiscal strategy, which an important driver for the whole economy.

2.119 The Passenger Movement Charge Amendment Bill 2012 increases the charge from $47 to $55 from 1 July 2012 and indexes it to the CPI. Similar to the MIT provisions, the issues revolved around an industry sector being concerned about how it would be affected by a revenue increase. Once again, however, the committee supports the provisions on a national basis because of the Government's overall fiscal strategy. The committee notes that the Government remains committed to the Tourism 2020 initiative and continues to support the industry through programs such as T-QUAL, infrastructure upgrades and maintaining and expanding tourism attractions.

2.120 The Bills represent a responsible package aimed at securing a sustainable revenue base for Australia, as well as protecting the superannuation entitlements of Australian workers. The Bills should pass.

Recommendation 1

2.121 **That the House of Representatives pass the Tax Laws Amendment (2012 Measures No. 2) Bill 2012, Pay As You Go Withholding Non-compliance Tax Bill 2012, Income Tax (Managed Investment Trust Withholding Tax) Amendment Bill 2012, and the Passenger Movement Charge Amendment Bill 2012, as proposed.**

Julie Owens MP
Chair
15 June 2012