
Native Title, Indigenous Economic Development and Tax

The Treasury

30 November 2010

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Introduction

The Law Council is pleased to provide the following submission in response to the Treasury's consultation paper on *Native Title, Indigenous Economic Development and Tax* released in May 2010 (the Consultation Paper).

In providing this response, the Law Council has drawn on the advice and experience of legal experts both in native title and taxation law on the Law Council's Indigenous Legal Issues Committee and Tax Law Committee.

The following submissions attempt to address the questions set out in the Consultation Paper with as much brevity as possible.

The Law Council would be pleased to respond to any queries regarding these submissions.

Existing arrangements

- (a) *In the context of your experience, when do the income tax implications of an agreement arise in the agreement making process?*

Income tax implications arise once a determination is made or an agreement is entered into, whether by ILUA or s 31 of the *Native Title Act 1993*, which results in the payment of compensation or any other taxable benefit to a native title claim group, which might be distributed to individual members.

- (b) *What has been your experience in seeking advice or guidance, either privately or from government agencies, on the interaction between the income tax system and native title?*

There is very little guidance available for native title holders, claimants or taxation professionals regarding the proper taxation treatment of native title income or benefits. It is also noted that there would be a large number of people who receive native title benefits who do not lodge an income tax return to declare that income.

It is noted that presently the tax system deals very awkwardly with native title agreements. As stated in the Consultation Paper, there is significant uncertainty as to when native title, as an inalienable, intergenerational asset with meaning peculiar to each native title claim group and subject to extinguishment, should be deemed to generate taxable income.

In particular, there exists some confusion as to whether a determination or agreement causes consequences for Capital Gains Tax (CGT) or Goods and Service Tax (GST), and there may also be limited understanding about income liabilities arising from native title agreements. It is further noted that payments under a native title agreement should not be assessable in the hands of a Prescribed Body Corporate (PBC).

- (c) *How could Government agencies assist to provide greater clarity regarding the tax treatment of payments made under a native title agreement?*

It may assist native title holders and their representatives or advisers if the Australian Tax Office were to regularly publish Interpretative Decisions or Rulings in relation to taxation issues arising from native title agreements and settlements.

Further, plain English explanatory materials should be developed for distribution by land councils, the National Native Title Tribunal (NNTT), Centrelink, etc, to ensure that the information is accessible by those affected.

(d) *What has been your experience in the use of charitable trusts as a means of managing payments received under native title agreements?*

Charitable trusts have been established following many native title determinations and agreements as a preferred entity to receive native title payments due to the tax advantages charitable entities enjoy under the *Income Tax Assessment Act 1997*.

Whilst they are partially effective in minimising the tax liability of native title holders, charitable trusts are not ideal vehicles for favourable tax treatment of native title agreements.

The primary problem is the very broad interpretation of a “charitable” purpose required to characterise benefits derived from native title agreements or determinations, or to ensure such trusts are eligible for ‘designated gift recipient’ status. Indigenous Land Use Agreements (ILUAs) and common law agreements, despite their social and cultural significance, are in essence commercial agreements for benefits to be paid for the use of land or the suppression or extinguishment of land rights.

In addition, designation as a charitable trust can create significant limitations on the use of benefits received by the trust, including that funds in the trust may only be applied for a charitable purpose. As noted by the Consultation Paper, this is unlikely to include any commercial enterprise or venture which might assist the economic development or infrastructure of a community. It is considered problematic that native title holders should be forced to fit into the mould of a charitable trust when circumstances clearly require a distinct vehicle or framework to ensure favourable tax treatment of benefits derived from native title agreements and determinations.

(e) *In the context of your experience, what structures or arrangements are used to manage the use of payments received under native title agreements?*

Most claim groups and PBCs rely on advice from Native Title Representative Bodies (NTRBs) regarding the structure of native title agreements.¹

The Law Council understands that the majority of settlements are structured to ensure the entity receiving benefits is a charitable trust, due to the taxation benefits.

Possible income tax exemption

(f) *How would an upfront tax exemption for payments made in respect of a native title agreement impact on the negotiation of agreements?*

It is considered that a blanket exemption would simplify agreement making, for the benefit of native title holders and claimants.

(g) *How should the concept of a native title agreement be defined? Should this concept be defined with respect to the Native Title Act 1993?*

¹ Dr Lisa Strelein, *Taxation of Native Title Agreements*, Native Title research Monograph No.1/2008 (May 2008), Australian Institute of Aboriginal and Torres Strait Islander Studies, Commonwealth of Australia, page 31.

The Law Council considers that it may be necessary to restrict the exemption to certain forms of agreements. For example, the exemption could be applied to ILUAs, for which there exists a rigorous development and registration process. Restricting the availability of the exemption in such a way would encourage the development of registrable agreements, or ILUAs, and limit the scope for applying the exemption to agreements which are reached with a group other than the true native title holders.

It seems reasonable for the concept to be consistent with the definition of the various types of ILUA under Part 2, Division 3 of the Act.

The Law Council also considers that any income tax exemption or other favourable tax treatment should be available not only in respect of payments made under native title agreements, but also in respect of payments made under agreements of a similar kind, for example, mining and other commercial agreements made under the *Aboriginal Land Rights (Northern Territory) Act 1976 (Cth)*.

(h) *Should the purposes for which an exempt payment may be used be prescribed? For example, should there be a restriction on an exempt payment being used purely of private consumption?*

The Law Council can see little justification for requiring that payments received under private agreements should be tied to a particular purpose. The Law Council is unaware of any other agreements or compensation frameworks which restrict the rights of beneficiaries to apply the benefits to whatever ends are deemed appropriate.

However, it is noted that there may be a reasonable basis for restricting the use of payments over which a tax exemption is claimed. The purpose of the exemption would primarily be to ensure that native title benefits are received by both current and future generations of native title holders, given the communal and inalienable character of native title land. Accordingly, there is a reasonable argument that expenditure of tax-exempt funds should be limited to investment in projects or items which will benefit the community (or part thereof) and future generations.

The Law Council considers that any restriction or prescription of the manner in which native title benefits can be applied should be given very careful consideration, in consultation with Indigenous communities, NTRBs, mining companies, state governments and land councils.

Indigenous Community Fund

The paper by Treasury proposes that an Indigenous Community Fund (ICF) be developed as a new tax exempt vehicle into which native benefits could be paid.

Initially, the Law Council was confused as to whether the proposal related to the establishment of a ICF into which all native title payments would be made (similar to the Aboriginal Benefits Account under the *Aboriginal Land Rights (Northern Territory) Act 1976*), or a framework under which many ICFs could be established, requiring at least one ICF for every agreement.

The Law Council has been advised by the Treasury that proposal is for the latter, being a framework under which ICFs could be established by native title claim groups. Assuming this is correct, the Law Council generally supports the proposal and would welcome the creation of a new tax exempt vehicle for native title benefits.

However, the Law Council would not support the creation of an ICF as a large single fund into which all native title benefits could be paid. In particular, the Law Council is concerned about preserving the rights of native title groups to self-determination, which may be compromised if the benefits from agreements are socialised into a single pool of funds.

(i) *If development of a new tax exempt vehicle is progressed further:*

(i) *What payments should such a fund be able to receive? Should the fund only be able to receive payments made under a native title agreement or should it be allowed to receive other payments?*

The Law Council does not consider that there should necessarily be any restriction on the source of funds paid into an ICF.

However, consistent with the Law Council's response to (h), it is considered that a tax exempt vehicle may need to be subject to certain strictures as to the purpose for which funds can be applied (as is ordinarily the case under any trust vehicle), to ensure the purpose of expenditure accords with the purpose for which the tax exemption is applied.

(ii) *Do you agree with the proposed permitted uses of the fund? What other uses could be considered?*

The Law Council agrees in principle with the proposed uses of the fund. The uses might be further extended to cover sporting and recreational investments and business ventures for members of the native title claim group or others. It is noted that these might be picked up in the catch-all provision enabling expenditure on "other purposes beneficial to all those for whom the fund was established. However, that clause could also be broadened to enable expenditure for "other purposes, as deemed appropriate by the ICF governance committee, for the long term benefit the claim group, individuals within that group, or the Indigenous people of Australia".

It is submitted that ICFs should not be expected to invest in infrastructure, amenities or services which would ordinarily be the responsibility of government to provide.

(iii) *What legal form should the fund be required to take?*

It is noted that the most obvious legal form for the ICF to take is a trust. This might largely be due to the tendency toward structures which support the administration of a single pool of funds or assets.

However, there may be greater benefits to be derived from a corporate structure. There already exists a framework for Indigenous corporate entities under the *Corporations (Aboriginal and Torres Strait Islander) Act 2006* (Cth) (the CATSI Act), in relation to which a tax exempt entity could be established. Corporate entities benefit from a less entrenched board of directors, a greater commercial focus and a capacity to structure in order to maximise wealth creation.

This option was recommended by the Law Council in its response to the Australian Government Discussion Paper into *Optimising Benefits from Native Title Agreements*.

(iv) *What kinds of governance requirements should the fund be subject to?*

If it is a fund established under the CATSI Act, the fund should be subject to governance arrangements under the CATSI Act. It is noted that Indigenous communities should not

be unduly restricted in their choice of business structure and there should be a similarly favourable taxation environment offered under the *Corporations Act 2001* (Cth).

The governance arrangements under those enactments are sufficient to ensure appropriate integrity in governance processes. Additional governance arrangements, including the appointment of independent directors and the composition of the board, should be at the discretion of the native title claim group.

It is noted that there is some overlap here with the matters considered by the separate discussion paper recently released into “Leading Practice Agreements: maximising outcomes from native title agreements”.

It is recommended that funding should be made available for corporate governance training for directors of Aboriginal and Torres Strait Islander corporations.

- (v) *How would the establishment of a new tax exempt vehicle impact on existing agreements?*

Native title groups with existing agreements and structures in place should have the option of moving their funds into a new tax exempt vehicle.

- (vi) *What kinds of transitional arrangements would be required?*

The government should make funds available to assist with transitional arrangements so that claim groups are not disadvantaged should they choose to transition to a new tax exempt vehicle.

- (j) *Within the context of your experience, what difference would a new tax exempt vehicle make to native title groups and Indigenous communities?*

The Law Council is advised that the creation of a new tax exempt vehicle for native title groups would be a positive development for native title claim groups and Indigenous communities. As previously noted, there is a strong interest in establishing flexible arrangements for the diverse needs and interests of native title groups and Indigenous communities. The capacity of charitable trusts to address those interests is limited.

Subject to further consultation over the detail and structure of Indigenous Community Funds (and the Law Council’s comments in this submission), the Law Council supports the creation of a new tax exempt vehicle for native title claimants and Indigenous communities generally, for certain purposes.

Native title withholding tax (NTWT)

The Law Council regards a NTWT as a simpler and more cost-effective solution than a statutory fund, which may be much easier to apply in practice.

However, the Law Council submits that there should not be a distinction between extinguishment or suspension. Impairment, rather than extinguishment of native title interests is becoming more common, particularly in light of recent amendments to the *Native Title Act 1993* and potential amendments in the future, which enable revival of rights and interests or extend the non-extinguishment principle. There is a compelling argument that the purpose for which a NTWT would be established applies with equal force to agreements arising out of both suspension and extinguishment of native title rights and interests. It is certainly not clear that there is any rationale for applying a tax concession to benefits received by way of compensation for suspension of native title

rights and interests, as opposed to permanent extinguishment (which should result in much more significant native title payments).

It is noted that the proposal for a NTWT was discussed during the development of the *Native Title Amendment Act 1998*. It is not clear why the issue fell off the agenda or whether the proposal has developed any further since that time.

On difficulty associated with a NTWT is that, if it applies to all monetary payments, it must be assumed that:

1. payments received would ordinarily be taxable; and
2. compliance and administration costs outweigh the revenue risks.²

Further, there must be assumptions about “the low assessable income of the final recipient individuals or entities, the likelihood of redistribution of money within the community, and low compliance levels with the self assessment regime.”³

In some cases, these assumptions may turn out to be incorrect, resulting in a tax liability where one did not previously exist. It is noted that most recipients of benefits under such agreements would be unlikely to declare it as income for taxation purposes. The proposed NTWT, if implemented, should not be used as a tool to extract.

(k) *Within the context of your experience, how would a NTWT affect:*

(i) *the negotiation of native title agreements?*

It is considered the application of a NTWT may make the negotiation of native title agreements less complex, through the creation of a single withholding tax to replace other forms of taxation, with the burden of administration managed by the party making payment to the native title claim group/traditional owners.

(ii) *the form of benefits provided under native title agreements, if a NTWT only applied to monetary payments?*

Depending on the size of the NTWT compared with other tax liabilities arising under taxation law, application of the NTWT only to monetary benefits may create an incentive to structure native title agreements to provide more in the way of non-monetary benefits, which would presumably reduce the level of monetary benefits. This appears consistent with the Government’s recent policies aimed at reducing the level of direct monetary payments to claim groups while increasing non-monetary benefits or direct investment in social and community infrastructure.⁴

It is noted that it seems unusual to apply a tax only to monetary benefits. Consideration should be given to the means by which non-monetary benefits could receive a similar concession.

² Streilien, *Ibid*, *op cit* 1, page 57.

³ *Ibid*.

⁴ See, for example, the Australian Government’s Discussion Paper on *Optimising Benefits from Native Title Agreements* (December 2008), which proceeds on the assumption that :

- direct financial contributions resulting from agreements do not necessarily translate into substantive benefits for Indigenous communities; and
- substantive benefits, such as employment options and community development initiatives often deliver benefits to all members of the community, not just the traditional owners.

It is also unclear how the NTWT would apply to up-front monetary payments, as opposed to profits-based payments over the life of the agreement.

(iii) the management of benefits received under a native title agreement?

The imposition of a NTWT on monetary benefits arising from native title agreements will tend to front-end load tax liability in native title claims and generally obviate the need for a specific vehicle, such as a charitable trust, or other tax-exempt entity.

This would remove limitations in apportionment of benefits etc that result from the use of tax-exempt vehicles.

Attachment A: Profile of the Law Council of Australia

The Law Council of Australia is the peak national representative body of the Australian legal profession. The Law Council was established in 1933. It is the federal organisation representing approximately 50,000 Australian lawyers, through their representative bar associations and law societies (the “constituent bodies” of the Law Council).

The constituent bodies of the Law Council are, in alphabetical order:

- Australian Capital Territory Bar Association
- Bar Association of Queensland Inc
- Law Institute of Victoria
- Law Society of New South Wales
- Law Society of South Australia
- Law Society of Tasmania
- Law Society of the Australian Capital Territory
- Law Society of the Northern Territory
- Law Society of Western Australia
- New South Wales Bar Association
- Northern Territory Bar Association
- Queensland Law Society
- South Australian Bar Association
- Tasmanian Bar Association
- The Victorian Bar Inc
- Western Australian Bar Association
- LLFG Limited (a corporation with large law firm members)

The Law Council speaks for the Australian legal profession on the legal aspects of national and international issues, on federal law and on the operation of federal courts and tribunals. It works for the improvement of the law and of the administration of justice.

The Law Council is the most inclusive, on both geographical and professional bases, of all Australian legal professional organisations.