30 November 2010

The General Manager
Business Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: nativetitle@treasury.gov.au

Dear General Manager

Native Title, Indigenous Economic Development and Tax – Stakeholder Consultation

We refer you to your invitation for submissions in response to the Consultation Paper 'Native Title, Indigenous Economic Development and Tax' dated May 2010 (**the Consultation Paper**).

South Australian Native Title Services (**SANTS**) is the Native Title Services Provider (**NTSP**) for South Australia performing all of the functions of a representative body pursuant to Section 203FE of the *Native Title Act 1993* (Cth) (**the NTA**).

Executive Summary

It is the policy of SANTS that self-sufficiency and the opportunity for wealth creation are paramount goals for native title parties. This is key to 'closing the gap' between Indigenous and non-Indigenous Australians. Such wealth creation is restricted in a complex and unsuitable tax system that fails to recognise the uniqueness of payments relating to native title. Indeed, SANTS supports a clear and appropriate tax system relating to native title payments. Accordingly, SANTS supports robust discussion for reform of the tax system that better reflects the nature and intent of native title payments.

By way of summary, SANTS submits the following:

> ***A new income tax exemption:*** *This proposal may be too limited and inflexible. Further, defining a 'native title agreement' may be too complex.*

Indigenous Community Fund: *The establishment and transitional costs of an ICF would be high. However, the benefits of a flexible ICF with effective governance are likely to outweigh these costs.*

Native Title Withholding Tax: *A blanket Native Title Withholding Tax fails to address issues other than those monetary payments pursuant to 'native title agreements'.*

In making these recommendations, SANTS makes the following points. Native title arises out of a unique common law right of traditional ownership of the land. The formal recognition of this right should not be subject to tax. Aboriginal rights and interests in the land existed well before settlement, and moreover, well before the formal recognition of native title and the passing of the NTA. In principle, the comparatively recent recognition of native title (and the consequences of the delay in recognition) provides further reason not to tax payments relating to native title. It is our belief that all payments for extinguishment and suspension of native title should be treated in line with the reality that payments are of a compensatory nature.

In the interests of consistency with the Consultation Paper, the term 'native title payments' will be used throughout this submission. However, SANTS expresses reservations about the use of such language. Payments to native title groups made pursuant to various agreements do not necessarily hinge on the provisions of the Native Title Act; especially where State legislation also makes provision for agreement making. In our experience agreement making may occur under either State or Commonwealth regimes on subject matters that falls under both jurisdictions. Nevertheless, the fact that there is a registered native title claim or determination will be a trigger to negotiations with the group. See, also, the discussion at g) and j) below.

Observations

This submission will assess each of the three reforms that have been identified in the Consultation Paper for consideration, responding to each question raised under those reforms. Before assessing the three reforms, consideration will be given to the general 'Consultation questions' raised in the Consultation paper.

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

From a matters-based perspective, the issue of potential tax implications of an agreement arises in all agreements, irrespective of whether the agreement is about the extinguishment of native title, suspension of native title or any other matters. In practice, often the agreements and resulting payments made therein are about a number of

matters. As the Consultation Paper envisages, the benefits under a native title agreement cannot always be clearly apportioned to those matters.

From a time-line perspective, the issue of potential tax implications of an agreement arise during the drafting of native title agreements. However, the issue is not one that is given significant attention, and is usually not fatal to the agreement negotiations. This is particularly true when tight timeframes pressure the finalisation of an agreement. Consistent with our response to b) below, there has been a general tendency to place less emphasis on the importance of tax implications when finalising an agreement. The issue arises more prevalently in the context of the daily administration of the native title agreement.

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?*

Our experience is that there has been a general reluctance to provide guidance on the interaction between the income tax system and native title given the current uncertainties. It would seem that there has been a desire not to confront the ongoing issues. However, there has been a general increase in the demand and necessity to seek such advice as the finalisation of claims and agreements progress in South Australia. We regularly seek independent expert advice in relation to appropriate governance structures and charitable trust arrangements.

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

We propose three methods of providing greater clarity regarding tax treatment of payments under a native title agreement. First, there should be widespread training for NTSP and Representative Bodies and Indigenous Corporations and their Communities to provide clear guidance on their respective tax obligations. Second, Australian Tax Office (**ATO**) private rulings on point should be widely published and easily accessible. Third, the publication of standard clauses in native title agreements that accurately state the appropriate tax treatment of payments.

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 are the most frequently used method of managing payments received under native title agreements. While the use of charitable trusts provides a level of security

over the receipt and distribution of the funds, issues have arisen in relation to the inflexibility of using funds from a charitable trust. Moreover, as raised by the Consultation Paper, the use of charitable trusts can be inconsistent with an Indigenous Community's ambitions for future wealth creation and other aspirations.

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

The structures and arrangements that are used to manage the use of payments received under native title agreements vary significantly. The variations are dependent on:

- The structure that has been adopted by the group;
- The stage of the native title claim and agreements that have been made to date;
- Whether there is an effectively functioning Indigenous Corporation and the purposes of that Corporation;
- The needs of each community;
- The specific terms of the native title agreement; and,
- The amount and nature of money received under native title agreements, including the purposes for which that money was provided for (for example, some payments could be specifically in relation to 'education, training and employment').

A typical structure in our experience, is the establishment of a native title corporation which is income tax exempt and has an associated trust or trusts where benefits are held and managed.

Reform One - Introducing an income tax exemption for payments under native title agreements

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

SANTS' position is that all payments in relation to native title extinguishment and suspension should be regarded as compensatory in nature and therefore be tax exempt. As raised in the consultation paper, the question of tax on native title benefits is less clear where those benefits are not related to matters of extinguishment or suspension of rights and interests. However, as Strelein states "the definitional issues around the capital and compensation arguments regarding native title payments are intractable and have stifled policy development in this area for many years.[1]

[1] Strelein, L, Taxation of Native Title Agreements, Research Monograph 1/2008, Native Title Research Unit, Australian Institute of Aboriginal and Torres Strait Islander Studies, Canberra.

Given the complexities involved with the interface of taxation law and native title, any regime must be as straight forward as possible and not require the application of complex and onerous assessment criteria.

If this reform was adopted to apply to only benefits stemming from extinguishment, the requirements for an upfront tax exemption may become the objective of any negotiated agreements. That is, an upfront tax exemption places the flexibility of making agreements at risk and may hinder creativity in matters to be covered by agreements.

g) *How should the concept of a native title agreement be defined? Should this concept be defined with respect to the NTA?*

Generally speaking, it is SANTS' submission that the concept of 'native title agreements' or 'native title payments' should adopt alternative language so as to be inclusive of matters other than those negotiated pursuant to the Native Title Act. For example, in South Australia, agreements with respect to mineral exploration and production may be negotiated pursuant to the Commonwealth Native Title Act or the South Australian Mining Act. Parties to these agreements may opt to make an agreement under either legislative regime however the subject matter would still characterise the agreement as a 'native title agreement'.

SANTS acknowledges the need for clear parameters for the purposes of assessing whether an income tax exemption applies, and the political desirability for a tax exemption to be limited to a unique set of circumstances.

In any event, if the concept of a native title agreement was to be adopted, the definition should be as broad as possible. Without doubt, the definition should be inclusive rather than exclusive, and should be flexible to meet evolving agreements.

The proposed solution - that the definition be linked to the NTA –would be too inflexible to meet the changing subject-type of agreements.

As for the possible involvement of an 'independent decision maker' to assess whether an agreement is a native title agreement, SANTS makes three brief submissions. First, if such a decision maker was necessary to assess whether an agreement was a native title agreement, this is likely to be indicative of a definition that is too complex. Second, if the agreements were to be assessed by a decision maker, this would create an extra burden and delay for agreement makers. Three, the decisions of this decision maker may conflict

with the findings of a statutory officeholder charged with reviewing agreements,[2] should such a proposal be adopted.

As a result, SANTS queries whether a definition of a native title agreement which is legally available, practically workable and politically acceptable is possible in the first instance.

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 for purely private consumption?*

It is SANTS' submission that the purposes for which an exempt payment may be used not be prescribed. Such a decision should be a decision that is made by the relevant parties. This is consistent with a flexible approach and would be an unnecessary precaution given that the agreements had been accepted by the parties.

Reform Two - Establishing a new vehicle, for example an 'Indigenous Community Fund' (ICF), which could receive tax exempt payments if they are used for certain purposes

i) *If developments 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 allowed to receive payments under a native title agreement or should it be allowed to receive other payments?*

SANTS submits that an ICF should be able to receive any funds, irrespective of whether the payments arise out of 'native title agreements'. For example, there should be provision for an internal transfer of funds into the ICF. This would assist in capturing funds that have been already paid pursuant to agreements previously made.

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

[2] See Macklin J, 'Harnessing opportunities for future generations of Indigenous Australians – Speech to Native Title Conference 2010, Canberra ', *Native Title Conference 2010, Canberra*, 3 June 2010, available at http://www.jennymacklin.fahcsia.gov.au/speeches/2010/Pages/native_title_conference_030610.aspx.

SANTS agrees with the permitted uses of the funds that have been included in the Consultation Paper, but emphasises that the permitted uses should be reasonably flexible. Other uses that could be considered include:

- Investments that are likely to assist in the accumulation of assets and resources for current and future generations;
- The protection, maintenance or advancement of the health and well-being of those for whom the fund was established;
- The protection, maintenance or advancement of the collective legal rights of those for whom the fund was established;
- Possibly, any other uses that are approved by an ATO private ruling in accordance with the general purposes of an ICF.

In approving the permitted activities that have been expressly raised in the Consultation Paper, SANTS notes that the activity of *the protection, maintenance or advancement of Indigenous cultural heritage* should be sufficiently wide in scope. This is to protect those community members who receive payments for conducting heritage clearances in accordance with any heritage protocols from having to pay income tax on those payments.

iii. What legal form should the fund be required to take?

SANTS does not have a position on the precise legal form that the ICF should be required to note. However, SANTS' submissions about corporate governance (at iv. below) are relevant to this issue.

iv. What kinds of governance requirements should the fund be subject to?

It is SANTS' policy that good governance is crucial to a functioning native title system. An ICF would have similar expectations and requirements of good governance.

In terms of specific governance requirements, SANTS submits that an Indigenous Corporation, including Prescribed Bodies Corporate, registered pursuant to *Corporations (Aboriginal and Torres Strait Islander) Act 2006* (Cth) (**the CATSI Act**) sets a very high benchmark for governance and reporting for Indigenous entities. Coupled with relevant legislative amendments, the CATSI Act may provide sufficient levels of accountability in the administering of the ICF. A Board that manages an ICF as well as the day-to-day business of an Indigenous Community will avoid duplication in decision making and reporting requirements.

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

SANTS submits that some existing agreements may require slight amendment to have benefits paid directly into an ICF. However, SANTS considers that, in most circumstances, existing agreements can still be complied with if there is provision that an ICF can receive funds from any source (and not just from the other party of a native title agreement).

vi. *What kinds of transitional arrangements would be required?*

SANTS acknowledges the need for transitional arrangements, but submits that the arrangements should be as less-complex as possible.

From a legal perspective, SANTS raises two points for consideration. First, transitional arrangements should follow the accrued rights principle. That is, during a transitional arrangement, entities that have been managing native title payments should not be immediately subject to more onerous duties. Second, if the process of governance through the CATSI Act is adopted, fairly extensive legislative amendments will be necessary to support transitional arrangements for CATSI Act Corporations, including:

- Board's functions and powers;
- Constitutions; and,
- Reporting requirements.

From a practical perspective, SANTS submits that extensive training and easily accessible materials will be absolutely necessary. SANTS submits that the initial costs of providing such proactive measures to promote effective corporate governance will far outweigh the longer term costs of poor corporate governance.

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

SANTS submits that the creation of a new income tax exempt vehicle will involve extensive transitional arrangements. The cost of such transitional arrangements will be high. However, these costs are likely to be outweighed by three primary benefits. First, the language is a more accurate reflection of the ambitions of most Indigenous communities, avoiding the connotations that are inherent with the use of a charitable trust. Second, an

ICF could enable Indigenous communities to better realise their broad objectives through a more flexible framework than that provided by charitable trusts. Third, an appropriately managed ICF is consistent with the objectives of good governance and self-sufficiency.[3] Effective governance of native title payments is intrinsically linked to effective governance on a whole.

Reform Three - Introducing a Native Title Withholding Tax (NTWT) requiring entities that make payments to NT groups for suspension of native title to withhold an amount of tax (around 4%)

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

i. The negotiation of native title agreements?

SANTS has some concerns that a NTWT would negatively complicate the negotiation of agreements, in particular the negotiation of quantum.

ii. The form of benefits provided under native title agreements, if a NTWT only applied to monetary payments?

SANTS submits that, should a NTWT only apply to monetary payments, significant uncertainty will still remain in relation to the tax treatment of other benefits and would not address the concern outlined in *(k) i.*

iii. The management of benefits received under a native title agreement?

A NTWT would largely maintain the status quo of managing the benefits received under a native title agreement, and would provide no incentives for the promotion of good governance or wealth creation. It would also mean that benefits would be taxed that might not otherwise be subject to tax, for example in relation to payments that should be considered compensatory or paid into a tax exempt entity.

Conclusion

l) Would adopting one or more of the options outlined above change the way in which you approach agreement making?

[3] See, for example, *Native Title (Prescribed Bodies Corporate) Amendment Regulations 2010* (Cth) and the purposes of those amendments.

SANTS submits that reform of the current taxation treatment of native title benefits is crucial to achieving sustainable social, cultural and economic outcomes. We believe that the ICF option would provide the most adaptable model for taxation that reflects the nature and intent of native title benefits. The availability of such a tax exempt entity would promote certainty and a broader approach by native title groups to what they could actually achieve through the native title process. Conversely, the availability of a tax exempt entity will hopefully facilitate a creative and progressive approach to agreement making by all parties.

Regards

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