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FINANCIAL SERVICES

Reference: Taxation Laws Amendment (Superannuation Contributions) Bill 2000

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SENATE
SELECT COMMITTEE ON SUPERANNUATION AND FINANCIAL SERVICES

Wednesday, 29 November 2000

Members: Senator Watson (*Chair*), Senator Sherry (*Deputy Chair*), Senators Allison, Chapman, Conroy, Hogg and Lightfoot

Senators in attendance: Senators Conroy, Hogg, Sherry and Watson

Terms of reference for the inquiry:

Taxation Laws Amendment (Superannuation Contributions) Bill 2000.

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Committee met at 3.17 p.m.

CHAIR—I declare open this public hearing of the Senate Select Committee on Superannuation and Financial Services. This is the second public hearing into the **Taxation Laws Amendment (Superannuation Contributions) Bill 2000**. The aim of today's hearing is to continue to take evidence from officials from the Australian Taxation Office. All the witnesses who appear before the committee are protected by parliamentary privilege with respect to the evidence given before the committee. This means that they are given broad protection from action arising from what they say, and the Senate has power to protect them from any action which disadvantages them on account of the evidence given before the committee.

As I said in my opening remarks at the first hearing, I would like to draw to the attention of both the committee and the witnesses that there are some matters which are presently the subject of legal proceedings and, as such, are covered by the Senate's sub judice principles. The committee would not wish to be a cause or a contributing factor to a judge dismissing a prosecution or aborting a trial because of prejudice arising from pre-trial publicity. The committee understands that there is a greater danger of prejudice to a trial in criminal cases because of pre-trial publicity and that the courts are more sensitive to that danger in such cases. However, the committee labours under the difficulty of not knowing what issues are likely to be vital in the course of such a trial and that seemingly innocuous matters of fact may actually be at issue between the prosecution and the defence and that publicity about them may cause a miscarriage of a trial.

In any discussion of proposals to close loopholes in superannuation and taxation areas, great care is needed. I therefore seek the cooperation of all witnesses in confining your evidence to issues which are relevant to the bill as, in this way, you will assist me and the committee to ensure that no matters are raised which may impact in any way on any legal proceedings and potentially prejudice a trial because of pre-trial publicity.

Before welcoming the participants to today's hearing, I also wish to advise those present about the status of some documents presented to the committee by Mr Petroulias at the hearing on Monday. During the hearing I advised that the committee would defer its consideration of the status of those documents until a later date. Having taken advice on the matter, the committee unanimously resolved not to receive the documents and to return them to Mr Petroulias. The documents have since been returned to Mr Petroulias. As a consequence, the documents are not covered by parliamentary privilege. I therefore add to my advice to the committee and witnesses that no evidence will be taken on the documents presented by Mr Petroulias as these documents may have possible implications for the current legal proceedings.

[3.20 p.m.]

COLES, Mr Tony, Director, Australian Taxation Office

FITZPATRICK, Mr Kevin, First Assistant Commissioner, Australian Taxation Office

SMITH, Mr Peter Gerard, Assistant Commissioner, Small Business, Australian Taxation Office

THOMAS, Mr Trevor John, Assistant Commissioner, Superannuation, Australian Taxation Office

CHAIR—I welcome again representatives from the Taxation Office. I have a couple of questions to start with. SISFA told the committee that regulated superannuation funds in Australia are permitted to accept transfers of benefits from foreign pension funds or similar vehicles but not vice versa. Would you like to comment or take that on notice?

Mr Thomas—I am certainly happy to comment on that now, Senator. Since 1 July 1998 permanent departure from Australia is no longer a condition for early release of benefits from superannuation funds in Australia. This change was intended to prevent nonresidents from reducing their income tax liability by receiving lower tax employer contributions in lieu of salary and wages and accessing those contributions on permanent departure. The government has indicated that it would be prepared to enter into bilateral negotiations with other countries to facilitate the transfer of superannuation benefits by nonresidents on permanent departure on a reciprocal basis—that is, so that Australians residing and working temporarily overseas could also transfer their overseas pension entitlements to Australia. Australia has yet to be approached by another country to begin negotiations on bilateral transfer arrangements and, of course, we are happy to enter into those negotiations when there is that interest from the other side. At the moment the government in its consideration of international coverage issues is looking to secure agreement on avoiding double superannuation coverage, and that has been the focus of our negotiations internationally to the present time.

CHAIR—The committee heard that US and UK employees are sometimes reluctant to invest in Australia because of risks associated with the currency. Perhaps a way around this might be through using an Australian based public offer master fund for investment where that Australian resident fund would make investment either in the UK or the US depending on the domicile of the person. Can you see any obstacles to this approach?

Mr Coles—We have had some discussion with some industry groups about that, Senator. As I understand it, the problem is that these individuals want to make contributions in the currency of the resident country. There is no Australian company or master trust, as I understand, which accepts the contribution in that resident country currency—

CHAIR—Why not? That is why I asked the question. Is there a way around that?

Mr Thomas—I think there is potentially but at the moment they have not seen a market for that.

CHAIR—I am suggesting that there may well be a market.

Mr Thomas—There may well be a market in the future.

CHAIR—But you said you have not been able to quantify it. If somebody is able to quantify it and finds that there is a market, isn't that the way around the problems that you mention are an irritant? Because there are a lot of other difficulties in sending moneys overseas, I just put that forward as a suggestion.

Mr Thomas—That is potentially one way that the issue could be addressed.

Senator SHERRY—Is it the general position of the tax office that the legislation we are considering restates existing law?

Mr Fitzpatrick—The change to the 'eligible employee' definition in subsection 82AAA, in our view, clarifies our view of the existing law. In relation to the other two measures, one measure is changing the law to make contributions to non-complying funds not deductible; in relation to the other measure, I think Mr Thomas could more correctly clarify that than I can.

Mr Thomas—It is the application of fringe benefits tax to contributions that are being made through salary sacrifice not to the employee's superannuation account but to an associate superannuation account.

Senator SHERRY—You are saying that they are definitely new provisions that change the law?

Mr Fitzpatrick—Two of the three.

Mr Thomas—Two of the measures.

Senator SHERRY—Mr Thomas, in the transcript of your introductory comments, you said:

The measures were introduced to stop continued promotion of tax cleaning arrangements.

It goes on:

It is indicated that it is amending the law because of the continued marketing of these arrangements by some promoters, despite clear public advice from the ATO that they fail both at law and in their implementation.

How do you view that statement, given your previous answer?

Mr Fitzpatrick—In relation to the clarifying amendment, it was our advice to government—which the government announced when it announced the measure in this bill—that to protect taxpayers from the continued marketing of these schemes it was appropriate to amend the law to clarify. In relation to the non-complying funds, it was our view that, for the reasons we gave in

the opening statement Mr Thomas read the other evening, the most appropriate way to prevent the ongoing marketing and to protect potential participants from entering into these arrangements was to change the law to make contributions to non-complying funds not deductible.

Senator SHERRY—Given that answer and the previous answer, it seems to me that your position has shifted. You are now saying that at least two of the measures are definitely new measures that change the impact of the law significantly.

Mr Fitzpatrick—I said the one measure concerning the meaning of ‘eligible employee’ in 82AAA was, in our view, clarifying our view of the present law. I gave the reasons a minute ago as to why we believed it was appropriate to change the law to clarify this matter.

That clarification would work for what we see as abusive arrangements but also in non-abusive arrangements—with the meaning of ‘eligible employee’. In relation to non-complying funds, for the same reasons we believe the abusive arrangements we have identified are not effective under the existing law—and we have made that clear—but, because of the ongoing marketing and for the reason to protect investors, it was our view that the most appropriate measure legislatively was to make them clearly not deductible. I restate that the arrangements we have seen, which we believe are abusive or are schemes, are not effective under the existing law. That is our view and that view is supported by senior counsel’s advice.

Senator SHERRY—We might come to senior counsel’s advice shortly. Looking at the introductory statement, the legislation we are considering from your perspective was more an anti-promotion device than a change to tax law.

Mr Fitzpatrick—In our view, those two measures—putting aside the third, less significant measure, that we have not discussed in much detail here—were designed to protect taxpayers. We believe that the existing law applies to make these not effective. But, to protect taxpayers from the ongoing promotion and marketing of these arrangements despite our publicly expressed view of the arrangements, we believe that amendments to the law were appropriate. The second measure in non-complying funds does more than clarify; the proposal would change the law to make contributions not deductible.

Senator SHERRY—It extends the law?

Mr Fitzpatrick—It extends the law, if that is the term you wish to use. It certainly removes deductibility under the relevant provision in the existing law.

Senator SHERRY—Isn’t it true that since 1991 various officials of the tax office have made a significant number of private binding rulings and also advance rulings in respect of the matters we are considering in this legislation?

Mr Fitzpatrick—The commissioner has publicly acknowledged previously that the ATO has issued a limited number of advices, including some private binding rulings, in relation to the superannuation arrangements.

Senator SHERRY—How many?

Mr Fitzpatrick—In relation to what we call the controlling interest superannuation arrangements we have issued, on our evidence, 19 advices, including only three private binding rulings. The majority of those advices were issued in 1998 and 1999.

Senator SHERRY—You say the majority, but haven't they been issued since 1991?

Mr Fitzpatrick—There was one issued in 1991 and the rest in 1998 and 1999. I need to make this clear: there were only three private binding rulings. Some, as you have alluded to, were administrative opinions; some were just general advice letters which are not binding. In some of those advices, and I think generally the case here, the FBT law was not covered. Depending on the particular arrangements, it is our view, as we have publicly expressed, that FBT may apply in respect of some of these arrangements, depending on what in fact happened. Some of those advices did not cover the anti-avoidance provisions. So, again depending on the facts of individual arrangements, the anti-avoidance provisions may have application. Only two of those advices related to non-complying funds. My understanding is that about seven or eight of those advices were issued, in our view incorrectly, to one tax agent, who has advised us subsequently that the taxpayers involved did not enter into those arrangements. In relation to offshore superannuation schemes, we are not aware of any advices—that is, nil—that have issued.

Senator SHERRY—Are you prepared to give a copy of the PBRs and the advices, the advance rulings, to this committee?

Mr Fitzpatrick—They would contain taxpayer names.

Senator SHERRY—Exclude the taxpayer names—we do not want that.

Mr Fitzpatrick—We will have to look at that. I can take that on notice.

Senator SHERRY—I would put it to you that at least in respect to some of those private binding rulings, from what you are saying—

Mr Fitzpatrick—Three private bindings.

Senator SHERRY—And the advices.

Mr Fitzpatrick—And the other advices, yes.

Senator SHERRY—You would be aware they are used by the profession generally.

Mr Fitzpatrick—I am aware that some advisers and/or some promoters use them inappropriately to market to other taxpayers. You would be well aware that, under the laws passed by parliament, the private binding ruling only applies to the taxpayer or the rulee to whom it is issued. Obviously, it has conditions on its binding nature, such as whether the arrangements entered into were, in fact, those described in the application for the ruling.

Senator SHERRY—You will take on notice that request?

Mr Fitzpatrick—Yes.

Senator SHERRY—Thank you. How many non-complying superannuation funds have you been able to identify that are in receipt of contributions?

Mr Fitzpatrick—The other night I was asked about the revenue impact based on identified arrangements split into the offshore funds and the controlling interest funds. My answer was that in deduction terms in relation to offshore schemes—which would be non-complying funds—we had identified around \$100 million in deductions.

Senator SHERRY—No, I did not ask that. I am asking about the number.

Mr Fitzpatrick—The number of what, please?

Senator SHERRY—Of non-complying funds.

Mr Fitzpatrick—Non-complying funds may involve certainly the offshore arrangements and also may involve onshore arrangements in controlling interest. I am not able to tell you how many non-complying fund arrangements covering both that we have identified. I have data, which I alluded to the other night and provided in some answers to you, on EBA arrangements including the controlling interest and the offshore arrangements. I gave you those figures the other night.

Senator SHERRY—I know what you gave us the other night, but I am interested in the number of funds.

Mr Fitzpatrick—I cannot give you that, Senator.

Senator SHERRY—Why can't you?

Mr Fitzpatrick—I do not have that information here, and I am not sure whether we can get that information on the number of funds, as distinct from the contributions or deductions claimed, as distinct from the number of participants identified. I can give you that data, some of which I have already given you.

Senator SHERRY—We will come back to that in a moment. We had AUSTRAC give information to the committee. Are you aware of that?

Mr Fitzpatrick—I am aware that they made a submission and gave evidence to the committee.

Senator SHERRY—In summary, what they are saying is that they provide you with a mass of raw material, which the tax office then examines in detail.

Mr Fitzpatrick—Yes, that is generally the case in many areas of our work.

Senator SHERRY—What does your analysis reveal, year by year, about the amounts of money going into the non-complying funds, both domestically and offshore?

Mr Fitzpatrick—We would certainly not be able to give you that data today, and I am not sure we can give you that data later either. Mr Smith might be able to assist me here. As I said the other evening, we have certainly looked at the AUSTRAC data to try to help us identify contributions to offshore funds and have used that data in other ways of identifying participants.

Senator SHERRY—But you use the data to identify participants.

Mr Fitzpatrick—To help to.

Senator SHERRY—Yes, and also to identify amounts of money, presumably. You can see the amounts of money?

Mr Fitzpatrick—I do not think the data tells us necessarily that so many dollars go into an offshore superannuation fund.

Senator SHERRY—AUSTRAC told us that. They said that you were the ones who identify the breakdown, the more precise details.

Mr Fitzpatrick—It gives us certain data, which we then use to make inquiries to try to identify what contribution has been made to these offshore funds, in relation to these arrangements which we believe are not effective, and then to try to identify the taxpayers. The data itself does not give us all that detail.

Senator SHERRY—That is the data provided by AUSTRAC?

Mr Fitzpatrick—Yes.

Senator SHERRY—Can Mr Smith help us on this matter?

Mr Smith—I can explain the process we went through in trying to identify some of the offshore superannuation funds. Firstly, we had a look at our internal data to try to identify some companies and trusts that we saw at risk that had large claims for superannuation contributions. We did AUSTRAC searches of those particular companies, and with some of those companies that took us to a couple of New Zealand entities. We then did some AUSTRAC searches on those New Zealand entities, which then led us to identify other companies and other entities in Australia that had also made contributions to those New Zealand entities.

Senator SHERRY—Do you have any idea from your observations about the total sums of money involved? I am not asking for information about individual taxpayers.

Mr Smith—The analysis we did at that stage identified two New Zealand entities. I am not sure of the years; I think this may have been over the 1997 and 1998 years—at least two years. We have identified about \$50 million going to those two New Zealand entities.

Senator SHERRY—This is New Zealand?

Mr Fitzpatrick—I am not sure whether I necessarily meant that equated to contributions to these offshore funds pursuant to these arrangements we are talking about. As I said before, we use that data to help identify.

Senator SHERRY—What about other destinations? You obviously got concerned about something. What were you concerned about?

Mr Smith—I was not part of the analysis at that stage; it is information that I have tried to obtain. But the analysis that they did of these companies with the large superannuation claims identified payments offshore to two entities and both of those entities were New Zealand ones. As I understand it, there were no other countries identified on any scale. It was the New Zealand ones that gave cause for concern.

Senator SHERRY—Is there anyone here who was part of that analysis team?

Mr Fitzpatrick—No, but as you know we look at AUSTRAC data for various sources of information and intelligence and, obviously, we looked at—as Mr Smith has indicated—large claims of superannuation contributions. That was our goal: to identify which companies or trusts may have made large claims. We looked at those to see what contributions were made offshore through those relevant trusts and companies and we analysed the data that way to help us identify what contributions were made to those funds which obviously we had some concerns about.

Senator SHERRY—I would like to have a more accurate picture of the sorts of data that you obtained—quanta, year by year and destination. Can you take that on notice?

Mr Fitzpatrick—We will certainly try to assist the committee with providing more data.

Senator SHERRY—As a general observation, was this movement of moneys on the increase?

Mr Fitzpatrick—We have to look at the data. I cannot answer that at the moment. As I said the other evening, these arrangements to our knowledge peaked around 1998. There were some in, I think, 1997-99 and 2000 based on what we have identified. Those are the contributions we have identified, as I mentioned the other night.

Senator SHERRY—From what you have identified, they peaked in 1998?

Mr Fitzpatrick—I think that is right.

Senator SHERRY—Obviously you had done some analysis in 1997: had you done analysis in earlier years?

Mr Fitzpatrick—I am not sure when the first analysis was done in relation to this aspect.

Senator SHERRY—You can take that on notice. Why did they peak in 1998?

Mr Fitzpatrick—I am not sure why they peaked in 1998. I do not know the answer to that.

Senator SHERRY—You must have some observation about why they would peak.

Mr Fitzpatrick—Perhaps they were being marketed more by tax advisers and/or promoters.

Senator SHERRY—You could take that other question on notice. Just coming back to the administrative arrangements in respect of the tax office: I have a letter that was sent to the tax commissioner, Mr Carmody, and to Mr D'Ascenzo, the second commissioner and Chief Tax Counsel. In part the letters states that it is quite clear that in respect of employee benefit arrangements there was a longstanding administrative practice in accepting the class of arrangements, and several advanced opinions and rulings had been received. The issue of control of superannuation is a clear example of a long held administrative practice. The notion that a controller of a private company can make deductible contributions in respect of him or herself has been consistently ruled upon by the ATO in 1991.

The ATO practice in this area is evidenced by the following letter to the National Institute of Accountants in August 1998 from the Chief Tax Counsel accepting that a controller can be an eligible employee in respect of himself and can, therefore, make deductible superannuation contributions. This is a clear public expression of the ATO view on the arrangement. The specialist superannuation technical unit in Bankstown led by Mr Graeme Colley has consistently advised as to the taxation treatment of these arrangements both orally and in writing—

CHAIR—Order! Is this a private letter from an outsider or is it—

Senator SHERRY—It is a letter that I have that is written to the tax office. The information—

CHAIR—From the outside?

Senator SHERRY—Yes, from the outside. Is the information that is detailed in this correspondence correct?

Mr Fitzpatrick—I am not aware of the letter that you referred to.

Senator SHERRY—Is the information correct?

Mr Fitzpatrick—I have indicated a few minutes ago that, to my knowledge, we have certainly issued what we believe to be some incorrect advices, particularly over 1998 and 1999, in relation to controlling industry regulation arrangements. And this has also been publicly acknowledged by the commissioner. I think it is fair to say that, when we saw movement into non-complying fund arrangements, we certainly examined this closely in all aspects of it, including the deductibility provisions relating to complying and non-complying funds, and

sought advice from counsel. We have acknowledged that we have given some incorrect advices over the period.

Senator SHERRY—When you say incorrect advices, do you mean advices given that are now viewed as being contrary to the existing law?

Mr Fitzpatrick—In our view contrary to the existing law; that is correct.

Senator SHERRY—Or within the existing law?

Mr Fitzpatrick—No, contrary to the existing law. To clarify that, we gave advices that, in our view, were incorrect interpretations of the existing law. As I said earlier, not all those advices covered every aspect of the provisions of the taxation laws, which related to these sorts of arrangements which we are talking about.

Senator SHERRY—Whether those advices were incorrect or not, why did those people get special treatment?

Mr Fitzpatrick—When a person receives a private binding ruling under the law, the commissioner will be bound to apply that ruling so long as the various conditions required by law are satisfied. Only then does the taxpayer get the benefit of the incorrect advice of those conditions for a private binding ruling. I recall saying that there were only three private binding rulings issued in this area, none in relation, to our knowledge, to offshore superannuation arrangements. I would not call that special treatment. I am not sure whether you meant outside the normal provisions of the private bindings ruling regime.

Senator SHERRY—It seems to me to indicate special treatment. But you are saying none of these were—

Mr Fitzpatrick—What is the special treatment. I am not sure I understand, Senator.

Senator SHERRY—You are saying that the advices are incorrect, as I understand it, not in accordance with the law.

Mr Fitzpatrick—Those advices I have referred to, yes.

Senator SHERRY—Well, they have received special treatment. They have acted on them.

Mr Fitzpatrick—I am trying to clarify what you mean by special treatment. I have explained that those who have received a private binding ruling, under the law we are bound to apply that ruling so long as the conditions are satisfied; that is, they have implemented in accordance with what they told us they would do. In relation to other advices—

Senator SHERRY—So these taxpayers are doing well.

Mr Fitzpatrick—Those three taxpayers?

Senator SHERRY—Yes. What sort of money are we talking about?

Mr Fitzpatrick—In the context of the number of participants in these arrangements we have identified it is insignificant.

Senator SHERRY—What do you mean by insignificant? You might take it on notice if you have not got the information.

Mr Fitzpatrick—I will just try to explain what I mean by insignificant. As I understand it—and I think I might have given these figures the other night to you—we have identified about 2,600 participants in these superannuation scheme arrangements. I have mentioned today that we have issued three private binding rulings. Three out of 2,600 in my terms is insignificant. To be fair, though—

Senator SHERRY—I think the amount of money is relevant.

Mr Fitzpatrick—I accept that it is relevant. In relation to those three—and I will move on to the other ones, because I need to be clear about what the position is with the other ones—I do not know whether they have implemented in accordance to what they have told us. We certainly are examining that. I do not know how much is involved in those three cases. We need to examine, if we have not already done so, those three cases and we will do that to see whether we are bound by the ruling. In relation to the other cases, it is certainly fair to say that we have issued those general advice letters and we will take that into account in determining our position in resolving these cases and to be fair to the taxpayers.

Senator SHERRY—So that means that those taxpayers effectively might get a special deal; they might pay less tax than everyone else has to pay.

Mr Fitzpatrick—Pursuant to our settlement guidelines, our code of practice, certainly that would be a factor taken into account in determining any settlement of these matters. I do expect most of these will be settled or conceded.

Senator SHERRY—It is not that they are settled or not settled; it is the terms on which they are settled. We will come to that later.

Mr Fitzpatrick—I should clarify if I could. The settlement, I would imagine, would not cover the primary tax but rather the penalties.

Senator SHERRY—We will come to that in a moment.

CHAIR—In relation to private binding rulings, could you just clarify for the committee whether that only applies to that particular person, providing all the circumstances outlined to the commissioner are fulfilled, and only for a specific period of time.

Mr Fitzpatrick—That is correct.

CHAIR—One would assume that, if one sought a private binding ruling for a minimum amount of money in terms of a transaction, it would not require as high a level of authority in terms of evaluation of the fine print as a ruling that might affect a significant amount of money.

Mr Fitzpatrick—That would be generally correct, that is right.

CHAIR—I think that is why we need to indicate that, although a taxpayer may have had a favourable ruling, if it is for an insignificant amount of money but nevertheless important to that particular person, it may even be different in terms of the rigour that is applied to analysing the details of what is involved or requested in that ruling.

Mr Fitzpatrick—Yes.

Senator SHERRY—Are you aware of an article in the *Financial Review* this morning written by Mr Cleary?

Mr Fitzpatrick—I am aware of an article in the *Financial Review* by Mr Cleary.

CHAIR—It refers to documents that we have returned, I think, or may have returned.

Senator SHERRY—Does it? I do not know.

CHAIR—That is why I think we have got to exercise a high degree of care.

Senator SHERRY—I am only going to go by what the highly authoritative Mr Cleary has reported publicly. I am not going to refer to documents that were sent back to Mr Petroulias. I do not know. Just before I get to that: Mr Fitzpatrick, you are saying there are only three taxpayers who were actually allowed to claim deductions for control of super schemes. You cannot tell me the quantity of money, and yet there is a multimillion problem, tens of millions.

Mr Fitzpatrick—As I have tried to explain, we have identified three out of a total of 19 advices issued, we believe incorrectly, to taxpayers. I have explained that, so long as the relevant conditions which Senator Watson referred to earlier and I have also referred to, are satisfied, under the law we would be bound in relation to those three cases. In my judgment, that we have identified three so far out of 2,600 is relatively insignificant. Certainly, I cannot tell you today what the amounts of contributions were in those three cases, or whether in those three cases we would be bound by the private ruling which we have issued. I have not got that information. We may not have that information yet.

Senator SHERRY—But these do not relate to offshore, non-compliant funds, do they?

Mr Fitzpatrick—They relate to controlling interest superannuation arrangements, not to the offshore funds.

Senator SHERRY—Are there any advices given on offshore funds?

Mr Fitzpatrick—No, not to our knowledge.

Senator SHERRY—According to the article in the *Financial Review* this morning:

An internal ATO briefing paper circulated in July 1998 admitted that the schemes could be valid under a “literal” reading of existing tax law.

The eight-page discussion of deductions under controlling interest super schemes, obtained by the *Australian Financial Review*, indicates that a loophole in the law allowed the schemes to flourish.

... ..

“In my opinion the arrangements are effective on a literal interpretation of the law,” ...

The paper was written by Mr Graeme Colley, a member of the ATO’s superannuation technical services team, and formerly a deputy commissioner with the Insurance and Superannuation Commission.

Did Mr Colley provide that advice?

CHAIR—Before you respond to this question, I urge you to exercise extreme caution.

Mr Fitzpatrick—I understand.

CHAIR—Senator Sherry has a question but there are possible implications, and I just urge your caution in the manner in which you respond to that.

Mr Fitzpatrick—Thank you. Senator Sherry, I think I know the document referred to in the article, but I believe it may be connected with a matter currently before the courts. In the circumstances, I think I need to seek the advice of the DPP before I can respond.

Senator SHERRY—This was publicly reported.

Mr Fitzpatrick—I understand it was publicly reported. I understand what document was referred to but, as I said, I think it may be connected to the matter currently before the court. I understand that in all those circumstances I need to seek advice as to whether I can respond to your question. I can talk in general terms about our position under the law, which I already alluded to, but not in relation to that particular document for the reasons I have mentioned. I hope you can understand my position in respect of that.

Senator SHERRY—I can understand you would seek advice. I do not agree that you cannot comment on this document. I understand you would seek advice, but that unfortunately delays us further.

Mr Fitzpatrick—But you can understand why I would want to seek advice from the DPP in the circumstances.

Senator SHERRY—This is a public report. This is public now.

Mr Fitzpatrick—It is not a public report.

Senator SHERRY—I am talking about the newspaper article—

Mr Fitzpatrick—A newspaper report was published.

Senator SHERRY—a public document that presumably thousands of people have now read.

Mr Fitzpatrick—I can only repeat what I have said, Senator, I am sorry. I think I know what document the article refers to but, for the reasons I have said, I need to take advice in the circumstances.

Senator SHERRY—Could you also take advice about providing us with a copy of the document?

Mr Fitzpatrick—I will take advice certainly in relation to the whole matter. I can answer in general terms to amplify our position under the law. The ATO view is quite clear. We do not believe these arrangements are effective under the existing law.

Senator SHERRY—You do not believe they are effective?

Mr Fitzpatrick—These arrangements we are talking about. We do not believe the controlling interest superannuation arrangements are effective under the existing law, as I mentioned earlier.

Senator SHERRY—Are there legal advices that say they are effective?

Mr Fitzpatrick—We have legal advices which say that these particular arrangements are not effective.

Senator SHERRY—Do you have legal advice which says they are effective?

Mr Fitzpatrick—No, we do not.

Senator SHERRY—None at all?

Mr Fitzpatrick—We do not have any legal advice to say that these particular arrangements we are talking about are effective under the existing law.

Senator SHERRY—Do you have legal advices about non-complying overseas superannuation funds?

Mr Fitzpatrick—We have legal advice that they are not effective, based on the arrangements we have seen.

Senator SHERRY—They are not effective?

Mr Fitzpatrick—Under the existing law.

Senator SHERRY—Why have we got the legislation?

Mr Fitzpatrick—For the reasons I explained earlier, Senator.

Senator SHERRY—If they are not effective, why legislate?

Mr Fitzpatrick—For the reasons I mentioned earlier.

Senator SHERRY—That is not what I am asking. If they are not effective schemes, why legislate?

Mr Fitzpatrick—As I indicated earlier, it was our view that it was necessary—because of the ongoing marketing of these arrangements by some people—to protect taxpayers. We need to have regard to this wider picture of the protection of taxpayers.

Senator SHERRY—You have talked about ongoing marketing a number of times. Why don't we just change the law to prevent the marketing?

Mr Fitzpatrick—It is for the parliament to decide whether it should be changed. We cannot change the law to prevent marketing.

Senator SHERRY—You keep talking about anti-marketing.

Mr Fitzpatrick—We are talking about the selling of these schemes to taxpayers on the basis that the taxpayers are told these are effective arrangements under the existing tax law when apparently they are not.

Senator SHERRY—How do you outlaw that? How do you outlaw tax promoters marketing anything as being tax effective within the law?

Mr Fitzpatrick—That is a good question. It is not within our responsibility or power to stop people marketing whatever sort of arrangement.

Senator SHERRY—But that is the reason you give for this legislation. You say you are concerned about the marketing of ongoing schemes that are, in your view, outside the law.

Mr Fitzpatrick—That is correct.

Senator SHERRY—If they are outside the law, what is your problem?

Mr Fitzpatrick—As I said earlier—and this issue is in a wider context which another Senate committee is presently looking at into the protection of taxpayers or investors into these mass marketing arrangements—that Senate committee has expressed quite clearly—

Senator SHERRY—I am aware of that.

Mr Fitzpatrick—What I am trying to say to you, Senator, because I obviously have not explained it clearly enough for you, is in that context—

Senator SHERRY—No, it just seems to me that your explanation is contradictory.

Mr Fitzpatrick—I do not understand why. It has not been unusual over the years for the tax office to take a view of the law but then to recommend a change to government to protect the ongoing marketing or selling of arrangements which in our view exploit the law. This has happened before. It happened back in the scheme 20 years ago, as I recall. There were occasions where the law was amended by the parliament to prevent ongoing exploitation, despite the fact that the ATO's view was that those schemes were not effective. Some of those were eventually litigated and decided in the commissioner's favour. This is not the first time this has happened.

Senator SHERRY—If the law is sound, why have you not prosecuted?

Mr Fitzpatrick—What do you mean by prosecuted, Senator?

Senator SHERRY—Have you taken any legal action that has led to a court action against the people that are supposedly breaching the law? That would be a good lesson to people promoting these schemes, wouldn't it?

Mr Fitzpatrick—If taxpayers want to take the issue to court, it will be heard by a court and decided by a court. That is correct, I agree. We are taking action—

Senator SHERRY—But that has not happened to date, has it?

Mr Fitzpatrick—In a number of areas it does happen, of course.

Senator SHERRY—I am talking about in respect of this area.

Mr Fitzpatrick— In this area there has been no case decided in court or the Administrative Appeals Tribunal at this point in time. But, as I said the other evening, we are taking action and continue to do so in identifying participants, amending assessments, looking at the individual circumstances of cases and amending those assessments, considering any settlement offers which have come forward, reviewing objections which come forward and then making decisions on those objections. If the taxpayers want to then lodge an appeal to the tribunal or court they will do so. I expect some will, but I expect most will not. I expect most taxpayers in these arrangements will either concede or seek a settlement, make an offer to us. Some have already done that.

CHAIR—You have already collected \$100 million.

Mr Fitzpatrick—We have, under various employee benefit arrangements, as I said the other night.

Senator SHERRY—I might come to that a little bit later.

CHAIR—Isn't it open to the participants to sue the promoters, where they have relied on that advice and the advice is deficient?

Mr Fitzpatrick—It is open to them to do that—depending on the facts, obviously, Senator. Just to finish my answer on the litigation of these cases: I think there is a small number

presently in the Administrative Appeals Tribunal or court awaiting hearing in relation to these arrangements—a small number.

Senator SHERRY—That is interesting. Will the legislation we consider impact on those cases?

Mr Fitzpatrick—No. The measures in the bill which you are considering are proposed to have effect from 30 June 2000. These arrangements I am talking about would have occurred before that date.

CHAIR—Is it a further problem you have that sometimes the courts put out the date for hearing by quite a long time, so you are left waiting at the court's pleasure for maybe quite some months or even years?

Mr Fitzpatrick—That is right. The timing of hearing by a court or the Administrative Appeals Tribunals, for that matter, is not within our control. In relation to these areas it is fair to say that we would do all within our power, where taxpayers wished to litigate the issue, to ask the court to bring forward a hearing of those cases, where a number of taxpayers may have similar arrangements.

Senator SHERRY—Just briefly going back to PBRs and the three that we were discussing earlier: is there a clause in the final public tax ruling issued in 1999 that specifically excludes TR995 from applying to people with a PBR?

Mr Fitzpatrick—As I said earlier, if a taxpayer has a PBR and all the conditions are satisfied, the law provides for that to be binding on the commissioner. Not a public taxation ruling but the law does that.

Senator SHERRY—These three cases that we were talking about earlier have effectively benefited from that?

Mr Fitzpatrick—Under the law?

Senator SHERRY—Yes.

Mr Fitzpatrick—As I said earlier, depending on whether the conditions have been satisfied, the law requires that the private binding ruling—to that taxpayer alone, for that particular year or those years alone—will be binding on the commissioner. The law says that.

Senator SHERRY—There was a draft ruling in October 1998.

Mr Fitzpatrick—That is correct. It was on the FBT consequences in relation to employee benefit trusts and non-complying funds.

Senator SHERRY—When was the final ruling on that?

Mr Fitzpatrick—In May 1999. The one you just referred to?

Senator SHERRY—Yes. That initial draft ruling in October 1998 was made known to the profession publicly?

Mr Fitzpatrick—Yes, as is normally the case. We issue a draft ruling for the purpose of consultation and to take on board the views through that consultation period, before finalising our view. That is the normal practice.

Senator SHERRY—Why shouldn't the legislation be made retrospective to that date, October 1998?

Mr Fitzpatrick—Let us clarify here: the legislation we are talking about in this bill concerns controlling interest superannuation arrangements. The final ruling did not deal with that particular issue, it dealt with FBT.

Senator SHERRY—Why not make that section retrospective to that date? Was that considered?

Mr Fitzpatrick—In providing our advice to government we consider all aspects of policy, including our view of the date of effect. Because in our view the existing law, as I have said a number of times today, applies against these schemes, it was not our view that the legislation needed to be retrospective. That is a question for the government and the parliament, of course. It is not a question for the ATO.

Senator SHERRY—I understand it is a question for parliament and government. But if these schemes should not have been operated in this, why not make it retrospective? Why not go back further?

Mr Fitzpatrick—As you know, retrospectivity is a matter of last resort, generally speaking, including in the tax area. From our point of view, we believe the existing law is effective to deal with these abusive arrangements. I have explained the reasons we believe that legislative changes are required which are in the bill. It is then a question for government and the parliament to decide whether they believe it should be retrospective.

CHAIR—Are you aware of any cases which involve retrospectivity where a general issue is being covered and some areas may be retrospective and others not? To my mind it would create a degree of confusion where we were dealing with one issue.

Mr Fitzpatrick—In relation to a particular measure it would create confusion if that was the case.

CHAIR—Would that be a precedent if we went down that track?

Mr Fitzpatrick—Obviously it is not a precedent to go retrospectively on a particular measure.

CHAIR—No, but in relation to the one issue?

Mr Fitzpatrick—It depends what the one issue is, to be honest. We have got three difference measures here.

CHAIR—We have got three measures in the one issue.

Mr Fitzpatrick—It depends what the one issue is. If it is employee benefit arrangements, which we believe on the face of what we have seen are of a tax avoidance nature, yes, that is the one issue.

Senator SHERRY—But you have said these arrangements are not effective under the existing law.

Mr Fitzpatrick—That is correct.

Senator SHERRY—So why not make it retrospective? If they are not effective under the existing law, what possible harm can it do?

Mr Fitzpatrick—I cannot add any more to my previous answer, Senator.

Senator SHERRY—That is in the tax office annual report. You say you have always had a consistent position on this.

Mr Fitzpatrick—Subject to those private rulings and advices I have talked about and that we have discussed today.

Senator SHERRY—Well, let's put them to one side.

Mr Fitzpatrick—Our position and our advice to government has been consistently that the law is effective to deal with the abusive arrangements we are talking about. But, for the reasons I mentioned earlier, we believed it was appropriate to protect taxpayers from ongoing marketing or selling of these arrangements to them despite the ATO's views.

Senator SHERRY—I still do not see why they cannot be made retrospective.

Mr Fitzpatrick—As I said, that is a question for the government and the parliament more than the tax office.

Senator SHERRY—What was your recommendation?

Mr Fitzpatrick—We make recommendations to government, but you know I cannot provide that information to you.

Senator SHERRY—I can always ask in hope. In respect of non-complying superannuation funds, from the introductory remarks it is clear that the way in which they have been used/abused is not consistent with the intention of superannuation legislation in this country, is it?

Mr Fitzpatrick—The use of non-complying funds in these arrangements?

Senator SHERRY—Yes.

Mr Fitzpatrick—That is our view and I think we made that statement in our initial opening statement given by Mr Thomas.

Senator SHERRY—It was never intended that people could avoid surcharge tax, contributions tax, those sorts of taxes, was it?

Mr Fitzpatrick—Not in our view—it was not intended, no.

Senator SHERRY—I agree with you. Why shouldn't that change be made retrospective?

Mr Fitzpatrick—For the same reasons I mentioned earlier: we believe these abusive arrangements are not effective under the existing law, but, again, it is a matter for government and parliament to decide the date of effect.

Senator SHERRY—You are saying they are not effective under existing law, but people—

Mr Fitzpatrick—With these abusive arrangements—these schemes we are talking about that we have identified and looked at—there may be in some of these arrangements, depending on the facts again, more than one taxing point as well. Non-deductibility of contributions, FBT applying and, of course, the anti-avoidance provisions might apply in any event as a last resort.

Mr Thomas—If I can just add, Senator, in the opening statement I did refer to the fact that when the SIS legislation was introduced in 1993 the deductibility for contributions to non-complying superannuation funds remained because a number of funds could not meet the prudential and supervisory requirements of SIS. It does not give the government or the community confidence about the use of the tax concessions which are being granted for contributions to superannuation when they are going to non-complying superannuation funds where there is no preservation regime and other protections to ensure that those moneys are being used to provide an income in retirement. The point you have made in respect of that is quite correct.

CHAIR—Senator Sherry, we only have a couple of minutes: do you want to put some questions on notice?

Senator SHERRY—No, I do not want to put them on notice, but I will just put this question and then I will see how we can conclude. Mr D'Ascenzo in his evidence to the House of Representatives committee told us—that was on 11 May and I referred to this earlier in the week—that if the ATO failed in the courts to recover the revenue at risk they would recommend retrospective legislation. Do you still hold that position?

Mr Fitzpatrick—We do not believe we will fail in the courts.

Senator SHERRY—You do not know yet though, do you?

Mr Fitzpatrick—Without a court case deciding it, that is correct. As I said earlier, I believe—and it is our experience so far and our view—that most taxpayers will concede the issue or settle on terms which are within our settlement guidelines. There may be some cases that will get to court. If we are unsuccessful in the court we will need to review the position then.

Senator SHERRY—Why did tax office officials tell the parliamentary inquiry into employee share plans on 11 May that there was no need for legislative change in relation to abuse of employee benefit arrangements, and yet seven weeks later on 30 June the Assistant Treasurer announced anti-avoidance legislation would be introduced?

Mr Fitzpatrick—They may have been referring—this is where it gets a little bit confusing I suppose for all of us—

Senator SHERRY—But this is Mr D'Ascenzo and I am not sure who else—

Mr Fitzpatrick—I understand. But they may have been referring to employee benefit arrangements involving employee benefit trusts as well. We are talking here about controlling interest offshore superannuation schemes. We are not recommending to government that they amend the law relating to employee benefit trusts or share plans. Again, we believe the existing law is effective to deal with those arrangements we have identified as being of an avoidance nature.

Senator SHERRY—But the Assistant Treasurer announced anti-avoidance legislation on 30 June, didn't he?

Mr Fitzpatrick—That is in relation to superannuation—that is correct. What I was trying to explain was that in the evidence before the House of Representatives committee—as I recall and as I understand what was said and what you have just read out—it was talking generally about employee benefit arrangements which include arrangements beyond the superannuation measures we are talking about here, and it is fair to say that—

Senator SHERRY—But there is overlap.

Mr Fitzpatrick—The employee benefit trusts are a different arrangement.

Senator SHERRY—Yes, but there is overlap.

Mr Fitzpatrick—To some extent there is overlap but not entirely.

Senator SHERRY—No, I understand it is not a total overlap but there is some.

Mr Fitzpatrick—Employee benefit trusts are essentially, as our ruling said, about applying FBT to arrangements. In finalising this answer to your question, we continue to monitor throughout the year as best we can what was happening in the ongoing marketing and selling of these arrangements and came to a view later in the year that, for the reasons I have explained

earlier, it was appropriate that the government consider amending the law for the reasons I have mentioned.

Senator SHERRY—Chair, I know we are in our last minute or two minutes, but it would have helped us if we were able to have had the tax officers present that I, through the committee, had requested. Did you reconsider?

Mr Fitzpatrick—I looked at that list and I explained the reasons the other evening as to why we believed we could assist the committee in its deliberations on this bill from those of us who are present. I did look at the list that you provided through the secretariat to us and some of those people in the tax office had nothing to do with this particular bill. So I was surprised to know why they would be on the list.

Senator SHERRY—In our view they did. They would not have been here long otherwise.

Mr Fitzpatrick—It was our judgment that we could assist the committee through those who attended—

Senator SHERRY—But unfortunately your assistance has been somewhat restricted.

Mr Fitzpatrick—To what extent?

Senator SHERRY—We have not got the answers to some of the questions we were seeking.

Mr Fitzpatrick—In what respect, Senator?

CHAIR—Order! I think our time has expired, Senator, so you might like to have a discussion with Mr Fitzpatrick outside.

Mr Fitzpatrick—Other than in relation to the AUSTRAC data, the more detailed analysis, I am not sure what else—

Senator SHERRY—There are some other matters. Chair, I know the time has ceased, which is unfortunate because there were a number of other questions. I am not satisfied.

CHAIR—Can you put them on notice?

Senator SHERRY—No.

CHAIR—We do have a problem.

Senator SHERRY—I know we have a problem, Chair. I am just raising this with you now. We do have a problem. Some of the issues we wanted to raise we have not been able to raise. This is important legislation. We have got material coming to us on notice, and it is extremely difficult for us to deal with the legislation, particularly the issue of retrospectivity, in these circumstances.

CHAIR—So there is no wish to have another hearing?

Senator SHERRY—Yes, there is.

CHAIR—Why didn't you request, for example, the permission of the Senate to sit for two hours?

Senator SHERRY—Because you and the secretary had said one hour. I did not have any say in that.

CHAIR—We gathered that that was all that was required.

Senator SHERRY—It has not been enough time.

CHAIR—You were at the meeting yesterday when that could have been changed.

Senator SHERRY—No, it couldn't be changed at the meeting yesterday. That was after the resolution was put down in the Senate, which I did not have anything to do with. I am not criticising you or the secretary; it is just that unfortunately we do not have enough time. The other problem is that there are some witnesses that we would have liked—Treasury has not changed its view on that—and could have been some help. Mr Colley's presence would have been useful, for example, but he is not here.

CHAIR—We have to conclude the formal parts now. On behalf of the committee I thank all witnesses who have given evidence for their participation.

Committee adjourned at 4.17 p.m.