COMMONWEALTH OF AUSTRALIA

JOINT COMMITTEE

of

PUBLIC ACCOUNTS AND AUDIT

Reference: Tax Law Improvement Bill (No. 2) 1997

SYDNEY

Wednesday, 28 January 1998

OFFICIAL HANSARD REPORT

CANBERRA

JOINT COMMITTEE OF PUBLIC ACCOUNTS AND AUDIT

Members

Mr Charles (Chair)
Mr Griffin (Deputy Chair)

Senator Coonan	Mr Anthony
Senator Crowley	Mr Peter Baldwin
Senator Gibson	Mr Beddall
Senator Hogg	Mr Broadbent
Senator Watson	Mr Fitzgibbon
	Mr Georgiou
	Mr Sharp
	Mrs Stone

Matter for inquiry into and report on:

Tax Law Improvement Bill (No. 2) 1997.

WITNESSES

BACK, Mr Gavin Alexander, Assistant Commissioner, Tax Law Improvement Project, 2 Constitution Avenue, Canberra, Australian Capital Territory 2601 4

BLAIKIE, Mr Allan William, Member, Consultative Committee, 1 O'Connell Street, Sydney, New South Wales 2000 4

BRYANT, Mr Robert James, Executive Director, Corporate Tax Association, Level 11, 455 Bourke Street, Melbourne, Victoria 3000 4

BURGE, Mr John Gregory, Senior Officer, Tax Law Improvement Project, 2 Constitution Avenue, Canberra, Australian Capital Territory 2601 4

DEUTSCH, Professor Robert Leslie, Director, ATAX, University of New South Wales, Sydney, New South Wales 2052 4

DRODER, Mr Stanley John, Chairman, Tax Law Improvement Consultative Committee, 3/111 Harrington Street, Sydney, New South Wales 2000 5

FRESHWATER, Ms Lyn Margaret, Technical Officer, Tax Law Improvement Project, Australian Taxation Office, 140 Creek Street, Brisbane, Queensland 4000 4

GAYLARD, Mr Simon James, Tax Law Improvement Project, 2 Constitution Avenue, Canberra, Australian Capital Territory 2601 4

GIBSON, Mrs Margaret Mary, Member, Consultative Committee 5

HALY, Miss Margaret, Assistant Commissioner, Tax Law Improvement Project, Box 10422, Adelaide Street Post Office, Brisbane, Queensland 4000 4

HARDERS, Mr Geoffrey, Consultant, Australian Taxation Office, 2 Constitution Avenue, Canberra, Australian Capital Territory 2601 4

KREVER, Professor Richard, Tax Law Improvement Project Consultative Committee, 2 Constitution Avenue, Canberra, Australian Capital Territory 2601 5

LANGFORD-BROWN, Mr Ian, Director, Taxation, Institute of Chartered Accountants, 37 York Street, Sydney, New South Wales 2000 5

MAGNEY, Mr Thomas Waymouth, External Consultant, Tax Law Improvement Project, Australian Taxation Office, 2 Constitution Avenue, Canberra, Australian Capital Territory 2601 4

MORGAN, Mr John Frederick, Private Sector Representative, Tax Law Improvement Project, Australian Taxation Office, 2 Constitution Avenue, Canberra, Australian Capital Territory 2601 4

MORTON, Ms Joycelyn Cheryl, Past President, Australian Society of CPAs, Level 3, 111 Harrington Street, Sydney, New South Wales 2000 5

NOLAN, Mr Brian Martin, Project Director, Tax Law Improvement Project, 2 Constitution Avenue, Canberra, Australian Capital Territory 2601 4

PARKER, Mr Anthony Joseph, Member, Tax Law Improvement Project Consultative Committee, Australian Taxation Office, 2 Constitution Avenue, Canberra, Australian Capital Territory 2601 5

REID, Mr Thomas Johnston, Second Parliamentary Counsel, Tax Law Improvement Project, 2 Constitution Avenue, Canberra, Australian Capital Territory 2601 4

JOINT COMMITTEE OF PUBLIC ACCOUNTS AND AUDIT

Tax Law Improvement Bill (No. 2) 1997

SYDNEY

Wednesday, 28 January 1998

Present

Mr Charles (Chair)

Senator Gibson	Mr Beddall
Senator Watson	Mr Griffin

The committee met at 9.54 a.m.

Mr Charles took the chair.

CHAIR—The Joint Committee of Public Accounts and Audit will now take evidence as provided for by the Public Accounts Committee Act 1951 for its review of the Tax Law Improvement Bill (No. 2) 1997. I welcome everyone here this morning to this first public hearing conducted by the recently reconstituted Joint Committee of Public Accounts and Audit. The committee's role has been expanded to include oversight of the Commonwealth Attorney-General, who is now an officer of the parliament. The committee takes this new role seriously, as it does any review of legislation referred to it.

The Tax Law Improvement Bill (No. 2) 1997 is the third instalment of the rewrite of the Income Tax Assessment Act 1936 and contains the important capital gains tax provisions. The parliament has asked the committee to review the bill and report by 12 March 1998.

The committee welcomes its continuing role in the scrutiny of rewritten taxation legislation. The committee's interests commenced in 1993 when it reviewed the Australian Taxation Office and recommended that the government establish a broadly based task force to redraft the 1936 act. Since then the committee has reviewed the first two instalments of redrafted legislation.

The task force, the tax law improvement project, will be giving evidence today together with its consultative committee, which represents a diverse range of stakeholders. Throughout discussions it must be remembered that the aim of TLIP is to clarify the law by eliminating unnecessary complexity, restructuring the law and using simpler and more direct language. This means that clearer tax laws will result in reductions in compliant costs and, therefore, benefit all taxpayers.

Today the hearings will begin by considering general issues concerning the rewrite process before proceeding to considering the bill division by division. Tomorrow the committee will take evidence from organisations and individuals with an interest in the bill. The final session tomorrow will provide witnesses with the opportunity to make final comments.

As we will be taking evidence from a number of witnesses, I ask that the following procedural rules be observed to facilitate the running of proceedings: only members of the committee may put questions to witnesses; if other participants wish to raise issues for discussion they will need to direct their comments to the chair who will decide whether to pursue the matter. It will not be possible for witnesses to respond directly to each other.

Before swearing in witnesses, I will refer members of the media who may be present at this hearing to the committee's statement about the broadcasting of proceedings. In particular, I draw the media's attention to the need to fairly and accurately report the proceedings of the committee. Copies of that statement are available from the secretariat staff present at the hearing.

Also, as a matter of procedure, could I ask that you preface any remarks with your name because we have so many people around the table. *Hansard* does need a bit of a hand. I now welcome the representatives of the tax law improvement project and TLIP consultative committee to today's hearing.

[9.59 a.m.]

BACK, Mr Gavin Alexander, Assistant Commissioner, Tax Law Improvement Project, 2 Constitution Avenue, Canberra, Australian Capital Territory 2601

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CHAIR—Mr Nolan, we have received written submissions to this inquiry from you. Do you wish to present any additional submissions?

Mr Nolan—I would only say that this is a very important stage of the rewrite of the income tax law by the tax law improvement project. Most of the things that I was going to say by way of preface you have already covered in your own opening remarks. We regard this particular bill as a very important one. A lot of energy and effort has gone into bringing it to the stage that it is at now. We believe it is a very good product.

I would like to put on record my thanks to the drafters and instructors on the project team who have assisted me in producing it and to the very many other people in the professional community—not the least of which of course are the people seated around this table from the consultative committee—who helped us by advising us on our work. I think the combined efforts of all the people who have been a party to the production of this bill has produced something which is eminently better than the existing law, especially in the capital gains area. We very much commend the bill to the committee.

CHAIR—Mr Droder, we have not received a submission from the consultative committee. Do you wish to make a submission?

Mr Droder—Yes, Mr Chairman, the consultative committee really has not formally met on this process. We did have a meeting earlier this morning, which started at 8 o'clock, and went over some of the remarks that I want to make. I might go into that straightaway. You will appreciate that the holiday period that followed after the introduction of this legislation made it very difficult for us because many were on holidays.

I guess that introduces the first point—that is, the haste, and some might say indecent haste, of the bill's introduction to parliament and the short time available for representative bodies and members here to make comment. The bill has been prepared in haste so as to meet the legislative timetable. While some may say that there never is enough time, we think in this case the haste was too much. We, for instance, only received some of the papers on the bill on Friday, 9 January.

So there are a number of points to be made about this: one, we think to allow proper time for the community to accept this legislation the introduction should be deferred to 1 July 1999; two, the haste opens the possibility of even more errors than would be normally acceptable; three, the consultative process came to a sudden end when the pressure expanded; four, the risk of unintended changes increases; and, five, confidence in the output declines not only with this bill but also with successive bills yet required.

One of the issues for us is that this whole process of rewriting the income tax legislation has to be concluded, as we understand it, in 18 months. There is an enormous amount of work yet to be done. If we are to have a fair time for the community to react to the bills, then we do not quite know how that is going to be managed and, certainly, we do not think the time with this one has been enough.

I guess the second point of that is the impact on the process for ongoing TLIP work. The project leader, John Burge, has done extensive consultative work but we wonder whether, after all this effort, those who have been consulted actually feel satisfied with the final product or that their issues have been adequately considered. We all, I think, appreciate the logistics of the consultative process are costly and time consuming, but the point remains that those making submissions, such as the joint professional bodies or the CTA, need tangible evidence that their work is not being dumped into a big black hole and ignored.

There are often small 'p' and big 'P' items contained in these submissions which the TLIP team may well and properly claim are well outside its terms of reference. However, ignoring the points does not generate enthusiasm to spend more and more funds making submissions that seem to disappear. While logistically the task of responding in detail is probably daunting, the fact is that it is necessary that it be done to maintain interest and involvement.

While submissions vary widely, I am sure the accounting bodies, for example, from their perspective and others, would like to have some return of the resources that they invest in the process. We think each of those, particularly the major submissions from accounting bodies or the CTA or other important bodies, should be responded to in four ways: first, whether the TLIP team accepts the point being made; second, whether the TLIP team rejects the point being made; third, if it is a small 'p' policy issue, that the team picks up the issue and will take it into government to address; and, fourth, we would

like to know when the whole thing is absolutely rejected so we can take up the issue in other forums.

I notice in today's *Financial Review* that Brian undertakes to give a response to those things, but the problem is that from the time of actually making the submission and then getting a response—and you will probably pass the bill anyway—will all be a bit too late.

I am going back over some old ground, but it is interesting that some of us—and perhaps all of us—feel that the history of the Australian tax legislation is that it has become extraordinarily complicated due to the tax office's enthusiasm to chase down in legislation every possible loophole. The fact is that the process appears not to have blocked every loophole and here we are continuing in the ongoing saga.

In my first meeting with the JCPA, I think I upset the tax office by saying that it had a culture based around three assumptions: one, that all taxpayers are cheats; two, that they must do everything to collect revenue; and, three, that the commissioner's interpretation of the law is always correct. So we have complicated tax legislation.

I heard one suggestion for this body—that is, that you, its members, set out to read the bill and if you understand it then pass it, if you do not then send it back. My particular detailed task at this hearing includes subdivision 165-CA, capital gains tax losses carried forward, and subdivision 165-C, bad debts. In subdivision 165-CA, section 165-93 is headed 'What this subdivision is about'. It states:

> In working out its net capital gain for an income year, a company cannot apply a net capital loss for an earlier income year unless:
>
> * it has the same owners and the same control throughout the loss year and the income year; or
> * it carried on the same business, entered no new transactions and conducted no additional business.

I do not know about you, but I read these last 15 words literally and came to the conclusion that if I sold anything, including that asset which gives rise to the capital gain, or employed any new person or served an existing or new customer I automatically breached the requirement of 'no new transaction or no additional business'. This is relatively simple language, it seems to me. I then get to subdivision 165-C and it seems to me that if I acquired a hire purchase finance business, conducted due diligence, accepted a hirer who had made his payments religiously on the due date and then who, after six months, for some unknown reason, defaulted, then I am denied the loss. Maybe that has been the intention all along, but it seems to me to be unfair and, in principle, wrong. That section also includes a carry forward test in 165-CA.

The continuing ownership test has problems for major public companies in chasing shareholders. I am sure Bob Bryant here will raise that with you tomorrow. I understand

though that for many this overall issue has declined into an acceptance that the tax office will be reasonable in its interpretation. But that in itself maintains uncertainty in the interpretation of the law.

As Director of the New South Wales division of the Australian Society of CPAs I receive many phone calls that constantly complain about the unreasonable attitude of the ATO. So I am not comfortable that the community generally accept that interpretations are unlikely to be reasonable.

That leads me to my next issue, which is the confidence or lack of it that professionals and practitioners have in the process. Some on the consultative committee continue to advocate the warehousing concept, but it seems to me that this is but one possible solution to a problem of confidence. The broad issue is that inherent in this whole process of consultation, changing the words, interpreting business processes and the underlying tax principles is the risk of error and the lack of certainty that an unintended error detected some time in the future will mean a reinterpretation of the law with adverse consequences to taxpayers.

This is why this committee pushed for section 1-3's introduction and for the tax office to reinforce the status of existing rulings. However, many feel—and many around this table feel—that, with the tax office's pro-active reinterpretation of the law and the judiciary's independence of thought, there needs to be even more protection against unintended changes. Others can speak as to why they see warehousing as the solution, but it is a complicated question and I am not sure a simple answer exists.

I personally have consistently pushed a view that, if an unintended consequence arises, a process is needed to introduce amending legislation quickly. An unintended change could occur through the tax office having a different view or the courts making a decision that changes the meaning. For instance, I recall at the second JCPA hearing into this process the mining industry had a view that the rewrite expressed the tax office's interpretation of the section with which the industry did not agree and were challenging the tax office's position in the courts. The question was then asked: what happens to the new law if the courts hold that the tax office's interpretation is incorrect? Is the tax office's now proven wrong interpretation of the law what should be the case or does the new law continue, giving the tax office what they wanted in the first place? I am not aware of this matter being resolved satisfactorily.

The point is that there is deep concern out there in taxpayer land. There have been solutions suggested and rejected by the tax office. This committee feels that rejection requires an alternate suggestion to the problem, and I for one would now like to see that emerge from the tax office instead of them simply saying 'trust us'. 'Trust us' is a problem.

I have to repeat the problems with small 'p' and large 'P' issues which still exist.

The point needs to be made that TLIP's team is to rewrite the law so it can be understood but not to simplify the law, except possibly as a by-product. Put another way, the rewrite is not simplification.

On small 'p' issues, we are heartened by Senator Kemp's advice to us at our December 1997 meeting that he will positively support a process to review small 'p' issues. He requested that this committee provide a list of important small 'p' issues, and we will do that.

On large 'P' issues, we note the government's team looking at tax reform. The team may well extend their consideration beyond GST, or the value added tax, to substitute for current indirect taxes. They may look at state versus federal tax collections, but it seems unlikely to us that the government would dispose of ordinary income tax; hence, reform of the current business income tax regime remains an important issue. Even then, some of us believe that it will take a long time before tax reform moves from the political process into reform status, particularly in the income tax provisions that so complicate business in this country, so this is not to us an acceptable excuse to delay the big 'P' issues.

The other problem with this is the application of our resources by the community to the future TLIP process. The CPAs, the ICA and the TIA have worked together on submissions, and it is a costly and time consuming task. Tax reform on the agenda will just provide more demand on their limited resources and those of other interested groups, meaning less involvement in the TLIP consultative process.

Finally I want to, if I may, express one more concern: this committee has always felt that, once the rewriting concepts and principles were established and settled by the TLIP team, all new legislation or even substantially amended legislation would fall into line. I do not think that we have confidence that the tax office is working together with the TLIP team to achieve this position.

The joint submission by the accounting bodies complains that the rewrite on capital gains tax incorporates well-known technical difficulties in current law, and it is disappointing that other government arms have not given priority to these issues so that TLIP could have removed those difficulties. Yet some of the consultative committee now say that the bill introduces new concepts in capital gains tax. I am sure that these will come out as we progress through the detail today.

Mr Chairman, most of what I have said repeats concerns that have been raised at previous hearings on this project. I at least should get credit for consistency and perseverance, and so should the consultative committee, which has been on this project now for 3½ years. All the project team have shown great dedication to the task. Their task has been complicated by many out there in the wide world wanting changes which are outside the team's terms of reference—but then that seems to be the nature of the beast.

We as the consultative committee are very pleased that Simon Gaylard will be supported by the recent appointment of the new private sector members in Professor Deutsch, Tom Magney and John Morgan. That is all I have to say, Mr Chairman.

CHAIR—Mr Nolan, would you like to respond to some of that?

Mr Nolan—Yes. Thanks very much, Mr Chairman. Stan has gone through quite a litany of issues, so I am unlikely to be able to pick up all of them but perhaps over the course of the day and into tomorrow we might be able to do more of that. This bill was put into the parliament towards the end of the last sittings. It is said that that was in haste—indecent haste, even. The impression conveyed by those remarks would be that the bill is a faulty product, a second-rate product, because of that. The other implication is that consultation has been at best less than adequate.

I would have to say that on the content of this bill the extent of consultation has been not just extensive but really the most extensive that has ever been given to tax legislation, in my knowledge. The haste, however, was directed to the fact that the legislation came in at the end of last year when there had been an expectation that it might be a little later, into the new year, and that there would have been more time to respond to the exposure draft on the second half of the capital gains tax rewrite.

The reason for bringing forward the introduction of the bill was very largely because of the fact that the parliament will not be sitting, because of the constitutional convention coming up shortly, until March to deal with legislation. The project team took very seriously the views of your committee, Mr Chairman, expressed to us on other occasions that it wanted adequate time to examine and deal with material that was put before it for review.

The consultation, however, has been going on for the best part of two years on some of the material in the bill. In the middle of last year around the country we ran seminars on CGT issues. There have been specialist groups whom we have been consulting with. Members of this committee and representatives of the other professional bodies have had very ready access to members of the project team. I think that John Burge in particular and a lot of his colleagues have been more open, more receptive, to comments and submissions than could really have fairly been expected of them.

The burden of the criticism, though, is that, whilst they have been open and listening, there has been no formal feedback in terms of a detailed response. To some extent that is true. It is not true that we have failed to respond to everybody who has written to us, but there is a major set of submissions from the joint bodies to which we have not yet provided a formal response. There are a lot of reasons for that.

The main one is that we spend a lot of time working through each and every one of the issues not only in the joint bodies' submissions but in the submissions of others to

try to absorb them and take them into account in completing the legislation. When we were doing that we were in dialogue with people right up to the date when the legislation was introduced, and we have continued to do that since that time.

The reality is that there has been almost an incessant number of meetings and discussions, over the telephone and face to face, with anybody who has an interest in the subject matter. They have been very fruitful. Many changes have been made to the legislation from what was put out as exposure drafts compared with what is now in the parliament.

We have, I think, a very good record of listening to people and taking their comments on board. Now that the legislation is in the parliament, we will ensure that there are fully reasoned, detailed responses provided to the bodies. Whilst we regret that we were not able to do that earlier, the main reason for that was that we wanted to actually take account of those comments and put our effort into improving the bill, rather than down tools from that more critical work in order to provide responses. But we will now complete the task.

I think the suggestions that come through from Stan's comments tend to blur the distinction between tax office attitudes, as they are represented to be, and a culture of treating people as tax cheats and so on. Whilst I do not for a moment accept that that is the case, I want to draw a distinction anyway between the work of the project team and anybody who might be seen to have that sort of view. I do not think that it has ever been suggested that the project team itself is less than fair and even-handed in its approach to the rewrite of the law.

Another major theme was that there are a lot of unintended changes likely; that there will be errors made, that we need a process for dealing with those and that there is less than full confidence in those processes. I think we have shown a good deal of willingness to correct legislation that has already come through this committee. Where there have been errors pointed out, those errors have been corrected. We accept that there is a responsibility to do that. In taking on a task of this size, nobody can be error free. It is obvious that when you produce something like 900 pages of legislation, which is what we have done so far, there will be some mistakes. But I think we have already shown—through legislation that went through the parliament last year, making a great deal of changes and corrections—that we have taken very seriously the responsibility for picking up any errors that are pointed out to us and getting them corrected. So I do not know why there is this lack of confidence in that process.

If you go to the base of the criticisms that have come in, however, a lot of them are about anxiety about the professional bodies' and practitioners' ability to cope with the rewrite output, and also the gathering clouds of tax reform. They are wondering how they are going to cope with dealing with putting in submissions on tax reform issues, and at the same time they are coping with their daily work and assisting with the rewrite process as

well. It is a costly process; it does take up the valuable time of professional people. We can understand that anxiety, but when you talk to practitioners around the country, to tax teachers who are dealing with tax law in universities and other institutions, there is a great deal of recognition that what we have produced is vastly better than the existing law, that it is welcome, that the structure is good and that the language and presentation are good. People are in fact using the new legislation, even in draft or bill form, as a way of opening up the mysteries of the existing law, which they have found quite impenetrable. They are saying, 'It is a good product.'

I think you have got to recognise that, whilst there are always anxieties and uncertainties—we live in a world where there is not sufficient trust, and that is regrettable—what we are trying to do in the project team is to demystify the law to make it easier for people to understand and read. I think we are succeeding very well in doing that. If we make errors we will correct them. That is probably enough on that subject.

As to small 'p' policy or larger policy issues, the charter of the project has been established right from the beginning. Essentially, as you articulated earlier, it is one of rewriting the law, restructuring it and presenting it better so that people can understand it and that compliance costs will be reduced. Those things are happening.

We are also making a number of small policy changes along the way—things that help in that direction of clarifying and reducing compliance costs—but there is also a process now agreed by the Assistant Treasurer, Senator Kemp, with the Treasurer's approval, whereby he will encourage the consultative committee to bring forward to him a range of small 'p' policy issues, and he will work through those with the committee.

Senator WATSON—Do you know what bill it is going to operate from? Can you elaborate on that arrangement?

Mr Nolan—At the last meeting of the consultative committee and project team with Senator Kemp present, I think Senator Kemp suggested that there would be opportunities for those things to be brought forward and considered. I do not think he put a timetable on it so much as that he would meet with the committee and receive its submissions. I think he was expecting that perhaps the first of those might be available coming out of the next meeting of the committee which is actually to be held next week. Whether that will emerge or not I am not sure yet.

Mr GRIFFIN—So it will be a statement of intent rather than any sort of program for action?

Mr Nolan—Yes, but what he is saying is, 'Bring forward, on some reasonable, prioritised basis, the issues that you would like me to look at and I will take them forward.'

Mr GRIFFIN—Brian, you would agree there is a need to flesh that out, given there are concerns about trust on these sorts of issues?

Senator WATSON—Is it a formal mechanism or process?

Mr Nolan—At this point I think there is a certain amount of onus on the committee to produce its ideas and take them to the minister. He has undertaken to deal with them promptly. Some of them may need to be fed into the budget processes, especially if there are any revenue considerations.

Mr GRIFFIN—I still reiterate that I think there is a need for a definitive process to be laid out. I refer you back to recommendations that we made in earlier reports on these issues. They related to some of the things that Stan was mentioning on the question of processes for resolution of issues of policy and other technical issues where there have been responses from government such as,'Yes, that's a good idea and we'll call you back. It's going to happen but we're not going to spell it out at this stage.' So I think there is a need for spelling out some of this stuff, don't you think?

Mr Nolan—I think the Assistant Treasurer actually has written to the chairman of the consultative committee and outlined the process to some extent. Is that the case, Stan?

Mr Droder—No, I am not sure that that is right; I cannot remember. I think we are all quite comfortable that the senator has in fact opened the door for us and it is reasonable to say that we are not going to let this process die, so we will keep pushing hard.

Mr GRIFFIN—Sure, I just do not want to be back here in six months time having the same sort of discussion which we seem to have every time.

Mr Nolan—I appreciate that.

Mr GRIFFIN—I am getting sick of those discussions.

Mr Nolan—The fact is that there is a process that has moved on now.

Mr GRIFFIN—Yes, there is some movement, Brian. I accept that. I have been looking through some of the earlier reports we have done on this and I keep seeing recurring themes. I keep seeing the situation, 'I'll call you next week,' 'It's all okay,' and 'I'll respect you in the morning,' coming out of this a bit, and that is what is worrying me. I am pleased to hear that Senator Kemp has given those undertakings, but I am also keen—and I suspect members of this consultative committee would be as well—to see that hammered out a bit more. So if there is a meeting next week, hopefully more detail will come forward about the question of processing this. I think it is needed.

Senator WATSON—Mr Nolan, does your team keep a register or two registers—one for small policy items arising from all the submissions that have come in and another one for the major policy issues? Although Stan has been asked to submit a list of policy issues, at the same time, with all the people you have been consulting with, you would undoubtedly have a very long list. We would like to see if you keep such a register because we want to keep abreast of this ourselves.

Mr Nolan—In all of the areas we have rewritten or are rewriting—and we propose to do it for future work as well—we have recorded in a compendious way all of the suggestions for policy change that are put to us.

Senator WATSON—Could you give us a copy of that register?

CHAIR—That would give us some idea of what we are talking about. You can leave the big policy issues aside because we are not concerned with them and, with respect, I think, neither are you. Could you give us, in your language, the small 'p' changes that have been suggested? How many of those, for instance, have there been on this bill? Are we talking tens, hundreds or thousands? With respect, I doubt very seriously that there would be one single person around this table who would one hundred per cent agree with anything that is in the bill. Everyone is going to have a different viewpoint and everyone is going to see a different problem with a different section of the legislation, and nobody likes to pay tax anyway. But in terms of reasonable suggestions for small changes that would simplify the policy and make it easier for everybody to understand, how many are we talking about?

Mr Nolan—I think on this bill alone, it would range into hundreds. Several hundred suggestions would have come forward. Of those, we may have picked up something in the order of 50. Maybe a quarter of the suggestions that have come forward have been picked up in some way. They are minor matters but they do go to improving the law. Not all of the several hundred are small 'p'. Some of them are larger than that and would have major revenue implications. I think we would have picked up in the order of 50 or more quite minor issues as we have gone through with the program.

CHAIR—Would most of those also be in the processing of tax office rulings—or associated with tax office rulings?

Mr Nolan—I was just trying to absorb the thrust of your question. There are at times opportunities for us to pick up and clarify the law by writing into it things that had been dealt with by rulings. Some of the changes that we have made do in fact reflect tax rulings, but that would not be the majority of the issues that I have just been talking about.

Senator WATSON—Two terms have been used that concern me—'a lack of return for investment in the process itself' and 'items going into a big black hole'. I think

our committee is at a fairly delicate stage in terms of this whole process because of the speed at which it is going through. Since some of the stakeholders have not been responded to, we may well be taking positions that could be at variance to our final outcome between these people because of the tight time frames that we are operating under.

Under the circumstances I see a partial solution to this. If the team could give the committee all the minor policy issues that have been raised, together with the response or action taken, and the larger items because I think that could also be useful to other groups such as Senator Gibson's team on tax reform in terms of the major issues.

What I am concerned about, though, is the nature of the response. I feel it is unfortunate in a sense that this committee is looking at legislation which is still in a sense very preparatory because the major players have not had a response to some of the major issues that they have raised. So we are going to be the melting pot for the resolution of those issues. I would have been far happier looking at a final result where there had been some sort of finality. True there may not have been agreement on some of these, but where there has not been any response whatsoever to some of the most significant players in a formal sense, then I see the position of our committee as being somewhat open to criticism in terms of an outcome that we may take because of the very tight frames in which the whole process is working.

I certainly would like to see, Mr Chairman—and I hope to get the committee's support for this—the policies issues broken down into small policy issues—some of which you may have taken up—and the larger policy issues.

CHAIR—Senator Watson, the last report No. 345 recommended a series of options, but it basically recommended that the government resource processes to review minor tax policy simplification and establish a joint standing committee on revenue. When the government responded, it said, 'A process is to be established to deal with the minor policy issues that arise directly from the simplification process.' I think Mr Nolan just said that that is now in process. Whether it is a formal process or not, it seems to be happening. The government went on to say that 'consideration currently being given by the government to tax reform issues provides an opportunity for all views and proposals on tax reform to be taken into account'.

Senator WATSON—But we have to have a role in that ourselves and that role I think is best expressed in the request for this information.

Mr GRIFFIN—Following on from that, my concern is that that was from the earlier report No. 345 as against report No. 348, which was the last one, so we are talking about a report that went down 18 months ago. That is why I am a bit concerned about the question of timing on some of this stuff.

I concede that there have been some developments, but I am concerned about the degree and the pace of those developments and issues. This is not a criticism of TLIP as such; it is a criticism of government responding. I also concede that this is a process which commenced under a government that I was part of, so my side is not without blame on this either.

But time is marching on. One of the things concerning me is that, each time we have one of these hearings, we tend to get these recurrent themes and a recurrent concern about the question of trust, if you like—I feel like we are almost talking about Northern Ireland in some respects. Those issues just are not going away, and that worries me.

The other thing that worries me a bit more about this particular hearing today is the message I got from Stan earlier. Correct me if I am wrong on this message, but the message I got was you were not in a situation where you feel confident you can respond on the detail of this legislation; is that correct?

Mr Droder—I think that is a fair comment.

Mr GRIFFIN—I think we can argue about the generalities quite a bit, but I do not know that we are going to go very far with that on this occasion. We need to get down to the detail of the bill. The worry I have then is that, if you guys are not in a position to actually say we have got a problem with X section or whatever, then we could well be in a situation where we do not properly consider the bill in any detail on this occasion. If you feel that is the case, then I worry about just how much we can get done over the next couple of days. That is the first point. The second point is: if that is the case, when do you think you will be in a situation where you will be able to respond with some certainty about the detail of the bill?

Mr Gaylard—Could I add some things to the debate and maybe help get to that answer, if not get there completely. Stan mentioned a big black hole and the delays in responding. It is something that I wish could be different. When you have all the resources directed towards completing the rewrite and you are also getting a great range of queries coming in, you have to ask, 'Which will we tackle first? Do we try to get the job done so that at least it is out in the market place, and then deal with the queries?' Except for some that came very late last week, there was an answer to all the queries and that will be part of evidence at these hearings. Now there has been a response, albeit quite late.

Just going back a little, I think the professions are under pressure. Personally, I think they have done a wonderful job in producing the information that they have produced, the queries they have raised. I know it is in the context of a very tight time frame. So I think the answers have been given—and that can be debated. The issues of small 'p' and large 'P' are always difficult, and government quite clearly wants a say in that.

What is small to someone may well be of a different size to someone else if there is revenue involved. There could be differences of view between the tax community and the tax office about what the revenue is, even on a particular issue. In going through the submissions the other day I saw that an enormous number of the points that have been made in these submissions have been taken up. I hope John Burge, who has had the running of this project, has some percentage figures that he may be able to share later, but a very significant number of the issues have so far been taken up.

That is not to say that the thing is 100 per cent right at the moment—it is not. Work is still going on to get things right—

Mr GRIFFIN—Simon, I hear what you are saying and I am not disagreeing with you with respect to that. I am not saying that there has not been a whole lot of work done on this. I am not being critical of anyone. My principal concern at the moment is the question of how far we can pursue this matter today. In a situation where we are operating, as we have in the past, with this round table arrangement where essentially it is TLIP in effect defending the detail of its legislative proposals from comment from the private sector and from the consultative committee, that is my main worry today.

Mr Gaylard—It seems to me that this hearing, as opposed to some of the earlier ones, should go to producing the best possible product. Some of the earlier hearings were about issues of whether the project should even go forward and issues of that nature. Everyone now has a vested interest in getting the bill as good as it possibly can be.

Mr GRIFFIN—There is a fair bit of dotting the i's and crossing the t's. I want to make sure that we are at the stage where we can dot i's and cross t's.

Mr Gaylard—I think we may have to go away and do some further work with some of the queries that are raised here, but certainly some of the issues can be tabled and discussed and at least a process worked out on how we address those—these are the small 'p' type issues, the quite small issues. If they are wrong they may have much more serious overtones, admittedly, but these things can at least be thrashed out here, I would have thought.

Mr GRIFFIN—Can I get a comment from Stan on the original question I asked.

Mr Droder—I will try to. The first point that ought to be made is that this group of people on my right-hand side does not have a great deal of resources. While they are all involved in tax, obviously they have to earn their own living at the same time. Senator Kemp made a positive move to us last year in terms of talking to Michael Carmody and offering the resources of the tax council network. I spent some time yesterday with a member of that tax council network talking about the two minor areas that I am supposed to cover.

However, again the speed of the introduction of this bill has not enabled us to talk a lot with the tax council network. Some people have been able to and some have not—because they have been on leave, as well as everything else. But I think everybody here can make some comments on the bill and has done some work on it over the last two months.

One of the disturbing things about this is that the final bill is still not there. The fact is that the team has done what it has had to do to hit the timetable, and yet we are still fiddling around with the bill. To say that it is fairly well accepted, I do not know. I have not gone through this, but the society and the Taxation Institute have produced 42 pages of commentary on it. My understanding is that that was put to bed only about a week ago, so any reaction to that cannot possibly be in the bill you are considering, and so that is a bit of a problem.

I thought Senator Watson's summary of the position we are in or of what I was trying to say today is that there needs to be a process in which the consultation is closed off. I think that is what he is saying. Everybody around has put in their submissions, but when do you see the final picture? When do you know that some of the points that you have made have been rejected? Is it too late to do something about that?

CHAIR—Mr Nolan, could you tell us what the resource implications would be if every submission were responded to by dot point?

Senator WATSON—Not every submission. I think in a sense what I was requiring was that every policy issue and every concern be divided into minor and major issues, because as a committee we have to make sure that not only the process is right but that the mechanism is right for consultation. Because consultation is an integral part of getting this tax law improvement correct. If we are not careful, our committee could be right in the middle of this and basically still be off the main agenda, because consultations are taking place outside our forum, which we expect. In a sense we would expect to be something of a control mechanism to ensure that there is an appropriate process and mechanism for response and, maybe, action or non-action, or the reasons for the non-action. Then we make our evaluation on that final outcome. But we have got to look at the global situation, in addition to the line-by-line analysis that we might be going through later on in the next two days.

Mr Nolan—Mr Chairman, your committee, through requests made to the project team by the secretariat, has in fact got responses on all the major submissions, indicating our views—the ones we have picked up, the ones we think worth picking up still and those that we disagree with. So there is already a great deal of material with the secretariat. I am sure the committee members themselves have not yet had the opportunity to deal with that.

The consultative committee has been provided with copies of the compendium

material on the areas that we have rewritten. That has been a process. Stan Droder has also acknowledged that the tax counsel network resources have been made available or offered. So a lot has been done. I really believe you are getting an impression that consultation has been at a low level, but it has not been. Quite honestly, we have been almost drowning in consultation. The fact that the bill was late going into the parliament, or exposure drafts were produced later than anticipated, was essentially because of the amount of time that people in the project team very conscientiously and earnestly put into dealing with people on their submissions.

Mr GRIFFIN—The problem we have got from our end is that essentially we have to sign off on this with a report and we are in a situation where I am a little worried that, although I think a lot of consultation has gone on, the question is the resolution of that consultation to a situation where we can say this is what is not agreed and this is what is agreed so we can actually define what are the issues of contention.

I am a little worried about how far we can go with that. We can go a fair way in the next couple of days to do that but I do not know that we can resolve that completely. Therefore I have got concerns about the question of how we as a committee are going to be able to sign off on a report given the time lines that we have been given and the legislative program. That is what is worrying me a little in those circumstances.

I am not wishing to be critical of TLIP or anybody else in respect of the process. I think that once again we have got a pretty bizarre and very tight timetable in which to consider this legislation; it is the third time it has happened. We have got to live with that but at the same time I do not want to be in a situation where I am pushed into signing off on something that I am not happy about. That does not mean that I need to be in the position where we agree with one side or the other about what is going on. My position is pretty clear on the question of the policy issues and that is that it is not your brief to do the policy issues; it is an issue for government to take up. We have recommended that government look at that and address it. There is some movement on that front.

I am pleased to see that but again it is not our issue. Our issue is about the question of trying to resolve technical matters and having consultation across the major players about seeing what can be resolved to make the bill a better bill and then report to government on that basis and that is about it. Some of the stuff we have talked about today is not really part of our brief, never was part of our brief and never will be part of our brief. At the same time what does concern me is whether we can resolve what is our brief if we are in a situation where the various parties are not happy that they are in a situation where they can actually properly consider what has been proposed and comment upon it, because if they are not we are going to miss things.

Ms Morton—The comments that have been made by Mr Griffin and Senator Watson are spot-on and ring true for most members of the consultative committee, particularly the point about this being the third year in a row that this has happened. I

believe that last year the chairman said, 'This tight time frame is never to happen again.' I do not blame the project team because originally this was not going to go into parliament until some time in March, which meant that there was still going to be another three or four months work done on it and circumstances have caused them to have to tighten the time frame.

There is no doubt that John Burge and his team have done a fantastic job in meeting with people and trying to hear what they have to say and to accommodate that where they can. There is no doubt that this is one of the most complex areas of our legislation and it deserves appropriate time and appropriate, thorough scrutiny after it is finished. The reality is that this bill is not finished.

You all know that this bill came out, and then on 9 January or so all that came out and still it is not finished and then there are all these submissions which we have all just received today. We have not even read what other people have thought about these issues. How can your committee sign off on something which is not finished? How can you report to parliament even if it is an ongoing process and you look at things later on? We have still got the experience of the last bill in regard to the recommendations that you put forward: although responded to in parliament, I do not believe they were appropriately responded to. So you are left exposed in trying to deal with something which is not in a completed state. I believe that no members of the consultative committee are in a position where they feel that they have come to terms with what is in here.

I work for a major corporation; we have just lodged our entire group's tax returns and I am supposed to have been able to comment on this. You are merely, in trying to comply with your corporate responsibilities and your obligations under the tax act, trying to do this as well, and the consultative committee has no resources.

Mr GRIFFIN—Tell us what we need.

Ms Morton—I would like to see a completed bill, one which is consolidated, not bits and pieces any more. As well, all the bits still missing out of it that are not even in this bill I understand. So on that basis once that is completed you need to allow people a good solid couple of months to read through it and really consolidate it.

There is no way that this can become law on 1 July this year because, if that is the case, there are 31 December companies, there are January companies in lieu of the succeeding June, which are already, today, operating under a piece of legislation which is not complete, which is not finalised, and they have no idea what they should be doing.

Mr GRIFFIN—Can I get a comment from Brian about that?

CHAIR—Just before that, I want to respond to say, on behalf of the committee, that we are not going to respond today to your comments on what the committee should

do. We will take your comments on board, we will deliberate privately and we will make our own decisions about those matters, but we are not about to make any decisions or any statements today. I want to make sure you understand that clearly.

Mr GRIFFIN—I think the time line issue is something that is absolutely crucial to what we do. It is why I want to get a handle on it now. I am not saying—

CHAIR—With respect, the committee is not going to debate it during this round table, either.

Mr Nolan—I make this observation: we are rewriting the totality of the income tax law. What we have on the table here in this bill is only a fraction of it, really. The entire rewrite stage to this point, including the two bills that have already been enacted, is substantially short of 50 per cent of the total job which we have been asked to complete initially within three years and now within five years. We believe that is possible, but it is a tight program and it has to keep progressing. There is a real need to get the job completed so that people can move to a stage where they have an entire new act, not an incomplete one.

What we are hearing is that your committee members, the consultative committee and individuals who want to look at the legislation are having trouble being sure that word by word, line by line it is all 100 per cent correct. I suggest to you that you will never be able to get to that position, the consultative committee will never be able to get to that position and, quite honestly, neither will we, despite the resources and effort that we put into it. There are always going to be possibilities of error, but it is a vast undertaking. You either go into a blue funk about that and say, 'Oh, we might be passing something that's not entirely correct yet,' or you accept that there may be some errors but that the project is worth doing; that the end result is a much better product.

Mr GRIFFIN—You could argue about degree, though. It is a question of how close we are to that position. No-one is expecting perfection.

Mr Nolan—We have actually responded—and you have the material—to virtually all the submissions that you have been given. The consultative committee members have not had the opportunity to absorb this material yet, but largely it comprises submissions that they have seen in one form or another. Once they come to look at it they will see that it is not so new at all. They are issues that they have seen before and many of them have been debated and discussed.

Senator GIBSON—Chairman, firstly, I suggest that the issue of our deliberations about the timing of this process ought to be delayed until we have finished today's and tomorrow's discussions and that we ought to then take on board looking at—

CHAIR—That is what I thought I said.

Senator GIBSON—Yes, I know. I just want to reinforce that so we have a clear understanding.

Mr GRIFFIN—I do not mind us postponing it for now, but we need to consider it and we need some advice from these people about how we consider it.

Senator GIBSON—Secondly, I reinforce Senator Watson's request: so that we have a better feel for the totality of what could be done, even though it is not our brief currently, some sort of synopsis paper from the TLIP team about the small 'p' and large 'P' policy issues—

Senator WATSON—Separated.

Senator GIBSON—Preferably separated, would be useful for us as a committee.

Mr Nolan—Mr Chairman, we will do our best to provide that material in the most effective way for you to digest it but, largely, it does not go to the accuracy or otherwise of this bill. It goes to whether other policy issues should be taken up.

CHAIR—We accept that. Could I ask a generic question? I am new to this process—let us accept that—and I have not read the bill, despite the fact that I am told I should have. If I understand it, we should pass it. I assure you that the House probably will, but in the Senate—who knows. The question is: does there need to be a more formal statement of the role or differentiation between TLIP and the committee of what you expect of each other?

Mr Bryant—Mr Chairman, could I make a quick comment on that? I think it goes right to the heart of what Mr Griffin was saying before. Our frustration is not with even the small 'p' or the big 'P' issues as much as with the very issues around which we do have disputation. We are not looking for sign off on grammar. I can articulate a number of issues where we have provided input. There might have been some discussion, but there has been criticism of the consultative process. Brian has defended it but the reality is that there are a number of issues where there has not been agreement or understanding reached and there has not been time. We have tabled a lot of them in submissions and the like, and we look to this committee because it is the only source that we have. There is nothing else in the process that enables us as external representatives through this consultative committee to go with those issues. The decisions very frequently, often on technical issues, are made within TLIP. We do not think that that is good enough.

CHAIR—That still does not answer my question. My question is: does there need to be a more formal statement of what each of the two of you expect of each other and how the process works?

Mr Gaylard—Mr Chairman, if we have not been able to work that out in 3½

years, I am not sure what a statement now would do.

CHAIR—How long are you going to keep going with the same sorts of arguments?

Mr Gaylard—To take Bob's exact point, the technical response at the end of the day does have to rest with the Tax Law Improvement Project team. It may well be disagreed with by everyone, but at the end of the day the project director must have the call on the issues. Hopefully, with private sector input, with consultative committee input, with public input, the right answer will be given. There is a great willingness on the part of the tax office to take up the issues. I challenged Bob on the issues that have not been taken up. They are, in the great majority, issues that are felt to be beyond the scope of the project. Certainly, argument can take place on that, but if you read the responses you will see that a great number of those issues have been dealt with. I think in all cases where things have not been picked up the answer is extremely fair.

The point about substituted accounting periods, which we have debated time and time again, is that it is just sensationalism of the issue. Everyone that is advising, certainly in the substituted accounting period area, knows what the old capital gains tax law says and everyone knows what is in the new law. There may be some differences—they may be unintended at the moment and they will be fixed—but it is just sensationalising an issue to say that there is a problem. The new law, as it is written, is very good material. It makes a lot of sense.

I will tell you a story, Mr Chairman, which would be very relevant to you. In the tax office in Sydney the other day a technical question was asked on the new law and a prize was given—quite a substantial prize—for the person who got it right. The person who got it right was one of the secretaries in the tax office. The comment was made that it was absolutely amazing that the new law was so easy to understand. Mr Chairman, I think that if you actually do sit down and read it, you will probably find it quite revealing. We have a very good product that is nearly there. There are certain issues to sign off on and I think we should get on with it.

CHAIR—We have listened to both sides. There is one other issue in general that we need to cover. We are going to have to move on or we are not going to get to the detail of this bill. I think all of you want to do that. There are five of you here. There is one issue that we have not really dealt with that we wanted to deal with. Mr Droder, could you comment on the outcomes of the increase in private sector representation on TLIP? Are you happy with that?

Mr Droder—We are very pleased with the selection of the three extra people on it, but they have not had much time on the project. They have working on it for about two or three months. We are certainly very hopeful that they will properly represent the private sector.

CHAIR—My understanding is that the last time what you did recommend and what we recommended has happened.

Mr Droder—Yes. We are all very happy about that. We are pretty happy with the people who have been selected. Can I make one point? We have talked about this consultation process and I will repeat what Joycelyn said. John Burge has done an enormous job on the situation. The accounting bodies—and I am one of those, but I was not involved in writing their submission—have put in these 42 pages. They are going to come to you tomorrow and burst off about what is in there, what is wrong with the new bill and everything else. They are coming in there without having any response to this.

So you are going to go through the same sort of crap as what you are worrying about here today. They will say that there is something wrong with some section or the conversion tables in the bill or whatever, and Brian will either say that we have fixed it up or that we have not fixed it up. It just needs to be closed off in some sort of fashion.

CHAIR—Can I say to you that they also put out a press release asserting that the JCPA had allowed 'draconian anti-trust bills to proceed through the parliament', which is a lot of rubbish.

Mr Droder—Unfortunately, I did not have control of that press release and I am really unhappy about it.

CHAIR—There is no member of this committee here today who is very happy about that press release.

Mr Droder—Give them a go tomorrow. They will all be there.

CHAIR—You can count on it. Can we close this section off now?

Senator WATSON—I have one last question. How important is the start-up date of 1 July for this legislation? We have heard Joycelyn Morton's point of view, which is quite relevant. I would like a response.

Mr Parker—Can I answer that from the small practitioner's point of view? With the exception of the last hearing, I have been at the other hearings. Up to date the record will state that I have comprehensively and passionately supported progressive implementation of the legislation and I still do. However, I feel this bill is different. There are more complex issues. There have been more changes in the CGT than in the two preceding acts.

Indeed, the community at large owes John Burge a debt of gratitude because without his dedication we would not have the product we have now. There are more than 50 changes. The consultation process was extensive over 18 months to two years. The

practitioners and clients will have three or four months to come to grips with what has taken the technical team two years to put together.

It is not good enough to say, 'We know the law.' CGT is a specialist area. Where would public confidence be from 1 July 1998 in the accountant advising the client? Put yourself in either the client's position or the accountant's. Will you be ready to advise prospectively or receive advice prospectively in relation to a CGT transaction which occurs on or after 1 July? I have some difficulty.

Then what about the practitioner? The practitioner falls into two groups. The small practitioner and the large practices. The large ones have their technical teams and they have and will continue to devote substantial resources to understanding and ensuring that the product is used properly within that practice. But the sole and small practitioners are struggling. They have adapted to and accepted the first package of legislation without a lot of public comment. Certainly, there were CGT seminars in 1997, but that was only a draft and in Brian's own words, there have been a number of changes. Sure, there has been further enhancement and improvement, but there are changes. Those practitioners who went to the seminars in July and August cannot just say, 'Oh, we know it.' The rewritten act is different in its layout and format, even in the ordering of the CGT events. There is a start-up process for all practitioners. I try to position myself by asking: if I were not on this consultative committee, how would I be ready for 1 July? My answer is that I could not possibly be ready.

At the end of the day, the public need confidence in this product. The government needs to know that it has community support. If and when the issues are resolved and it is passed, then it needs to be sold to the public at large, the practitioners and the clients. At the end of the day, when the product is used in the community, it will be a tremendous product, but it is not ready yet. I do not think there is any way possible that you should implement it on 1 July 1998.

Mr GRIFFIN—Can we get a quick TLIP response on that?

Mr Nolan—I understand Tony's point of view that practitioners will have difficulty being able to put their hands on their hearts and say, 'We fully understand this new legislation.' I will ask this rhetorical question: would they be able to put their hands on their hearts and say that they understand the existing legislation? My suggestion is that they will have a much better chance of saying that they understand the new legislation than saying that they honestly understand the existing law, which in very many respects is quite impenetrable. Much of the darkness of that legislation is now being enlightened and made clear. I can understand people saying, 'We are not sure whether we will be across it all by 1 July,' but they will not be in a worse position than they are with the existing legislation, which is so difficult for them to follow and get answers from.

We do have a progressive, rolling program. The first tranches of the legislation are

now in progress. I suggest to you that, if you give those everyday suburban practitioners another year to get used to that legislation, they will not start looking at it tomorrow, they will not start looking at it on 1 July, they will start looking at it on 30 June next year. That is the nature of the beast. People are swept up in their day-to-day work, and they will keep putting off until tomorrow anything that gets in the way of their doing today's work.

That is one of the advantages of progressive implementation and things coming on stream: people do have to face up to it and get used to it. There is no painless way of doing that, but it has to be done. What I am saying is that once they start the process of looking at this legislation they will at least have a reasonable chance of finding the answers that they need, which they cannot do under the present law.

CHAIR—The committee has heard Mr Parker's and Mr Nolan's opposing views on this issue. We will consider both sides and decide what we will or will not do. We do not make decisions about when legislation is tabled or when it comes into effect. All we can do is make recommendations in any case. But we will consider those matters further at our private meeting. Thank you for the opening session.

Short adjournment

CHAIR—We will recommence the hearing. We are now going to consider the bill in detail. Prior to that, Senator Watson had a request.

Senator WATSON—Mr Chairman, I would like to add my congratulations to the new members of the team who have joined Brian Nolan's team. I think it is a significant development. It is one that the committee pressed for for quite some time. I am pleased not only to see the positions filled but also with the quality of those people who have filled them. How do you find your positions? Are you getting involved in the detail or haven't you had time to get across all the major issues?

Prof. Deutsch—I will respond to that first if I could. I have been involved with the other new private sector representatives since August last year. Essentially, I have been involved on the international rewrite, which was started almost immediately and has been continuing since. I have had very little to do with any of the other processes, so all this is a bit of a familiarisation process for me. Today has certainly been—how shall I put it?—illuminating so far, although in some respects confusing.

I was just saying to Gavin Back a moment ago that I am not entirely sure what our role is in some respects as private sector representatives in a process such as the one we are going through today, but that is just a difficulty I guess I am going to have to sort out for myself. In response to your question, Senator, I am very heavily involved in the detail of the international rewrite which is essentially my area of expertise.

Senator WATSON—Could we go through each of the members, Mr Chairman. I

asked this question because it was my understanding that the new members would be fully involved in all the intricacies of the rewrite, and I can understand your particular expertise. What about Ms Freshwater?

Ms Freshwater—I am a tax office representative. I am not a private sector—

Senator WATSON—No, but you are just an adviser?

Ms Freshwater—Yes.

Senator WATSON—Mr Morgan, I welcome you to the team, from the perspective of the committee. It has been a recommendation for some time that the team be augmented by an increased number of private sector representatives. Briefly, what is your involvement to date?

Mr Morgan—Continuing with the same theme, with Simon I am meant to be one of the general representatives budgeted for two days a week and therefore have responsibility across the board in a way. That does not stop us being involved in particular projects. Like Bob Deutsch, we have been feeling our way in some respects about working out what our role is. Speaking personally, that has involved attending a good many of the seminal meetings on the new projects that are being undertaken, in particular the superannuation international tax, collection and recovery, some of the leadership group meetings and the like, together with consultative committee meetings and some of the planning sessions for the remainder of the project.

Senator WATSON—So will they be brought onto the team? You are only working in a fairly specialised area. Is that right?

Mr Morgan—No; in fact, the reverse at the minute in that I have broad-ranged across most projects. I have started to get involved in a specific project, which is reviewing the imputation part of the rewrite. But a large part of what I did was to see a need for a particular kind of ruling which I thought would have smoothed the introduction of the new law. Really it is an extension of the TR 97/16 ruling. So I put a bit of time into putting up that proposal and seeing whether it could fly or not, and then I suppose some involvement with this committee as well.

Mr Magney—Like Bob Deutsch, I was appointed for the equivalent of one day a week on the committee, although some weeks one spends four or five days and other times maybe less. I have become heavily involved at a very detailed level in the rewrite of company distributions, which is quite a big area. I have been working there virtually from the beginning with the team in Brisbane. There are three members of the briefing team in Brisbane that I work with regularly and I have been to Brisbane on a number of occasions for the day to have working conferences in which we have actually been through in great depth a lot of the technical matters which have to be resolved. The other area in which I

have spent a lot of time is in capital gains tax. Indeed, earlier in January I went through the bill in some depth and prepared some recommendations.

So I suppose my time on TLIP to date, which is about six months, has very much been hands-on involved in two large and complex areas which I got into because they are my particular areas of expertise. I attend the consultative committee meetings, of course, and get only marginally involved in the sorts of matters that we were discussing this morning. So, like Bob, I am still not completely absorbed in the politics, for want of a better word, but I feel that I can make my best contribution by getting into areas where I have some experience and giving aid in those areas to the people who are preparing the brief for Parliamentary Counsel.

Mr Back—To clarify a point for Senator Watson, in pursuance of the committee's recommendation last time around to increase the private sector representation, we thought it would be of great assistance if in fact we could bring in some specialist private sector experience to assist in some areas that we were rewriting. I think you had recommended that we should go up to three private sector representatives. We thought that we should go to four but that we would distinguish two who would be generalist and would have roving commissions across any aspect of our work and who would work for between two and three days a week, as an average of their input. But, in relation to the two specialists who we would appoint on the basis of their expertise in particular areas, the budget and the nature of their contribution, because of their other conflicting priorities, we thought about a day a week was what they could actually contribute.

You made the point about their not being involved in all aspects of the work. Professor Deutsch and Mr Magney are not expected to become involved in all aspects of the work. They are not prohibited from taking out an involvement in anything, but they are encouraged to take an active role in their areas of expertise. For example, Professor Deutsch is a well-known international expert and he is providing quite crucial assistance to our people in rewriting the international areas.

Senator WATSON—I will just raise another question. This is an integral part of the consultation process and how effectively it is working and I think we as a committee have to ensure that we are satisfied with that. Obviously it takes a lot of time. Does everybody on the consultative committee get paid?

Mr Droder—I was asked that question by Joycelyn about six months ago and I said that I got paid 10 times as much as she did. It stopped her for a while. We get paid zero. We get paid by employers.

Senator WATSON—For example, we have Mr Bryant, who obviously represents an industry group, and there are others. I may be wrong in naming Mr Parker, who comes from the private sector and runs his own business, but do you get paid, Mr Parker? Obviously not if the others do not.

Mr Parker—This is a sport. I get paid by rushes of adrenaline.

Senator WATSON—Quite seriously, though, it raises a question of equity in terms of an expectation by the government and by the parliament to put in a lot of effort because the outcomes are important. The amount of effort that people are able to put in obviously has to be measured by the impact it might have on their other business. This is an issue that we may need to consider in some way, Mr Chairman.

Mr GRIFFIN—Can I suggest that some of these issues are ones that we could consider in the final round-table session tomorrow. I am worried about the time.

CHAIR—I am absolutely worried about time. We are now an hour behind time. I am sure you have detailed issues you want to discuss in some depth. With respect, I think we will start now to consider the bill. We will start with division 100.

Prof. Krever—Mr Chairman, I might start with that. I will start with two preliminary comments. The first is that we have listed all these divisions and sections all the way down. What has happened is that the consultative committee and the private sector representatives have worked together looking through technically what issues should be addressed in the bill.

There are two comments that are worth noting. One is that we have divided responsibilities by divisions—the way we have listed them in the program here. We have discovered that it is not always possible to look at divisions in isolation because each division contains a measure that draws on provisions in other divisions. While we are discussing measures, we are quite likely to jump around the program a little bit. To make sense of some sections we have to talk about other sections elsewhere.

The second point that I think is very important to note is that this morning we have been talking about the distinction between pure technical improvements—fixing the act—and small 'p' policy issues and larger 'P' policy issues. In practice, we have found it is very difficult to make those distinctions. To cite an example, very often provisions technically do not work but they also did not work in the old act. The reason they did not work was by inadvertence or mistake or whatever, something was left out of the old version, and because this version reproduces the flaw it appears in this one too. But to fix it, technically, it could be argued, involves a small 'p' policy change—that is, if words were missing from the old act that inadvertently omitted some people or included some people who should not have been there, the same is going to happen with this one. Our technical recommendations, it will be argued by some, could be across that threshold to small 'p' policy issues.

Mr GRIFFIN—You talk about the issue of practice. What was the practice?

Prof. Krever—For a lot of these issues, practice varied on a case on case basis

depending on who the auditor was and who the taxpayer was. There are no rulings on most of the issues we are going to look at and it was simply a matter of ad hoc decision making on the run. But we recognise that changing the legislation to address these problems does involve adding or deleting something from the law that was not there in the old one.

So on the first couple of divisions that I and Todd Magney looked at—which takes us almost down to division 104 perhaps—I think we came up with about eight issues. Perhaps it would be appropriate for Tom to start since he was the one who first reviewed the whole legislation.

Mr Magney—I went through with Rick the capital gains tax events and a number of suggested problems arose.

CHAIR—I am sorry, I do not want to interrupt, but we did set the schedule so that that was an issue we were going to discuss this afternoon in the area of possible contention. So perhaps we can go through those areas where there is possibly broad agreement and determine whether there are any issues that need to be resolved in those areas and leave the ones that are likely to be contentious. In other words, let us get rid of the bulk, let us get rid of all the magazines, and get down to the real correspondence. Is that all right?

Mr Magney—Yes. Most of these deal with 104, so it might be better, if they are to be dealt with, to deal with them later, although there are some that go beyond that. It might be a good idea if we could get these very short submissions copied. It would make it much easier to discuss them at a later date.

CHAIR—We can take care of that. That is not a problem. Let us go back then. We will do division 104 in detail later. We are trying to get rid of the bulk. Does that make sense?

Mr GRIFFIN—It must make sense.

CHAIR—Thank you. I will try again—division 100; 102; 103; 106.

Mr GRIFFIN—It is proposed that 104, 118, 138, 140 and 373, which are all matters that have been flagged as having a number of amendments and possible controversy, be considered after lunch—for those who have not read their agendas.

CHAIR—Or before lunch if we get through this lot. Division 106; 108; 109; 110.

Prof. Krever—I have a comment on division 110, if we are discussing that now. Division 110 reproduces a formula that is used in the 1936 legislation defining what the cost base is of an asset, and it is defined separately for the purpose of measuring gains

and for measuring losses. When the 1936 act was drafted, by inadvertence a slightly different formula was used for measuring gains and losses. For measuring the cost base of an asset for losses, words were inserted so that you could not double count the cost. That is, if you have deducted as an ongoing expense the cost of acquiring an asset, you also count the gain towards the cost base of the asset when figuring out your loss, and by inadvertence those words were left out of the cost base for calculating gains.

So it is possible to double count that, as you can take a deduction for the cost of acquiring an asset in some circumstances—and there is a lot of case law on when you can do that—and you can count it again when calculating your gain. Quite clearly it does involve a policy change since it was a defect in the previous version of the law, but it was suggested that the words 'cost base for losses' be added to the words 'cost base for gains', namely, that if you have already deducted the cost of an asset it does not count towards your cost base.

Mr Burge—Perhaps I could reply to the points that Professor Krever has made. The government has given attention to the issue of standardising the approach for reduced cost base, which is used for calculating capital losses, and cost base, which is used for calculating capital gains. It is true that in the 1936 act deductible expenditure could not also be taken into account when calculating a capital loss but in many circumstances could be taken into account when calculating a capital gain.

In last year's budget the government foreshadowed measures to deal with that situation. Legislation is now before the parliament to ensure that deductible expenditure cannot also be taken into account for cost base purposes in calculating a capital gain. However, it did involve a change to the law. The government decided, as a policy decision, that those new rules, subject to particular refinements, should apply to assets acquired after budget day. So our legislation will be reflecting that change, but the government has dealt with that issue at the policy level.

CHAIR—Would that occasion an amendment to this bill?

Mr Burge—Yes. In the material that the project team has provided to the secretariat and is provided in the green volumes we have indicated where catch-up work needs to be done to bring the bill into line with bills that are before the parliament or in some cases very recently enacted, and that includes these measures. So there will be some minor changes to the bill to reflect that.

Mr GRIFFIN—Does that take into account the question that Professor Krever raised?

Mr Burge—Yes, it does.

CHAIR—Division 112; 114; 116; 121; 122.

Mrs Gibson—I have some concerns on division 122. I have not had time to deal in full detail with these provisions yet: this is more of a querying remark. Running through the provisions of 122, there is a concept that, if you roll over assets either from an individual to an entity or as part of net assets of a business to an entity, that asset, once rolled over, cannot be trading stock to the entity acquiring it. I am just interested as to why that distinction has been drawn.

Mr Burge—In this context where you get a transfer of asset from one entity to another rollover relief basically means that you get the same treatment for the transferee entity. This particular rollover is concerned with incorporating a business. For the very first time the tax law improvement project has specific rules dealing with the incorporation of a whole business rather than just on an asset by asset basis.

Because you are trying to put the transferee, the person to whom the asset is transferred—in this case the company—in the same position as the transferor, it cannot be trading stock because that would mean that the capital gain would drop out of the system. So, rather than having a deferral of the tax, which is what rollovers are all about, the gain would drop out of the system because trading stock has an exemption relating to it. It is important to emphasise that we are reflecting the existing law in this area and the policy is appropriate.

Mrs Gibson—Under the current law, trading stock is excluded from the capital gains tax provisions. So, if you have trading stock and you are transferring it, under rollover it is simply not appropriate. If I as an individual transfer assets to a corporation in return for shares in that company and I use the rollover mechanism to do that, if I have a block of land, let us say, which is one of those assets which is not trading stock in my hands and I then roll it to the company, it becomes trading stock in the hand of the company.

Mr Burge—The same mischief would apply and that is, by allowing a rollover in that circumstance, what would have been a capital gain on the land is converted into tax-free treatment as trading stock. It is just not consistent with the general approach of rollovers of allowing a deferral of capital gains tax, not allowing its elimination.

Mrs Gibson—What if that land has been owned by me prior to CGT taking place? There would be no avoidance of tax.

Mr Burge—One of the characteristics is that you have the same treatment. The basic principle in relation to a pre-CGT asset—and by that I mean an asset acquired before 20 September 1985 and therefore generally outside the CGT system—where you get a rollover of it, the transferee is also treated as having acquired the asset before 20 September 1985. That treatment is provided for, and that is the appropriate treatment. It is not appropriate to convert one type of asset into another type of asset where you have a different CGT treatment for that asset.

Mrs Gibson—I display that as an ongoing concern. I will not hammer it to death here. I am also interested in section 122-55 where you have assets which are all pre-CGT assets. If you roll all of those pre-CGT assets into a company, again in return for shares, and one of those assets happens to be a precluded asset—that is, an asset that is defined in 122-55(3) as including cars, trading stock and other things—you are unable to treat all of the shares you acquire as pre-CGT shares. I am curious as to what the problem is with precluded assets. This is a change that has not been flagged.

Mr Burge—I think the important point to emphasise here is that we are dealing for the first time, as I mentioned previously, with the rollover, specifically contemplating the transfer of a business generally, whereas under the existing law the strict terms require an asset by asset transfer. So it is a measure that we expect to be welcomed, and we know will be welcomed, by the small business sector as facilitating a sensible approach to rollovers. The fact remains that rollovers should not result in the elimination of capital gains, only their deferral. If rollovers were allowed in relation to the precluded assets, and those precluded assets are essentially those assets which are CGT exempt, then the basic approach to rollovers would not be respected.

Mrs Gibson—I am not sure I understand that. Have we actually flagged in the explanatory memorandum all of the changes? Is that a change in law from the old law to the new law? It is a change in my view.

Mr Burge—The change here is facilitating the rolling over of all the assets of a business. That is a change made by TLIP and that is certainly flagged in the explanatory memorandum.

Mrs Gibson—It is flagged as an in globo thing. I could not pick up this change in going through the listed changes in the explanatory memorandum. That is why I am raising it. We are not listing all of the changes and all of the implications as they come through.

Mr Reid—As I understand it, the whole rollover is new; so there is nothing to compare to it at that line by line level of detail. It is a new rollover which has certain qualifications built into it, or it is an extension.

Prof. Deutsch—Under the old law you would roll over each individual asset. Could you under the old law roll over a car? You couldn't, could you, under the old law because it was a precluded asset under the old law?

Mrs Gibson—No, it would just retain its status as a non-CGT asset, but it would not affect the shares in your company.

Prof. Deutsch—That is right. But if you are trying to do a global transfer of all assets now it seems to me to be consistent to say that some proportion of your shares

which represent that asset cannot get the same protection. I think the fundamental point is that what is happening here is a completely new rollover. So it is impossible to say, 'Is it consistent with the old law?' because it is not the old law; it is a completely new rollover.

Mr GRIFFIN—Is that policy?

Prof. Deutsch—That is a policy decision.

Mr Burge—Yes, it is a change to the effect of the law which is noted in the explanatory memorandum. As a direct result of representations made to the project, the asset by asset treatment required under the existing law was commercially unrealistic. There is still that option of an asset by asset rollover, but there is also now the alternative of dealing with all of the assets of a business.

Mr GRIFFIN—On that issue, playing devil's advocate here, from my layman's perspective it seems like it is a new thing and therefore it has policy implications. All that it makes me wonder or worry there is that on one hand the argument has been pretty much consistently through this whole process that TLIP does not do policy, and we seem to have a policy here. It might be a good policy, it might be a great policy, it might be a fantastic policy; but we have a policy. How come we have a policy?

Mr Nolan—We have never, including in the previous bills that you have dealt with, been a completely policy free zone. We have always said that there are minor policy improvements, especially where there is little or no revenue implication but where the outcome will be either clearer law or easier compliance and that, if the government agrees to do those things and the parliament supports it, they can be accommodated within the reasonable bounds of our terms of reference. This is one that fits into that easier compliance. We are saying that the existing law had a commercially unrealistic aspect to it, as John Burge noted.

Mr GRIFFIN—So the issue is that there are basically no revenue implications on this one; is that correct?

Mr Burge—We sought advice on the revenue implications and we were advised that, yes, basically there were no revenue implications.

Mrs Gibson—Can I just challenge that. Let us assume that all of the assets are got here, because in 122-55 we are dealing with pre-CGT assets. So if in my pre-CGT assets I have a number of excluded assets—let us say I have a number of vehicles that I want to deal with—and I put all of those assets into a company in return for shares, some of my shares which represent the value of the motor vehicles are now going to be captured for CGT. Is that my correct reading of that rollover provision?

Mr Burge—Yes, that you cannot get the rollover in relation to those vehicles; nor

can you under the existing law.

Mrs Gibson—But at the moment if I sold the vehicles there is no capital gains tax to be paid; there would be no tax to be paid if they were pre-capital gains tax vehicles.

Mr Burge—That is right, and even if they are post-capital gains tax vehicles.

Mrs Gibson—That is okay; I am only dealing with the pre-CGT one at the moment. If you roll those assets into a company and take shares back, your position before the rollover should be the same as your position after the rollover, the only difference being I had all pre-CGT assets and now I should have all pre-CGT shares, but I do not.

CHAIR—What happens if she sells the car after rolling it over?

Prof. Deutsch—It is not the car that is the problem, it is the shares. What previously happened was that you would have an individual who might hold a series of assets. They would individually have to transfer each asset to a company and receive shares in return. The assets that were pre-CGT assets would be transferred and you would receive shares which were themselves pre-CGT shares. In relation to a car, you would not do that; you would just transfer the car without receiving any shares. It would just be a transfer which was free of capital gains tax.

What TLIP has decided to do is to, in a sense, make life easier for taxpayers who did not have to do an asset by asset transfer but a global transfer of the business assets. The upshot of that is that—Margaret is right—you are going to end up with, in the way that the legislation is structured, some shares that are post-CGT shares, because you cannot roll over the cars and receive back pre-CGT shares; you will be receiving a number of post-CGT shares which will reflect the value of the cars to the value of the total assets. So the planning that people will do is that they will go back to the old system and transfer the assets individually.

Mrs Gibson—They would have to.

Mr Burge—An important point to note in this context is that under the old law equivalent, which is section 160ZZN and section 160ZZN(A), you could not get a rollover for the transfer of a car to the company because the rollovers applied only to assets. In the old law, in section 160A, which has the definition of assets, cars were excluded from that definition. So it follows that, if the rollover applies to the transfer of an asset, if a car is not an asset, you cannot get a rollover for it. In the rewrite we have taken a more sensible approach. We treat the car as an asset; it just becomes part of the general definition of 'CGT asset'. But we have a specific exemption for it. We have not actually changed the effect of the law in that area; it is just a more sensible way of conferring the exemption.

No change has been made at the level of the specifics of an asset by asset transfer. For general transfers of assets as part of a business the approach is consistent with that in the existing law. The explanatory memorandum on pages 108 and 109 does deal with this general issue of the incorporation of a whole business and it does have some discussion about the treatment of precluded assets. But the emphasis of the explanatory memorandum is to deal with the changes that are being made. It will not always deal with the intricate detail of those changes but give a broad overview of them. That is what has been done here.

Mrs Gibson—I still think that what we are doing is bringing into the capital gains tax net assets, now shares, which were not in the capital gains tax net before. If all we are dealing with in 122-55 is all pre-CGT assets, which is what we say—you are taken to have acquired all of the shares before September 1985 if you acquired all of the assets before that day—then I do not understand why you needed to remove precluded assets. You could say 'including precluded assets'. The objective, I would have thought, would be to make sure that you are in exactly the same position after the rollover as you were before. I cannot see any reason for pulling out of that and making subject to the capital gains tax net shares which relate to the value of non-CGT assets.

Mr Reid—I think the answer lies in the fact that, in general, the ownership by a company of exempt assets does not impact on the CGT treatment of the shares. In other words, the exemption for the car does not carry through to an exemption of the shares under general circumstances. So why should it here?

Mrs Gibson—It could well do. If we take the approach that Bob Deutsch was talking about and simply roll over all of the CGT assets other than precluded—you get pre-CGT shares—you then sell the car and you still get pre-CGT shares. It does not affect your shares. Why we have to go through a double whammy to do it when we could simply do it under the provision is what is of interest to me. I have made my point on that.

Mr BEDDALL—Now that we realise we are not a policy free zone, with an issue such as this, which the TLIP team has identified should be fixed, what process is followed to get (a) ministerial approval and (b) cabinet approval before it is actually put into the bill?

Mr Nolan—Generally, because these are very minor matters, the process is that we first of all would get Treasury's tax policy people to have a look at the proposition and see whether there are any policy implications that perhaps we have not understood. If they are of the same mind as the project team, that proposition will be put to the minister, the Assistant Treasurer, and proposed to government and it will be approved there. There would be very little that we would do that would need—

Senator WATSON—Does that go to the consultative committee as well?

Mr Nolan—Yes. At each consultative committee meeting there is usually a progress position—papers are provided generally indicating the kinds of changes that we have in mind. We get the consultative committee members' views on those. Sometimes members of the consultative committee actually work more closely with some of the subgroups of people working on particular parts of the rewrite so that, outside formal consultative committee meetings, individual members with an interest in a particular area of the law might work more closely on those aspects. Generally, areas of proposed change are floated past the consultative committee. We give them an opportunity to express their views about it.

Senator WATSON—Do Treasury sit on that consultative committee?

Mr Nolan—Very rarely. On occasions they have come to meetings, particularly where there has been advance notice that there is an issue about which the consultative committee wants to hear the views of Treasury. But the usual situation is that Treasury do not attend consultative committee meetings.

Mr GRIFFIN—What criteria do you use to decide whether a small 'p' policy issue is something which can go through the process of referral to Treasury and then to the Assistant Treasurer regarding the question of approval versus those which do not? Is it simply a matter of the revenue question?

Mr Nolan—Revenue would be the main issue: 'Is anybody's position going to be cheaper or more expensive as a result of this proposition?' That will be one issue, but it can be more than that.

Mr Back—We have always taken the position that, if any change has the potential to alter any taxpayers' rights or obligations, it would require at the minimum the endorsement of the relevant minister, which is the Assistant Treasurer, and the endorsement of the Prime Minister.

Mr GRIFFIN—Yes, but the question still goes back to the matter that there are a whole lot of policy things flying around. Some get referred up and considered through this process and some do not.

Mr Back—Basically we get a lot of policy proposals, some of which are simply, by articulation, outside our terms of reference. Some seem like good ideas, so we have principles we apply to see whether from our experience they are capable of being a product of the tax law improvement project. Basically it has come down to whether there are any losers. Every time you start to articulate a loser there is someone who is going to get upset. People do not like to see, as a product of this process, measures which get people upset.

Mr GRIFFIN—So when we say small ‘p’ policies we mean small ‘l’ losing positions in effect. That is fair enough.

Mr Back—I think it is important to understand on this project that we have a look at a lot of policy issues which do not see the light of day. It might be assumed that we never advance them but in fact they disqualify themselves because they identify impacts that may not have been obvious to other people.

Mr GRIFFIN—I accept that.

Mr BEDDALL—What is the process if something comes forward, you do this process, you run the test over and say, ‘This will have a revenue impact. There is a loser but, gee, it is a good idea’? Is that process then up through to the budget process or is it just left?

Mr Nolan—Those would be things which would get on to the compendium of issues that have been raised and so they are available for budget or other processes.

Mr BEDDALL—There is a fine line here between where you stop—

Mr Nolan—It is a fine line.

Mr BEDDALL—and where you actually can see that this really needs to progress. Do you actually ever pursue any of these issues rather than just put them on compendiums?

Mr Nolan—I think that goes to the issues that Mr Griffin was very interested in before the break. There is a process for handling small ‘p’ policy issues that are marginally seen as outside our immediate charter.

Mr GRIFFIN—There sort of will be after 18 months, Brian.

Mr Nolan—Yes.

Ms Morton—Mr Beddall, the fact is that that compendium has really basically been sitting. That has been one of our great concerns. Bearing in mind that the consultative committee does not have any resources, we have been very dependent also on the project team keeping that compendium. As you know, a lot of these issues have been of concern to us from day one. I have come up with a number of issues over time that I think would really have helped in various instances and I know that the project team would have in many instances would have liked to have taken them on. The depreciation area is one area which, with a little bit of foresight, we could have cleaned up enormously instead of having something like 30 different taxing regimes under depreciation. But that was a policy issue, and we have lost that opportunity now because we have moved on. I

do not believe that listing has gone to Treasury for budgeting purposes, and I think it would be excellent if it were recommended by this committee that that compendium be looked at in detail and taken into consideration.

Could I answer the question that Senator Watson was asking before about what policy issues the consultative committee actually sees prior to their coming out in an exposure draft. Brian was right in saying that there are some issues that are brought to us very specifically and we are told, 'This is a fairly major change we are thinking of,' and they are addressed with us, sometimes within a greater or lesser time frame. But in a lot of instances an exposure draft comes out in its entirety, and then it is really our responsibility to work through—looking at the explanatory memorandum—and finding out what changes have gone through. John would just never have had the time and our meetings would never have allowed for us to sit down and address every change that is in here and give a tick to it. Can I just make it clear that we have not ticked off on these changes and, in many instances, the first time we saw a lot of the changes is when they came out in exposure draft 10 or 11, and then further ones would have come out again when this came out just at the end of November.

CHAIR—I think we understand that, but that is one of the reasons for today.

Ms Morton—Yes.

Mr BEDDALL—Can I ask Ms Morton a question, because there was an issue that she raised at a previous hearing about fixtures. I think that was to do with depreciation then. Did anything ever come of that?

Ms Morton—It has still not been fixed.

Mr Nolan—I think my colleagues want to say something, but could I make one observation because it is an element of this process that has not been registered before and I think in fairness it should be. The minister who is responsible for this project—the Assistant Treasurer—has made it very clear to the consultative committee members that he is willing to entertain issues that they regard as important, that submissions from the committee to him would be welcomed, and there have been instances where that has occurred, but it is a process that is open. It is not entirely just the project director sitting there with his foot saying yes for that one and no for the other. There are other processes that go beyond that.

Mr BEDDALL—Brian, isn't that already a double up itself? If these submissions are made to the tax office—that is, TLIP—they are, in effect, made to the Assistant Treasurer right from the start and they should go there without having to have another round.

Mr Nolan—The reality is that we talked earlier about several hundred ideas being

put just on this bill alone. I do not think it is really feasible to expect a minister to get to that level of detail across such a range of issues. There has to be some sort of filtering process.

Mr BEDDALL—But a submission to the minister, in all due deference, is a submission to the tax office. I do not see Senator Kemp sitting there with a light on going through the tax bills. He is going to refer it on for advice. That is the role.

Mr Nolan—Obviously ministers take advice. Whoever happens to be in government, that has always been the case. But, at the same time, ministers also take an educated interest in the matters that are being put to them. I think the consultative committee would agree that, on matters that have been raised with Senator Kemp, he has looked at them very carefully. He has sat across the desk with them when they have wanted that process. I just repeat that it is not just the project team exercising an ultimate right of veto. It goes beyond that.

CHAIR—Gee, I thought ministers only did what the mandarins told them to.

Mr Nolan—That is a myth.

Miss Haly—I would like to add that, as part of the approval processes, we draw to the attention of the Assistant Treasurer issues which have been contentious during consultation, where key stakeholders—whether they are on the consultative committee or are part of other bodies—have drawn to our attention issues they might take with the bill. He does in fact look at those issues, and we will often have to brief him on them. Also in the past he has allowed people who have raised such issues to meet with him privately so that they have a private audience to discuss them, so he feels fully informed on them.

CHAIR—All right. Are we happy with 122?

Mr Langford-Brown—I have a concern which I would like to direct to John Burge. You talk about liabilities within the provisions, particularly 122-37(2). John, do you believe that the wording in there is adequate to embrace provisions such as accrued long service leave and holiday pay in the rollover of assets? I am concerned that it gives the impression at least that you are directing yourself to actual liability as distinct from the provision concept.

Mr Burge—We have addressed that issue in some detail in the responses we have given the committee. It is quite a detailed position. Basically, we do consider the wording to be adequate. If I could draw attention to that specific answer, it would be in the volumes that we have provided.

Mr Langford-Brown—That we have just got.

Mr Burge—Correct.

Ms Morton—I have an extension of that question to John Burge.

CHAIR—No, ask me, and then I will ask him.

Ms Morton—Okay. I have been struggling with 122-20(3) and (4), in particular (4), which talks about:

In working out if the requirement in paragraph (3)(a) is satisfied, if the market value of the shares is different to what it would otherwise be only because of the possibility of liabilities attaching to the asset or assets, disregard the difference.

But when I look at the example it says, 'The market value of the shares will reflect these contingent liabilities.' I am confused as to which ones are supposed to be brought into account and which ones are not. I know that John and I have had discussions on this point before, but in reading it I am not quite sure what the provisions are actually doing at the moment.

Mr Gaylard—It would be hard to read the liabilities in that context as other than all liabilities, including contingent liabilities, surely?

Ms Morton—Subsection (4) says 'disregard the difference'.

Mr Burge—Could I respond to that?

CHAIR—Please do. If you could clarify it, it would help.

Mr Burge—We included this provision as a result of concerns that had been raised with us that, under the existing law, where its wording requires exact equality in the market values, it is not possible, strictly speaking, to satisfy the terms of the provision. An example would be because of contingent liabilities, including an accruing capital gain. This provision is simply directed at ensuring that you can disregard the difference attributable to that type of liability and treat the values as though they are the same. That is what that is directed at.

CHAIR—Could I suggest that TLIP have a look at the wording. If Jocelyn is confused then perhaps we have not simplified the language enough.

Mr Burge—We would certainly be happy to look at those issues.

CHAIR—Thank you. Would you be happy with that?

Ms Morton—Yes, I will speak to him later.

CHAIR—Is there anything else on subsection 122?

Senator WATSON—Have contingent liabilities always been taken into account?

Mr Burge—This particular change here is dealing specifically with the contingent liability problem, so they were not taken into account under the previous law. The view was put to us that, strictly speaking, you could not get a rollover because of those contingent liabilities. It is to deal with that specific concern that was raised with us. It has also been referred to in a number of the textbooks on capital gains tax.

Prof. Deutsch—I have one query. There is no actual definition anywhere of what a rollover is. If we are trying to make this user friendly for a larger segment of the community, could we have a box which indicates what a rollover is? We come close to it in 122-1 where we say what the effect of a rollover is—it can delay the making of a capital gain or loss. It does not quite do it, though, because a rollover is a scary term if you have not come across it before. It simply means a CGT event, if you like, which is protected from tax for whatever reason. Could we have something in box form to indicate that?

CHAIR—Is there a generic definition of 'rollover'? I have often wondered that myself, because it applies to more than one area of tax law. Is that possible?

Mr Nolan—I wonder whether Geoff Harders, who has been the main drafter of the capital gains tax section, could comment.

Mr Harders—There is a reference to rollovers in division 112, which is the finding table which sets out a number of finding tables for rules affecting cost base. If you have a look at 112-105 and 112-140, there is a description of what replacement asset rollovers and same asset rollovers provide.

CHAIR—Are you happy with that, Bob?

Prof. Deutsch—To be quite candid, not really. I think that those sections in a sense tell you what the consequence is. In 112-105 it says, 'A replacement-asset rollover event allows you to defer'. But what actually is it? It perplexes me that we cannot actually say—

CHAIR—Are you talking about the transfer of an asset from one entity to another?

Prof. Deutsch—That is correct. A transfer of one asset. In old terms you would have said it was a disposal from one taxpaying entity to another one which was protected from tax consequences. The wording I have is a bit untidy. Now it is more complicated in a sense because you have to deal with CGT events. But there must be a way in which you

can state to the public at large, 'What are we talking about when we talk about a rollover?' We tend to assume that everybody knows what that means, but I think that is a false assumption.

CHAIR—If you were going to address that by defining what 'rollover' meant, wouldn't you have to make sure it encompassed superannuation events as well? You would not want one definition for a rollover in terms of capital gains tax and another in terms of superannuation, would you?

Mr Reid—If I could respond to that—

CHAIR—If you really want to confuse people.

Mr Reid—The fact is that the term is used in superannuation but really in quite a different sense. The broad similarity is that you are turning one thing into another but basically treating it as the same thing. That is the most generic description I can give for it. But the technical incidence of a rollover is quite different in CGT to what it is in superannuation. Perhaps this does not exactly meet Bob's point, but I suppose we would say that 'rollover' is a jargon term which is used by people who know what it means, if you like, but it does not actually have a precise meaning, so we have actually stated the consequences of a rollover very specifically, and we have used the label because it is familiar to people.

CHAIR—I know what it means but it does not mean anything.

Mr Gaylard—I am sure, on the first point, the superannuation industry would be very interested in trying to extend the rollover of CGT assets to super funds, but I think Bob has a good point. It is really a question of where you locate. Often it is an issue that we deal with—where do you best locate a description of a particular type of event. I think Bob would be quite happy if there was some sort of description as to where you would probably expect to find it more obviously in the actual rollover provisions themselves.

CHAIR—Will you take that on board, John?

Mr Burge—Yes.

Senator WATSON—It is using the words of section 112-105 anyway. It would be an event that allows you to defer the making, so all you would really be doing is adding another word or two because you already have the words in 112-105. It is there, but you are just putting it into a little definition section—'is an event that'. That is the only difference that I see in it.

Mr Nolan—There has been a bit of a drafting panel working away down here. Could we come back to you at some time during—

CHAIR—I thought we had left it. Now, 124; 126; 128; 130?

Mr Bryant—I have got one on 131, but first I want to make a very general comment. I have got in this document here today a response to a submission we made which had over 100 issues—some of them minor but there is quite a range of issues—in the areas we have just been passing through. My difficulty in commenting on some of these is that I am not clear what the response is. I might just add that this commentary is dated 23 January, last Friday, and I have not seen it before this. It does make the observation that 40 per cent of the items we had referred to in earlier submissions have been adopted in some way or other. Of course, it is the other 60 per cent I am concerned about. One of those is an issue which I raise, through you, in general terms. In section 130-60, we find there is no re-translation or picking up of a provision in the old law, namely 160ZZ(a), dealing with the consequences of the conversion of a convertible note. We raise this as a concern because, unless that is properly addressed, you do not get a proper transition between the old law and the new, and something needs to be done. It has been said in response to that that it has now been picked up and there are proposed amendments 88 to 91 and they will be dealt with—it is a fairly convoluted sentence here but essentially, as I understand it, within the transitional provisions. So can I ask John, through you, where I can find those amendments. I would still be keen to test them to make sure that they address the point that I am raising.

CHAIR—Can you respond to that, John?

Mr Burge—Certainly, Mr Chairman. They are contained in the draft amendments circulated on 8 January of this year. The amendment numbers are in that document, so, by looking at that document you would find that material. The reason that we included it as a transitional measure is that it really does affect past transactions and it is more appropriately dealt with that way. But the transitional measures will have appropriate signposts to them to alert the reader to that. We made that material available on 8 January to enable comments to be made to us, so we would welcome that attention by Bob to that particular issue.

Mr Bryant—Thanks, John. I just register the point that it is only now, quickly trying to scan this, that I have that connection. It just reflects the difficulty we are having.

CHAIR—We understand that. We are cognisant of the difficulty.

Mr GRIFFIN—I think it is fair to say that everyone reserves the right to come back at a later time about aspects of this stuff.

Mr Bryant—Yes. I have to do it on this one, and many others, of course.

Senator WATSON—Can I get some free advice in relation to 130 investments. If I receive consideration in relation to a takeover and part of that relates to part of a payment through a share premium reserve, is that subject to capital gains tax or not under

the new rules?

Mr Burge—I would like to have to take that issue on notice and report back to you after the break.

Mr Morgan—My notes only go to 128. Perhaps I have missed it, but I cannot believe we are skipping over the effect of death without some comment, as it has been a problem area. Would John Burge like to make any comments about the difficulties in that area?

Mr BEDDALL—One of the effects is that you don't care about tax anymore.

CHAIR—You certainly don't.

Mr Burge—John Morgan invited me to comment on issues relating to deceased estates. We have provided some minor clarifications of issues in the rewrite of what I call the CGT death provisions. We were unable to provide more detailed rules in relation to life estates and remainder interests and those types of areas. The reason for that was the government's review of the taxation treatment of trusts. Once that review was announced, we gave attention to other areas, and we did not pick them up in the rewrite. But we have reproduced the existing law, with a number of clarifications which are outlined in the explanatory memorandum.

Senator WATSON—Could you explain that in a little more detail?

Mr Burge—We have rewritten the existing law, but there are some issues where we have clarified the application of the law. If I could give an example, there is an issue about whether under the existing law the favourable CGT treatment at death—basically not recognising a disposal or CGT event at death—is limited to assets owned by the deceased at death or whether it can apply to assets acquired by the legal personal representative after death. We have clarified the point to say that it is only those assets acquired before death. That is in accordance with the tax office's interpretation of the existing law. So there are examples of clarifications of that sort. They are set out in the explanatory memorandum. What we did not do was to provide detailed rules in areas not covered by the detail of the existing law in relation to, for example, life estates and remainder interests.

Mr Morgan—I can briefly assist. I think they cannot deal with the major problems because they have received a directive not to do anything to do with trusts. The major problems relate to life estates and remainder interests, and it is true that some of those sorts of interests are mediated by trusts, but many of them need not be. They can be legal interests.

Senator WATSON—What does that mean?

Mr Morgan—It means they have turned a blind eye because they have been told to. There are limits.

Mr Gaylard—There is a major project going on to deal with all aspects of trusts including deceased estates, as I understand it, and it is basically a no-go area. We did have some reasonably good plans to improve the law in that area, and the government said, 'Don't go any further, don't do it, because there is another review under way.'

Ms Morton—That is one of the fundamental problems with two things running at the same time, because you do not get them linking in properly.

There was a major issue at a number of the meetings about the timing in this provision, whether it was just before death or at death. Could you ask John to clarify whether the law now reflects the old law exactly?

Mr Burge—It was not entirely clear under the old law whether the favourable CGT treatment at death was limited to assets acquired by the deceased before death. The ATO's view, as reflected in a relevant tax determination, was that the favourable treatment did only apply to assets acquired before death and that is generally—but not unanimously—accepted as being the correct position. The rewrite clarifies the law to make it clear that it is only those assets. That clarification is in the explanatory memorandum. It is our view that we have reflected the existing law in the rewrite.

Senator WATSON—By virtue of an acceptance of a tax determination.

Ms Freshwater—It was also the joint body's recommendation that that was the appropriate view. They accepted that the commissioner's view in that case appeared to be correct.

CHAIR—Thank you. Division 136.

Prof. Deutsch—Sorry, Mr Chairman, I was hoping to deal with 132, if I can, very briefly. It seems to me that there is one problem with 132. It deals with leases but what it does not deal with is the expiration of a lease. That is because that is CGT event C2, and it is explained in CGT event C2, but a novice reader of this would reasonably assume that division 132 deals comprehensively with leases. I just wonder whether we could have some cross-referencing from 132 to event C2 so it would be clearer.

Mr Burge—We have received a number of requests for additional signposts in the legislation, those cross references. I must say that it is a very welcome fact that this feature of TLIP legislation is so much accepted now that people are asking for more of these cross-references. It is the case that, if we were to deal with every request for an additional signpost, they themselves would begin to clutter up the legislation. What we will be doing is listing all of the suggestions, including this one, and I would expect that

we would be picking up a large number of those suggestions.

CHAIR—Thank you. Is 132 all right? Division 136; 149. Subdivision 165-CA; 165-CB.

Mr Droder—You are into my area, Mr Chair. I really do not have a learned comment to make, except that I said in my opening address that I had a problem with the same business test and how it is worded and it seemed to me that automatically in reading that you would exclude everything. My colleagues on the right here say that the courts ruled it in a different way, or a more specific way. It just seems to me, to take Bob Deutsch's point, that if you are reading the act you need to be able to understand it and it ought to be self-sufficient. The team have tended to help that out by, in capital gains tax, for example, having things like 'in these circumstances' and CGT events.

It seemed to me that these two divisions might be a bit improved in terms of elaborating what is the same owners, the same control and what is the same business by having a list of certain events, because there must be a whole rage range of standard events that could be explained and that would help people read it. It is not a technical issue.

Mr Burge—The project has already rewritten the main income loss provisions. These capital loss provisions are the capital gains or capital loss equivalents of those, so as far as possible we have followed the same approach that the rewrite has already taken in the income loss provisions.

Mr Gaylard—I have had a fair bit to do with the particular revenue project and, while it was an aim at one stage of trying to spell out, for example, what 'same business' meant—it seems a very simple term when you say the two words—by the end of some consultation on it both the tax office and the professions felt there was absolutely no way that you would afford to clarify it because there was no firm view on what it meant. It is one of those areas that there is a fair bit of case law on and it has been left delightfully vague.

CHAIR—You are saying that codification in itself might in itself create problems?

Mr Gaylard—Yes, most definitely. That was the view of, as I say, the professions and the tax office.

Ms Morton—This issue was hotly debated at the time of the other losses. I think you will note in *Hansard* that I spoke strongly against the words that were there at the time because it seems it was not all the professions that were in favour of those words. This is destructive to business. To put in the words 'conducted no additional business' is just against all the principles of good business.

CHAIR—Sorry; you have lost me there.

Ms Morton—If you have taken over—

CHAIR—What are the words again?

Ms Morton—The reference is 165-117 at page 406. In that box down the bottom, it says 'entered no new transactions and conducted no additional business'. So, if you have a change in ownership in your business, and you have losses—

CHAIR—Which part are we talking about?

Ms Morton—In the box.

CHAIR—The last bit, beyond the dot: 'or if there has been a change of ownership or control'. I have to say, John, that I do not understand what that means.

Mr Reid—If I could just clarify this point—

CHAIR—You will want to. To me it does not seem to be very clear English.

Mr Reid—We are not looking at the right provision. This is a summary provision that is intended to give an overview of what the subdivision is about. It quite clearly appears in an area described as a guide to subdivision 165-CA, and it is quite clearly marked out as appearing before the operative provisions. The actual provision that creates the same business test is in 165-210. As Simon was just saying to me, it is not in itself a model of certainty, but it is generally regarded as correctly restating the law that existed before the rewrite. As Simon was saying, codification in this area is regarded as more dangerous than non-codification. But the words 'entered no new transactions and conducted no additional business' are simply a condensed paraphrase of the more explicit tests that are contained in subsections 165-210(3) and (4), for which you will need to refer to a consolidation of the 1997 act. It is not actually in the bill.

CHAIR—If I own a company and I transfer it to my wife, that satisfies the test of there being a change of ownership or control, and if the company has since carried on the same business so we keep doing the same trading but we enter no new transactions and conduct no additional business, how on earth can you have a trading business that does not have any transactions?

Mr Reid—'New transactions' is a condensed version of the words 'transactions of a kind that it had not entered into in the course of its business operations before the test time', which are technical words that were carried forward from the old law. So this is a simple way of saying it is not literally 'no new transactions' as in 'no transactions at all', but it is saying no transactions of a new kind.

CHAIR—As a layman, with respect, if this is the tax law simplification bill, I have to contend that it does not appear to me to satisfy the test. That is just my opinion.

Mr Morgan—If you just put the words ‘no new types or kinds of transactions’, it might help to make it a more apt summary.

CHAIR—Something needs to be done to it.

Mr Gaylard—It is an exact translation of the existing law. If the government wants to change their position on that—which is a very major policy area—then certainly, I am sure, lots of people will be very pleased to see that happen.

CHAIR—I am not talking about changing the position; I am talking about plain English.

Mr Bryant—What it really should say—and this reflects the difficulty of trying to simplify something else and getting caught up with new words, and this is only a guide in the provision—is ‘carried on the same business’, and then refer you to where that concept is further detailed. That attempt is very clumsy, and it is quite misleading; I agree with you.

Mr Blaikie—The summary is wrong.

Ms Morton—Not only that, it is not right to say that this is a correct translation of what the old law said. There was lots of contention about the old law anyway. It says, ‘a business of kind that it did not carry on or from a transaction of a kind that it had not entered into in the course of its business operations’. The way people are looking at these new words implies that, if you took on a new customer, you could breach these new laws.

CHAIR—That is the way I read it.

Ms Morton—Exactly. If you read it that way, I read it that way and half a dozen other people are reading it that way and we are told that we are going to have to live by the words that are in this act, then the words should be more careful. At the time this old law was written there was a lot of problem in Australia with people buying loss companies, feeding in profits and all that. You have to take why they were written in the first instance and then look at what our environment is now.

If we have anti-avoidance provisions and other things that protect us, surely what we want is struggling businesses to be able to take on new business, to develop and to keep employing people. It goes against all good economic sense to have a law which is contrary to what businesses should be encouraged to do.

CHAIR—It is not our job to get involved with technicalities. I was a building

contractor and as I read that I would have to say that, had I transferred the company from my name to my wife's name, when I signed the next contract I could forget about claiming any bad debt on the last contract. I think it is very poorly written and that is bad.

Mr Gaylard—It is not the correct interpretation.

Mr Nolan—We can undertake to look at the words in the guide to see whether they can be made clearer. They are not intended to be a full statement of the law; they are a guide. Even performing that function they are not doing enough for you. We will see how that goes.

CHAIR—I just wanted to make the point.

Senator WATSON—We have got very specific words here. What we really need are the additional words 'essentially of the kind' to free it up a little bit, because as I read it, it is just too tight.

CHAIR—I do not think we want to rewrite it. What about subdivision 165-CB?

Mr Morgan—I draw attention to the use of multiple capital letters. I have not had the time to consult with my other colleagues on the project, but as the use of multiple capital letters was such an identifiable fault with the 1936 act—

CHAIR—Why is that a fault?

Mr Morgan—For instance, a lot of the provisions that are being rewritten here in capital gains tax had up to five capital letters such as 160ZZPAAB. It was one of the objects of the law that brought it most readily into ridicule. Perhaps there are plans to fix that. As I say, I have not had the time to have a chat with my colleagues to find out exactly what the plans are to remedy that, but it seems a shame if this is to be cemented for all time.

Mr Reid—One of the features of the new numbering system is that we have left gaps in the numbering so that you can insert further material. The only place we have not done that is in the numbering of subdivisions because they have letters in them. We have done it in a few places, but we have not as a regular thing left gaps between subdivision numbers because we thought progressions like 165-A, 165-E, 165-M or something would look odd.

Where we have wanted to insert two extra subdivisions between existing subdivisions we have had to resort to the old technique of using multiple letters. That is a very rare thing. We have managed to avoid it so far in the other levels of numbering, such as divisions, parts, sections and so forth. It is certainly not right to infer from this that we are going to have a repetition of the situation under the old act.

Senator WATSON—How often does the multiple lettering that you have drawn our attention to occur?

Mr Reid—I think it occurs twice. There are two subdivisions inserted into 165 which have multiple letters, similarly with division 175. They are the only places it has happened so far.

Prof. Deutsch—It will happen again. Inevitably there is a tussle here between do you allow this or do you say you have subdivision 165 and the next subdivision is 169 to allow for expansion. As Tom says, that is not a great solution. It tends to look a bit clumsy. It is really a question of what do you prefer? Do you prefer gaps or do you prefer to have C, CA, CB? It is really a question of what is the lesser of the two evils.

Mr Reid—With the divisions we have, in fact, left gaps. Even if you leave gaps, ultimately the gaps will be filled. So in the fullness of time you have to find a number between 169 and 170. But the way we have set the numbering system up has minimised that; it has put it off quite some way in the future for all levels of numbering other than subdivisions. The way we have structured the numbering system should make it less necessary than it has been in the past.

CHAIR—Thank you for that.

Luncheon adjournment

[2.07 p.m.]

CHAIR—In response to a question by Senator Watson, I believe John has a comment he would like to make.

Mr Burge—Before the break Senator Watson asked about the capital gains tax treatment of amounts paid out of share premium accounts on a takeover. It is really a question relating to the existing capital gains tax law and depends on the particular factual circumstances. We have arranged for the tax office's capital gains tax cell to get a detailed response to Senator Watson.

Senator WATSON—I have a follow-up question in relation to an issue of some concern that was raised this morning. It was indicated that some of the subsequent amending law is not written in conformity with the style of the tax law improvement program. If that is true, do we distinguish between the old 1936 law and amendments to the tax law improvement law of which there have been two tranches already? I could probably understand it if it were in relation to the technical intricacies of the 1936 act, but I would be perturbed if that same comment applied to the already written law. Can that be clarified for me please.

Mr Nolan—By far the majority of the legislation that has been coming, apart from

ours, has been amendments to the 1936 act, so I think in the main the comments would be relating to that. I did not make the comment—it may have been Stan Droder—so I am not quite sure what the person had in mind.

There has been an imperfect transfer so far of the tax law improvement project team's methodology and style to what we refer to 'as business as usual legislation' done outside the project. We are working to maximise the transfer of that style and we are doing that at the parliamentary counsel level. Tom Reid regularly has sessions where he briefs and gives lessons in the new method, in effect, to other drafters. We are doing the same thing with instructors in the tax office. We expect that that convergence of the two will be quite strong from this point on.

It is difficult. It took us quite a long time to develop our own style and to understand how you better communicate with readers. That involved for us some learning and unlearning of old habits. You have to convey that in ways that others who have similar old habits to break can absorb. I can accept that there has been a less than perfect transfer. I think there is quite a strong take up of the new method at least in relation to the 1997 act and we will be working to reinforce that.

Senator WATSON—I am pleased to hear that you are working to reinforce that. But I must express some concern that there has not been a more robust approach in terms of the drafting of amendments to reflect the tax law improvement style and methodology. What is the purpose of trying to get it right if we are not transferring that style, that methodology, that technique exclusively in terms of amendments to the 1997 act. We are going to slip back into the problems of past practice if we do not keep our standards according to this new level. Perhaps there may need to be some closer interlinking if there are different people doing these drafting jobs.

I can appreciate the problem of using the old methodology in relation maybe to the 1936 act because of the particular wording of that act. I would find it very difficult to accept any departure from the high standards that John Burge and you have set in relation to the amendments affecting the 1997 act.

Mr Nolan—I am encouraged to take that as support for what we are trying to achieve. We will certainly use your remarks as reinforcement when we are talking to other people who have responsibility for that business as usual legislation.

CHAIR—I would like to propose a small change in procedure. I would like to stop discussing these subdivisions, which I believe are not very contentious, and go down to the areas of possible contention. If we get through the contentious issues then we can go back to the others. We will start with 104, capital gains tax events.

Mr Magney—I am trying to arrange to have the points we wanted to make on 104 photostatted so that it is easier to talk to them. One of the points we are going to make I

notice has, in fact, been picked up in these amendments which we got the other days. That was one of the more difficult points to explain. That has reduced the submissions we want to make. If anybody else has something on 104 they wish to put whilst our submissions are being photostatted they can go ahead.

One point I could make which is not in our written submissions is that these submissions are really being made by Ric Krever and me as we have been liaising on this. We believe—and this is something that was brought up earlier—that it would be extremely useful if we could have a table at the end of each CGT event which referred the reader to every provision of the CGT legislation which related to that event.

Let me say that, having looked at the CGT event method of setting out the capital gains tax legislation, I think that it is a great improvement on the previous method of all these deemed disposals scattered right through the CGT provisions. I am reasonably experienced in this CGT area, and when I went and looked at the events I compared the corresponding legislation from the 1936 act to satisfy myself that the event was an accurate reproduction of the previous provisions but I also knew from my experience that there would have to be some provision in the cost base subdivision or the capital proceeds division in relation to a particular CGT event to cover certain aspects which were covered in the 1936 act.

Sure, when I went and looked for these modifications to cost base rules and modifications to capital proceeds rules, I found them there relating to that particular CGT event, as I would have expected to find them if it were an exact replication of the 1936 act, but it was only because I knew those provisions would have to be there and I went looking for them and found them that I was aware of all this. As for somebody coming to this legislation without a great knowledge of capital gains tax, the idea is they will go straight to the events and those events will help them see in a reasonably short period of time whether there is anything they have to worry about—instead of flicking through a hundred pages or so of deemed disposals—but that same person may then not be aware that there are five or six other provisions in the cost base division, in the capital proceeds division or in the definition of assets that impinge on that particular event and does so in a special way.

So I think it is very important that anybody who reads about an event has a guide to know which provisions impact on that event. You do not have to set out anything more than the number of the provision and also maybe the little heading that each provision has so that someone can go off and look for it and see what it has to say.

CHAIR—Are you talking about ‘see also clause whatever’?

Mr Magney—Yes—‘see also’.

CHAIR—Could we have a response to that from TLIP?

Mr Magney—I have mentioned this to John Burge.

Mr Harders—While it is very useful to have notes indicating other provisions that affect a particular event, in the end it is really a question of length as to whether this suggestion ought to be adopted. If it is going to require a quite a lengthy provision at the end of each CGT event, I think on balance I would prefer not to clutter division 104 with that type of indicator.

Senator WATSON—Couldn't you have another comment column in section 104-5, the CGT events? You have got four columns. You could add a fifth column and in that you could put your cross-referencing. Isn't that the place for it?

Mr Reid—The short answer is that the list would simply be too long. I am not sure whether the intention of the proposal is that every provision in the rest of the two parts dealing with capital gains tax would be listed or only those that applied specifically to that event, but even if it is the second you would have quite a long list of sections. As Geoff Harders has said, it really boils down to a question of length.

We are already being criticised in some quarters for the fact that there is so much non-operative material in these bills. We have tried to keep it to an absolute minimum consistent with the functionality we are trying to add to the legislation. I personally foresee that if we were to do this in a thorough way, in a way that would make it useful, in the way that it was intended, we would be adding considerably to the length of that particular division and therefore of the whole rewrite.

A lot of the work that is sought to be achieved by the proposal is already achieved in the divisions dealing with concepts like cost base and capital proceeds where, as part of the definition of those key terms which are used in the CGT events in division 104, and it is signposted by the dictionary, there is a statement of what the general rules are on something like cost base and then there is a series of tables which list the modifications to the cost base. You already have at that point in the narrative, if you like, a lot of additional material that helps readers to find the rules that are specific to their particular case. What is proposed would involve a duplication of that, in effect. As Geoff said, I think we would find that the length of the legislation would become unmanageable if we kept doing that. There is the long-term cost of maintaining that material when you amend the legislation in the future.

Mr Morgan—There is obviously a question of balance. Can I ask Tom Magney and Tom Reid whether just a short note at the end of each event just listing the exceptional sections, not even any description about them, would suffice? I think the force of Tom's suggestion is that the drafting approach is something a one-stop shop per event. You can look at the event and get a view of what is going on for that event. I think there

is some force in the suggestion obviously tempered by length.

Mr Gaylard—Just to slightly modify the point Tom Magney has made—I have a lot of sympathy with it to some extent—I am not sure whether we need to take this notation type approach to things other than the CGT events themselves. I give you an example of two particular cases. If you turn to 104-135 on page 59 of the legislation, which deals with capital payments for shares, you will see that we talk there about CGT event G1 happens if a company makes a payment to you for a share you own in a company, except for CGT events A1 or C2 happening. It was the trust one that I intended to refer to, which is 104-70 on page 42, which states:

> (1) CGT event E4 happens if:
>
> (a) the trustee of a trust makes a payment to you in respect of a unit or an interest in the trust . . .

It then goes on and gives a number of exemptions. It does that by way of narration.

If you turn to another example of the same thing—this is my point—if you turn to 136-20 on page 320 you see in relation to non-residents, which is a very usefully set out new facet of the law, that this table sets out those CGT events from which you cannot make a capital gain or a capital loss. Then there is set out there in a much easier way to grapple with, I think, the CGT events which are not relevant—C3, D3, I1, I2, K2 and K5.

I would like to see that approach taken in those areas like E4, and there are two or three others. Principal residents provisions, even though they are not necessarily part of the CGT event, also have a fairly complex series of CGT events in division 118. I do not know whether tabularising and in some cases saying why the event is not relevant may be too difficult. Sometimes you do not exactly know the reason why the event is not relevant. Spelling it out in a better way like we do in non-resident provisions, I think, would be a useful thing to do. I think there is quite a bit of merit in spelling out a little bit more detail in some areas.

Prof. Krever—I think it is also important to realise that we are not talking about every CGT event. There are just some of them where there might be some cross-referencing. There clearly must be a trade-off here because one objective of the new legislation is to keep it short, simple and more concise. As Tom has pointed out—and this is probably a good example—in this particular area we had two people working their way through the events who have done nothing but specialise in capital gains for the last 14 years.

We knew there must be cross-references because we know the law fairly well, but had we not known it as well as we did we would not have known that where this event says something happens there must be a modification somewhere in cost base and there must be a modification somewhere in proceeds, otherwise it will not give us the right

results. Just some very short signposts in a handful of events would make life a lot easier for other people who do not have the expertise. That should be one of the purposes of the redraft.

Mr Magney—I take Tom Reid's point that we do not want to make the act longer and longer. It seems to me that these CGT events now become the principal focus of the new provisions. I think it is a very good idea to find all the operative provisions in the one spot. To give an example, subsection 116-20(2) on page 140 says:

> This table sets out what the *capital proceeds* from *CGT events F1, F2 and H2 are:

Then it sets out special rules for those CGT events. All I am suggesting is that under F1, F2 and H2 you have a little note saying, 'For calculation of capital proceeds see 116-20(2),' or even just a note saying, 'See 116-20(2).' I will not bore you with too many examples. Subsection 116-30(2) states:

> However, subsection (1) does not apply to *CGT event D1 . . .

I think that is a classic example that if it is not already—and I do not believe it is—that should be referred to in the material on event D1. It would be simple enough for somebody who did not know their way around to miss the fact that that general rule does not apply in the case of D1. That is the market value substitution rule—just assume it did. It needs a little warning, even if it was just referred to the section and did not say what it was about, but just to warn you that you should go and look at that section.

CHAIR—It is enough to make you wish you never had a capital gain.

Mr Magney—Sure, if you go to 116-30 you find all these things clearly set out, but it is just to let some poor, suffering suburban accountant or solicitor who is trying to advise on this know that they should be looking somewhere else for other rules that are applicable to this event. I speak as an ex-practitioner who struggled for years, although specialising in tax, to make sure I had found all the relevant provisions.

Mr Morgan—Underlining these comments is that, efficient and all as the CGT event approach has become, referring to it as CGT event A1 or BX, or whatever it is, is very alienating in the sense that it carries no inherent meaning. Normally one would strive to pick a term that has inherent meaning. That has not been possible here. I think the suggestion is that whatever aids we can afford would be timely.

CHAIR—Don't you think you have to be careful that if you start doing too much signposting then particularly the local accountant will think, 'That is it. I do not have to bother looking anywhere else?' If you miss a couple, then he has misled the client inadvertently. I am not a lawyer.

Mr Morgan—If you are asking me to respond, I agree. Of course, you can take it to the opposite extreme and have none, which was the drafting style for the last 200 years.

Senator WATSON—That would go underneath the example, wouldn't it?

Mr Magney—Yes. I suppose where it says ‘capital gain’ and ‘if the capital proceeds’ and then gives an example, it would go just after the example, ‘note also section 116-20, subsection 2’ or whatever it was that I just referred to. Yes, just put it in there.

Prof. Krever—In response to your concern, I do not think we are suggesting signposting above what is already in the act. The problem is that what happens in the act is that it only goes one way. Once you get to the exception it says, ‘This applies back to C1.’ It would be useful in C1 if it said, ‘By the way, there is an exception down there.’ We are not adding new signposts, just putting all the signposts there running two ways.

Senator WATSON—With the signposting, are you asking for just section numbers or what is behind the section number?

Mr Magney—In an ideal situation, you would have not only the section number, but a brief statement of what it was about. The risk of that is that, as Tom Reid says, it will clutter the act up too much and make it too lengthy. So I would settle, if it were necessary, for just the section number.

Mr Burge—Could I repeat a point we made earlier? We will be looking at all the suggestions for additional signposts. There will be a need to balance the greater clarity that any one signpost gives against the effect on the legislation as a whole.

Mr Nolan—I was going to make the same point. It is really a question of balance. There are competing interests. Everybody wants to get the best result in terms of readability. Length goes against that, but extra signposting can also help. We should try to strike that balance by having a look at the total picture after all of the suggestions have been gone through.

CHAIR—Tom, what have you got here? Is it capital payment for trust interest?

Mr Magney—Yes. There is a peculiar situation which one was aware of under the 1936 act and it has not been picked up under this act. That is that in some circumstances the income of a trust of a particular year, year one, because no beneficiary was presently entitled to it in that year, will be taxed to the trustee. That income will possibly be distributed the next year to the beneficiaries.

There is no provision in the 1936 act to say that, when income that has been taxed to the trustee is subsequently in the next year distributed to the beneficiaries, the beneficiaries do not pay tax on it. But the High Court held in the Neville Shute case back in 1969 that that was in fact the case. Therefore, if you had the unfortunate situation where the trustee was taxed on the income in year one because no beneficiary was presently entitled to it, but a beneficiary became presently entitled to it in year two and it was distributed to that beneficiary and the beneficiary was not taxed on it because of the High Court’s dicta in the Neville Shute case, that would be exempt income or non-taxed

income. Strictly the provisions of the old section 160ZM would apply to require that amount to be taken off the cost base of the beneficiary in his or her interest in the trust.

That income has been taxed fully, in fact, taxed at a penal rate to the trustee. It just was not taxed again to the beneficiary. It would be very unfair to require the beneficiary to now reduce his or her cost base in the trust by the amount which represents the after tax proceeds of income which has been heavily taxed to the trustee.It is just one of those quirks that has been there. I would imagine that the commissioner has never taken the point, but this is an ideal time to stop having to rely on some proper—what's the word I want?—

Mr Gaylard—Concessional construction.

Mr Magney—Concessional construction by the commission. It is quite clear in black and white that, if it has been taxed in the trust—whether to the beneficiary or to the trustee—it should not go in a reduction of cost base.

Senator WATSON—Would that apply to all elements of taxation or just to the penal rates such as in the 99A case?

Mr Magney—The case I had in mind was that that I have just described, which comes under 99A. But it could possibly be argued that under other provisions—98A and various other provisions—where the trustee is taxed on behalf of the beneficiary indeed the beneficiary again is not being taxed, that is, in the case of an infant beneficiary, for example, where the trustee is taxed on the income of the beneficiary.

Mr Gaylard—I think it is held on a separate trust, though.

Mr Magney—That is held on a separate trust. Yes, there are other instances over and above 99A where it could apply but 99A was the most significant of those, I suppose, inasmuch as the tax income is taxed at a penal rate in the hands of the trustee.

Mr Gaylard—And it is the section that most normally applies where there is undistributed trust income—in fact always.

Mr Magney—The other part to this was—

Senator WATSON—Can we get a response from the tax office on that, because I think the committee would be interested?

Mr Burge—It is important to recognise that the suggestion would involve a change to the effect of the existing law. The existing provision, section 160ZM does very much focus on whether the amount is not assessable income of the taxpayer. The opening words of section 160ZM are:

Where the trustee of a trust pays an amount to a taxpayer that is not assessable income of the taxpayer . . .

In the rewrite, we have conveyed the same effect by paragraph (b) of subsection (1) in section 104-70 as 'some or all of the payment is not included in your assessable income'. So the important point is that it would be a change to the effect of the existing law. The government's preference is that all matters relating to trusts be dealt with in a general way as part of the trust's review and, for that reason, we would not be proposing a change in this area.

Senator WATSON—We are going to have some problems here, aren't we, with trusts?

CHAIR—Disposal by beneficiary of capital interest?

Mr Morgan—I think Mr Magney was well aware that it involved a policy change when he was making the suggestion, and there has been some discussion about policy change already this morning.

Mr Burge—I thought it was important to emphasise, for the benefit of everybody present, that it does involve a change to the existing law. It is the case that in some areas, in a number of areas, the rewrite does propose changes of a minor nature to the effect of the law, but we have made clear that in the area of trusts the trust review precludes us from making changes of this sort.

Mr Magney—I would have thought that this does not really impinge so much on the changes that are being made to trusts as on capital gains tax. I think John is coming at it from the other angle. Yes, I was aware that it was a change of policy, because I thought that, probably by inadvertence, nobody thought of this peculiar situation under 99A when the original provisions were drafted. I thought, 'Now is a chance to correct this.' If it does involve capital 'p' policy, it ought to be referred to the government. But I do not think it requires you to change anything in the law of trusts; it just requires you to recognise that a beneficiary can in effect have paid tax on trust income, even though that income is not included in the beneficiary's assessable income if that very income has been assessed to the trustee. That was my point, but I will not labour it. I would suggest it is something that should at least be looked at.

Mr Gaylard—I think the trust project is more interested in making sure that income is taxed once rather than not at all. This is being taxed at 47 per cent and potentially taxed again or at least serves to reduce the cost base of the asset so that it can be subject to tax at some stage in the future, so I cannot see any good reason not to make that change, I must say.

Mr Morgan—The review of trusts manifests itself in different ways. It has not

stopped the rewrite of the capital gains tax provisions that do touch on trusts nor, I think, is it really stopping the rewrite of certain international provisions that also involve trusts. On the other hand, it has somehow prevented moving forward on the principal trust provision—division 6 of part 3 of the old act. It is interesting, as I said, how it manifests the embargo and manifests itself in different ways at different times.

Mr Nolan—I do not know what inference is to be drawn from that proposition, but—

Mr Morgan—It is clear that the rewrite of the international provisions, for example, has still got a long way to go; it is proceeding ahead with the rewrite. I think that is not to the point of the immediate discussion. But generally there is a real difficulty with bringing forward suggestions for changes in the area of trusts when the government has a major review on. It is about as simple as that, really.

Ms Freshwater—The draft of the rewritten CGT provisions relating to trusts was exposed before the trust embargo was put in place.

Mr Nolan—But essentially those are just a rewrite. We are sticking to the rewriting of the capital gains tax provisions that touch on trusts.

CHAIR—Would it make sense to bring this issue to the attention of whoever in Treasury is working on those issues?

Senator WATSON—I think it has got to be in our report, Mr Chairman.

CHAIR—In what?

Senator WATSON—To the parliament.

CHAIR—In our report?

Senator WATSON—Yes. There is inevitably a difficulty in terms of the rewrite because of the embargo that has subsequently been placed upon it.

Prof. Krever—To put it more accurately, there is a possible perception that there may be a difficulty in this particular case because, as has been pointed out, it was never the intention of the old act to tax the same income twice in two people's hands. Because of a technical flaw in the initial drafting it could have happened. All we have suggested is that now is a good time to fix up what was never intended—to fix up a technical flaw. If there are later policy changes as a result of the trust review, this will not have any effect on them at all.

CHAIR—To the best of your knowledge, nobody has ever been caught by this?

Prof. Krever—That is to the best of my knowledge, and I have not heard of anybody else.

CHAIR—I suggest that, as we have pretty well exhausted this one, we move on or we are going to run out of time.

Mr Magney—Mr Chairman, if you want me to speak to paragraph (b) under that heading: that was merely a suggestion on my part that, having read section 104-70, I did have trouble seeing exactly how it was meant to work. I think I understood it, but it was by no means leaping at me from the page. I guess that, as this was supposed to make it simpler for the ordinary reader, at least some examples would be helpful to show what the drafter had in mind. It is a provision that attracted some criticism when it was first drafted. It has been rejigged, but I still had trouble with it. That might just be my limitations, but I guess if I had trouble it is likely someone else did.

Mr Harders—Again, in reviewing the explanatory material that we are going to put into the bill, we can consider putting examples into that section.

Senator WATSON—How can you put examples in if the law itself is not clear? You cannot put examples in that are not in conformity with the rewritten law.

Ms Freshwater—This specific issue is related to timing is it not? I think we can make an example of that.

Mr Burge—I think the point is that the effect of the law is clear. It is legally effective. The inclusion of an example would just make it easier to grasp.

Mr Magney—I think a 'not' has been left out. It is as simple as that. As I have a habit of misreading, I went back and read these provisions many times, and this seems to say the exact opposite of what the 1936 act said. The 1936 act required that the beneficiary not have given any consideration for acquiring his or her interest and not have acquired that interest by assignment. Unless, as I say, I have perpetuated my habit of misreading, this one requires the beneficiary not to have given any consideration but to have acquired it by assignment. I think it should read, 'that the beneficiary did not acquire his or her interest by assignment.' I thought it was as simple as that. The existing section is 160ZX, is it not?

Ms Freshwater—I think the existing provision is 160ZYB.

Mr Harders—Yes, that seems to be a mistake, which we should fix.

CHAIR—Well done, Tom, you are on a real roll.

Mr Magney—I did find 104, 225, sub-section 4 a little difficult to grasp when I

first came across it. I went back and looked at the 1936 act in the same context. Also, when I read on down in the provision, lights started to shine in darkness when I got to the little bit at the bottom of 225 where it says, 'Note, the capital proceeds for the event are replaced with the market value.' Then I started to see what being replaced meant. But I am conceited enough to work on the basis that, if I, after 30 years of trying to master tax law, get confused along the line, someone else also might get confused, especially if that person is not a specialist. It seemed to me that the drafting there might be changed or varied slightly so that the meaning of 'being replaced by' becomes obvious before you get to the note after paragraph C.

Mr Harders—Could we take that one on board? I think Tom has a point there as well.

CHAIR—A score of two.

Mr Magney—I passed.

CHAIR—By golly, this does not sound like what we started out with this morning. I just make the point.

Mr BEDDALL—I think this is exactly what we started out with. It is proving the point.

Senator WATSON—This is part of the process.

CHAIR—I want to point out to ASCPA that this committee is good at getting people together.

Mr Langford-Brown—I would like to record in *Hansard* what is described is a series of undisclosed changes in a submission from Deloitte Touche Tohmatsu. I do not wish to debate them at any length, but I ask the committee or the TLIP team to revisit those particular issues, which are spelt out in some very good detail on pages S. 360 through to S. 366.

CHAIR—We will move on to division 118—exemptions.

Prof. Krever—This is a general comment on the structure of the exemptions. The Australian capital gains provisions have been designed as a discrete set of rules attached to the Income Tax Assessment Act rather than fully incorporated into that. That leaves the possibility that gains can be assessed twice: once under the capital gains provisions and once under the ordinary provisions of the income tax law. We have attempted to prevent that through a general reconciliation provision in the former and the current laws. The general reconciliation provision, which is now 118-20, said, 'If a disposal that is caught under capital gains is also caught under another part of the act, it is only taxed once under

the other part of the act.' Under 118-20, we now say that it should be, 'If a transaction that leads to an event causes a tax liability under the capital gains and the other provisions, you are only taxed once.'

A problem with the former provision, which has been replicated in the current provision, is that often transactions which give rise to a disposal under the old system, or a CGT event under the proposed law, can lead to a tax liability under the non-capital gains provisions, but not as a result of a particular transaction. I will give an example: if you buy a government T bill, or a deeply discounted debenture or bond, we have provisions in the old law still in existence that say the gain from your purchase price to the price when the government, or whoever the borrower happens to be, redeems it will be assessed to you as if you were receiving compound interest over the life of the debenture. So you are taxed on this gain, but you are not taxed as a result of the disposal when they eventually redeem the thing, you are taxed because of other provisions in the legislation. The double counting provision does not operate in that particular situation. It does not operate in any situation where you are assessed under provisions of the act other than because of an actual disposal or CGT event.

CHAIR—Does that lead to a real double tax?

Prof. Krever—It could lead to it if the commissioner were so inclined to use it. So far he has not. But I think, as a general proposition, we would feel more comfortable with a law that precludes the possibility of double taxation rather than one that relies on the commissioner's discretion. For example, it could happen over different years and when a person is audited 10 years afterwards the auditor may not realise that this person has been paying tax in the past.

The reason this particular provision operates in the way it does is that the old one also operated that way. It was a defect in the old act. This is clearly a small policy change, although the policy change is not one that counteracts anything the government ever intended; it was simply an unintentional oversight the first time around.

Mr Burge—It is an issue of which we are aware. As Rick has mentioned, there is the same difficulty in the 1936 act. The difficulty was to come up with a form of words which still had a sufficient nexus to the capital gain, and that has so far proved elusive. The ATO does give a practical and sensible interpretation to ensure that there is no double taxation. It is something that we are prepared to look at further, but the solution to the difficulty is not immediately apparent.

Prof. Krever—Perhaps we will communicate further with the TLIP team. I am sure that we can come up with some words which will solve the technical problem.

Mr Burge—Any suggested wording would be most welcome.

CHAIR—I was going to encourage you to do that, well done. Anything else on 118?

Mr Bryant—I refer you to the new section 118-25 dealing with trading stock. The proposition that I put is that what is now presented is perhaps not totally unheralded but is certainly a change in what was there before. There are two aspects. One is that we would prefer that the old words be retained. The other one is a matter of process as to how such a change could come about. I will just explain it briefly by saying that the objective of this provision is to take outside of the CGT arena disposals of trading stock. The old section 160L subsection 3 says that this part—meaning the whole of part IIIA—in its totality will not apply in respect of the disposal of an item of trading stock. There has been quite a shift in meaning here because this is a much reduced scope. What this now says is that a capital gain or loss from disposing of trading stocks shall be disregarded.

It does come up in the context of transfers particularly between related companies where we get into the value shifting rules in division 138. I refer you to page 171 of the explanatory memorandum. We have a recognition that there is a shift of meaning here, potentially, and there are two competing views. If I take you through that briefly, it is awkward in the sense that it takes us into division 138, and I do not want to specifically deal with that. In the explanation in the second sentence, it refers to section 118-25 which seeks to achieve a certain result. Further down it says 'but an alternative view is available'. The very last sentence of that section says that the 'rewrite reflects the ATO's interpretation of the existing law'. I question what the authority is for that decision-making process and it does have a significant impact in the value shifting rules. Firstly, I say that we do not have a faithful rewrite of the existing law. Secondly, I say that the process whereby that has been delivered has been made, as I see it, as a decision within the TLIP team without any further testing.

Mr Burge—One of the approaches that we have taken in the rewrite of the capital gains tax provisions is to have a standardised approach to the conferring of exemptions. In the old law, exemptions were conferred by a great many ways. Cars were exempted by excluding them from the definition of assets. Trading stock was exempted by providing that part IIIA did not apply to it. Other exemptions relied on providing that a capital gain or capital loss did not arise. Yet other provisions—for example, assets held for the purpose of only producing exempt income—were exempted as part of the calculation method of capital gains. We wanted to have a standard approach. It does promote understanding of the law to have that.

The interpretation of the exemption for trading stock is provided for in existing section 160L. It provides that this part does not apply to a disposal of trading stock. That provision's words do contemplate that the part does not apply to a disposal of trading stock. It does not prevent other consequences such as cost base adjustments in existing division 19A or division 138 from applying. Our view is that we have maintained the effect of the existing law in this area. Certainly from a policy perspective that is an

appropriate result.

We acknowledge that it would be possible to construe the provision differently, that we have, in fact, clarified the law, in rewriting the CGT law, in a way to make its meaning clear. It is inevitable that at times clarifications will be made, and this is one of those occasions. We have included the clarification of the law in the explanatory memorandum, as Bob Bryant has pointed us to.

Mr Bryant—There are two points to be made. The explanation highlights the two competing views. I am saying that the tax office has chosen that they be the one to make the tie-breaker decision, and I am not convinced that that is an appropriate way of resolving a tension of this type.

Further, I suggest that all that John has said is not quite correct in the sense that in section 160ZZO this question of excluding trading stock does come up. It does it in a manner that is quite explicit. It says that the transfer of trading stock will be excluded for the purposes of this act other than for division 19A.

In this particular context, the section we start with, 160L, which is the existing law, does not give that clarity. In fact, the alternative view as put here is one I understand is held commonly within the tax profession. In fact, the view that is now being put in this document, which is attributed to the tax office, is not one, to my knowledge, that has any public recognition or publicity.

I am saying two things. The rewrite is not faithful to the old. More importantly, it is an example of a process whereby when a tension of this type has arisen it is left to the TLIP team to make the final decision. I do not think it is good enough. In our view, in this context it works to the detriment of taxpayers.

CHAIR—Bob, how would you, in your ideal world, propose to resolve such an impasse?

Mr Bryant—When you get a situation like this, at least there is a fall-back. If you do not have an adequate process to get testing of this, you should not shift from the original words.

Senator WATSON—That is why we have private sector representatives on the TLIP team.

Mr Nolan—In the end, there are many instances where you have to make a judgment about what words you should use to express the law. John Burge has been saying that we have reached a view about what the scope of the law is. We are not saying that we have adopted the ATO view because it is the ATO view; we have said in the

explanatory memorandum that the position we have taken happens to be the ATO view. We have independently looked at this to reach our conclusion about what the appropriate outcome is in terms of both what the existing law says and whether that accords with the policy intention.

CHAIR—We note your concern, Mr Nolan.

Senator WATSON—Were the private sector representatives happy with this outcome?

Mr Gaylard—Senator, when you mentioned that before, I must admit I thought about the answer I am going to give. It is not right to see changes like this in absolute isolation. For every one of these, I believe there are a large number that have gone the other way. One issue we were talking about a little while ago that I would like to see go the clarification way is the 160ZM issue—the return of capital to make sure that we do not get a double taxing.

There are a number of issues that have been clarified in the way that the taxpayers want it. I cannot remember looking at this particular one that closely, but the position that has been taken seems to me to be a reasonable view. I am not aware, either way, of whether the public companies and the like think that the other view is the correct view.

On that particular point, I must say that I have not had a large input. What I have been very concerned about is looking at the totality of things that have been done to make sure that I think there is a balance, and I think the balance really goes the taxpayers' way overall. From that point of view I am not so worried but I am happy to look further at that particular issue if it needs it.

Mr Burge—Bob Bryant raised the issue of whether there are others outside the ATO who take the view of the ATO on this issue. I would like to have on the record that the *Australian Taxation Practice* CGT loose-leaf service commentary on division 19A, which is to be replaced by division 138 in this bill, records the view that transfers of trading stock at undervalue do give rise to cost base adjustments under that division.

Mr Bryant—I still stand by what I have said. It is quite clear that there is a different expression now and a different meaning—it seems to me to be without authority. Might I add that the fleshing out of this explanation on page 171, to my knowledge, did not appear in the earlier versions of exposure draft material. I would suggest it is possible that it has been here to defend the position that has already been taken.

But I say again at least there is a fall back. We had it with the mining provisions at an earlier hearing, and there was some resolution of that in the taxpayers' favour. When you get attention of this type, I believe that the project should have no authority to do other than to go to the government and promote this as a change and get government

approval for that. I am not aware that that has happened and there is no evidence to suggest that that has happened. Alternatively you stay with the existing words of the statute or otherwise it is unfair.

CHAIR—The committee notes your concern. We will turn now to division 138.

Mr Bryant—I have one comment about 138. I think it is no better—in fact, it is possibly worse—in terms of the way it is expressed compared to the original legislation in the 1936 act, which itself is largely unintelligible. We have made representations that a better attempt should be made at rewriting this particular area of the value shifting rules. I have not yet had any response to that proposition.

Mr Burge—I would be pleased to respond to that suggestion of Bob Bryant's. We believe that the rewrite of division 138 does represent an improvement on the existing law. Reading the two side by side, I think that you do have to come to that conclusion. That said, we acknowledge that there may well be scope for further improvements in its expression and structure. We are sympathetic to reviewing the wording and structure to ensure that we have the best possible product.

CHAIR—Do the private sector representatives on TLIP have any comment?

Prof. Deutsch—Yes, if I could look at division 138 and division 140 together, I must say that I share some sympathy with what Mr Bryant has said, because having read them together I am almost a little bit concerned that we have not made any significant improvement on the original. In one sense at least they both deal with value shifting, which they talk about, and, as we have just seen, there are other areas which also touch on value shifting issues.

To try and make a constructive comment rather than just a general glib one: the way that I view a lot of these provisions in making them more user-friendly is that sometimes you need, in a sense, to draft in the negative by saying when these divisions will have no application. Those of you who have been working on the international will know that this is a sort of favourite of mine with the international because I want to knock out people to whom complex divisions are not relevant. One of the strategies that may be useful—I would like to hear some comment on this—in both 138 and 140 is that in the boxed section at the beginning it might be useful to try and develop a statement of the negative: when do you not have to deal with the issues raised by division 138 and 140? I would like to find out whether anybody thinks there is any value in that and whether it would enhance the drafting.

CHAIR—Does anyone have any comments?

Mr Nolan—The square-boxed introductory material to division 138 could stand some improvement. But in saying that we also would need to bear in mind that it is part

of guide material. We would not want to put all of our eggs in that basket if what is required is to give greater clarity. We will certainly try to improve the clarity there, but there are things that can be done in division 138 itself—without being major reconstructions of the division—which, I agree with John, is an improvement on the existing law. Read that, if you dare. We are quite keen to take on further examination of that division.

CHAIR—Mr Bryant, have you made any suggestion as to particular words?

Mr Bryant—No, we have not got to that stage as yet, but I would be more than happy to organise some input on that. I might add that this is a very significant body of the law, because we have a number of major public companies in this country which are looking to rationalise their groups and, because of the unworkable features of these provisions, are left with totally unwieldy provisions that would cost them an arm and a leg to simplify their corporate structures. I am aware of a number of companies that cannot liquidate subsidiaries and so on, because of enormous compliance demands and unreasonable features. Some of it goes perhaps to the small 'p' elements of this too. But there are two requirements: one is better writing of the law—and we would happy to assist with that—and some revision of some of the design features; they are really restricting a lot of companies from tidying up their organisations.

CHAIR—Are the design features very minor non-cost policy or are they—

Mr Bryant—We have explored some with modest success. I would like to take that on board and promote that in a more formal manner. We have not done that yet.

Senator WATSON—I am quite interested in Professor Deutsch's approach, but I still think you would need, in addition to what it does not include, to have the positive it is designed to overcome. I would not mind after that positive statement: 'However, it is not intended to . . . ' and then use your negatives there. I do not think I would like to just put the whole lot in the negative because I think the whole purpose is: what is the purpose of the division? It is to do something. However, it is not designed to do that. My recommendation is to try to pick up both aspects of it actually. Yours is a secondary one and I still think you need that first positive direction statement.

Prof. Deutsch—I do not disagree with that. I am not saying that we have got to make it all negative, but it appears to me that, to address some of the concerns that Mr Bryant has expressed, you might be able to develop a section which can be kept reasonably brief and which indicates to taxpayers when they do not have to worry about it. At the moment, it just strikes me that what happens with a division like this is that you have to go through a complex tangle to sometimes find out at the end of the day that you have not got a problem. That is very frustrating for taxpayers. In a way, it is much better to be able to try to do that up-front. I am not sure that it can be done, I am just flagging it as a possibility.

If I could add one other thing. There is a map that is very useful at the start of division 140. I am wondering whether there may be some possibility of having something similar at the beginning of division 138. I have not actually thought that through in terms of: this is the map of 104-5. That is very useful and it helps you to understand what the thing is about. Whether something like that could be developed for 138, I am not sure, but I would be interested.

Mr Harders—We are looking at including some diagrams at the start of 138 as explanatory material.

Mr Burge—Because Professor Deutsch has referred to the map at the beginning of division 140—it is on page 356 of the bill—I would like to draw attention to how we have tried to pick up the sort of suggestion that he has made. At the consultation meetings that we held after the release of exposure draft No. 11, we were asked to make it clear right upfront that division 140 basically applies to associates or to pre-CGT shares. In the relevant boxes, we added the words: 'But only if value is shifted to shares owned by an associate of the entity (or, in certain circumstances, shares owned by an associate of an associate . . .)' The corresponding box talks about pre-CGT shares. But there is an example of, as a result of a useful suggestion made at consultation meetings, where we did make a change to deal with the concern.

Prof. Deutsch—Can I also mention one other thing? I know that this may be obvious, but I wonder whether in 138-21 at page 328: 'You will not have to make an adjustment in these cases': (a), (b), (c). The word 'these' hints that they are alternatives, but I wonder whether we need to see 'or' between them. At the moment, if you look at it very quickly you may think that that is a cumulative provision. It clearly is not. But at the moment there is no 'or' and 'and'.

Mr Harders—There has been a drafting tradition for some time not to include any link word between paragraphs that are preceded by the word 'following': like 'any of the following' and then a list of paragraphs with no link. We had actually translated that into this format as well, so that where we say 'these cases', we have omitted link words. If that is proving to be unclear to people I am sure we can have a look at it.

Prof. Deutsch—It is not a huge issue for me, but I just read it very quickly the other day and all of sudden I thought, 'Do they mean 'and' or 'or'? Of course, when you read it more slowly you very quickly realise they are talking these cases, so it must be alternatives.

Mr Reid—'Any of these cases' would be better.

Prof. Deutsch—In the event, it is a minor point. It just struck me that it was a touch confusing.

CHAIR—Anything else on 138? Are there any questions on 140—Share Value Shifting?

Mr Magney—I was surprised to hear Bob say that he did not think 140 was any improvement on the original provisions. Because I slaved through those original provisions when writing a chapter for a book and trying to work out where you got to and how you got there half-killed me. I was very pleased to see here that they have got examples. If the original provisions had had these examples that kept taking you through cases and showing you what the draftsperson had in mind, it would have been enormously helpful to me three or four years ago.

For my money, I think that is a marked improvement and the setting out is better. I do not say that it is perfect, but to me these did read a lot more simply than the original ones. I would like to say that in that respect I beg to differ from Bob.

CHAIR—Does TLIP accept those comments?

Mr Burge—We are delighted to accept them.

CHAIR—Is there anything else on 140? Number 373 is intellectual property.

Mr Parker—Before we go on to capital gains, can I raise one matter concerning death in division 128? I have been very quiet on capital gains. This concerns death and 128(15). The legislation is on page 293 and the EM is on pages 141 and 142. Page 142 on the EM highlights that there has been a change in the way in which the legislation has been written. It has endeavoured to overcome the lack of symmetry between the old section 37 of the 1936 act which talked about trading stock. The best example was a father who owned shares as a share trader and he died. In section 37 death deemed the disposal to take place at market value.

However, an election was available and, if the trustee of the estate carried on the business, he could elect cost. Any profit on the deemed disposal of the share trading was deferred to a later date. If the trustee or the son did not carry on business, the election was not available. So the disposal was clearly at market value and taxed emerged in the return to date of death.

When you look at the CGT provisions, because there was no symmetry, 160X said that the asset was acquired at cost or indexed cost base. For some years the tax office grappled with what was the correct approach in the return to date of death in the estate. Is it cost or market value? You might recall that it was too difficult. In the rewrite you now have clearly defined the exercise and the solution. I do not have a problem with that, but, in doing so, in the last two sentences of the EM you have identified that there could be in some case an injustice to other taxpayers.

I wonder whether that is clearly a small ‘p’. We have attempted to solve the problem. It can occur where the market value may have gone up or down since the date of death. You may therefore have a profit at date of death on a deemed disposal and a capital loss which is not recoverable in any way in the estate at a later date.

It seems to me that, in endeavouring to solve one problem, which you have, you have potentially left open the other one which does require a small policy attention. It is a common problem. There are plenty of share traders out there—the mums and dads of this world—and when they pass on, their sons or daughters may not as trustees carry on that role as a share trader. So, the election process is not available, there is a disposal at market value and there is an acquisition by the estate at market value. Then, when that disposal takes place by the estate or sale by the trustee, there may be a capital loss which is quarantined and not distributable in some cases. So the Commissioner of Taxation ends up with a tax on a gain that was not real, but was notional because of death. I commend it to them.

Mr Burge—We were concerned to establish a general principle and that is that the value for capital gains tax purposes should be the same as that for trading stock purposes. The application of that general principle gives the result that we have here. We believe the change to be appropriate. Overwhelmingly, the change will favour taxpayers because you would expect the value of the assets to increase and that the market value would be higher than the cost base.

CHAIR—Not necessarily.

Mr Burge—Not necessarily, I agree, Mr Chairman, but in the circumstances in which it was lower, the same treatment should apply. The value that is assessed for trading stock purposes, if it has been trading stock, is the appropriate opening value for CGT purposes.

CHAIR—I suggest that a lot of people who bought shares in the market in 1993 and died in 1994 or 1995 would have incurred a capital loss in their estate.

Mr Burge—I accept that, but once you accept that the principle is valid for those cases where the market value is higher than the cost base, then it is equally valid in those cases where the market value is lower than the cost base.

Mr Parker—There is no doubt that the rewritten law has endeavoured to come to a solution where the previous act lacked any symmetry at all and the tax office was not in a position to provide any final clear-cut answer.

CHAIR—Is this a big ‘P’ policy change?

Mr Parker—No, I think it is probably in the area somewhere between small and

big. It is not big'P'; it is small 'p' policy. But it is not uncommon to have individual taxpayers as share traders. The question of whether, in terms of moral justice at the end of the day, if dad had not died and had disposed of them, then the realisation of that lower value or whatever would have brought to account tax on the actual profit. You are actually taxing a deemed profit in the event of death—

CHAIR—When dad dies, if dad had one son or daughter and left all the stock to them, there is no reason why they could not trade it, is there?

Mr Parker—There is no reason why they could not, but that would not be share trade. If there is a share trading situation continuing, then you do not have a problem.

CHAIR—You mean they may wish to dispose of the stock?

Mr Parker—Yes. But if they dispose of it as an asset in a non-trading capacity, then there is potential for injustice, for inequity.

Mr Nolan—This may be one of those issues that the consultative committee would like to put on its list of propositions to the Assistant Treasurer.

Mr Droder—That sounds all right to me. Was that the Harry Hattersley business?

Mr Parker—The old share trader and dad dying thing.

Mr Droder—Yes, it was Harry Hattersley, the golfer who carked it when Poseidon hit the top.

Mr Parker—I just wanted to state that they have tried to solve the problem, but in doing so they have created another problem.

CHAIR—It is not an issue that you want us to address?

Mr Parker—I do not think you can.

CHAIR—We move to 373, on intellectual property.

Mr Droder—This is mine, and I am not sure that I am going to make a big issue about this. I notice that Bob has made a submission anyway, so he can probably talk a little more authoritatively than I. I was looking through there and I came to section 373-90. It talks about the allocation of the cost of intellectual property being used overseas to generate income. While it is very clear, I think it would be helpful to people—and other people have said to me that it would be helpful—if there were some guiding lights as to how that allocation might be made. Whether that should be contained in the act is another question.

‘

The second point is that this committee, way back at the start of this, really felt very strongly that anything that was capital and had capital allowances should be incorporated in the depreciation provisions. I was thinking about that when I went through and read the write-offs that are allowable on petty patents, which is a new thing, which is a six-year write-off; a registered design, which is 16 years; and a patent, which has now been extended from 16 years to 20 years. I was saying to myself, a bit like Joycelyn was saying earlier, ‘Is that a proper way of matching the depreciation of a patent or a copyright against the market?’

The picture I have in my mind is that a patent probably increases with value very quickly and then declines over a gradual time as more competitors come in with alternative products. So I was saying to myself, ‘Why does this provision not carry the written-down value incentive or ability to do that with this one, which is definitely a capital asset, no different in my view to any other depreciable asset? Why is it not parallel and equal to it?’ Bob’s paper talks about another issue, which is the unidentifiable intangible assets. I am not quite sure what the solution is to that.

Having made that point, my third item arose when I started reading at page 440. I kept reading about unrecouped expenditure on patents, intellectual property and whatever. It took me to page 456 before all of a sudden ‘written down value’ came out of the woodwork. I am afraid I cannot understand where written down value comes from, why it is there, why it was used or what impact it has.

Mr Reid—I think some of my colleagues might be grinning when they hear Stan’s remarks because that same proposition was put to me a number of times during the drafting. It was pointed out earlier by Stan and previously by Joycelyn that it is very desirable, so far as possible, to standardise the treatment of capital allowances. Unfortunately, the policy constraints under which we are operating have meant that we have not been able to rationalise the treatment of capital write-offs as much as we would have liked.

One respect in which we have made the treatment standard is by providing a common form of provision for the calculation of balancing adjustments. That depends on basically comparing what is called the written down value of the property with its termination value. The purpose of relating the concept of recouped expenditure to written down value was so that intellectual property would be treated in a similar way to the other capital allowances in respect of calculating balancing adjustments.

Mr Droder—I just kept reading it line by line trying to understand it. When I came to page 456 all of sudden there was mention of ‘written down value’ and I said, ‘Where did that come from?’ It is something that escaped my knowledge. I went back and read it again and I still could not find it again. I understand why he would use the expression ‘written down value’ but, on the other hand, the expression all through the

legislation is 'unrecouped expenditure', which I understand to mean expenditure on a patent or intellectual property that has not been claimed previously as a tax deduction. It seems to me that the expressions are synonymous.

Mr Reid—Not quite. The written down value is the unrecouped expenditure at a particular point, which is where you make the balancing adjustment. As I have said, we use the concept of unrecouped expenditure for one purpose and the concept of written down value for a different purpose. It so happens that, at the point at which you make the translation, their content is synonymous, but I am not sure why that is a problem. Are you saying that it is not easy to find the definition of written down value because it is asterisked like all the other definitions.

CHAIR—I probably have no right to comment, but I am with him. That is confusing. Written down value means that you had an initial capital value of a good and at any point in the depreciation cycle that is what is left on the books. When you are talking about intellectual property it is what you spent to develop the property which may continue to grow over time. You do not just get a patent and that is the end of it. I would say to you, Stan, that with some intellectual property it is fair to say that it continues to escalate in real value and at some point in time it disappears to almost zero instantly overnight. I will give you an example of drugs. If you take Amtac, which 'Galaxil losses' this year, it has been worth a fortune to them and then all of a sudden everything in the world will compete with it.

Mr Droder—I guess it is a policy issue, but it did strike me that it would be an improvement if the taxpayer had the ability to go to the commissioner and say that the life while it might be legally 20 years is in reality not and be allowed to convince him that it is different.

CHAIR—That is big policy.

Mr Droder—I might raise that as well. I should conclude by saying also that I found it fairly easy to read, except from his putting a shaft into me.

Senator WATSON—Can I ask Bob Bryant a question on his recent submission in relation to intellectual property. There you raised the problem of bundled intellectual property rights, and in some instances it is not possible to unbundle them. You do not appear to have given us a solution.

Mr Bryant—The proposition is to frame the law in such a way that, if what you are talking about comes within the broader definition of what we are focusing on here, which is copyright material, patents and material of that type, you should not be caused to be stuck with a precise identification of a specific right. There can be licence arrangements which involve more than one specific right and the law is a little bit awkward around that. It is only a clarification as a sort of compliance. At the moment the

taxpayer has got to identify the specific rights. I think the law is written in that fashion; it sticks with a specific identifiable—

Senator WATSON—If you cannot unbundle them, how can you know what component belongs to each?

Mr Bryant—I think you can unbundle them to the extent that you can identify from the licence agreement, for example, the characteristics of what is there and what is underlying all of that. The question is you do not have a capacity to allocate values to each component. It is not dealt with in that manner. It does cause a problem for some taxpayers.

Miss Haly—This issue which Bob has raised is one which we considered to be a big policy issue with revenue implications. The difficulty is that the approach would require us to expand the scope of the capital allowances to include all forms of intellectual property, such as trademarks, plant variety types, circuit layouts et cetera, and those particular types of intellectual property are not now within the capital allowance. So it was simply outside our terms of reference. I think in the submission which I was given a copy of today from Bob it is acknowledged that what is being proposed is extending the regime to intellectual property rights which are not within it at the moment.

CHAIR—You are saying those other items are simply expense items.

Miss Haly—I am not sure that is right.

CHAIR—Well, it has got to be one or the other.

Miss Haly—They are outside the division.

Mr Bryant—I think the point is that they are items for which no tax deduction can be obtained at all.

Senator WATSON—Such as plant variety rights.

Mr Bryant—That is the real point to this issue. If you take the view that is being put, that is quite possible under the existing law. So we have got one of these so-called black holes.

CHAIR—Are you saying that if I either spend the money—

Mr Bryant—I am talking about a capital outlay. By definition, we are only about expenditures which are of a capital nature.

CHAIR—Okay, but there are two ways to go about plant variety rights. I develop

the plant, spend the money to get my lawyer to get the rights assigned, describe the plant and its characteristics, advertise it and all the rest and accumulate that amount of money. I either call it capital or I expense it—and if it were me I would rather expense it. Or I buy the right from somebody else, which again is a sum which, if it is not capital, then expense it. You are saying you cannot expense it.

Mr Bryant—Not in this category, no.

CHAIR—No, I am not talking about capital gains but for income tax purposes.

Mr Bryant—In this category of intellectual property, there are examples of this. To come within this it cannot be expensed. It is not a revenue type item, it is a capital item. It is an intangible that you are acquiring. What we are saying is that these provisions are too narrow. It is a policy question; I hear that. But we are saying that through this committee there ought to be an opportunity of having this brought to the attention of government, if it cannot be dealt with in the TLIP process.

CHAIR—I must admit you do surprise me. I have got numbers of horticulturists in my own electorate and not one of them has come to me and said, 'Hey, I can neither expense nor depreciate plant variety right expenditure.'

Miss Haly—There is a horticultural plants regime as well as the one for intellectual property.

Mr Bryant—We are talking here now more about outside that horticultural area. Probably your colleagues have not had tax audits, perhaps; I do not know. There may be a surprise waiting!

CHAIR—Who's here from the ATO? Leave them alone!

Senator WATSON—Is it really a question that the law has not caught up with modern technological developments? Is that the issue?

Mr Bryant—That is the issue on both points we are making.

Senator WATSON—Okay. Could you therefore give the committee those areas where the law has not caught up with modern technological developments in the area of licence agreements or whatever it might be?

Mr Bryant—Yes, I will do that.

Senator WATSON—Thank you.

Miss Haly—We have, where we could within our terms of reference, addressed

gaps in the law, such as recognising for the first time petty patents. In relation to what we are talking about here, the magnitude of this is such that it is big policy and outside our terms of reference.

Senator WATSON—But, again, this is what the committee should be aware of. If there are defects in the law, there should be a mechanism for reporting it to government to ensure that any injustices as a result of modern technological developments are somehow picked up by tax law.

Miss Haly—This issue is identified in the compendium prepared on this particular area as something which has been raised along with the details of the people who raised it and what the position is. So it is very clearly flagged.

Senator WATSON—But the committee needs to be aware of it.

Mr Gaylard—There is an enormous area where you can incur very large amounts of expenditure for projects that do not go ahead. That expenditure may not be deductible in any way, shape or form. There are literally hundreds and hundreds and hundreds of millions of dollar tied up in exercises like that. You are not talking about just ordinary policy area there, you are talking massive tax—

Senator WATSON—I regard that as a separate category from the issues that Bob Bryant has raised.

Prof. Krever—I do not know whether you want to follow this point through—I am not sure whether it is a separate category—but it is indicative of a general problem that we have with the legislation anyway; it is a problem with the Australian Income Tax Act which no other country suffers from. When we came up with our concepts of what is a revenue expense we looked at certain indicia, such as regularity and so forth, and we allowed deductions for certain expenses. If you bought a long-term benefit, we said that you can amortise it or depreciate it under a provision. But our provision happens to be the narrowest in the world, so it applies to only plant and equipment.

Over the years we have added other categories for certain types of intellectual property, or horticultural plants or whatever. But since we have done it by a category by category basis we have never brought in a general amortisation regime. There still are an enormous number of expenses that clearly have a limited life; indeed they might have an almost instantaneous life and then be worthless. But they do not quite fit into any of the regimes, so we just do not recognise them for tax purposes and they are called nothings. Other countries have brought in a general amortisation regime for these expenses. It would be a mistake to fix it at horticultural plants or with intellectual property, because it is a major problem with our act generally.

Miss Haly—The revenue implications are very big.

Senator WATSON—But that does not mean to say that somebody should not be looking at it.

Miss Haly—No; it is just that we could not look at it within the terms of our project.

Mr Droder—For example, if somebody bought the rights to Coca-Cola, the formula for Coca-Cola, they would not get a tax deduction for that in any way; it would just be a capital outgoing. There is argument whether they should or should not, but currently they do not.

Prof. Krever—There is a category of expenditures that may buy you a long long-term benefit, so long that you would give it a deduction or depreciate—for example, if you bought the name Coca-Cola, the formula, presuming it lasts forever, until something dramatic happens. But it happens all the time that a drug company spends an enormous amount of money to stop a competitor from marketing something that is basically the same. They spend that money. We call it a capital expense. The benefit is gone immediately because another drug company could come in tomorrow with another one. We call it a capital expense. It does not fit into our capital loss provisions. It does not fit into any of our depreciation provisions. They have spent the money and it is never recognised for tax purposes. As I say, I think we are the only country in the world that does not give recognition to those expenses.

Mr BEDDALL—Coca-Cola is a good example because Coca-Cola is not patented and never has been. Does it make a difference if you buy a patented product?

Prof. Krever—Yes. If you buy a patented product you can amortise it over the life of the patent but, if you spend the money to defend your right to have an exclusive market, we do not recognise that.

Mr Langford-Brown—Mr Chairman, let us not forget trademarks. That is probably the most common descriptor we know of which you do not get a tax deduction for.

Miss Haly—Trademarks are not within the intellectual property regime because they are not regarded as a wasting asset. That is the explanation.

CHAIR—That finishes section 373—intellectual property. We will return to division 149, subdivision 165-C—deducting bad debts—after a short adjournment.

Short adjournment

[4.04 p.m.]

CHAIR—Senator Watson has a question he would like to ask.

Senator WATSON—I have not so much a question but a clarification, Mr Chairman. I would like to take this opportunity of commending those who have picked up errors in the legislation to date. I also think it is appropriate that we do put on the public record the increasing sophistication of what has happened in terms of the rewrite, because when we first started there were so many more problems which we encountered than we seem to be incurring at the present time. So, while I thank those who have picked up those errors—and I think it is important that we pick them up earlier rather than later—I think it is important that we do put on the public record this increasing sophistication and the internal processes which have obviously eliminated the error-type situation that did tend to exist in the very earliest of days. I think that augers well for the process in future.

CHAIR—Are there any comments on subdivision 165-C—Deducting bad debts?

Mr Bryant—I have a comment—and I might seek a reaction from the TLIP side. There is an issue in the midst of this: it is a provision that deals with deduction of bad debts. As we know with these sorts of areas where you have got something happening one year and a deduction in another year—and we run into some issues that have been raised in other discussions around this—companies seeking to get a deduction for a bad debt where the debt was incurred in an earlier year have to either maintain that continuity of ownership or else carry on the same business. It is the ownership test that I am particularly concerned about because in an earlier version of a rewrite there has been the introduction by the good graces of government of some relaxed tracing rules. I have raised before with the TLIP team that, when you come to this provision, for major public companies these relaxed rules are the ones you are going to use. If you cannot use them, you cannot satisfy the tests, and they do not get enough attention. They are tucked away in Note 1 to section 165-120. You start to go through all this and you are talking about ownership, and tucked away there is the reference to 166-C and I think that it does need a stronger highlighting. I had feedback that said, ‘We’ll address that’, but I do not think what is there is good enough. I think the companies or public entities need a stronger flagging that when caused to trace their shareholdings they should be very up-front directed towards these new tracing tests.

CHAIR—Does TLIP have a comment?

Mr Nolan—I suppose of all the categories of taxpayer groups public companies are the ones most likely to have sophisticated tax advice and people who know their way around the law—people like Bob and Joycelyn, for example, and others. That note is a pretty straightforward pointer. I would be interested to hear what Bob says might be done in addition to that, but for my own part I would have thought it highly unlikely that a public company eligible for those provisions would be advised in such a way as to miss it.

Mr Bryant—I think it is so important that it does need to be highlighted, and I

think it could be done a lot better than what is there.

CHAIR—Would you be happy with it in black print?

Mr Bryant—Oh well! As I say, I think it does need to be put more up-front. It is the reverse of what has been there before—they become virtually the mandatory tests—and yet it is tucked away as a subset. I do not need to go any further, but that is the major reaction to those provisions, otherwise they do fairly faithfully repeat what is already in the current law.

Senator WATSON—On a point of explanation: if an entity trades as a discretionary trust, would it be very difficult to comply with these provisions in terms of writing off a bad debt?

Mr Gaylard—The provisions are only for companies, so trusts have their own issues to deal with. You are right, discretionary trusts do have some issues with continuity, which I am not sure extend to the bad debt area now or not. I think they do. They certainly extend to trusts and trust losses. Basically, a discretionary trust cannot write off losses unless it is a family trust and makes an election to be treated as a family trust. The government quite outside our project has just introduced some very strong rules that make it a lot harder for discretionary trusts that are not of the family trust variety to write off losses.

Senator WATSON—It is for that reason that I asked the question. The threshold question is: not having 165, which I agree applies to companies, can discretionary trusts therefore be in a position to claim a bad debt?

Mr Reid—The trustee would normally be carrying on a business and the trustee is the legal owner of the business and vis-a-vis outsiders is really in much the same position as a company or an individual carrying on business in their own right. So it would be in the same situation as a normal business arrangement where a debt goes bad. The fact that the profits of the business are distributed to beneficiaries is not really relevant.

Senator WATSON—It is not relevant?

Mr Reid—It does not affect the character in which the debt is incurred, no.

CHAIR—What you are saying is that the trustee, the company, carries on a business like any other business but the distribution of the income is different and that is what attracts different rules?

Mr Reid—Correct.

Senator WATSON—They have got different shares. Surely it is the same principle

if they have different shareholders or different people are entitled to the distributions. I would have thought that they would find it difficult to be able to claim the write off of a bad debt.

Mr Reid—Are you referring to the operation of these provisions? These provisions in 165-C apply only to companies carrying on business in their own right. Simon has mentioned the case of the discretionary trust itself. But you are dealing with the threshold point—

Senator WATSON—I am dealing with the threshold point in the terms of write off of bad debts. Given that the government has recognised sone changes in relation to losses, how do bad debts fit into this situation? It has got nothing to do with 165.

Mr Gaylard—The threshold issue is: do they have an amount that has been brought to account as assessable income?

Senator WATSON—Yes, no problem with that.

Mr Gaylard—And then is that amount bad subsequently?

Senator WATSON—No problem; it satisfies all those tests. Because over the years they have been distributing money to different beneficiaries—A, B, C, D and E—with an inconsistent pattern, do they lose that right of writing off the debt?

Mr Bryant—It is my understanding—and I have not looked at it closely—that these rules we are looking at are for companies. With the move to the containing of the trust losses area I am not aware that it encompassed bad debt arrangements. These are anti-avoidance provisions.

Mr Gaylard—I honestly cannot remember.

Mr Bryant—I do not think it does, so therefore a question of this type does not seem to arise for discretionary trusts. They do not have to satisfy these tests. There is not the same anti-avoidance—

Mr Nolan—Has the debt been accounted for?

Senator WATSON—Yes, there are no worries about that.

Mr Nolan—If the basic rules have been satisfied, then there is a deduction.

Senator WATSON—Given the scenario of the changes to companies viz-a-viz this legislation, and the changes in relation to trusts in relation to losses, what is the position in relation to bad debts of trusts that are of a discretionary nature?

Mr Reid—In commercial terms, they can be owed debts that go bad just as any other trading entity can. As Brian was saying, the tests for deductibility are the same. Subject to whether the trust loss provisions also deal with bad debts, then there may be further ownership rules that come into play. But if you are just dealing with the process of the primary right to the deduction trusts of any kind are in essentially the same position as companies, partnerships or individuals.

Mr Bryant—Your question is really, John, whether the trust's recent initiatives should encompass bad debts. I cannot answer that.

Mr Reid—I think they do, but we can find that out and get back to you.

CHAIR—We move to 166C, also deducting bad debts; 170B; 175CA; 175CB; 175C; 175D. Here we go—387C, horticulture plants.

Mr Parker—Ian Langford-Brown and I have the dubious honour of agreeing to review the last four segments—this and the next three. Both of us have read the legislation with close scrutiny—all since about 11 o'clock last night. On a lighter note, we have had a cursory glance at the legislation because of the shortness of the time. I made a few comments to Margaret Haly in the break with a view to expediting the outcomes. I want to talk on three points on horticultural plants and then Ian will add one or two.

First of all, there is the definition, and the reference is page 222 of the EM and page 469 of the legislation. The definition in the legislation—

Mr BEDDALL—When did we get a plant kingdom? Is it like the animal kingdom?

Mr Parker—Something of that nature, yes. I will not deal with the actual definition of a horticultural plant, but (2) and (4) exercise my mind a bit. Subsection (2) says:

A horticulture business is a business of horticulture.

It also gives you an asterisk to go to section 995, which brings you back there—and I am not trying to be too flippant here. Subsection (4) says:

Use for commercial horticulture means use for the purpose of producing assessable income in a horticulture business.

Elsewhere in the EM on page 222 we are told there is a change, that these terms have been defined.

There has been a problem in the past—and I have not had to grapple in any appeal

cases with the tax office—and my understanding is there is an ongoing difficulty to determine when a deduction might be available for plantation of certain trees that may not produce nuts or income for eight, nine or 10 years. I am not sure in the information I have at the moment that these definitions add anything to the solution to the problem—or indeed at the end of the day whether the TLIP team tried to resolve the problem.

The first definition—'a horticulture business is a business of horticulture'—does not add anything, but you really come back to what the indicative factors of running a business are. And it says that the use for commercial horticulture means use for the purpose of producing assessable income . . . ' Carrying on of a business would normally include the derivation of assessable income at some point in time. So I would be interested in TLIP's comments as to how these amendments have enhanced the legislation and the understanding for the user.

Miss Haly—Can I take it on a case by case basis. The answer is that we have not sought to clarify in the legislation this particular point of when the deduction commences. We sought faithfully to reproduce the level of uncertainty in the existing law. The reason we have done that is that at the time of introduction there was quite heavy lobbying for this particular deduction for horticultural plants, for the regime to be on the same basis as that for grape vines, which would have meant that the deduction was available from the time the plants were planted rather than the time at which they were likely to produce a commercial crop. The government's decision, announced by press release after weighing all that up, was that the deduction would commence when the plants reached the stage of coming into commercial production. That was very clear in the EM but, arguably, it was not quite so clear in the law.

Since that time we are aware, and we have had representations to the team—not that there seemed to be any uncertainty in the minds of the people making the representations as to when the deduction was allowable—that they simply wanted a change of policy to bring their regime into line with the other. We were not prepared to do that but, on the basis of past experience, we decided that we would not remove what some might think would be a reasonably arguable position given the level of contention likely to arise and the fact that it is preferred that our project does not stir up contention. So we have left people with the clear statement as to when the regime commences in the EM.

Senator WATSON—It does impact fairly adversely on certain horticultural products such as walnut trees, which take a while to come to bear fruit and often have a life of 30 years or more.

Miss Haly—It is very clear that at the time that was the policy outcome the government wanted. The different treatment for grapevines was because they suffer a particular disadvantage in that they are subject to sales tax at a higher rate. Horticultural plants generally are not or they are subject to a lower rate. So the difference in their

regime was to compensate for that particular disadvantage. If you put all the other horticultural plants on the same basis as grapevines in terms of when their deduction commences, you would in fact advantage them vis-a-vis grapevines, which was not the policy intention. You would also take them out of line with deductions for capital expenditure.

The reason that the policy decision was taken not to allow a deduction when their plants were planted was that during that period their value is increasing not decreasing; you would be giving them a deduction before there was any income to offset it and you would actually be allowing a write-off at a faster rate than you would under the depreciation provisions. That was the thinking behind it.

Senator WATSON—Not for walnuts.

Miss Haly—So the short answer to Tony is: we researched it very thoroughly. We established what the policy position was, what the government's announcement was. We also established that there had been some contention about the issue and we sidelined it.

CHAIR—It think it is fairly clear that is big 'P' stuff.

Senator WATSON—It is fairly harsh on certain types—

CHAIR—It might, but that is big 'P', and that is not their bailiwick.

Mr Parker—I accept that. The point I wanted to make in presenting it today was to say that the definitions have not in any way resolved the problem.

Miss Haly—We tried very hard not to.

Mr Parker—And have succeeded.

CHAIR—As I understand this, you both agree.

Mr Parker—Yes, absolutely.

CHAIR—Well done. Next?

Mr Parker—Correct me if I am wrong. Number two is section 387-175, the determination. It is only a very small point. It is at the bottom of page 470 of the legislation, subparagraph (b). We have just suggested to Margaret that maybe the grammar could be improved a bit there. We are talking about the determination. What happens is that the new owner can seek from the original provider of the horticultural plant information to enable the new owner to write off the relevant amount over its life, et cetera. No, sorry—I apologise. On this one the commissioner can make a determination.

However, he can only make it retrospectively if the first determination relates to a kind of plant or the retrospectivity will create an advantage to the entity in working out the effective life. It just needs to be tidied up a bit so it makes it very clear. The grammar could be improved substantially.

CHAIR—Does TLIP accept it as pretty awkward wording?

Mr Reid—No.

CHAIR—You do not?

Mr Parker—What is the problem?

CHAIR—I think I am with Tony.

Mr Parker—The retrospectivity advantage is entered in working out the effective life. I know what you are trying to say, but I do not think it says it very clearly. It can only be used if in applying the retrospectivity it will be an advantage to the entity in working out the deduction. It is only small.

Mr Reid—Is this a suggested change of wording?

CHAIR—The wording of 387-175(7) subdivision B is shocking; it is not in clear English.

Mr Nolan—It is the use of the word ‘advantages’.

CHAIR—The ‘retrospectivity advantages’ is not plain English.

Mr Nolan—At first you read it as if it is a noun, and it is not.

Mr Parker—Another one that is very light-hearted, before Ian has a go at something, is on page 476. Now we are talking about the giving of a notice, and I do apologise. We are talking about section 387-205. What happens in that situation is where you have a new owner who requires information from the outgoing owner. The last paragraph, subsection (4), says:

You can give only one notice relating to that acquisition of the horticultural plant.

If you read that quickly you ask, ‘Who is "you"?’ In fact, it is you the buyer who can ask for only one notice. I think it could be clearer. You do get the right answer if you go back to subsection (1) which says ‘if you become the owner’. ‘You’ in that context is talking about you becoming the new owner of the horticultural plant.

Miss Haly—The heading to that section, which is obviously not operative, also says 'Getting tax information if you acquire a horticultural plant'. So I suppose in drafting subsection (4) the meaning of 'you' depended on the entire context and direction of the section. I think you will find that consistently—

CHAIR—But, with respect, in subsection (1) you say 'if you become the owner', in (2) you say 'the last owner', in (3) you say 'if the last owner' and in (4) you change the whole sequence and all of a sudden say 'you can give'. He is right.

Mr Parker—That was quick.

CHAIR—TLIP will look at that, won't they?

Mr Parker—The next one is to borrow something from submissions A, volume 2. I have flipped through both volumes 1 and 2. The only submission on horticultural plants comes from Deloittes on page S349. They brought to my attention—and I missed this—a conversion table that talks about section 387-200 and it does not exist in the legislation. But it did exist in the draft on page 35 of exposure draft No. 9. It is probably now incorporated in section 387-205. What it tried to do was talk about change of ownership. Previously you had two subsections—200 and 205—to get to the answer. You have consolidated and put two into one but you have not fixed up your indexes. I think that is the solution.

CHAIR—Will you take that on board?

Miss Haly—Yes.

Mr Langford-Brown—Mine are certainly not heavy technical issues, either. Firstly, I would like to suggest to the TLIP team—and this is contrary to the concept of reducing the wordage—is that in the old section 124ZZE you had a very beautiful description of what this particular division was all about. What you have done now is condense it into a very sanitised thing that does not read with the same encouragement that the other one did. Seriously, I ask you to think about expanding the guide note.

Secondly, I got highly intrigued when I looked at the explanatory memorandum on pages 222 and 223 looking at 387-195 in respect to expenditure you cannot deduct. It was intended to correct an error whereby the old act got itself in a knot in terms of the deductibility or otherwise of expenditure in this particular division. I believe that the wording you have now in 387-195(2), which reads:

> You cannot deduct an amount for any income year under this Subdivision for expenditure to the extent you or another entity can conduct an amount for the expenditure . . .

does not really get to the crux of the point that you are trying to make in the explanatory

memorandum. I ask you to look at that and see whether I have totally misread it.

Miss Haly—Thank you. We will do that.

Mr Langford-Brown—Mr Chairman, as I said to you, not very highly technical.

CHAIR—But it is important. We are now down to division 392.

Senator WATSON—Before we go onto that: I presume we have a Tax determination, ruling or something that would put raspberries, blueberries, apples, strawberries, black currants, apricots, et cetera into the various effective lives in terms of that depreciation chart. Have we?

Miss Haly—No, we do not. There are no rulings for that at the moment.

Senator WATSON—If I am a blueberry grower, an apple grower or an apricot grower, how do I really know that I am going to fit in? I am referring to the effective life. For example, an income tax auditor will give you depreciation for various items of machinery. Why can't we have it for horticultural products as a guide?

Miss Haly—As far as I know, the ATO has never had requests directed to them.

Senator WATSON—Perhaps we should make it now.

Miss Haly—There are plenty of claims under the regime. It seems to be being administered without that level of support.

Senator WATSON—But at least it gives a guide that you will not be a long way out. If you are just one category out you might be able to have an arguable position as to why you selected that but, if you selected one, two or three out, you are obviously going to be in trouble in an audit. They are very useful guides certainly under depreciation.

Miss Haly—I would be happy to refer the comment to the particular area that look after primary producers, including the horticulturalists. I am sure they would be happy to see whether they thought there was a demand for it. I think that there has not been any demand for that to date, so I would not like to commit the ATO to doing work in that area if it is not considered important.

Senator WATSON—It might be useful to go back to the debate on the bill. I think this issue was raised during that debate, and I thought there was some sort of undertaking to look at whether this might be possible.

Mr GRIFFIN—Why don't you guys have a look at it and come back to us?

Miss Haly—Yes, all right.

CHAIR—We move on to division 392—long-term averaging of primary producers' tax liability.

Mr Parker—About the averaging provisions I would like to make two comments. They are both to do with page 231 of the EM and they identify the two potential changes. In turn they relate to sections 392-10 and 392-95. The first one now codifies the commissioner's practice where, if you had ceased the business of primary production but still continue to receive income from primary production, the averaging provisions will continue to apply if it is in your favour. If it is not in your favour, you elect off the averaging provisions. So that is codified. That is fairly clear cut.

The other one I have more difficulty with. I would like to read the EM and then see whether the legislation equals the EM, because I do not think it does. It first talks about a change and says:

Clarify that it is optional to recommence averaging when a permanent reduction in income occurs.

I will just go on to the explanation:

. . . averaging recommences if a taxpayer establishes that taxable income has been permanently reduced.

That might occur where you have run a business of primary production and also had a very high salary income from the government and you take a package and in the following year you are no longer going to work in government employment and your income is substantially reduced. The rewritten provisions make it clear that the averaging does not recommence automatically—it is saying that very clearly—but only if a taxpayer shows the commissioner that a permanent reduction has occurred. This is consistent with the current admin practice.

I then go to the legislation on page 498, and that is my difficulty. I refer to page 498, 392-95. It is headed up, 'You are treated as if you had not carried on business before.' Paragraph (1) is the main subsection: 'If you show the Commissioner that, because of retirement', et cetera, your income 'is permanently reduced during the reduction year'—the same as exists now—'to an amount that is less than two thirds of your *average income for the reduction year', then the following happens:

(a) this Division does not affect your income tax liability for the reduction year; and

(b) this Division applies to assessments for later income years as if you had not carried on a *primary production business before the reduction year.

What it tells me—and I may be wrong—and my people who read it is that automatically,

if I qualify for the permanent reduction, the old 155, I think it was, then what happens in the year succeeding the reduction year is it automatically recommences the averaging provisions, unless I elect off. That is different to what is said in the EM, which says it is optional to recommence. It is still optional—you can always elect off—but the legislation actually gets you back into the system automatically, and then you opt out.

Miss Haly—I think the 1936 act was clear as to whether this happened automatically or whether it was at the option of the taxpayer. We have sought in the legislation to make it clear that it is at the option of the taxpayer. It may not be as clear as perhaps you would like it but, looking at the legislation, the emphasis is on the word 'show', so it says 'If you show the Commissioner', which I think is meant to imply an initiative on your part rather than—

Senator WATSON—His problem is not with the legislation but with the explanatory memorandum. Is that right, Tony?

Miss Haly—No. What he is saying, I think, is that the EM is clearer than the legislation. The EM correctly says what the position is. I think this is right, Tony. What you are saying is that the legislation does not state as clearly as does the EM what the position is, namely, that it is at the taxpayer's option.

Mr Parker—With respect, I think the legislation is correct and the EM is wrong.

Senator WATSON—That is right. That is how I read it.

Mr Parker—There are two steps to it. The first is to demonstrate the permanent reduction, and that is the first part of (a), and then the impact of demonstrating permanent reduction is subparagraphs (a) and (b). So, in the order of events, you demonstrate to the commissioner with a submission—and you have to do a special attachment on your tax return, no problems with that—and then, having demonstrated that, what are the results of that demonstration? They are identified in subparagraphs (a) and (b). There is nothing optional in (a) and (b). They flow on automatically from the event.

CHAIR—Don't the words 'if' and 'one' require that it be optional?

Miss Haly—The option is at the point that you do not have to demonstrate that to have that automatic flow on. If you choose to raise with the commissioner the permanent reduction, then those consequences flow. If you choose not to raise that with the commissioner then those consequences do not flow.

Mr Parker—Mr Chairman, I hear what Margaret is saying. A number of people who have read it have all indicated to me, and I agree with them—and I will go back a step—that if you do nothing, the averaging continues to apply as it is in the present law, and you are disadvantaged, effectively.

Miss Haly—Yes.

Mr Parker—If you do something like put an attachment in your tax return demonstrating the permanent reduction, that then says that those issues flow automatically. The EM indicates that it is optional to recommence the averaging. You are saying the whole—

Mr Nolan—It is optional whether you make—

Mr Parker—But it is optional now.

Miss Haly—Yes, but we are trying to reproduce the current situation. This is simply an attempt to recreate the position under the 1936 act. The 1936 act provision in section 155 was, we thought, less clear on that than the way we had rewritten it. But we would be happy to look at it to see if we can effect a further improvement. We are agreed on the outcome.

CHAIR—Division 400, environmental impact assessment and environmental protection.

Mr Parker—No great drama, Mr Chairman, and we note the word 'environment' is no longer defined. It is taken as common terminology. The rest I have no problems with.

CHAIR—Section 405, above-average special professional income of authors, inventors, performing artists, production associates and sportspersons.

Mr Parker—The main comments I would make is that we have now removed the commissioner's discretion and have introduced two objective tests—the tests of reasonableness—and we have improved the definition for standardisation of associate. On a light-hearted note to finish off my little bit, I grappled with page 518 of the legislation. I tried to work out whether an international chess player was a sportsman. I tried that very hard under section 405-25(7), which says that a sporting competition is a sporting activity to the extent that it involves human beings. In subparagraph (iii) you compete with natural obstacles—those chess pieces would have to be obstacles—or natural forces or by overcoming them. Subsection (b) says that participation by humans involves primarily their exercising physical prowess—they sit at the table for a long time—physical strength or physical stamina—they stay overnight. So I think a chess player is probably a sportsperson.

CHAIR—My schedule of things to do now says schedules 2 to 8, consequential amendments and transitional provisions.

Mr Bryant—Mr Chairman, before you move on, if I may, with definitions you did

not deal with a dictionary. I have one specific example.

CHAIR—We have other issues.

Mr Bryant—Do you want me to leave it until then?

CHAIR—No, do it now.

Mr Bryant—At the risk of sounding trite, it goes back to process again. It is an issue that takes us back into capital gains tax, and I do not want to go back into that very far but there is an arena there that is called collectables. They are significant because if you make a loss by disposing of a collectable—that is, jewellery and those sorts of things—that loss is quarantined against the gain from the disposal of similar items. You have to keep it within that category.

In the definition—and this is a touch trite—on our reading of this, the concept of collectable is defined and we have a new definition of the word 'artwork'. We have not had before photographs incorporated within that. We now have that. That is not a significant thing in itself. But, again, I question a process whereby there is this shifting of something from what was not there to incorporating it in what is there now.

CHAIR—Would TLIP like to comment?

Mr Burge—We believe that we have preserved the effect of the existing law. The relevant part of the 1936 act is subsection 160B(2)(a), which refers to a print, etching, drawing, painting, sculpture or other similar work of art. We believe that a photograph would be included by that definition.

One of the points that has frequently been made to us is that we need to take a standardised approach as far as possible. The definition of artwork was included in the new law as part of the depreciation provisions. It was to do with excluding accelerated depreciation. We considered it appropriate that we used that definition here, but the effect is the same. To illustrate the point, I will refer to a controversy in Melbourne recently about an artwork, and that was a photograph. It illustrates the point that photographs do come within the existing definition.

Mr Bryant—In response to that, I have no problem with putting photographs—especially when they are works of art—into the definition of 'a collectable', but it was not there before and you cannot point to that fact. You can say that the interpretation of some old words could lead you to that, and I say, 'Yes, but they could lead you to a contrary view.' I just throw it in as another example of the shifting in a very minor way in this case. The TLIP team having an authority within themselves to make those sorts of shifts, I do not think is good enough. I would like to refer that to the committee to consider in its report.

Senator WATSON—What is the difference between an art work perhaps and some of those pictures behind Professor Bob? Essentially, they serve the same sort of purpose in terms of the gallery. I would regard those as having a similar classification, wouldn't you?

Mr Bryant—I am not concerned to debate the issue. I am just saying that we have some words now that were not there before. It is a simple as that.

Mr GRIFFIN—I think that is the issue. I am culturally challenged so I am not going to comment on that.

Senator WATSON—Just looking behind us, is it unreasonable?

CHAIR—You have asked us to have a look at the addition of that word to the definition, and we will do that.

Mr Bryant—It is more a process issue.

CHAIR—We will do that.

Mr Bryant—As a process issue, thank you.

CHAIR—But not right now.

Mr Burge—Given that Bob Bryant has referred to process issues, it would be an appropriate opportunity for me to spell out that, based on comments that Bob Bryant made earlier, it would be wrong to infer that in relation to the issue of trading stock in division 138 that TLIP had unilaterally gone ahead without advising the relevant minister. We take our duty to brief the Assistant Treasurer very seriously indeed on issues as they arise.

It became apparent at our consultation meetings that there was an issue here. When seeking approval for the introduction of the bill we fully briefed the Assistant Treasurer on the relevant issue and then there was correspondence about the bill between the Assistant Treasurer and the Prime Minister which covered the same point. I just want to emphasise that we did go through the proper processes in relation to that issue.

CHAIR—Schedules 2 to 8, consequential amendments and transitional provisions.

Mr Bryant—For my part, can I say that we have not had these long and I have not had time to do justice to them. That may well be the position of most others on this side of the table. Are we talking about schedules 2 to 8?

CHAIR—Yes, the consequential amendments and transitions, which are mechanical devices generally anyway.

Mr Bryant—We have only just got them.

CHAIR—Yes, but generally speaking, they are simply mechanical because they have to do with anything that is displaced.

Mr GRIFFIN—Obviously, what will happen now is that you will go through what you have not had a chance to go through. If you have other issues or anything that arises out of today's proceedings as well, you will come back to us, I would imagine.

Mr Bryant—There is one issue on that in relation to capital gains tax. It was suggested to me, and I have not had a chance to check it, that, with the move to some changes that had been undertaken—and I do not know the answer and you might get a quick comment on this, Mr Chairman—and with the proposal to introduce this law as of 1 July this year, where there were some changes in the calculation of cost base, we stick with the new law and do not have an appropriate tick-tack. The real focus will be on when you dispose of the asset, and in doing so could be caused to rely on the process outlined in this law, notwithstanding that, when you bought the asset you were governed by the 1936 act and may have calculated your cost base slightly differently. An example is 160ZN which is the exempt trust distribution. I have not had a chance to check it, but I just raise that and, if there is a comment, I would like to hear it.

Mr Burge—In working out an appropriate transitional regime to the new law, we were conscious of having the simplest and smoothest possible transition to the new law. A possible approach would have been to have the new law apply only to assets acquired after the commencement of the new law, but that would have had the effect of keeping open the old law for many years, perhaps even decades, to come.

Yet another approach would have been to have the taxpayer calculate a notional capital gains tax position under the old law and to carry that into the new law. That would have required the taxpayer to work out three sets of figures—a notional cost base, an indexed cost base or a reduced cost base—because it is only when you dispose of the asset that you know which of those is relevant. That would have imposed a very considerable compliance burden on taxpayers. We wanted the smoothest and simplest transition to the new law.

We propose in these draft amendments that the new law apply in relation to CGT events that occur on or after the commencement date of the new legislation, meaning that it is the new legislation that is used to calculate the taxpayer's liability. Bob Bryant referred to the particular example of the section 160ZM adjustments. TLIP has made a change to simplify the record-keeping requirements of it. Those provisions in the old law require an adjustment each time a non-assessable distribution is made. TLIP proposes to have only annual adjustments. Provided the relevant unit or other interest in the trust has not yet been disposed of when the new law comes in, that taxpayer will get the full benefit of the new law with the annual adjustments.

Mr Bryant—I thank Mr Burge for the answer to that question, because I had not had a chance to check it. One consequence of that—and I think it is important that it be understood—is that after 1 July 1998, as you dispose of assets, you may have to go back and revisit the cost value that you have already recorded, because when you bought the asset prior to that date you were governed by the old law and you may have put in a system of recording values and the like. The way that John has now explained it, I may have to revisit that. There is an awkwardness in that we have not really fully tested its full implications, and I think it is a feature of the consequentials that needs to be addressed. I cannot say on behalf of my constituency that I am happy with that outcome.

CHAIR—Would you say that there is no simple solution to that problem?

Mr Bryant—Off the top of my head, I think there are some possibilities of giving some options to people to stay with what they have already got, because they will have a record of a cost base.

CHAIR—How do you propose to do that?

Mr Bryant—I will articulate that when I have had a chance to digest the implications of that and I will report that to the committee.

CHAIR—Thank you. Are there any other issues?

Mr GRIFFIN—I am conscious of the time but, given that practically everyone is still here, I raise the question of the operative date and how significant that is. It is something I have spoken about privately to some of the people here today, but I want to talk about it for five minutes. There are several arguments. We had this issue on the first tranche of legislation. We went with the latter date and the walls did not come tumbling down. Can I get a comment from both the consultative committee and also from TLIP on the operative date?

Mr Nolan—I made some comments about this earlier, particularly in response to Tony Parker. We believe that if you extend out the date for another year it will not put people in a position of being much better prepared than they will if it applies from 1 July. That is because people will not, in all honesty, face up to learning about the new law until it is right on them. If there is a year longer for them to put it off, then that is what will happen. There are other consequences though. There are many things in this legislation that are actually improvements in terms of their application to people—small 'p' changes that are beneficial to people. I do not believe that those benefits should not be available when most of that has been foreshadowed and can readily be made available under the process that we have in place now for the legislation to be passed by 1 July.

The other thing is that we have a large project which is only part way through—less than halfway—in terms of the amount of material that has been introduced to the

parliament. The time frame will inevitably blow out if each time we come up to a bill we say, 'Let's give it another year.' This bill is a large one but the next one will be larger still and the one after that of the same sort of order. There is an awful amount of material for you to yet come to terms with and digest. That is really one of the things that underlines to me why progressive delivery—in other words, digestion in stages—was the right way to go. You helped that process by passing legislation in stages, not stacking it. If you delay this one for another year, you are either going to say that the next bill should also be delayed for a year or you are going to have those two bills—this one and the next one—come into operation at the same time and that will be a massive amount of material.

This is essentially, and I think the comments have shown this, a rewrite with very little of real controversy. There are lots of points of minor detail and a lot of clarification there. I believe that the best way to move the process forward and to get as close towards having an entire new act is to let it operate in stages sequentially. This is the next stage. I think that by putting it off for another year might give some temporary comfort to people but will not really achieve very much.

Mr Langford-Brown—In my professional role, I am the director of taxation of the Institute of Chartered Accountants. I have a tremendous amount of contact with our members. One of the things we have gained at long last with the assistance of the TLIP people is an awareness within our membership that, firstly, the new legislation is there and, secondly, how important it is. That is point one. Point two is that we have a litmus test here in CGT. It is one of the most convoluted, complex areas of our law. We also note that we have not fully rewritten CGT as yet. I note also that, in the amending legislation that is part of what we are looking at, there are 125 changes in that piece of legislation alone. The message I am getting very clearly from our members is, 'Yes, we accept that progressive implementation as a concept is what we are faced with.'

What I am also hearing from our members is that, with CGT, we have had the benefit of consultation with the TLIP team, but we really need further time to see the complete legislation on CGT. Therefore, it is almost the unanimous view of the members I have spoken to, who may or may not be a fair cross-section, that they believe that they would rather see this whole thing totally done for all the various issues which have been raised, say, in the joint body submission, to be considered in harness with the TLIP people. For that purpose—and I know Brian may not believe it when I say that I am speaking on this bill because of its special position within the income tax scene—I believe the appropriate step is to delay its implementation until 1 July 1999.

Mr Gaylard—I am happy to support what Brian said. I am sure Ian is reflecting the views of the people he speaks to, but I do not hear any difficulties from the people I talk to out there. There is an enormous amount of legislation coming through, and the thing I do know is that tax advisers, taxpayers and people who read the law only pick up the law and start reading it when the whole thing is about to descend on them. It is human nature. In another year maybe it will get an extra couple of per cent nearer to perfection,

but people are not going to read it until they have to. We could have exactly the same argument produced again next year.

The best way to get the law understood and to get people using it is to put it out there, make it operative and away it goes. There will be some issues, and people will struggle, but people will be a lot better off in the long run. As Brian said, we can get each major tranche of legislation in, a year at a time. That seems to be a much better way to deal with it. If I really felt that there was any strong reason for delaying it, I would certainly be in favour of it as well. But I see that the best position is to get the legislation out there, 97 per cent right. That is going to be a lot better than waiting and trying to get an extra one or two per cent onto it.

Mr Parker—I made most of my comments earlier, but in 1997 I did go out to sell the gospel. I spoke at 15 seminars around the state. During at least two-thirds of those I spoke on TLIP. I have spoken to practitioners from the city to the bush, and I spoke to probably about 800-odd in total, so I got a reasonable feel for what was going on. I support Ian's concept that practitioners have now accepted the process by and large, and the progressive implementation. As I said earlier, I have been passionate about that to this point in time.

This bill is different to the 1997 act. There are substantially more changes. The end product that we will have in 1998 will not be available as early as the 1997 product was available. Indeed, by March 1997 the only real issue outstanding was the controversy on trading stock, which involved meetings on the key issue. Most of the rest of the bill which you had before you in parliament at that stage was the end product. There were technical amendments, but there were two packages there that practitioners could get their hands on.

Following today's meeting and following your report I believe there is still a degree of work to be done by TLIP before the practitioners can get their hands on what will be the end product. At best, even if the publishing houses are geared up for it, a practitioner may have a month or two months in which to come to grips with the 1 July transactions.

Given that, I must strongly say from the small practitioners point of view that in this issue an extra 12 months would be preferred. If there had to be a compromise somewhere between the two, I would reluctantly say that there are precedents within government in terms of the rewrite, particularly in relation to substantiation, where the law was introduced on 15 December—or whatever date it was—and the taxpayer had the option of taking the new or the old.

I do not doubt for one second—and indeed I strongly support and will continue to say—that there are substantial improvements in what is being offered. That should be made available to the practitioner and the tax-paying community as soon as possible. The question I ask is: will the average practitioner be in a position to be reasonably organised

to apply the law for the benefit of the tax-paying community from 1 July? I have a real doubt.

Mr Bryant—We are already experiencing that the progressive implementation is creating a fluid state of our law. In many situations it is very difficult to know what is the express provision that we are trying to deal with. We have to go through many acts. It is clear from today, and I think we will find it even more tomorrow, that at the stage we are at what you have got before you in terms of that draft legislation has its inadequacies and is incomplete.

We are racing against time to give it a fair testing, and we are going to run out of time. Finally, we have a number of taxpayers, mainly companies with December year ends, and if this were passed and enacted with the 1 July date, they would already be subject to this law, and that is just not fair. It has to be delayed another 12 months.

Senator WATSON—If the government is to be committed, as it is at the moment, to a July election, from a practical point of view in the Senate—

Senator GIBSON—We didn't know that!

CHAIR—Senator Watson, have you been talking to God?

Senator WATSON—No. I would be the last one to know, but I do have years of experience in the Senate and I would think that if people are anticipating an early election that a tax bill of this nature would not be given a high priority, certainly by the opposition, because it would be seeing fit to concentrate on other more politically charged issues.

At the present time, I would say from experience that the chances of getting this bill up, given that the first session is going to be quite a short session and I think there would be other bills that the government itself would be giving priority to that it would want to get up, the practical chances of being able to debate this before June are not very good. That is from one point of view.

The second point I want to make is that I think this committee would have to meet again so that we could have a similar sort of arrangement to the one we had today to ensure that all these new changes have been accepted. We have had the problem that a number of people around the table have not had the opportunity to look at this new raft of changes. I think the committee therefore owes it to everybody to meet again so that we have the opportunity of looking at the impact of those new changes as we have had today.

I would like to think that we could do that reasonably quickly, with the agreement of everybody around here because, without that, it is going to be very difficult for us to

prepare a report.

Senator GIBSON—Mr Nolan, given our timetable of reporting by 12 March, what would be your expectation of when this bill would be ready to give to the government?

Mr Nolan—I think the changes that we would be needing to make to the bill are already being roughed out and recognised. Some more will perhaps arise tomorrow and as a result of looking at today's issues, but I think we could have that bill in a state where the amendments we are proposing—and the bill is already in the parliament—could be put together quite quickly and be ready for debate in the House of Representatives soon after your scheduled report-back date.

Senator Watson was prophesying about the election date. Naturally, if the bill does not get through the parliament before the election is called then, like any other legislation, it lapses and would need to be reinstated at some later stage. But I do not think that the possibility of an election should be a reason for saying, 'Let's give up the ghost on this at this stage.' In fact, who knows when that date will be. I do not think we should take that into account at all.

CHAIR—Could I remind you that the session begins on 2 March and concludes at the end of the first week in April, I think. After the budget itself—and you would not expect anything to happen in the Senate with respect to this bill then—there are only four sitting weeks. The last one finishes on the second day of July, so there is not a lot of sitting time. That is a fact.

Mr Nolan—I think we have recognised that in our thinking. We have looked at the calendar—

CHAIR—Have you taken into account that a Senate committee may examine the bill as well?

Mr Nolan—The point is that we think we can get the material to a stage where, if the government is able to secure passage in the House of Representatives and get it into the Senate, there would be time, subject to the Senate's other business commitments, for it to be looked at. Whether that happens or not, in my judgment, ought to determine what the operative date is. If the Senate can deal with it, then it can start on 1 July.

CHAIR—Fair enough.

Mr Langford-Brown—I have a feeling when we started this discussion this morning that there would be an opportunity for those who had made major submissions to have a discussion with the TLIP team in respect of a number of the points raised. Through you, Mr Chairman, may I ask Mr Nolan: is that an opportunity you intend to allow?

Mr Nolan—If the proposition is that the 320 issues which the joint bodies raised in their submissions, including a lot of policy issues, are going to be debated, then clearly the answer is no. We will be giving a response to the joint bodies and to other submissions indicating our thinking on why some things were outside our charter or undesirable for other reasons, those that we have actually picked up and had built into the legislation. As for a full range of full-blown additional consultations, there has to be an end to the process, and I cannot see that as being an appropriate way to go. On selected issues, like division 138, there are already expressions of readiness from our side of the debate to consult with the people who have particular interests in those, and we will do that, but it cannot be a complete reworking of everything that has ever been raised.

CHAIR—The committee agrees that additional submissions No. 13 from TLIP dated 27 January 1998 and No. 14 from TLIP Consultative Committee dated 27 January 1998 be accepted as evidence and authorised for publication.

Resolved (on motion by **Mr Griffin**):

That this committee authorises publication, including publication on the parliamentary database, of the proof transcript of the evidence given before it at the public hearing this day.

Committee adjourned at 5.15 p.m.