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Official Committee Hansard

**HOUSE OF
REPRESENTATIVES**

STANDING COMMITTEE ON INDUSTRY, SCIENCE AND
RESOURCES

Reference: Increasing value-adding to Australian raw materials

THURSDAY, 5 APRIL 2001

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HOUSE OF REPRESENTATIVES
STANDING COMMITTEE ON INDUSTRY, SCIENCE AND RESOURCES

Thursday, 5 April 2001

Members: Mr Prosser (*Chair*), Mr Cadman, Mr Hatton, Mr Lloyd, Mr Allan Morris, Mr Nairn, Ms Roxon, Mr Cameron Thompson, Dr Washer and Mr Zahra

Members in attendance: Mr Cadman, Mr Hatton, Mr Allan Morris, Mr Nairn, Mr Prosser, Ms Roxon, Mr Cameron Thompson, Dr Washer and Mr Zahra

Terms of reference for the inquiry:

To inquire into and report on the prospects of increasing value-adding to Australian raw materials. The Committee will start with an evaluation of the current state of value adding in Australia, and how that compares internationally. This will provide a base from which to evaluate the following topics:

- incentives and impediments to investment;
- intellectual property rights;
- national/international marketing factors which may encourage or hinder Australian value-adding;
- government intervention, both nationally and internationally;
- the location of value-adding industries and projects in regional Australia;
- resource licensing/permit arrangements;
- the impact of vertical integration within particular industries; and
- the Australian skills base and any associated impediments.

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Committee met at 11.32 a.m.**COOPER, Mr Ian Donald, Segment Leader, Innovation Segment, Large Business and International, Australian Taxation Office****MILLER, Mr Geoffrey John, Assistant Commissioner, Law Design and Development, Australian Taxation Office**

CHAIR—I declare open this public hearing of the inquiry into value adding to raw materials in Australia and thank the officials from the Australian Taxation Office for their attendance. I am obliged to remind you that the proceedings here today are legal proceedings of the parliament and warrant the same respect as proceedings in the House. The deliberate misleading of the committee may be regarded as contempt of parliament. The committee prefers that all evidence be given in public, but if at any stage you should wish to give evidence in private you may ask to do so and the committee will give consideration to your request. I will invite you to make some introductory remarks before we go to questions. I presume you have read the information as to the reason why you are here. The ball is in your court.

Mr Miller—The previous *Hansard* does not in some ways lead us to what questions you might be wanting to ask, so obviously we will wait for those questions. I should say at the outset that the Australian Taxation Office has the responsibility of administering the tax laws but in itself it is not a policy department. So to the extent that the questions may relate either to taxation policy or to industry policy, those questions really should be directed to the various policy departments involved. Other than that, we are at your mercy as to what questions you would like to ask.

CHAIR—That is the first I have heard the taxman use those words. Mr Morris was the member of the committee that was most interested to follow down these matters.

Mr ALLAN MORRIS—Gentlemen, there are three or four different strands I would like to follow today, but perhaps we can start with the one that I raised at the hearing with the department. I am very mindful of your situation. But you also have things called private rulings and all kinds of other ways in which you interpret the law, and often our confusion is with how you have interpreted stuff that we may have interpreted differently. Often what we are looking for is an interpretation.

I will start off with an example of a company wishing to establish a new plant with relatively newish technology trialed and piloted but not necessarily operational. Apparently such a company seems to be told by the tax office that, because it has been tested and piloted, it is therefore not a risk technology. However, the investment community tells the company that, because it is a new plant, it is a capital risk venture. Therefore, the investment they have to raise is substantially more than is actually required because of the so-called capital risk. I was trying to find the harmonisation between what is a risk from your point of view compared to what is the risk from the capital market's point of view. In other words, how do you decide what is a risk and what is not a risk?

Mr Miller—In the area of what is R&D expenditure, the question of risk and innovation that comes within a definition of R&D expenditure, we defer interpretation in that area of the law to the Department of Industry, Science and Resources. In fact the act requires us—in interpreting

what is R&D expenditure—when we are uncertain whether there is R&D expenditure to refer it over to DISR to get that interpretation. Mr Cooper might be able to explain the actual processes the tax office goes through in that determination process about what is R&D expenditure, for example.

Mr Cooper—As Geoff said, it is a jointly administered concession but the distinction arises in that DISR are responsible for making decisions as to whether activities qualify as R&D activities, and the ATO is then responsible for making decisions as to whether expenditure which relates to those activities qualifies for a deduction.

Mr ALLAN MORRIS—You would have read the *Hansard* where I asked a similar question of DISR. Basically you each refer to the other, it seems to me.

Mr NAIRN—What is the difference between R&D expenditure that fits within the guidelines and determining whether it is deductible? Surely, if the department says that that is within the R&D expenditure, as far as the ATO is concerned is it not immediately deductible?

Mr Cooper—No, they look at the activities per se, and then they make a judgment as to whether those activities qualify for the concession.

Mr NAIRN—So, if it qualifies for the concession, what are you determining?

Mr Cooper—In a classic case they would make a decision regarding the activities and then we look at the expenditure relating to those activities.

Mr ALLAN MORRIS—And?

Mr Cooper—And determine whether or not that expenditure qualifies.

Mr ALLAN MORRIS—Or part of it?

Mr Cooper—Or part of it.

Mr ALLAN MORRIS—How do you decide that?

Mr Cooper—Based on the interpretation of the rules within the R&D concession.

Mr ALLAN MORRIS—Can you give us some hypotheticals about that—cases where the department says it is R&D but you say it is not allowable. On what grounds would it not be allowable?

Mr Cooper—It is the expenditure that we look at, not the activities themselves.

Mr ALLAN MORRIS—Whether all the expenditure would not be allowable or part of the expenditure—why would you say part of the expenditure is not allowable?

Mr Cooper—I guess in a simple case you could look at the salary of a scientist. That scientist may be working part time or full time in relation to particular R&D activities. For the time in which he is working full time on those activities, the expenditure relating to that would be allowed; for times when he is doing other things, it would not. That is at a very simple level.

Mr ALLAN MORRIS—Even though the whole project may be classified as an R&D project, you therefore have the skill to be able to disaggregate it into the components which are not strictly contributing to the R&D part of that project, have you?

Mr Cooper—That is our job, yes.

Mr ALLAN MORRIS—And that is where the argument has come up, is it not?

Mr Cooper—Which argument?

Mr ALLAN MORRIS—When people say that Tax interpreted it differently from the department and give a different interpretation of R&D and when people say they have great trouble persuading Tax that the expenditure they are making is R&D when Tax says it is not. It is in that interpretation, I guess. You are saying that, of the \$1 million, only three-quarters of it is actually directly on the project because you think part of it is separate and therefore not allowable. It may be perhaps a conference overseas by that scientist.

Mr Cooper—That is right.

Mr ALLAN MORRIS—Even though it may be on that topic, you say it is not directly contributing and therefore it cannot be allowable. But, if he does not go, he does not stay a good scientist, so he does not retain his position.

Mr Cooper—There is some expenditure, of course, which qualifies for deduction under the general provisions of the tax act as opposed to qualifying for the 125 per cent concession.

Mr ALLAN MORRIS—I was not raising that; I was trying to raise this question about the arbitrary nature of your judgment in that.

Mr Cooper—I do not know about arbitrary.

Mr ALLAN MORRIS—Can you tell us the rules then? How do you decide? For anybody working on a particular project, a decision on whether or not 100 per cent of their time was spent on that project or whether part of it was spent on something that they did six months ago that will have to be documented is fairly arbitrary. It is hard to try to document that. Say that retaining your current educational levels as a scientist is pretty essential to the thing you are working on but not directly on that particular project. You would say therefore that that re-education, doing that additional course or reading a particular paper that retains your scientific currency but does not contribute to that particular project would not be allowable. That is pretty arbitrary, because it would depend on what paper it was, would it not?

Mr Miller—It is usually a mixture of both the law interpretation and the fact interpretation. If it is a simple clear-cut thing that he spent 50 per cent of his time on the project and 50 per cent doing something else, that is just a factual thing that he spent 50 per cent of his salary or time towards that project. So there is a 50 per cent allocation. There is little that is complicated about that. When you get into the area of whether self-education falls within R&D expenditure or is just self-education under the normal deductible provisions, that is getting into case law. We would have to start into discussions about case law. If you wanted us to give you something fuller on the case law in this area, we could take that on notice and provide that to you. But I am not sure if this is just an example—

Mr ALLAN MORRIS—We have talked a bit about this but often it has been informal while we have been on inspections. Certainly one company we were talking to made it very clear that they had enormous arguments with Tax on the interpretation of a lot of the activities, and tax interpretation was the end of it. It was not worth while taking it to court but they found Tax both arbitrary and ill-informed scientifically about their project. They said that Tax was making judgments that were ill-informed because they did not understand the technology anyhow and what people were doing.

Mr Miller—That is why we do not make decisions on the activities. That is why we hand it over to DISR as to what expenditure relates to that.

Mr ALLAN MORRIS—But within the activities you were making judgments that were arbitrary because you were not fully understanding what the technology was. Therefore, you were making judgments about what technologists were doing which was arbitrary and unreasonable given the interconnectivity of so many of these things. You were putting lines and boundaries that were arbitrary. They had to go to enormous costs to argue with you about them. What was put to us was that this was very arbitrary and therefore very discouraging. They got sick of trying to argue with Tax about what was what and trying to educate you about a project—not you personally but your office.

Mr Miller—It is a matter of, once we know what activities are R&D, deciding what expenditure relates to those activities, and most of the time it is just a factual thing. There is not that much room for argument about the factual nature, whether it does or does not relate to it. There will be some things at the edges, and that is where we will have to negotiate with the taxpayer and discuss with them whether something does or does not relate. But that is more at the edges than a core issue, I would have thought.

Mr NAIRN—Would you go back to the department in those circumstances and get further advice? If they are the ones making decisions about the activities, they are probably better placed to understand the intricacies of those activities. So if you got to that point, would that be something that the tax office would automatically do or would it require pushing from the applicant?

Mr Cooper—Certainly, if there was any doubt about our understanding of what activities were eligible and which arose from an issue around expenditure, we would go back to the department and seek clarification.

Mr NAIRN—So you would go back and say, ‘Look there is some argument about whether this expenditure is really part of these R&D activities or whether it is part of other activities. We think this and what is your view?’ Is that how it would happen?

Mr Cooper—We would probably go back more often to define the boundary line of the activities, which would then enable us to possibly make a better judgment on the expenditures.

Mr NAIRN—Sorry for jumping in, Allan.

Mr ALLAN MORRIS—That is okay. We are all trying to better understand this, because it is not something we have dealt with often. We sent you the *Hansard* where I posed this question to industry representatives. Mr Jones said:

As I said, I am aware that the issue has been around for yonks, but it is other people in the department—

He confirmed my assertion that there is a constant dispute between you and the industry department on this interpretive stuff. I have asked them for more information. They have not provided it to date. I think neither of you actually wants to help us to try to understand it better. I am just concerned that in the meantime people are very discouraged by this system. My feedback from industry people is that it is such a hassle. That is why the rate thing is so important.

Mr Chairman, there are further issues I want to raise but I am at a bit of loss as to where we go on that particular topic because we end up almost at a stalemate. There are matters that are interpreted. Whether it is discouraging or not is subjective. We are being told it is subjective. You are saying it is relatively minor; others say it is major. You are saying it is the department that interprets the project. When I ask you your parameters for determining internally, you say it is what they tell us about how much goes towards the project. But there must be an argument about it. You say you negotiate; but they say you tell them—you send the bill; there is no negotiation; you just tell them what they are going to get.

Mr Miller—Remember, they all have rights to object against an assessment we raise. If we talk to them and we decide that this is in and this is out, they can, of course, object against that and take it through both the AAT and higher to the courts if they think we have incorrectly allocated the expenditure to the project. We are always subject to that and, because we are subject to that, we try to do our best to make sure allocation is right. We do not want to go to the courts; we do not want to be in dispute.

Mr ALLAN MORRIS—Mr Miller, the bottom line of all that is that the people who have been talking to us get the real view that the tax office do not really support this kind of scheme and people are very discouraged by it. They thought the scheme was there to help get investment and help get their industries working. The impression they get from Tax is that this is somehow a business welfare scheme that really they should not have access to and that Tax will do all they can to minimise that access. That is the body language and the mindset that seem to come through.

Mr Miller—From the ATO’s point of view, we want to administer the law in the most simple and efficient way to ensure that we carry out what the government intended to be carried out.

We do nothing more than that. We do not encourage or discourage something from an industry perspective—that is more for the policy departments to do than us. We just ensure that what parliament has decided in the law is carried out. I cannot see how our actions to apply the law can be interpreted to say that we are for or against a particular government measure.

Mr ALLAN MORRIS—Go and read Barwick then. There are 1,001 ways of interpreting the same law, it seems to me. I am disappointed that you did not make a submission, because I would have liked to have heard from you how you do interpret the law and how you see that responsibility. I would like to know what you do to make sure that people have access to arbitration or other procedures without necessarily going to the huge expense of an AAT hearing—they may as well end up in court three or four years later—which is not an option for most people to pursue unless they are very big with a lot of money and a very big project. When you say all those things, it might sound okay to you but, to a person who is dealing with you, it is not really an option. I am disappointed you have not seen fit to tell us why you are so effective at what you do and how you help companies. I would have liked to have heard a bit more about that.

CHAIR—On another matter, Mr Zahra has a question.

Mr ZAHRA—Are you finished with that?

Mr ALLAN MORRIS—I have three or four others but I have finished with this topic.

Mr ZAHRA—I have a different matter that I want to raise. Our chief task in our inquiry is to look at impediments to value adding. You will not be surprised that we have a particular interest in rural and regional Australia as well, because this is where most of our resources come from. There has been a bit of talk about things like enterprise zones—I welcome that debate here; I think it is a great thing—and it has some implications for the administration of tax policy. Just to give us some background to that, I am wondering what the tax office's view is of the efficiency of that type of zone—or taxation I think is the jargon. Do you think that would be a useful public policy measure to employ to try to create the right circumstances in those rural areas for less exporting of just base materials or raw materials and more focus on value adding at the site where those raw materials are found or produced?

Mr Miller—I am not at all wishing to sound negative, but a tax policy question like that should be directed either to the government or to the Treasury, which looks after tax policy. ATO would not have a view on that at this point of time—in fact, any point of time.

Mr ZAHRA—Do you have a view about whether or not it is effective to use zonal taxation?

Mr Miller—Effective in what way—from a tax administration point of view?

Mr ZAHRA—Yes.

Mr Miller—To my knowledge we have not considered that—not in the R&D sector anyway. There may have been other considerations in the tax office, but I am not aware of that.

Mr ZAHRA—Is there anyone else from the tax office who is here and might be able to advise? It is a fairly straightforward question. We do have a zonal taxation system in place for various revenue collection processes that the ATO uses.

CHAIR—Are you referring to the zone rebate system?

Mr ZAHRA—Yes. This is an important debate for us. I do not know how everyone else feels but I do not want to go down the path of thinking that zonal taxation is effective and useful, which is my instinct, if you have experiences to the contrary. This is why I am asking the question. I do not think it is a hard question.

Mr Miller—I am not sure exactly the full scope of what you are talking about. I have seen what has been reported in the newspapers, and that is about it. I am not sure how they would relate to, for example, the administration of the zone rebate. The ATO from an administration point of view would have to consider that in some detail.

Mr ZAHRA—Mr Chairman, I wonder whether I could ask the ATO to perhaps take it on notice. I am positive that there must be some work being done in the ATO in relation to this.

CHAIR—I think the point was made that in a policy sense it might well need to go to Treasury. They will administer something when they are told what they have to administer. We will certainly cast a bit wider and, if appropriate, we can go back and ask Treasury.

Mr ZAHRA—Correct, but ATO have to implement it. All I am asking is: in their experience, is it effective or is it one of those things which creates a bureaucratic nightmare so that you have people on one side of the boundary and on the other side of the boundary having different rates of taxation? That is what I want to know. I am not asking for an opinion.

Mr Miller—The difficulty is to give you any straight sort of answer. Until the policy people actually put a box around it and say, 'This is what we would like to do,' it is very difficult for us to say how that is going to impact on Australian taxpayers. As far as I am aware, they have not yet determined—the government or Tax from the tax policy point of view—what is the option that we are discussing.

Mr ZAHRA—The point I was trying to make is that, whilst that is not out there in relation to enterprise zones, it is not too much of an extension to consider things to do with the diesel fuel rebate scheme, which employs a similar idea, and the efficacy of that and to draw some conclusions from that. I am sure that the Australian Taxation Office would have been in touch with the state revenue offices and whatever relevant government departments exist in states and territories in relation to the way that they have implemented payroll tax, which for a period of time was implemented on a regional basis—there were regional exemptions given and the like. I just want to know whether or not it is an effective way to go about taxation from the point of view of the ATO, which would be charged with the responsibility of administering it.

Mr Miller—But, again, in that question of effective taxation, that really is a matter for Treasury rather than Tax in determining whether a particular option is the best way of going forward. In the ATO we will certainly give advice when asked to the government or to Treasury on what—

Mr ZAHRA—I am asking you to give us the advice.

Mr Miller—But at this point of time we do not know what we are giving advice on.

CHAIR—That is right; there is no policy on the table.

Mr Miller—There is no policy.

CHAIR—The diesel fuel rebate scheme is on use. It can be used anywhere so long as it fits the criteria.

Mr ALLAN MORRIS—If I can raise with the gentlemen a hypothetical company, called CIQ, that builds a large plant. It does not succeed or it goes seriously wrong, and they write off, say, \$1 billion. That \$1 billion is written off against tax losses of about a net \$300 million—would that be right?

Mr Miller—Somewhere around there.

Mr ALLAN MORRIS—It then goes and spends \$100 million on repairing the plant to make it good. How would that then sit within both your R&D and your write-off provisions? It has cost you \$300 million so far in terms of write-offs which you have no say over—that is just an automatic thing, isn't it? You do not actually assess that. In other words, a failed R&D project gets written off without any assessment by yourself or the department because it is a tax write-off. Is that correct? If a company were negligent or incompetent and lost money on a project, does Tax say, 'You cannot claim that. It is unfair to the taxpayers because your shareholders should carry that burden because it is your own stuff-up?'

Mr Cooper—Providing it meets the criteria for being written off; if it is destroyed or sold for nil value then certainly there is a full deduction available.

Mr ALLAN MORRIS—So the plant is still operating with the whole lot being written off and it has a \$300 million tax liability. It then starts to spend money on repairing it and making it effective to get it functioning. So they spend \$100 million. Would that be an R&D investment?

Mr Cooper—I am having a bit of difficulty trying to conjure up the situation where, if it has been written off, it is then going to subsequently be used. Normally you would think that, if it were intended to repair it, it would not be written off. It may not qualify—

Mr ALLAN MORRIS—Perhaps you and I are both bad in interpreting the minds of boards but these things happen. That actually happens. What happens next?

Mr Cooper—Certainly if you had an item of plant on which \$100 million was being spent under the general provisions and it could be a repair or an improvement, then in one way or another that would attract a tax deduction under the general provisions.

CHAIR—I think what we need to do is to determine—

Mr ALLAN MORRIS—We cannot talk about precise cases of companies because they are private.

CHAIR—That is right. But there is a difference between writing off something from a company's books and writing something off from a tax point of view—the two are not necessarily consistent.

Mr NAIRN—It is not necessarily the same thing.

Mr ALLAN MORRIS—In this case it is.

Mr NAIRN—Are you sure?

CHAIR—I am just saying they are not necessarily consistent.

Mr ALLAN MORRIS—With the company CIQ it is a lot more money than what I put forward—work it out for yourself—the actual write-off is \$2½ billion, the tax loss is \$800 million and the expenditure on R&D is probably going to be about \$250 million. I am at a loss as to how that comes together in taxation terms. On the one hand we are trying to get money for R&D and it is very difficult to get a few bucks at all. But then one company takes \$100 million of that in one go. That is fine; that is within the law. I find it a bit difficult arguing over thousands of dollars on the one hand while we write off hundreds of millions on the other. But then the next stage when they want to reinvest, which I am pleased they are doing, to get the thing going, is that then R&D? How does that actually work if you have written off a plant and then you are spending money on it?

Mr Cooper—You would have to look at the new items of expenditure to see whether it was a qualifying activity in terms of the R&D concession.

Mr ALLAN MORRIS—I think you will find it is. If it is a malfunctioning plant and they fix it with engineering changes that are scientifically based, it has to be within R&D.

Mr Cooper—There are criteria that have to be satisfied. There has to be innovation—

Mr ALLAN MORRIS—Let us go slightly further then: let us say a petrochemical company establishes a plant and it does not work. Can the whole plant be written off against R&D at 125 per cent rather than 100 per cent, because the write-off is 100 per cent effectively?

Mr Cooper—The plant would have to meet the qualifying conditions. In other words, there would have to be R&D activities there. If the qualifying activities were present, then you look at the expenditure. If the plant was used exclusively for the purpose of carrying on the R&D, then it may qualify for the concession.

Mr ALLAN MORRIS—Mr Chairman, I would like the ATO to go away and think about it, because the conjunction of those two tax issues that I have raised is not all that uncommon—that is, the conjunction between write-off of losses and R&D—because often in this frontier land we get those two things happening at once. This particularly occurs if it is an existing company with other substantial profits to write off against. If it is a startup company with no

with other substantial profits to write off against. If it is a startup company with no income and no profit, then they cannot necessarily write it off. But I am interested in the conjunction of write-off of losses for plant failure and R&D for subsequent activities—if the plant is now on-stream and actually operational, does the \$800 million of tax losses ever get recovered?

Mr Cooper—I would have a bit of difficulty in seeing how the plant could be written off in the first place, if it were still being used—

Mr Miller—In the first place if you were able to repair it—

Mr ALLAN MORRIS—Just read the newspapers.

Mr Miller—They may claim to have written it off in their accounting books but, for taxation purposes, it may not be written off.

CHAIR—That is right.

Mr ALLAN MORRIS—Their shareholders are going to be in for an awful shock if it is not, because it will have a big effect on their bottom line if \$800 million of tax losses were actually classified as part of it—

Mr Miller—We cannot comment on that particular case. Firstly, I do not know the facts behind that case—

Mr ALLAN MORRIS—I am giving you a hypothetical and I understand this is the case. I am not asking the question whether they could; I am saying it has happened. It is actually a fact. I am trying to work out the interpretive matter. I have one company saying, 'I cannot get \$10,000 worth of R&D write-off,' when here is another company that writes off \$800 million in one go for a technical failure and then keeps the plant going. I am just puzzling how that works out.

Mr Miller—We will take that question on notice—

Mr ALLAN MORRIS—If you can try to give me an interpretation.

Mr Miller—About when is plant written off for R&D purposes and what happens if you then want to add additional expenditure to that plant. We will come back to you on that.

Dr WASHER—Historically we had a 150 per cent tax deduction, and that was removed before my time in parliament. One of the reasons given was that it was because of rorting, that it was abused in a large way. What is different now about this particular scheme from that original 150 per cent that was dropped to 125 per cent? I believe that this has to go past industry and science criteria, but would that not have existed before? What is different about this scheme now, which we did not have before, such that people cannot say, 'We need to change this because of rorting'?

Mr Miller—Again, we are moving back a bit into the policy area. I am not sure if it was an absolute statement that rorting was what caused the reduction from 150 to 125 per cent. At the same time as all that was happening there were all those changes to the law in regard to syndication. So the messages may have become a bit mixed up in all of that, because there was certainly people talking about rorting in regard to the syndication at that time. I am not sure if it is a correct basis to say that the 150 went to 125 per cent because of rorting. Again, it is outside the purview of the ATO as to what is the reason for bringing it back. As far as what has changed since then, the syndication disappeared and there has been a few changes to the definition of R&D. We have also had that recent statement by the Prime Minister about the changes that are yet to happen—some of them have already started—on innovation and research and development. I am not sure what I can help you with there.

Dr WASHER—If I could continue with a hypothetical example, say I am a company that wants to apply for the 125 per cent and a component of that is going to 175 per cent because I am extending. Do I get the paperwork from the tax office? How do I access the paperwork to fill in the forms?

Mr Miller—Perhaps Ian could run through that process.

Mr Cooper—To be eligible to claim the concession there is a registration requirement, and companies have to provide certain information to the Department of Industry, Science and Resources. In other words, to claim the concession you must be registered and the registration process is through Industry, Science and Resources.

Ms ROXON—Just to follow up on that, who will actually make the assessment? You will be able to claim a different level of concession depending on whether it is new research or an investment in R&D which is over and above what you have done previously and depending on what industry you are in and all those sorts of things. So is that something that the tax office will administer or will an assessment be made at the time of the registration and using the process through the Department of Industry, Science and Resources?

Mr Cooper—The system for registration will continue, and that is effectively a self-assessment basis in the first instance. Then, following on from that, it will be up to the company to calculate its entitlement in accordance with the new rules—some of their outlays may qualify for the 175—and make the appropriate claims in their tax returns, which can then be subject to review at a later point.

Ms ROXON—So there will not be any separate assessment made by the Department of Industry, Science and Resources about the industry that people are in or the work they are doing. Basically a company will register, assert what their claims are and it will be the same as any claim that anybody else makes—the tax office may or may not review them?

Mr Cooper—That is right.

Mr ALLAN MORRIS—I want to come back to some other questions. This inquiry is about value adding and that is often about new technologies. I want to compare and contrast the climate here to other tax regimes in recent years. As you would know, CRA-Rio Tinto has shifted its headquarters and closed down most of its research in Australia and BHP has done

something similar—most of its research has now closed down. It has kept a fairly nominal research capacity in Newcastle, and that is about all. We are being told by companies that our systems are so difficult and often so incompatible that to invest here in resource development with anything new and scientifically based is not that attractive. We find that very hard to evaluate. Can you give us an indication as to what tax regime people would find in other countries? We are being told constantly that there are a lot more incentives to invest in resource value adding in other countries—including Africa, South America, Venezuela and Mexico. Is that more so than here?

Mr Miller—Firstly, I am not aware of all those countries that you have talked about. Secondly, trying to compare the tax systems of different countries is again well outside the ATO's purview. It really is something you should direct at Treasury.

Mr ALLAN MORRIS—But if you have companies dealing both here and overseas, such as BHP in Venezuela and Rio Tinto in more than one country, you are therefore required to know what they are doing in other countries, aren't you, to be able to work out whether they are paying the appropriate tax here?

Mr Miller—You may or may not need to.

Mr ALLAN MORRIS—I think nowadays with the legislation on company responsibility, they are required to advise you of what other countries they are involved in and where they are being taxed at.

CHAIR—It depends on whether we have a double tax agreement with that particular country.

Mr ALLAN MORRIS—No, not quite, because we did extend that some years ago so that it is automatic. Whether there is a tax agreement is one part of it but, if it is not, you can follow it through. So they are required to tell you. I am trying to find out if what some people are saying is correct that there should be a discernible movement in accounting and tax with company investment going away from Australia into other countries where they have similar investments? That would be invisible to you because you would need to be the ones that were actually doing it.

Mr Miller—We obviously do not have that information on hand at the moment. We can take it on notice. Just to clarify your question, you are looking for what knowledge the ATO has about movement of—

Mr ALLAN MORRIS—Investment focus in resource developments.

Mr Miller—Into other countries. I am not sure if the tax office would have that. The DISR might have that—

Mr ALLAN MORRIS—No, they would not know. You would know, for example, from the BHP accounts of their investment in Venezuela in HBI compared with their investment in HBI in Australia. They have identical plants in two separate countries with two separate tax regimes. They tell us that it is much more competitive to invest in other countries than to invest here. We do not know. You have CRA and Anglo—certainly CRA were listed here and they have now

moved. One of the real fears we are being told about Shell is that they will shift their focus of their investment into other countries' accounting systems and tax systems rather than here.

Mr Miller—The best I could do is say that we will look to see if we have such data or information and take it on notice and provide that to you, if we can. Remember that we are in a self-assessment environment. We do not sit in with each company on a day to day basis to know what they are doing. It is only when we audit and investigate a particular company that we might see that they have moved investment. It will not necessarily be something we will record because it will not necessarily be relevant from a tax point of view.

CHAIR—Mr Miller, could you bring back to the committee information on the basis that what we are keen to assess is if there are any impediments to investing in Australia. If those impediments happen to be tax and investment impediments, we would like to be alerted to those. We do not necessarily want the solution; we just want to be made aware of those impediments. Dr Washer, did you have another question?

Dr WASHER—Basically it was that point. Geoff, I think you summarised it very well. I guess the paperwork does not fit into your portfolio, so we need to take that back to Industry because I think it would be very valuable for us to have a look at that paperwork. We will chase them on that.

Mr ZAHRA—I want to come back to that point I was trying to make earlier because I am a bit worried that maybe you misunderstood my question. The point I was trying to make and the opinion I was trying to get from the ATO is, from an administration point of view, are things like zonal taxation straightforward to administer or difficult to administer? I do not want to know how much revenue you get or any of those things; I just want to know whether or not it is straightforward or difficult to administer. That is all. Would you be able to give me an answer in relation to that or is it that outside the purview of the ATO?

Mr Miller—Zonal taxation—we have the zone rebate. I do not think we have too many others in zonal taxation, and that is just a very small one. We could talk about the administration of the zone rebate. It has to be from the experience we have, and the experience we have is with the zone rebate. We could say whether that is easy or not easy to administer and we could come back with something on that, if that would help.

Mr ZAHRA—Yes, that would help. But surely within the ATO you would have been asked to investigate from time to time other types of zonal taxation?

Mr Miller—Not to my knowledge.

Mr ZAHRA—This is not a new idea. It has been around for a long time. Could you perhaps undertake to have a look through ATO records to see if any analyses have been done on whether or not it is straightforward from an administration point of view? I am sure other people on the committee would welcome that as well. It is very important to us because there is no point our making a decision in relation to it if you end up with all sorts of anomalies and a system that does not work.

Mr Miller—I will check our records to see if we have had any consideration of that.

Mr ALLAN MORRIS—I have just a few more questions. Can you tell me the taxation significance, perhaps not now, if a company shifts its corporate base from Australia to London, for example, and changes its stock market listings predominantly from the Australian Stock Exchange to the London Stock Exchange? I am thinking here about Rio Tinto, Billiton and Shell Woodside—those kinds of examples. What is involved in shifting the tax liability? What does the company have to do? Can it list on the London Stock Exchange totally and still pay taxes in Australia or does it—

CHAIR—I think my colleague is talking about the withholding tax earned on Australian earnings. Then, of course, the franking dividend would go back to shareholders if the company is then listed on the London Stock Exchange or the New York Stock Exchange as opposed to the ASX.

Mr ALLAN MORRIS—If it eventually shifts its company base, corporate registrations or whatever it is. I mean, I understand that BHP will be 60 per cent foreign owned with the BHP-Billiton merger. What makes a company pay tax in Australia? Can it choose to therefore shift its tax payments system to London or to somewhere else and therefore we lose the \$1½ billion a year that BHP pay in tax less their write-offs? Can you give us a bit of paper explaining that to us, because that is a bit of a mystery to most people in the community, particularly to us?

Mr Miller—I will take that on notice and refer to my international colleagues who are probably more familiar with this area.

Mr ALLAN MORRIS—I will try to explain my first question to you again. A company wants to say to its investors, ‘We are going to be terrific. We have tested our technology really well.’ You say that, because you have done all that, you are low risk. But the market says that, because you are new, you are actually a high risk. That constant tension between high risk and good investment is a real problem for us in terms of value adding, particularly in resources.

We have asked Industry about it and they say it is partly tax office. Then you say it is partly them. Is it possible to get a joint position on the differential between a technical risk in terms of a new project—for example, if a company wanted to establish a plant for magnesium, which is one that we know about ignoring the individual companies, or a new technology such as the new iron making technologies—and a capital risk as an investment from the investment markets; that is, the capital risk compared with the technical risk from the Taxation Office point of view, because it seems to me they get locked out of both. They get punished on both ends. They are treated as high technical risk by the investment market and not technical risk by Industry or tax office, whichever of you make that final judgment.

Mr Cooper—It is certainly Industry that makes the judgment as to whether—

Mr ALLAN MORRIS—We asked them and they keep saying, ‘We don’t actually administer the tax act.’ There is constant buck passing, and we need to get an accurate picture. I am not satisfied we have one at the moment.

Mr Miller—That is why they have the IR&D board. When these issues come up that are hard to resolve, they get referred off to the IR&D board and these decisions are made. The tax office does not have any input to that. We have to ask them for the advice as to whether these activities

are research and investment or not, and that includes all the risk factors and technical factors, because we are not experts in this area. We do not have the expertise to make those decisions.

Mr ALLAN MORRIS—That is what the companies tell us and they insist that you do. The perception is that it is the tax office that makes those judgments.

Mr Cooper—That is quite wrong.

Mr ALLAN MORRIS—Either you are being scapegoated or someone needs to explain it somewhere. I asked Industry the same question, and you saw the *Hansard*. Can you get your people in Tax who talk to Industry and the people in Industry who talk to Tax to give us a joint statement of some form that actually clarifies this? It is not much good you telling us one week and they telling us something different next week. We just cannot get a common position. That would be really helpful.

Mr Miller—Okay, we will try.

CHAIR—We need to wrap this up.

Mr ALLAN MORRIS—Today has been very useful. I am sure that will help us a lot with our investigations. The other area that is a bit messy for us—back to that tax write-off issue—concerns a small startup company with R&D where the owner puts his house on the line effectively and the tax office holds him personally liable for the debts that may be accrued. Yet a large public company writes off \$500 million of tax losses, and no-one is even asked a question about it. There seems to be a big differential between how you apply the rules to a small company in that R&D area in terms of their personal liability for negligence, incompetence, insolvency and so on but not to a large company. A large company writes off half a billion dollars. There have been some quite visible ones in very successful companies where they write off very large amounts without a question; yet if a small company does that the owner loses his house.

CHAIR—Hang on, it depends on whether he trades under his own name or a corporate structure.

Mr ALLAN MORRIS—Under a corporate structure he can still be personally liable for the company debts. But in a public company they are not.

CHAIR—It is a limited company; that is why. The small ones are Pty Ltd; the other is just a limited company. Are you going to chase all the shareholders?

Mr ALLAN MORRIS—They are both limited. It is not the shareholders who make the problem; it is the directors that make decisions that the company gets burnt on and writes off shareholder value.

CHAIR—What is your question to the ATO?

Mr ALLAN MORRIS—I am trying to clarify the concern we get from small companies where the tax office seem to be tough on the small companies, but when large companies write off large amounts then no-one even asks a question. How do you evaluate company losses and company write-offs at that large corporate level? Do you investigate whether or not they were properly accrued?

Mr Cooper—Certainly at the large corporate level there is a risk assessment process in place that is quite detailed, whereby the affairs of companies are reviewed, scrutinised and, where appropriate, audit action is taken.

Mr ALLAN MORRIS—So when a company writes off half a billion dollars or \$1 billion on a failed project, what investigation takes place to ensure that is actually done properly?

Mr Cooper—With the amounts you are talking about, it is the sort of thing that would come up in a review, and an auditor would go out and ask questions.

Mr ALLAN MORRIS—And produce a report that goes to the ATO?

Mr Cooper—Yes.

Mr ALLAN MORRIS—That is all private, is it not? Even though it is a public company, that is a private process.

Mr Cooper—Certainly the secrecy provisions prevent any public disclosure of the tax affairs of any corporate, large or small.

Mr ALLAN MORRIS—If a small company goes broke, a liquidator is appointed and that becomes a public process. I find it mystifying that on the one hand we have huge write-offs happening almost invisibly but, on the other hand, relatively small companies get a very high level of scrutiny, particularly from you. I have dealt with the tax office on a few company failures where you are absolutely merciless on people with liabilities. But I have watched them write off billions with large companies and it is not a problem.

Can you give us a note on the processes that are involved on large company write-offs and failed projects of a technology nature, because that is probably what is causing a problem in the investment market? They see this is happening and think there is no scrutiny, no accountability. Therefore, they are wary about getting involved. If you try to get people to invest in iron making now, they say, 'No, after Port Hedland, forget it.' A lot of money was lost on that stuff. We do not know why. No-one seems to understand what went wrong or what happened; but, because it happened, they are not going to let you do anything about it. They will not invest any more.

Mr Miller—I am not sure what you want from the tax office.

Mr ALLAN MORRIS—Your processes when companies write off large amounts on failed large projects, whether it be copper, iron ore or whatever. What are the processes with oil drilling and oil exploration stuff which gets written off with gay abandon? They write off a

refinery or a large project here, there and everywhere—what investigation takes place? What accountability? What assurance does the taxpayer have that that has been properly evaluated?

Mr Miller—Okay.

CHAIR—Thank you very much for that. I take it that you are not doing anything over Easter!

Mr ALLAN MORRIS—If I can just ask one more tiny question: it has been put to me that what we should be talking about is investment allowance rather than R&D write-offs for large projects. There must be a paper in taxation, because investment allowances were around in the past, somewhere as to how they operated.

Mr Miller—How investment allowances operated?

Mr ALLAN MORRIS—Were they an effective form; were they difficult to monitor, difficult to police or whatever?

Mr Miller—I do not know if there is anything—

Mr ALLAN MORRIS—The Fraser government, for example, had an investment allowance and things of that nature.

Mr Miller—We can certainly give you a description of what it was. Whether there are any papers assessing—

Mr ALLAN MORRIS—It is just that people are saying that would be a better way of doing it than R&D write-off or other ways—

Mr Miller—Those sorts of papers that look at whether it is better to do it one way or the other you find in Treasury, not in Tax. Treasury does that assessment of what is the best tax outcome. I will have a look but I am not sure we will have anything.

Mr ALLAN MORRIS—If you can have a look, thanks. I am mindful of this boundary area between Treasury and Tax.

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

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

Committee adjourned at 12.26 p.m.