



COMMONWEALTH OF AUSTRALIA

Official Committee Hansard

SENATE

ECONOMICS LEGISLATION COMMITTEE

ESTIMATES

(Budget Estimates)

TUESDAY, 30 MAY 2006

CANBERRA

BY AUTHORITY OF THE SENATE

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SENATE
ECONOMICS LEGISLATION COMMITTEE
Tuesday, 30 May 2006

Members: Senator Brandis (*Chair*), Senator Stephens (*Deputy Chair*), Senators Chapman, Murray, Watson and Webber

Senators in attendance: Senators Brandis, Chapman, Ferris, Fielding, Ludwig, Mason, Murray, O'Brien, Parry, Sherry and Watson

Committee met at 9.04 am

TREASURY PORTFOLIO

Consideration resumed from 29 May 2006.

In Attendance

Senator Minchin, Minister for Finance and Administration

Department of the Treasury

Dr Ken Henry, Secretary

Outcome 1: Sound Macroeconomic Environment

Output Group 1.1: Macroeconomic Group

Dr Martin Parkinson, Executive Director

Mr David Parker, Alternate Executive Director

Dr David Gruen, Chief Adviser (Domestic)

Mr David Pearl, General Manager, International Economy Division

Mr David Turvey, Manager, International Economy Division

Mr Nathan Dal Bon, Manager, International Economy Division

Dr Steven Kennedy, General Manager, Domestic Economy Division

Mr Jason Allford, Acting Principal Adviser (Forecasting)

Ms Angelia Grant, Domestic Economy Division

Mr Graeme Davis, Manager, Macroeconomic Policy Division

Mr Paul O'Mara, General Manager, Macroeconomic Policy Division

Mr Greg Coombs, Macroeconomic Policy Division

Mr Russell Campbell, Manager, Macroeconomic Policy Division

Outcome 2: Effective Government Spending Arrangements

Output Group 2.1: Fiscal Group

Mr David Tune, Executive Director

Mr David Martine, General Manager, Budget Policy Division

Mr Jason McDonald, Manager, Budget Policy Division

Mr Rob Heferen, General Manager, Social Policy Division

Mr Peter Robinson, Principal Adviser, Social Policy Division

Mr Michael Willcock, General Manager, Commonwealth-State Relations Division

Ms Maryanne Mrakovcic, General Manager, Industry, Environment and Defence Division

Mr Frank Di Giorgio, Specialist Adviser, Industry, Environment and Defence Division

Mr Ian Robinson, General Manager, Corporate Services Division

Outcome 3: Effective Taxation and Retirement Income Arrangements

Output Group 3.1: Revenue Group

Mr Mike Callaghan, Executive Director

Mr Paul McCullough, General Manager, Tax System Review Division

Mr John Lonsdale, General Manager, Superannuation, Retirement and Savings Division

Mr Trevor Thomas, Principal Adviser, Superannuation, Retirement and Savings Division

Mr Patrick Boneham, Senior Adviser, Superannuation, Retirement and Savings Division

Mr Mark O'Connor, General Manager, Individuals and Exempt Tax Division

Ms Marisa Purvis-Smith, Manager, Individuals and Exempt Tax Division

Mr Nigel Ray, General Manager, Tax Analysis Division

Mr Phil Gallagher, Manager, Tax Analysis Division

Mr Colin Brown, Manager, Tax Analysis Division

Mr Peter Greagg, Manager, Tax Analysis Division

Mr Colin Johnson, General Manager, Business Tax Division

Mr Mike Rawstron, General Manager, International Tax and Treaties Division

Ms Jo Laduzko, Manager, International Tax and Treaties Division

Mr Hadyn Daw, Manager, International Tax and Treaties Division

Mr Bruce Paine, General Manager, Board of Taxation

Outcome 4: Well Functioning Markets

Output Group 4.1: Markets Group

Mr Jim Murphy, Executive Director

Mr Gerry Antioch, General Manager, Foreign Investment and Trade Policy Division

Mr Chris Legg, General Manager, Financial System Division

Ms Vicki Wilkinson, Manager, Financial System Division

Mr Damien White, Manager, Financial System Division

Mr Trevor King, Manager, Financial System Division

Mr Andre Moore, Manager, Financial System Division

Ms Kerstin Wijeyewardene, Manager, Financial System Division

Mr Geoff Miller, General Manager, Corporations and Financial Services Division

Mr Andrew Sellars, Senior Adviser, Corporations and Financial Services Division

Mr Matt Brine, Manager, Corporations and Financial Services Division

Mr David Love, Manager, Corporations and Financial Services Division

Ms Ruth Smith, Manager, Corporations and Financial Services Division

Mr Bede Fraser, Manager, Corporations and Financial Services Division

Mr Jorge del Busto, Senior Adviser, Corporations and Financial Services Division

Mr Steve French, General Manager, Competition and Consumer Policy Division

Ms HK Holdaway, Manager, Competition and Consumer Policy Division

Ms Sandra Patch, Senior Adviser, Competition and Consumer Policy Division

Ms Louise Seeber, Senior Adviser, Competition and Consumer Policy Division

Mr David Hall, Manager, Competition and Consumer Policy Division

Mr Brad Archer, Manager, Competition and Consumer Policy Division

Mr Peter McCray, General Manager, Financial Literacy Foundation

Mr Grahame Crough, Manager, Financial Literacy Foundation

Mr John Riley, Financial Literacy Foundation

Mr Peter Martin, Australian Government Actuary

Australian Taxation Office

Mr Michael D'Ascenzo, Commissioner

Mr Greg Farr, Second Commissioner

Ms Raelene Vivian, Deputy Commissioner

Ms Donna Moody, Chief Finance Officer

Mr Mark Jackson, Deputy Commissioner

Ms Stephanie Martin, First Assistant Commissioner

Ms Margaret Crawford, Chief Operating Officer

Mr Mark Konza, Deputy Commissioner

Mr Shane Reardon, Deputy Commissioner

Inspector-General of Taxation

Mr David Vos, Inspector-General

Mr Rick Matthews, Deputy Inspector-General

Australian Office of Financial Management

Mr Neil Hyden, Chief Executive Officer

Mr Paul Power, Chief Operations Officer

Mr Michael Bath, Director, Financial Risk

Mr Gerald Dodgson, Head, Treasury Services

Mr Pat Raccosta, Chief Financial Officer

National Competition Council

Mr John Feil, Executive Director

Takeovers Panel

Mr Nigel Morris, Director

Financial Reporting Council

Mr Charles Macek, Chairman

Australian Securities and Investment Commission

Mr Jeffrey Lucy, Chairman

Mr Jeremy Cooper, Deputy Chairman

Mr Mark Steward, Deputy Executive Director, Enforcement

Australian Prudential Regulation Authority

Dr John Laker, Chairman

Mr Ross Jones, Deputy Chair

Mr Charles Littrell, Executive General Manager, Policy Research and Statistics

Mr Brandon Khoo, Executive General Manager, Specialised Institutions

Productivity Commission

Mr Bernard Wonder, Head of Office

Mr Garth Pitkethly, First Assistant Commissioner

Mr Michael Kirby, First Assistant Commissioner

Australian Bureau of Statistics

Mr Dennis Trewin, Australian Statistician

Mr Jonathan Palmer, Deputy Australian Statistician, Services Group

Ms Susan Linacre, Deputy Australian Statistician, Population Statistics Group
Mr Dennis Farrell, A/Deputy Australian Statistician, Economic Statistics Group
Mr Paul Williams, Assistant Statistician, Census and Geography Branch
Mr Carl Obst, Assistant Statistician, National Accounts Branch
Mr Mark Whybrow, Chief Finance Officer

Corporations and Markets Advisory Committee

Mr John Kluver, Executive Director

Australian Accounting Standards Board

Mr David Boymal, Chairman

Mr Angus Thomson, Technical Director

Australian Competition and Consumer Commission

Mr Graeme Samuel, Chairman

Mr Joe Dimasi, Acting Chief Executive Officer

Mr Mark Pearson, Executive General Manager, Enforcement and Compliance Branch

Ms Rose Webb, General Manager, Enforcement and Co-ordination Branch

Mr Tim Grimwade, General Manager, Mergers and Asset Sales

Mr Scott Gregson, General Manager, Adjudication Branch

Mr Robert Antich, General Manager, Policy and Liaison Branch

Mr Nigel Ridgway, General Manager, Compliance Strategies Branch

Mr Michael Cosgrave, Executive General Manager, Communications Group

Mr Gary Dobinson, Director, Transport and Prices Oversight

Ms Helen Lu, General Manager, Corporate Management Branch

Mr John Bridge, Chief Finance Officer

Ms Lisa Anne Ayres, Executive Branch

Mr Peter Maybury, Director Finance and Services

CHAIR (Senator Brandis)—I declare open this hearing of the Senate Economics Legislation Committee. The Senate has referred to the committee the particulars of proposed expenditure for 2006-07 and certain other documents for the portfolios of Industry, Tourism and Resources and Treasury. The committee may also examine the annual reports of the departments and agencies appearing before it. The committee is due to report to the Senate on 20 June 2006 and has fixed Friday, 28 July 2006 as the date for the return of answers to questions taken on notice.

The committee today will begin its examination of the Treasury portfolio, beginning with the Australian Taxation Office and the Revenue Group of Treasury. It will then continue through the printed agenda that has been circulated. Under standing order 26, the committee must take all evidence in public session unless it resolves to take evidence in private session in accordance with the privilege resolutions. I remind all witnesses that, in giving evidence to the committee, they are protected by parliamentary privilege. It is unlawful for anyone to threaten or disadvantage a witness on account of evidence given to a committee and such action may be treated by the Senate as contempt. It is also a contempt to give false or misleading evidence to a committee.

The proceedings today are governed by privilege resolutions passed by the Senate, and I draw to the attention of witnesses and honourable senators those resolutions dealing with the question of relevance. Privilege resolution 1(9) provides:

A chairman of a committee shall take care to ensure that all questions put to witnesses are relevant to the committee's inquiry and that the information sought by those questions is necessary for the purpose of that inquiry. Where a member of a committee requests discussion of a ruling of the chairman on this matter, the committee shall deliberate in private session and determine whether any question which is the subject of the ruling is to be permitted.

The Senate in 1999 adopted the following test of relevance:

Any questions going to the operations or financial positions of the departments and agencies which are seeking funds in the Estimates are relevant questions for the purposes of Estimates hearings.

Privilege resolution 1(10) deals with objections to answering questions taken by witnesses and provides:

Where a witness objects to answering any question put to the witness on any ground, including the ground that the question is not relevant or that the answer may incriminate the witness, the witness shall be invited to state the ground upon which objection to answering the question is taken. Unless the committee determines immediately that the question should not be pressed, the committee shall then consider in private session whether it will insist upon an answer to the question, having regard to the relevance of the question to the committee's inquiry and the importance to the inquiry of the information sought by the question. If the committee determines that it requires an answer to the question, the witness shall be informed of that determination and the reasons for the determination, and shall be required to answer the question only in private session unless the committee determines that it is essential to the committee's inquiry that the question be answered in public session. Where a witness declines to answer a question to which a committee has required an answer, the committee shall report the facts to the Senate.

I remind officers that they are subject to the foregoing. There are no areas in connection with the expenditure of public funds where any person has a discretion to withhold details or explanations from the parliament or its committees, unless the parliament has expressly provided otherwise. However, I also remind witnesses and honourable senators that by custom and practice of this committee there are certain questions that will not be pressed or required to be answered at least in public session, including in particular questions concerning the confidential affairs of taxpayers and questions concerning investigations by agencies. The Senate has resolved that an officer of a department of the Commonwealth or of a state shall not be asked to give opinions on matters of policy and shall be given reasonable opportunity to refer questions asked of the officer to superior officers or to a minister.

[9.09 am]

Australian Taxation Office

Treasury

CHAIR—I welcome the Commissioner of Taxation, Mr D'Ascenzo, and officers of the Australian Taxation Office and officers from the Revenue Group of Treasury. I am told that the minister is delayed, but subject to your cooperation, Mr D'Ascenzo, if you do not have any objection to us starting in the minister's absence, we will begin.

Mr D'Ascenzo—I have no objection.

CHAIR—Mr D'Ascenzo, do you wish to make an opening statement?

Mr D'Ascenzo—No, I do not.

CHAIR—For the information of senators, the way in which I propose to deal with the order of questioning today and for the rest of the week, subject to flexible arrangements that might be made between individual senators, is to give the first call to opposition senators, the next call to government senators, the next call to minor party senators and then, if there are other senators who wish to ask questions and who have not been reached, I will give them the call.

Senator LUDWIG—I think this is more of a clarification than asking for the call, because it will be later on in the program. I do not want to take the first question in that sense. I was with Customs the other night, and they referred me back to Treasury for costings of what is called an accredited client program output. They sent it to Treasury for costings. Which output group would that fall within?

Mr Callaghan—It would be Revenue Group.

Senator LUDWIG—That is 3.1?

Mr Callaghan—Yes.

Senator LUDWIG—So that is tomorrow?

Mr Callaghan—No, it is today.

Senator LUDWIG—The *Rethinking regulation* report would obviously fall within the Productivity Commission, but where in Treasury would it fall?

Mr Callaghan—The report covers many aspects. There is some dealing with tax, but there are many dealing with all parts of the program. Which particular area of the report is it?

Senator LUDWIG—The part dealing with Customs, the accredited client program and the like.

Mr Callaghan—Well, that is Customs.

Senator LUDWIG—No, it also relates to Treasury, as in the costings.

Mr Callaghan—It would be this output.

CHAIR—We will be asking questions of Revenue Group under outcome 3, Effective taxation and retirement income arrangements. Senator Sherry, do you have a question?

Senator SHERRY—I just want to start with some matters dealing with the forecasting of revenue. Over the last two years of budget papers in particular, we have seen a surge in tax revenues, particularly corporate tax, apparently associated with the profitability in the mining sector. Has Treasury sought to quantify what level of additional company tax revenue can be attributed to the current commodity price cycle?

Mr Callaghan—That is included within reaching our aggregate numbers, when we are doing the projections, of what the revenue projections are. The information, with a lag, becomes public as to the breakdown of the components of company revenue.

Senator SHERRY—What do you mean by lag?

Mr Callaghan—I think it is available in the taxation statistics in terms of that being when you would see a breakdown, but we do not itemise within our projections. There is some information included in the budget papers which shows the growth of various industrial

sectors, and we have seen strong growth in many aspects of the corporate sector, not only in mining, but also in the financial sector, for example.

Senator SHERRY—You refer to published. Do you do the calculation and not publish it?

Mr Callaghan—Yes, we do not have an itemised breakdown of the various sectors of the corporate area. We look at it across the various components in order to be able to make our forecasts and then our projections.

Senator SHERRY—Does Treasury quantify the level of additional revenues that are cyclical rather than structural?

Mr Callaghan—No, we do not.

Senator SHERRY—Why don't you?

Mr Callaghan—It is very hard to determine it. In doing the revenue forecast, it is very hard to back out how much of it is coming from what we would say are structural components and how much is coming from the cycle. We are looking at the overall developments in the economy.

Senator SHERRY—So Treasury has not been able to determine whether there is a cyclical boost to personal incomes tax revenues, for example?

Mr Callaghan—What is the definition of the cycle? We are looking at what the drivers are behind things. For example, if it is personal income tax, we are seeing growth in employment and in wages. They lead to increases in personal income tax. We do not back out and say how much of this is the cycle and how much of it is coming from some underlying structure. It is a very difficult—and conceptually difficult—estimate to make. We are focusing on trying to come up with the aggregate numbers.

Senator SHERRY—How has personal income tax, for example, been affected by the commodity price cycle?

Mr Callaghan—As we have seen, you would see growth in employment in areas that are directly related to the mining sector. We would see growth in wages in areas that are directly related to the mining sector. And then it would go right through the economy. You would see it then through increases in company profits—increases in dividend payments, for example; and increasing consumption activities, which could then lead through to greater economic activity. So it is a diffuse process that works its way through the economy.

Senator SHERRY—Let us take the commodity price cycle. What does it feed through to? Does it feed through to almost all revenue heads—income tax, company tax, superannuation tax? Are they all impacted?

Mr Callaghan—All aspects of the economy are interrelated, almost by definition. That is the way the economy functions. We see one sector impacting on another. So, yes, you are right.

Senator SHERRY—Treasury's projection of commodity prices is, I understand, falling in two steps to long-run averages. Has that been reflected in revenue forecasts by revenue head?

Mr Callaghan—In terms of preparing the forecasts, yes, it is.

Senator SHERRY—Could you describe how it impacts?

Mr Callaghan—As I think was outlined in last year's budget papers, it is affecting the projections. The projections are not forecasts—they are really just projecting out a long-run trend growth. We have seen a very strong growth in commodity prices, which has seen a very strong growth in nominal deflator. If we had adopted the normal methodology, we would have just applied a continuing long-term growth rate to this very high level. That would have fed through into very high corporate profits. We have assumed that there will be a step-down in the prices that aspects of the mining sector receive. That will then feed through into our estimate of the growth in corporate taxes coming from those aspects of the mining sector.

Senator SHERRY—Let us take corporate tax revenues. Over the forward estimate period they appear to hold up, despite the projection that commodity prices—and, presumably, commodity related profits—will fall to long-run averages. So how do those corporate tax revenues hold up as a consequence of that background?

Mr Callaghan—If we had not made what was described as a prudent assumption about the rate of growth in commodity prices of the step-down, you would have seen an even stronger growth in corporate profits. You are looking at the difference between one that would have been much stronger, coming off a higher level in corporate profits, to one that is being stepped down.

Stepping it down does not mean that corporate profits are going to fall at all. It does not mean that mining sector profits are going to fall. We are looking at rates of growth. As I have said, with this very strong growth in prices, if we had just adopted the same methodology you would be starting from that very high base and projecting forward on long-term growth rates. We have stepped it down, so there is still a rate of growth but not as much as if you had projected off those very high levels.

Senator SHERRY—If you take a look at company tax revenues, it is apparent there have been significant revisions since the last budget.

Mr Callaghan—Yes.

Senator SHERRY—Even in MYEFO, they have been very, very significant, particularly in the latter years of the forward estimates. For instance, company tax revenues have been revised up by \$8.7 billion in 2007-08, which is a significant figure, isn't it?

Mr Callaghan—Yes.

Senator SHERRY—If we compare that to the last budget, it is a 17.5 per cent increase. What accounts for that?

Mr Callaghan—If you look at the last budget—and we have discussed this in Senate estimates before—you will see that one of the things that started off accounting for it was that people, not solely ourselves, did not project or forecast the extent of the rise in commodity prices. That is one factor. We have seen that there has been very strong, continuing growth in corporate profits. In last year's budget papers we outlined some of the factors we were looking at to try to explain why we are seeing corporate profits that are growing much stronger than the rate of growth of income or profits. I should say that tax payment is occurring faster than the rate of profits. That is what we are focusing on with corporate taxes.

There are a number of elements we have been exploring that have been outlined in the previous budget. In the most recent budget there are some further factors we have looked at that may explain it. There are reasons for us looking at what is the greater responsiveness we are seeing of tax revenue to the changes in profits. Underlying that, we still have seen very strong corporate profitability coming off the back of the mining sector, but, as I said, we have also seen it in the financial sector and more generally across the corporate sector.

Senator SHERRY—With regard to the increase in tax revenue that I have referred to—the revision up of \$8.7 billion in 2007-08 from the last budget—how does that relate to corporate profitability in the mining sector as distinct from the non-mining sector? Have you seen a significant impact in terms of additional revenue flowing from the mining sector compared with other sectors?

Mr Callaghan—I think we have seen an increase coming from the mining sector, and we have seen an increase coming from other sectors. If you look at the budget papers you will see that there is an explanation as to why we think we are going to see even stronger growth in corporate profits in 2006-07 coming from the mining sector. This is because in 2005-06, for a number of reasons, there were bottlenecks and there was also adverse weather, and some of the mining companies had interruptions in their ability to fulfil contracts at much higher prices. Previously we had assumed that they would be fulfilling these contracts at higher prices, their profits would have been that much higher in 2005-06 and there would even have been a higher corporate tax rate. What we have seen are delays in their ability to be able to fulfil those contracts, and that has pushed that profit into 2006-07. It is not as though we saw a hole at all in 2005-06 in the profits coming from the mining sector. So we are still seeing very strong profits notwithstanding that we see factors that are pushing some of that higher profitability into 2006-07. Again, it is just coming back that what we are seeing is some very significant strength in corporate tax rates coming from what we are seeing in profits. It is one of the reasons we are devoting resources to try to have a better understanding of some of the factors that may be accounting for this. As I said, in last year's budget we outlined some of the factors we are looking at, and in this year's budget we are looking at some of the other factors. We are trying to understand why we are seeing much stronger company tax coming from given levels of corporate profit, but we are also seeing that profit rise very strongly.

Senator SHERRY—You are saying that you are devoting resources to examining these factors to better understand them. What issues are you looking at, aside from the ones we have already touched on?

Mr Callaghan—We did not touch on them; we just covered them in general, I suppose. In last year's budget there was a discussion about elements of, as we have seen, the long-term growth in the corporate cycle that may be reductions in the amount of losses available to deduct over your taxable income. We have seen, with refundable imputation credits, that there is a very high premium on the share markets for having fully franked dividends. There is almost a premium on companies paying their tax. It reduces their cost of capital to shareholders. There were a range of other discussions. There was the movement of government business enterprises into the corporate tax sector. There were a few other factors referred to in last year's budget. In this year's budget we have looked at a number of other elements. One of them is that we have seen a lowering in gearing by companies. There are

fewer deductions in terms of interest payments. We have seen a significant shift in the gearing ratios of companies. This means that going back into the eighties and before higher interest payments were being deducted to determine what their taxable income was and what taxes were being paid.

We have also been—and the corporate sector has focused on this—looking at why the effective company tax rate has increased. If we make comparisons going back, companies are now paying tax essentially on the income they are earning in the given year; in the past it was always paid the year after. In a period of rising profits, in the previous approach you would have had a lower effective tax rate because you were paying tax on the previous year's profit and when you put it over your current year's profit it would seem that you are paying less. With the change in the way companies pay their tax, they are paying their tax on rising profits, which can seem that there is a higher effective tax rate. There are a number of these elements we are looking at.

Senator SHERRY—Going back to the mining issue for a moment, can you tell me the mining sector's approximate share of total corporate profits?

Mr Callaghan—I am not sure; I would have to look it up.

Senator SHERRY—Is there anyone who can assist us in that regard?

Mr Callaghan—I am not sure. 'Small' is the only advice I have.

Senator SHERRY—I have been told about five per cent. Is that what we are talking about?

Mr Callaghan—That sounds about right.

Senator SHERRY—We have talked about the various factors that you have had under examination which are leading to an increase beyond that projected for corporate profits in last year's budget. Do you make an assumption in relation to corporate profits as a share of GDP?

Mr Callaghan—That comes out from looking at the forecasts that are made where we derive the parameters that drive our growth in taxable income. That is one of the factors that comes out of the area of the Treasury that looks at the macro forecasts. That is certainly one of the things that falls out from the bottom.

Senator SHERRY—Is the level of corporate profit as a percentage of GDP trending upwards?

Mr Callaghan—Yes, it has been trending up. I think it is now at record levels.

Senator SHERRY—Why would it be the case that corporate profits are trending upwards as a percentage of GDP?

Mr Callaghan—All the factors that you have talked about before are driving it. We have seen this very strong growth in mining. Mining might be small but it has had phenomenal rates of growth. We have also seen other areas in the corporate sector—in particular, the financial sector—performing very strongly.

Senator MURRAY—On the same issue, could you perhaps tell us what effect the integrity measures and the base broadening have had in corporate revenue growth since 2000? My

impression is that those integrity measures have led to a greater number of SMEs paying tax that formerly did not pay tax—they were either avoiding it or were not subject to more stringent audit and controls. My impression is that the actual net tax rate per dollar of revenue has risen. So although the nominal tax rate has fallen, the net tax rate has risen and integrity measures have had a lot to do with the growth in corporate tax revenue. If that is true, and I think it is true, are you able to measure the effect?

Mr Callaghan—I think that is true. That was one of the factors that was outlined in the last year's budget. It could be the integrity measures that have taken place as well as the increased audit activity of the Australian Tax Office, but it is very hard to have the counterfactual to attribute how much of the growth in taxable income we are seeing is from better compliance activity by taxpayers and the increased audit activity of the Australian Tax Office. I am not aware that you could isolate how much can be attributed to that factor.

Senator MURRAY—I seem to recall—and the tax commissioner might know—that something like 35 per cent of SMEs were not paying tax at all. If that percentage has dropped, would that be a signal that more corporate taxpayers were being pulled into the net?

Mr Callaghan—As I said, I am not aware of estimates as to how much had not been and how much has since been brought into the net.

ACTING CHAIR (Senator Watson)—On the same topic of revenue estimates, Mr Callaghan, while you and your colleagues appear to have a very good understanding of the factors which affect corporate profitability, for a number of years now federal government budget surpluses have been quite spectacularly underestimated because the government continues to get a lot more revenue than expected. The main source of this, of course, is company tax, as you have stated. This consistent pattern of underestimating company tax could well have caused a situation of not proceeding with some worthwhile tax reforms on the basis that they were unaffordable at the time. I can appreciate that all revenue authorities have difficulty accurately forecasting company tax, and Australia is probably not the worst offender. In terms of possible improvement, which is where I always try to come from, I understand that the US Treasury is currently working on some arrangement to try to improve the situation. Could you give us some advice as to whether what the US revenue authorities are doing could have any relevance here in Australia? Are you undertaking work in relation to modelling to try to improve the revenue forecasting area, as the Americans are embarking upon?

Mr Callaghan—I do not know what the Americans are doing, but I do have a few comments on what you have just said.

Senator SHERRY—Do you know what you are doing in terms of this issue? As Senator Watson and I have said, the forecasts in this area are very inaccurate over the forward estimates.

Mr Callaghan—First of all, we are not the only ones who have been missing out. Look at others—and there are not that many people who would be forecasting what is happening in terms of revenue. Access Economics, for example, in the most recent *Budget Monitor* they put out said, 'Here we go again. We, along with Treasury for the last number of years, are now going to revise up significantly our forecast for revenue.'

Senator SHERRY—You are pre-empting my quotes from Mr Richardson, which I was going to get to—and some other ones, too.

Mr Callaghan—As you see, he has acknowledged that, and previously he said there was something weird going on in the economy. What was that weird thing going on in the economy? It is all about commodity prices—well, not all about commodity prices, because we have seen other elements and other components growing strongly. One of those is ‘other individuals’. What is being picked up in there is capital gains tax. We have seen very strong growth in capital gains tax coming from the very strong growth we have had in asset prices.

Going back to the company side of things, it does come down to the fact that we have seen this very strong growth in commodity prices. If we go back a few years, and you are talking about performance over a number of years, no-one predicted that we were going to be seeing the growth in coal and iron ore prices of 70 per cent to over 100 per cent. If you go back and have a look at what some of the analysts in the market out there were saying, there are quotes we can produce. One I can recall is: ‘You would have had your head read if, 12 months ago, you had said we were going to see rates of growth of this order of magnitude.’ We have seen developments in commodity prices that no one anticipated. That is one factor.

But, as we were talking about, there are other things going on in terms of the performance of tax revenue to company profits that we are trying to understand. And, yes, other forecasting authorities are doing the same. We are trying to look at and improve our forecasting methodology and we are trying to understand the relationship between what we are seeing with company tax performance and company profits.

As we noted in last year’s budget paper, we have essentially made a change in our forecasting methodology. We are now factoring in that we will get, in very simple terms, higher tax revenue for any given change in company profits. Chris Richardson from Access Economics referred to it as an accelerator, but it is not really an accelerator. It is just saying that, yes, we believe that, for the number of reasons that we are seeing, we will see—compared to previous approaches to the methodology—faster growth in corporate taxes occurring from a given rate of growth in profits. This comes out of us looking at it and trying to get a better understanding of what is going on. These are the types of things that we are trying to do to try and improve our forecasting methodology.

ACTING CHAIR—But in your response you seem to be unaware of what the US revenue authorities are doing in terms of their improved modelling processes to more accurately forecast company collections in that country. In the light of that, I ask: don’t you have links with other revenue authorities in terms of what they are doing, given the problems that you have had fairly consistently in recent years with accurately estimating the forward projections?

Mr Callaghan—There are general links that take place through international organisations. I think I have referred in the past to work that the IMF has done in looking at this over a 20-year period, which showed that we performed very well and did not have a bias in our forecasting ability. It is a general link in attendance at international meetings, for example, but we would not be having a very intense dialogue with other countries on this matter. We are

focusing on ours. As I say, we pick up when we can intelligence of what other countries are doing and we look at it to see what we can learn.

ACTING CHAIR—Don't you think there is a good opportunity to establish greater links between yourselves, the US and other revenue authorities in developing best practice where they may be somewhat ahead of us?

Mr Callaghan—I am not sure if they are ahead of us, but, yes, we will learn from whomever we can. Whenever we can find some information, certainly we will look at it and see whether it is relevant and can improve our situation.

ACTING CHAIR—If that could be done, that would be good.

Senator SHERRY—On this issue: if we look at a more comparable economy—in terms of commodity dominance, for example—Canada is not a bad one to look at. Have you looked at the Canadian experience and at what is happening there?

Mr Callaghan—Only in the sense of the reports that the IMF has put out. Canada has a very different approach. It builds in a very explicit conservative bias. In these performances that have been analysed, you see that, over a very long period, Canada's forecasts are significantly different from its outcomes. One of the reasons for this is that it explicitly builds in a conservative bias to underestimate the revenue.

Senator SHERRY—Given the record of the last two years, it seems to me that that is what is happening here.

Mr Callaghan—As I said, this is also quoted in the budget papers, but it is not for us to quote. If you look at what others have done, looking at our performance over a 20-year period, you will see that we were one of the countries identified as not having a conservative bias. Over a long period, over a couple of years—or it is becoming longer than a couple of years—we have been seeing some significant things occurring in the Australian economy that do make it difficult to forecast revenue. That goes for not only us but others. We are seeing some quite dramatic changes: what is happening in commodity prices, the impact of China, the very significant rise in our terms of trade. These are all quite extraordinary developments occurring in a very short period. In many respects, if you go back and look at more of an averaging over what you could say is a more normal length period, how has our performance gone? Our performance is, on international standards, not too bad. Do we show that we continually overestimate or underestimate? No, we do not. That is not to say that we are not trying to improve. Yes, we are. We are always trying to improve.

Senator SHERRY—This is what concerns me. We had this discussion last year, a year ago. You referred earlier to the issues with respect to company tax, many of which we have been discussing this morning and which we discussed last year. You outlined then, and you have outlined again today and referred to those discussions, the factors that you considered and thought about and revised with respect to the budget 2005-06. But I remind you that in the budget for 2005-06, you had \$47½ billion projected in company tax. The total figure going forward over the three forward estimates was just a shade over \$198 billion.

We had this discussion last year, then this year we come back in budget 2006-07, and the figure for 2005-06 is \$49.8 billion, which is a \$2.3 billion increase, and the increase over the

three forward estimates in 2009-10 has gone from just under \$199 billion to \$223.7 billion. This is a very significant upward revision in company tax forecasts, isn't it?

Mr Callaghan—Yes.

Senator SHERRY—You were taking into account and examining these factors in last year's budget, when we had a very similar discussion, and we come back this year and there is a truly massive upward revision from \$198 billion to \$223.7 billion in the shade of one year. It is a very significant increase, isn't it?

Mr Callaghan—One thing I would point out is, when you look at that over a five-year period, what happens in your base year is very important. Let us go back to 2005-06, and look at the rates of growth. If you are looking at the order of magnitude that you gain, you could say that, since MYEFO, we have revised up our estimates by \$4 billion or so. That then goes into your base, and if you just applied the same rates of growth that you thought were going to occur, that compounds. Then you can say the further out you go, that magnitude increases and increases and increases.

To look at it, yes, that is really part of the arithmetic that comes out. Yes, we have revised up our estimates because of what happened in 2005-06. What happened in 2005-06 since MYEFO? We saw stronger full-time employment than we had anticipated, we saw stronger capital gains than we had anticipated and, yes, we saw company profits stronger than we had thought. Those combined together resulted in us revising up that estimate for 2005-06. We go into 2006-07, and if we had changed nothing else, but we assumed—first of all, we would have to assume that there would not be the same rate of growth—that it is growing with nominal GDP, then that would compound and you would see much higher levels as you go forward. If there is the same rate of growth, then you would get those numbers exactly—that is just the arithmetic.

It would have to be something special happening if, based on what we have seen in the outcome—almost what we are seeing in the year to date—we did not believe it was going to continue. You would then believe that your tax performance is not going to move more generally in line with the growth of the nominal economy. There are really no factors that we can point to where we see that. In fact, we have identified one that we believe we are going to see stronger and revised up—company profits in 2006-07 for the factors I referred to previously. Yes, the economy has performed differently than we had anticipated. Yes, we are seeing still stronger performances in elements of company tax relative to profits than we had seen. They lead to changes in just the year we are talking about, and then the arithmetic results in these substantial numbers as we go forward.

Senator SHERRY—If we take the MYEFO figures, just dealing with company tax again. In MYEFO in 2005-06 you upgraded the company tax forecast from \$47.5 billion to just over \$48.2 billion approximately. Over the forward estimate years, 2006-07 through to 2008-09, your forecast of total collection was a shade over \$204 billion for company tax in MYEFO, which was up from the \$198 billion in the 2005 budget. That seems to me to be reasonable in the circumstances. Then when the budget papers are presented this year, in 2006, you went from \$198 billion in 2005 budget to MYEFO, a shade over \$204 billion—and then, six months later in the 2006 budget, it jumps spectacularly to almost \$224 billion.

Mr Callaghan—Sorry, are you quoting that \$224 billion for 2005-06?

Senator SHERRY—In this year's budget—budget 06. It is \$49.8 billion for 2005-06; \$56 billion for 2006-07; \$58.6 billion for 2007-08; \$59.2 billion for 2008-09; and a shade over \$61 billion for 2009-10—a total of \$223.720 billion.

Mr Callaghan—Yes.

Senator SHERRY—You referred earlier to MYEFO. The upgrading in forecast that took place in MYEFO 2005, from the budget.

Mr Callaghan—Yes, MYEFO from the budget.

Senator SHERRY—Budget 2005, a total of \$198 billion; MYEFO 2005, just over \$204 billion, six months later. Then six months later in budget 2006, \$223.7 billion, a very substantial upgrade. I am still not sure we are getting to the root cause of this very substantial increase in company tax take forecast.

Mr Callaghan—If I could come back to 2005-06. For each reconciliation we have done at the MYEFO we identified where we saw the components of the stronger growth occurring that led to the upward revision. We have done the same in this year's budget for 2005-06 in terms of what we see are the components for the upward revision since MYEFO. So that is what is happening in the economy; that is what we are seeing in the collections that occur. As I have said, we have seen stronger than expected corporate profits. Looking at the 2005-06 estimate, on what we had at MYEFO, we have seen stronger growth in income tax coming from individuals, because we saw stronger growth in full-time employment than we had previously anticipated. People were earning more; they were paying more tax.

Senator SHERRY—I wanted to touch on these other factors: employment forecasts and wage forecasts. They have not been substantially upgraded.

Mr Callaghan—We are talking about 2005-06. There has been some upward revision there that has led to higher income tax coming from individuals. We have seen stronger capital gains tax coming under individuals.

Senator SHERRY—Yes, I accept that there has been some. But by itself does it account for the substantial upward collection and revision of the forward estimates in respect of company tax? I am going to come to income tax shortly.

Mr Callaghan—Adding them all up together: yes.

Senator SHERRY—When you say 'adding them together'—

Mr Callaghan—We are talking about the combination of factors.

Senator SHERRY—The wage employment forecasts?

Mr Callaghan—We are talking about the combination of factors that have led to the upward revision in the revenue estimates that are outlined in the budget papers for 2005-06 compared with MYEFO.

Senator SHERRY—So, on current trends, what is going to happen in this year's MYEFO?

Mr Callaghan—That is an impossible question to answer.

Senator SHERRY—Let me put it this way: do you think you will be more accurate than you were last year?

Mr Callaghan—We try to give our best forecast.

Senator SHERRY—It is not just company tax, of course. We touched earlier on the income tax forecasts, superannuation tax forecasts—although there are some other factors there, which we will get to later, not with you, which are going to impact on that. If we look at income tax revenue from MYEFO to budget—net of tax cuts: 2006-07, the change, \$3.9 billion; in 2007-08, it was almost exactly \$3 billion; in 2008-09, it was \$2.75 billion. That is after taking into account the personal income tax cuts. Again, I am puzzled, as many others are, as to why the estimates are being revised so significantly, taking into account these factors.

Mr Callaghan—It is just as we have said before. One of the reasons is that it is the actual collections that we are seeing coming in. As I say, this comes back to our base. Yes, our estimates and our forecasts, going back, underestimated the strength of the revenue that has been collected. That is something we have seen for a number of years. When it happens you cannot ignore it; you have to factor it in. As I explained before, once you factor that in and you are coming from a higher base, the arithmetic is such that, over the five years that you have been talking about, you will see much stronger numbers.

There are perhaps two different aspects to what you are commenting on. One is: why did we underestimate revenue that we have actually seen? The other is: why are we seeing this strong growth in general government revenue over the forward estimates period? To a large extent, it is because we are seeing the base rise. So there are two aspects, I think, to what you are commenting on.

Senator MURRAY—That is what I was groping for earlier. It seems to me that, if your corporate tax share of GDP is lifting, it must mean that your base has been adjusted. And I think that we do not give enough credence to the effect of integrity measures and base-broadening in lifting the base contribution. So, regardless of how the profit cycle moves, effectively we have a more sustainable base of taxation revenue coming in. And, indeed, in the figures we have at the moment, there is no sign of a significant shift from the wage share to the profit share; it is not such as to account for what is happening.

Perhaps I could ask you—on notice, because you could not give a full answer—to go away and think a bit more about giving us a considered answer on what contribution, on a sustainable basis, you think the integrity measures have cumulatively made to the health of our corporate tax revenue.

Mr Callaghan—Certainly. We will see what further information we can give you. But I think it is very difficult to identify because it is always trying to find that counterfactual. In many respects, if you are changing the behaviour of companies in that they are now paying tax, the fact that you could not identify that they were not paying tax before—or should have been paying tax—is going to be very difficult to do. But we will certainly have a look and see if there is any information we could give you. We will see what we can do.

Senator MURRAY—I think the ATO could give us some good information because of their systems.

Senator SHERRY—You mentioned Mr Richardson. I want to touch on him in respect of his recent Budget Monitor and his notion of an accelerator. In his recent Budget Monitor, at page 74, he said

In the 2005-06 budget, Treasury allowed for a downswing in commodity prices in its projections, but at the same time it added a second feature—an accelerator. This accelerator essentially assumes revenues from profit taxes grow faster than profits themselves. The net impact of these two changes was that, whereas Access sees a fading boost to revenues from the current boom in later years, Treasury sees a climbing one. Make no mistake here: the shape of Australia's future depends heavily on which picture of our future proves to be more accurate.

Going back to company tax revenues, we have discussed the significant increase of 18.8 per cent in the fiscal year 2005-06. That is the growth in company tax revenue. If we look at the company profit before income tax, we see a rise of 12 per cent in the fiscal year—business indicators, company profit before income tax, Australian Bureau of Statistics table 9. The ABS reveals company profit before income tax increasing by 12 per cent and, over the same period, company tax revenue in the budget papers increasing by 18.8 per cent. So would you accept that company tax is growing faster than company profits? On the face of it that appears to be what is happening, doesn't it?

Mr Callaghan—Yes.

Senator Murray interjecting—

Senator SHERRY—That is probably a factor. How sustainable is it in terms of the future forecast projections? How sustainable is having company taxes increase more rapidly than company profits? Is it sustainable?

Mr Callaghan—It is something we have always seen. Let us come back to what we are talking about and what Chris Richardson was saying. As I said, it was the responsiveness we are seeing of company tax relative to what was happening to company profits. History has shown that, just as you have quoted, we have seen much stronger growth in company tax relative to a given growth in company profits. That is what the experience has shown us, that is what we have gone back and had a look at and, in many respects, that is why you have been questioning us about why we did not anticipate that earlier. To the extent that you look back and look at history, in doing many of the forecasts you are guided by what the data tells you and what you can understand from the data. We have made an adjustment to our revenue forecasting methodology and, in the future, we do expect to see a continuation of what we have been seeing in stronger growth of company tax payments relative to a specific growth in company profits. As we said before, along with the factors Senator Murray has just been questioning us about, these are all trying to get an understanding of what may be some of the driving factors behind that.

But if I come down to the very initial point of your question, where you quoted from Access that they have not allowed for this, we then have to try to understand why we will not see this continued responsiveness. Is there some reason we think it will not be? It comes down to judgments. It comes down to trying to understand what is driving the behaviour, and we always have to look at the data. We have to look at where the performance has been going. Just as much as Access has been wrong in underestimating the growth in company profits, they believe that they do not have to make this adjustment. You could say that we are

responding to the very things you have been questioning us about—why we have been revising upwards our estimates and why our estimates have not been in line with the outcome. This is all part of the response of it. Do we believe that it is the appropriate response? Yes, we do; it is our best judgment.

Senator SHERRY—I will come to another tax where revenue has increased very significantly—the PRRT or petroleum resource rental tax. In the budget 2005 it was a shade under \$6.3 billion over the four-year period, but MYEFO revised it upwards again substantially to a shade under \$9 billion and in the budget 2006 it is just under \$11½ billion with the additional 2009-10 year added. Again, it was a substantial percentage and money increase. What has accounted for that?

Mr Callaghan—The PRRT is a profit based tax. It is one that is affected by the growth in oil prices.

Senator SHERRY—So there is a direct correlation between the higher oil prices and the higher revenues from PRRT?

Mr Callaghan—Yes.

Senator SHERRY—That was not anticipated?

Mr Callaghan—That is right.

Senator SHERRY—The budget is getting a tax windfall from higher oil prices, isn't it?

Mr Callaghan—As I said, the PRRT is positively related to the oil price.

Senator SHERRY—Would that relationship to oil prices account for the bulk of the increased tax collected and forecast?

Mr Callaghan—I am not sure, but I would think so. I would have to check.

Senator SHERRY—It seems reasonable to assume it would be the bulk, overwhelmingly, doesn't it?

Mr Callaghan—I would have to check, but it would seem to be. One of the fields has been declining in production, so, yes, I would think so.

Senator FIELDING—I have some questions on the petrol tax and the inflationary impact of petrol prices. In the Treasurer's budget statement called *Continuing Tax Reform*, at page 43, he states that the GST has 'replaced inefficient taxes' and goes on to talk about how the government last cut petrol excise in 2000—six years ago. Can you outline to me what the department has done with regard to the issue of looking at petrol excise tax? What analysis have you done on it?

Mr Callaghan—Senator, I am not sure what you mean in terms of analysis. Given that it is fixed, it really responds to volume. We have seen decline in the volumes of petrol consumed, I understand, but beyond that I am not sure what type of analysis you would be thinking about.

Senator FIELDING—Let me try and clarify it. What analysis did the department do on the income tax cuts that were put forward in the budget?

Mr Callaghan—Again, could you be more specific about what you mean in terms of the analysis? What we have done is the costing and there has been work done in a whole series of

cameos as to what would be the relative impact on various households of the whole package of changes that were in the budget. Beyond that—

Senator FIELDING—Let me go back a step, then. I assume the department would have done a fair bit of analysis like who would be impacted on the most and who would benefit the most if the tax rate were changed this way or that way.

Mr Callaghan—What the impact would be would flow from the breakdown of taxpayers within particular income thresholds. We have done it in looking at, as I say, the cameos of the whole package of measures that were contained in the budget and how they would impact on different household segments and household sectors. Yes, that type of work has been done.

Senator FIELDING—Let us go back a step. Could you outline to me what the process was for determining what tax cuts were considered and not considered? Just walk me through the process. I am just interested. Do you think that someone just dreamed these up and did not look at the impact it would have on certain types of households or families?

Mr Callaghan—The decisions are clearly the ones of government to take on this. We provide policy advice to the government. What goes through in that decision making by the government, as to what is going to be in the budget, is really beyond our competence to comment on in these hearings. It is very much the nature of the policy decisions that are taken.

Senator FIELDING—My question is not so much about the policy decision. I am after what analysis the department did—with taxpayers' money—of any scenarios with regard to tax cuts.

Mr Callaghan—A series of scenarios in terms of what will be the impact of the tax cuts and the increased family payments has been published, yes.

Senator FIELDING—I will come back down to this. Did the department look at a cut in the inefficient excise tax in this budget?

Mr Callaghan—The inefficient excise tax?

Senator FIELDING—I will go back to what I said before. In the Treasurer's budget statement called *Continuing Tax Reform*, at page 43, he states that the GST has 'replaced inefficient taxes' and goes on to talk about how the government last cut petrol excise in 2000—six years ago. My question is: did the department do any analysis on a cut in the inefficient petrol or excise tax for this year's budget?

Mr Callaghan—There are a couple of things, Senator. I am not quite sure you are getting the connection between 'inefficient' and 'excises'. That was what the intent of that sentence of the Treasurer was. I thought he was talking about state taxes. The work we do or whatever policy advice we may have prepared for the government, again, are not the matters that I think we normally comment on. That really does go to what would be our advising capacity for the government. They are very much policy questions for the government.

Senator FIELDING—I am not after policy. Quite clearly, I have asked what work the department has done. This is a taxpayer funded area and I am interested to know whether there was any work done on that area of looking at petrol tax cuts.

Mr Callaghan—I know. But, again, you could ask what area, what was the range of options or what work was done on a whole variety of different possible changes that could take place. If we look at it very generally, I think the nature of your question is asking us to get into the nature of the work that we have or have not done for the government. It really is very difficult. We cannot really comment on that here. You are asking questions at the heart of what was behind any advice we had given to the government. What advice we did give or did not give is really going into policy issues.

Senator FIELDING—I will come back to it. I will come around from a different angle and I will come back to that issue. In Budget Paper No. 1 there is acknowledgment that fuel excise taxes are inflationary. On page 3-6 it says:

There remains a risk that higher fuel prices, combined with solid wage outcomes, will feed into higher prices for other goods and services.

In its May statement on monetary policy, the Reserve Bank said:

Although petrol prices had little direct impact on the quarterly inflation outcome, they did boost the annual rate of inflation, following their increases of around 20 per cent over the last year.

Did the department consider the inflationary effect of petrol prices and look at a cut in the petrol tax?

Mr Callaghan—The quote you read, yes, was for petrol prices, not excise. Yes, the department in preparing its forecasts—and now we are into areas that are outside this output; this is the forecasting that the macro people do—has to look at all the various components that might be driving inflation. That goes to preparing the forecasts that underline the budget. But, again, any advice that was given to the government or any work that was done in the government is, I am afraid—and I am not trying to be difficult—coming back to the general nature of what policy advice we gave or what work we did for the government. It is very much getting onto policy issues, by definition. You are asking what work we did on possible policy options to advise the government. Why not ask that across any aspect of the work we are doing? It is a policy question. They really are matters that have to go to the government. As I say, we are not trying to be difficult, but you are raising a fundamental issue. You are asking what the advice was that we gave the government. Really, it is policy advice and those are questions that really have to go to the government.

ACTING CHAIR—Senator Fielding, I think the witness from Treasury is correct. You are impinging on policy issues rather than on administration.

Senator FIELDING—Let me rephrase it, then. I am not trying to get at the policy; I am trying to work out what work has been undertaken by taxpayers' money with regard to looking at petrol tax. That is not a policy issue. I am asking whether you have done any analysis at all.

Mr Callaghan—As we said before, of course the analysis of what happens with petrol prices and what impact it may have on the economy are factors that have to be done. That is an important component in what might be affecting the performance of the economy. When it comes to what is the nature of any of the policy advice or work we might be doing for the government as a consequence of those developments that are occurring in the economy, again they are policy issues.

Senator FIELDING—Can you answer the question as to whether you have done any analysis on petrol excise tax cuts? Has the department done any? That is not a policy question.

Mr Callaghan—Again, I am not trying to be difficult on this; it is just a point of principle. If we change it to ask what analysis we have done for further cuts in particular company tax rates, what analysis we have done for further changes in income tax rates or what analysis we have done for additional changes in the depreciation of capital gains tax—all that would be suggesting possible consideration of policy matters. I am not targeting the particular excise; it is just the general question you are raising about what work we have done on particular aspects that have the inference that this is part of policy advising. It is going to policy issues.

Senator SHERRY—Senator Fielding is asking whether, as a matter of fact, any work has been done.

Mr Callaghan—I appreciate that but, again, if we then say, ‘Has any work been done’—

Senator SHERRY—We are not saying that yet. You would have a right, I think, if I then followed it up, but I am not. Senator Fielding is asking: as a matter fact, has any work been done—yes or no?

Mr Callaghan—The work we do is for a purpose. I am looking at the broader question, and if you look at the broader one, where does it stop?

Senator SHERRY—We are not asking about the broader one.

Mr Callaghan—I know, but where do you draw the line?

Senator SHERRY—A specific question is being posed.

Mr Callaghan—But where do you draw the line? You are asking about the nature of—

Senator SHERRY—We are not at that line yet. A specific question is being posed by Senator Fielding, and I am asking exactly the same thing: has the work been done—yes or no?

Mr Callaghan—I am sorry but I find it difficult to comment on a particular area, because then, by inference, it is suggesting that you want to know the nature of it.

ACTING CHAIR—Order! I repeat what the chair of the committee stated when he commenced these proceedings:

The Senate has resolved that an officer of a department of the Commonwealth or of a state shall not be asked to give opinions on matters of policy and shall be given reasonable opportunity to refer questions asked of the officer to superior officers or to a minister.

This resolution prohibits only questions asking for opinions on matters of policy and does not preclude questions asking for explanations of policy or factual questions about when and how policies were adopted. We now have a situation, and I remind the Senate, including the witness, that if a witness objects to answering a question the witness shall state the ground upon which the objection is taken and the committee will determine whether it will insist on an answer having regard to the ground on which it is claimed. Any claim that it would be contrary to the public interest to answer a question must be made by the minister and should be accompanied by a statement setting out the basis for the claim. Hopefully, I think that clarifies it.

Senator FIELDING—In response to that, quite clearly I am not asking for an opinion, quite clearly I am not asking for a policy opinion and quite clearly this is a matter of fact. If you want to gag me from asking questions about petrol tax when this is hurting Australian families more than I think anyone around this table really realises, it is just a joke. I am asking a specific question, and it is not about policy. What has the department done with taxpayers' money with regard to anything with petrol tax? Have you done any work?

ACTING CHAIR—Just before you respond, Mr Callaghan, there is no attempt at gagging, Senator Fielding. It is merely an upholding of the standing orders of the Senate.

Senator SHERRY—With respect, Chair, it seems to me that what you have read out requires the witness to answer the question that Senator Fielding has posed as a matter of fact. He is not asking for an opinion and he is not asking for figures; he is asking for a matter of fact—has a study been done on this issue? Given what you have read out, it is quite reasonable for the witness to respond yes or no. What flows from that is a different set of questions and issues perhaps.

ACTING CHAIR—If you wish, Mr Callaghan, you can refer it to the minister or the parliamentary secretary if you would be more comfortable in responding in that way.

Mr Callaghan—Certainly. But can I just explain a bit further about it? I believe the government has made a number of very clear statements that it is not considering any change in petrol excise rates. I think that has been put on the record by the Treasurer and the Prime Minister.

You have asked whether we have done work on any change in a particular tax, where the government has made a very clear statement, as I understand it, that it is not considering any change in that tax. To me, it seems that you are asking us to almost comment on that, by inference—whatever answer we gave. Again, rightly or wrongly, I am extrapolating that across a general principle—that you could, on any statement by which the government has made it clear that it is not proposing anything, ask, as a matter of fact, 'Have you done any work on that?', and that would be asking for a comment. It goes to the heart of the advice that we give the government.

Senator FIELDING—I am amazed by this. You have made comment on policy with regard to the government quite clearly not wanting to look at the issue on petrol tax. But I have asked the question, 'What has the department done with regard to analysis on this issue?' You can say you have done nothing because the government has instructed you that it is not a policy issue they are interested in; let me know. But I am interested to know whether the department has done any work with regard to petrol tax and its cutting.

Senator Colbeck—Senator, you have made a couple of comments this morning in relation to the potential impact of fuel excise: first, that it is inflationary, which clearly it is not—it is a fixed tax; it does not move; so in that respect it cannot be inflationary. Second, you have made some inferences about its inefficiency. I understand that you are trying to make a political point here this morning—that is part of your exercise and your right. I have no problem with that. But, clearly, the government does not have a position where it is looking to change the excise. I understand your position is different from that.

The Prime Minister has quite clearly stated that we made significant revisions to the regime in 2000-2001, where we reduced the excise in 2000 and we removed the appreciation of the tax, the indexation of the taxation, in 2001. When fuel prices were at 90c the fuel excise was 38c, and now that it is \$1.40 it is 38c, so it has absolutely no impact on the price of fuel. The government has a very firm position on that. It is quite clearly stated and articulated, and the officer has quite clearly indicated that that is the case.

Senator FIELDING—We will come back to the core of the issue. Can I just clarify: are you saying that petrol prices are not inflationary?

Senator Colbeck—No. You need to listen to what I say very closely, Senator Fielding, as I listened carefully to what you said. I said that excise was not inflationary; excise is a fixed part of the fuel tax. You made a comment, or an inference, earlier that fuel excise was inflationary. I do not think there is any dispute. The officer has indicated that the impact of increasing fuel prices is considered as part of the budget process.

But what you were talking about, and the inference that you made earlier, was, quite clearly, from my recollection—and I am quite happy to have the *Hansard* checked on that—that fuel excise was inflationary. Yet that is a fixed component of the price of fuel and therefore it cannot have any inflationary impact. The impact comes from the rising price of oil.

Senator FIELDING—We can come back to that issue as well. I am going to come back to this issue; I am not going to go away. I have asked a question: what specific analysis has the department done on fuel excise—

Senator Colbeck—I can say to you that the government has not asked the department for advice on excise.

Senator FIELDING—That is what has been asked. I am now asking the department: have you done any analysis on cutting the fuel excise?

Mr Callaghan—As I said before—and I am answering this as a point of principle—I believe that given what the parliamentary secretary has said, he has stated again clearly what the government's policy is, asking this question of analysis is bordering on asking the department for the nature of the policy work that it is doing.

Senator SHERRY—You are required to answer the question put to you.

Mr Callaghan—I believe that is the case, Senator.

Senator SHERRY—And if we get to that point, you may not be—

ACTING CHAIR—Order!

Mr Callaghan—May I take that on notice. I believe that that is what it is. May I take it on notice, Senator?

Senator FIELDING—I do not understand why you need to take it on notice; you either know what your department is doing and has done, or you do not. It is a fact. It is a matter of fact question: has the department done any work in this area? I will ask it again: has the department done any work or analysis on cutting the fuel excise tax?

Mr Callaghan—Again, Senator, we are going over the same thing. I believe that the government has stated a policy on this. To ask has the department done any work on this can be interpreted as going to the nature of what work we do in our policy advising capacity to the government, and because I believe that it is going to elements of policy, it is on that basis that I will take it on notice.

Senator FIELDING—I did not ask whether the minister has gagged you from talking on the issue. I have asked the question: has the department done any work on it? It is a fact. It is a question of fact. I thought Senate estimates was to find out what the departments are actually doing with their budgets, where their work is going and what issues they are up to. I thought this is something the Australian public would like to know. Petrol is hurting Australian families, and I am asking a simple question and the department will not give me a simple answer: yes or no.

ACTING CHAIR—Senator Minchin?

Senator Minchin—I was in the coalition party room meeting; my apologies. Through you, Mr Chairman, as has been said, there are clear guidelines for the conduct of estimates committees that internal policy advice to the government on policy options is not a matter for discussion in Senate estimates. These are estimates committees to deal with appropriations. Obviously they traverse ground wider than that and that is tolerated and reasonable, but when it goes to policy advice to government on policy options open to the government, that is not a matter to be canvassed in estimates committees. It is a matter for the government rather than departments to discuss publicly what options the government has in mind or what its decisions are, and why and why not. Estimates are not for officials to be grilled or expected to answer questions that relate to internal policy advice to the government.

ACTING CHAIR—Mr Callaghan has agreed to take the question on notice. Are you happy with that now?

Senator FIELDING—I am going to have to be. I am not going to get an answer here. I have asked a number of times. There is no use continuing to ask the same question if you are not going to get an answer on the issue.

ACTING CHAIR—The next question?

Senator FIELDING—The next question was related to the answer on the first. I was going to ask what the department found between cutting income tax versus cutting petrol tax. They are both tax cuts. Quite clearly, from listening to people—in the *Age* on Monday, 22 May it was reported that when the public was:

Asked to rank their priorities for reducing taxes, 45 per cent nominated cutting petrol tax, 30 per cent income tax, while only 23 per cent opted for reducing tax on superannuation benefits ...

Senator SHERRY—What percentage was that last figure?

Senator FIELDING—Twenty three per cent.

Senator SHERRY—Was it specified if it was contributions or exit?

Senator FIELDING—I was going to ask what analysis was done between the two and whether there was any done between the two, but quite clearly I am not getting an answer to the first question to ask the second.

Senator Minchin—It should be obvious to the committee that the government, through the Prime Minister and the Treasurer, have for quite some time made it clear that having made the substantial changes to fuel excise arrangements back in 2001 that no further changes were contemplated. We believed that the current policy setting in regard to fuel excise was appropriate and we, the government, have given no indication of any intention to change that, nor speculated on that. Indeed, it is fair to read from all that has been said in the public domain that we believe the current policy settings in relation to excise are the right ones. It is not appropriate for the department to speculate about what internal work may have gone on between excise and income tax. The fact is the government's position is that the current flat excise on petrol is the right policy setting. Against that background, we have done an enormous amount now to reduce the income tax burden on Australian families.

Senator SHERRY—Just on that point, you were not here earlier when I gave the figures. We had a discussion with Mr Callaghan about petroleum resource rental tax. In the budget for 2005, it was \$6.3 billion—that is the revenue for 2005-06 on the three forward years of the estimates—and in this year's budget, it has gone up to \$11.45 billion, just under \$11½ billion. Mr Callaghan and I had a reasonable discussion about that, and yet we cannot have an answer to Senator Fielding's question.

Senator FIELDING—It is still related.

Senator Minchin—It is quite a different question—

Senator SHERRY—I know it is a different question, but it seems to me to be eminently reasonable, given the discussion we had prior to you coming in.

Senator Minchin—There is no connection between the discussion about publicly available figures on revenues derived from a particular form of taxation and a question about internal modelling that you think might or might not have occurred within the Treasury in relation to the respective forgone revenues in certain areas. It is quite a different question.

Senator SHERRY—So we can have a discussion about a figure that is published and its components and the way it is made up?

Senator Minchin—I gather you have had such a discussion and the officials felt no hesitation in participating in that, as I understand it.

Senator SHERRY—We can have that discussion, but in terms of what you outlined, do you not think—

ACTING CHAIR—You are arguing on a completely different subject.

Senator SHERRY—It is on the same issue of the revenue collected from tax on fuel. Given what you have just said, last year we fronted up here, in 2005 for the 2005 budget, and you had \$6.3 billion in revenue. This year we front up and it is a shade under \$11½ billion in this year's budget.

Senator Minchin—That is the resource rent tax?

Senator SHERRY—Yes, PRRT.

Senator Minchin—I thought we were talking about fuel excise.

Senator SHERRY—It is a related issue.

Senator Minchin—No, not at all. Resource rent tax is a special profits tax on one sector of the Australian resources industry.

Senator SHERRY—It is a related issue.

Senator Minchin—Not really. I do not see any relation between revenues derived from an increase in the profitability of oil and gas producers and the excise levied on petrol.

ACTING CHAIR—Maybe we should go back to Senator Fielding.

Senator FIELDING—I want to make a point of clarification. There was talk about petrol tax and its effect on inflation. I think the overall comment should be made that petrol prices are inflationary, to use the Prime Minister's terms, and we understand that world prices are causing that issue. But the real issue is that when you are taking it collectively, petrol excise makes up a substantial part of that and cutting the petrol tax has two benefits: it takes off the pressure from inflationary effects and also helps families. That is the reason why I was asking this question on behalf of Australian families. I understand I am not going to get the answer. It is on notice, and I will be interested to see what answer I get back through the notice papers.

Senator Minchin—The trouble is that reducing or abolishing any tax, whether it is tax on cigarettes, beer, petrol or anything, is obviously going to 'help Australian families'. Governments have to devise a tax system which reasonably and properly and fairly and efficiently collects the revenue required to provide the services which Australians demand of government. Forever and a day, and in every country on earth, there is a tax of one kind or another on the consumption of petroleum products. We made a very significant change to those arrangements five years ago when we ended the indexation of that tax. That tax used to rise every quarter, or whatever it was, with inflation and it no longer does.

The real return from that source of revenue is falling every year for the government. Not only did we end indexation, we reduced the excise. As a result of that it is a flat tax; it does not go up with the price of petrol. There are—not you, Senator Fielding—others devious enough to suggest that the revenue that we gain from this goes up with the price of petrol. Indeed, it may well be the opposite to the extent that petrol consumption falls, we receive less tax. From the government's perspective, we have acted properly in relation to this particular tax. We think the setting is right. We have, I think, the second or third lowest level of petroleum taxation in the developed world. Our petrol prices are among the lowest in the developed world. We think that setting is right and, to an extent, the government has the capacity to forgo revenue. We believe what we have done in this budget is much more appropriate in terms of the needs of Australian families and the needs of the economy.

Senator FIELDING—I will reply to that. The issue here is that quite clearly—and it was in the *Age* on 22 May—there were more people wanting a cut in the petrol tax than income tax cuts. Now the issue here is that quite clearly—the Prime Minister would not say it—petrol prices are inflationary. Petrol prices are made up of a number of things, including a substantial portion being petrol tax, and a cut in the petrol tax would see a drop in the inflationary impact of the petrol prices. Quite clearly, families are seeing that as a major issue. It is hurting them on a weekly basis.

Quite clearly, people have looked at the tax cuts, and my question was going to the heart of the issue. I would rather have a department that thinks rather than one that is totally, totally, I

think, narrow-minded and does not look at an issue that quite clearly Australian families are interested in. They would like the department to have a look at petrol tax impacts and what impact petrol tax cuts would have compared to income tax cuts. Why did we go down the income tax cuts road rather than petrol tax cuts, when quite clearly the Australian public—communities and families—would prefer to see the other? I am interested to know what analysis has been done.

Senator SHERRY—I think the senator can accuse the minister but not the public servant.

Senator Minchin—Yes. I think that is a political discussion, Senator Fielding. It is perfectly proper for you to say to the government that as a matter of government policy you think we should have cut the excise rather than cut income tax. It is not fair to attack the bureaucracy for that. The Treasury well knows the government's policy position that the current arrangements regarding excise are appropriate and we do not intend to change them. However, we do believe that income tax arrangements are not satisfactory and that is why we have made the change we have, and the Treasury did all the work on that. But the starting point is it is the government's public position that excise arrangements are appropriate, so your attack should be a political one—and that is perfectly proper—and not one demanding the Treasury officials go off on a jaunt of their own.

Senator FIELDING—I think to infer or imply I am attacking the department is wrong. I asked my question because I am interested in knowing what research or what analysis has been done on the issue. It is an important issue. It is not as if it is an issue that just—

Senator Minchin—If the Treasurer, the minister responsible for this portfolio, wishes to say anything on that subject then he is at liberty to do so, but the officials are not and nor am I. I am certainly not aware of any work having been done on it against the backdrop of the government's—

Senator SHERRY—You had a fine contributions tax on super, and you went off on a—

ACTING CHAIR—Order!

Senator Minchin—clear position, which I support. The current arrangements with excise are the right arrangements for Australia. It really is very bad public policy, in my view, to change taxation arrangements every time there is a rise in the price of oil for a whole lot of reasons. You are suggesting that if the oil price were to collapse 20 cents—which, of course, could happen—then we put the excise back up. That is the logical consequence of your argument. That would be very bad public policy, and one that I am sure the alternative government would not support. Yes, we are sensitive to public opinion. Yes, we understand that petrol prices are a big impost on family budgets, but we do not think the solution to that is a knee jerk panic response by the government that would forgo what would be billions of dollars of revenue to make any difference in a panic reaction to a particular spike in petrol prices, which then begs the question: what do you do when the petrol price goes back to \$50 a barrel or something.

Senator FIELDING—Thank you, Chair.

Senator SHERRY—Just as a matter of fact on this issue, looking at budget paper No. 1, table 5.8, excise duty on petrol is estimated at \$7.28 billion in 2005-06, \$7.3 million—a very

slight increase, \$30 million. Diesel excise duty is, I thought interestingly, estimated to go up from \$6.24 billion to \$6.420 billion—

Senator Minchin—That is diesel, is it?

Senator SHERRY—Yes, that is diesel—which is a 2.9 per cent increase. My first question is to you, Mr Callaghan. Do you believe that those forecasts are robust, and on what basis do you believe they are robust?

Mr Callaghan—The answer to the first question is yes, we hope all our forecasts are robust.

Senator SHERRY—You are not going to come back here next year and give me an explanation as to why they have changed significantly, if they do? We are not going to have a discussion, like the one we had earlier, about the lack of robustness in the forecasts last year compared to this year in other revenue areas?

Mr Callaghan—All I can say is that yes, we do try to give as robust forecasts as we can. It is stating the obvious that we know that no forecaster is ever going to be accurate.

Senator SHERRY—Have you examined the issue that Senator Minchin referred to earlier, a possible reduction in excise duty due to a drop in consumption because of higher fuel prices? Did you examine that issue when these estimates were put together?

Mr Callaghan—As I recall, I thought it was referred to that there has been a volume response to higher prices, which is impacting—

Senator SHERRY—You have examined the issue.

Mr Callaghan—That is a fact.

Senator SHERRY—So you have examined that issue. Why the lower rise in petrol excise as distinct from diesel excise? What is the explanation for that?

Mr Callaghan—I think it is the impact of exactly what you were talking about, the higher prices impacting on volume on the petrol. I am not sure what is driving diesel; I would have to check.

Senator Minchin—All of us are aware of the significant increase in the sale of diesel-powered vehicles and the many more diesel-powered vehicles on the Australian market. There clearly is a switch from petrol to diesel passenger vehicles, which no doubt is reflected in this.

Senator MURRAY—Especially since the Democrats and the government agreed that we would improve the environmental characteristics of diesel and brought forward the desire to cut the pollutants.

Senator Minchin—Too true, Senator Murray; you are quite right. I would have thought that is a positive outcome for Australia.

Senator SHERRY—But the extent to which that switch occurs, as one component it would have a relatively slow impact on diesel revenue, would it not? My assumption is, and you can tell me whether this is correct or not, Mr Callaghan, that excise from petrol has a more immediate impact, if it goes up. The revenue is more immediately impacted on, because the proportion of consumer consumption of petrol would be higher than diesel, presumably.

Diesel is primarily used, but not exclusively, for transport. That would seem to be a reasonable assumption, wouldn't it?

Mr Callaghan—That is right, and by business. I think you are answering the question to some extent, that it is not as responsive in business.

Senator Minchin—And the economy is still growing at two to three per cent, which means the freight load, as we all know, is increasing. There is a lot of freight movement, which is largely diesel-powered.

Senator MURRAY—On the same issue of fuel, I would assume, because of the various policy discussions that have gone on in government, that the Treasury is actively engaged in the broader issue of alternative fuels, of the bio-diesel issues, of the ethanol issues—in other words, all the areas of trying to find energy sources for transport which supplement or complement traditional sources of petrol and diesel.

Mr Callaghan—Yes. Policy advice has been given to the government when these factors have been considered.

Senator MURRAY—Those of themselves, whilst they have environmental and supply considerations—in other words, alternative sources—they may have a price benefit sometimes attached to them, namely, an alternative fuel could be cheaper than a petrol and diesel component.

Mr Callaghan—Some of the alternative fuel already has a tax advantage over petrol.

Senator MURRAY—That is right. So Treasury is looking at the broader issue of the component parts of transport fuels—if I can use that in the broadest sense?

Mr Callaghan—Again, in the context that it goes to the nature of policy advice, these are issues that the government has made announcements about and decisions upon. Yes, in the context of us providing advice to the government, it is the range of elements on which we do provide advice to the government.

Senator SHERRY—While we are on fuel: \$257 million was allocated to the Fuel Sales Grants Scheme in 2005-06 in the federal budget. That is to be scrapped, isn't it?

Mr Callaghan—The Fuel Sales Grants Scheme?

Senator SHERRY—Yes.

Mr Callaghan—I would have to check on that.

Senator SHERRY—I am sure there would be someone in the legislative area who could confirm that. It is just that there is no appropriation for 2006-07.

Mr Callaghan—Sorry; you are right. It is being abolished from 1 July.

Senator SHERRY—So it is being abolished. Won't that increase the price of fuel? If you abolish a Fuel Sales Grants Scheme that reduces the price, won't that increase the price?

Mr Callaghan—I think the judgment has to be made whether it was effective in influencing the price.

Senator SHERRY—But I am not asking that. I will get to that.

Mr Callaghan—To be able to draw that conclusion, I think that is what you would have to be—

Senator SHERRY—Reasonable?

Mr Callaghan—I am not sure.

Senator SHERRY—Come on. If you are paying a subsidy under a Fuel Sales Grants Scheme and you remove the subsidy effectively—because that is what it is, to the tune of \$257 billion—and take it away, given all other factors, that must increase the price, surely. That is a reasonable conclusion.

Mr Callaghan—The assumption you are making is that it was being passed on and was being effective in influencing the price.

Senator SHERRY—Right. So the price will go up.

Mr Callaghan—No—

Senator Minchin—No, there is some evidence that the subsidy was not being passed on to consumers. That was one of the problems with this scheme. So, to the extent that it was not being passed on to consumers, its abolition will have no effect on the end price.

Senator SHERRY—Why did you introduce the scheme in the first place then, Minister?

Senator Minchin—Obviously, we were seeking at that time to provide relief to beneficiaries—I think they were in outer country areas—

Senator SHERRY—Yes, rural and regional Australia.

Senator Minchin—who were at that time concerned about the high price of fuel because of the distances they have to travel. This scheme was devised to try to alleviate that. One of the reasons it is being abolished is that it would appear that it is not clear that that subsidy was being passed on to end consumers. My recollection—I am pretty sure—is that the moneys that were going into that scheme are being put into rural roads.

Senator SHERRY—Is that through AusLink?

Senator Minchin—Yes—well, whether it is through AusLink or the direct grants to local government I am just not quite sure. But my clear recollection, subject to confirmation, is that instead of spending this money on that scheme we are spending it on rural roads, either through AusLink or through the direct grants to local government. But I can have that confirmed.

Senator MURRAY—My recollection is that that scheme was targeted to users, not consumers. The subsidy was for the user, not for the consumer.

Senator Minchin—What is the difference? What do you mean? The users of petrol and diesel?

Senator MURRAY—Because the subsidy went to the truck company or the—

Senator Minchin—That is the point, yes.

Senator MURRAY—It did not go to the consumer.

Senator Minchin—No. It was difficult for us to get it into the hands of the consumers—

Senator MURRAY—That is right.

Senator Minchin—so it was done through a chain. And there is a fair bit of evidence that it did not end up in the consumers' hands.

Senator MURRAY—But there was no audit to make sure that the user was passing it on to the consumer.

Senator Minchin—Yes, because it is extremely difficult. So what we have done—and I think local government is certainly supporting it—is that those moneys are being invested directly into improving rural roads.

Senator SHERRY—Could you just confirm, Minister, whether it is going through AusLink or what the other mechanism is for the funding that is apparently being redirected?

Senator Minchin—Yes, we will get confirmation,

Senator SHERRY—This is the last question on this issue: you referred to what you believed were inefficiencies in the \$257 million. Was a study done on the efficiency or otherwise of the impact of the \$257 million Fuel Sales Grants Scheme? You referred to alleged inefficiencies. You may or may not know.

Senator Minchin—I am not sure whether a formal study was done.

Senator SHERRY—Was a study done?

Senator Minchin—The decision would have been made by way of a cabinet decision based on the submission.

Senator SHERRY—You referred to an alleged inefficiency. I do not know whether or not that is true. What I am asking is a matter of fact: was a study done? Given there is an announcement to get rid of it, presumably there would have been some study done as to the efficiency and effectiveness of this measure.

Senator Minchin—We regularly review the effectiveness and efficiency of all programs, and I am sure that would have been the case with this.

Senator SHERRY—What I am seeking—and I am not expecting you to say yes or no now—is whether there was a specific study analysis done of this program in respect of its effectiveness. You can take that on notice.

Senator Minchin—We will see whether we can get an answer to that. I think it is reasonable to presume one was done, but I will get you an answer.

Proceedings suspended from 10.46 am to 11.03 am

ACTING CHAIR (Senator Watson)—The proceedings will resume. Minister, you have a comment to make.

Senator Minchin—In relation to questions on the Fuel Sales Grants Scheme, I refer the committee to a press release from the then Minister for Transport and Regional Services, John Anderson, of 22 January 2004, in which he announced that the government would wind up the Fuel Sales Grants Scheme from 1 July 2006. I quote:

The savings from winding up the Fuel Sales Grants Scheme, some \$265 million in the first year, will be committed to improving our transport infrastructure in outer metropolitan, rural and remote areas.

I believe that is being done through AusLink. That appears to be the context in which this was announced, and I think it is right. There was one other matter. As is said in this release, there was a fuel tax inquiry in 2002, which was known as the Trebeck inquiry. David Trebeck did an inquiry into all of this. The press release of 22 January 2004 said:

However, the Fuel Taxation Inquiry in 2002 concluded that there was difficulty in ensuring the benefits were passed on to regional consumers and that significant boundary anomalies were encountered under the scheme.

I am happy to table that release; it is there for those who are interested.

ACTING CHAIR—If you would not mind, we would like it tabled, at the request of Senator Sherry.

Senator Minchin—That is fine.

ACTING CHAIR—Thank you.

Senator SHERRY—Mr Callaghan, I just want to come back to an issue around the discussion we had about revenue forecasts. Has there been any increase in staffing in the forecasting area in the last year or two?

Mr Callaghan—Working on revenue, yes, there has.

Senator SHERRY—Do you know approximately how many staff? I only want an approximation; I am not going to hold you to it.

Mr Callaghan—Let me just double-check. Three extra staff have been assigned to it.

Senator SHERRY—Is that—that is, more staff—an attempt to get the forecasting right?

Mr Callaghan—It is an attempt to improve our performance.

Senator SHERRY—Are the extra staff persons who have been selected because they bring particular new expertise and new angles?

Mr Callaghan—They are people who we believe have the appropriate attributes to do the type of work that we are looking at, yes.

Senator SHERRY—While we are on the revenue estimates: there were a couple of budget announcements. One would reduce income tax collected over the forward estimates. That is the removal of income tax from lump sum annuity super at age 60. You are aware of that, aren't you?

Mr Callaghan—The government's plan on superannuation?

Senator SHERRY—Yes. The announcement about the income tax treatment at age 60.

Mr Callaghan—Yes.

Senator SHERRY—The other was the exit tax abolition. You are aware of that as well?

Mr Callaghan—Sorry, perhaps I am not with you. You are talking about the government's plan that there would be no tax from a tax fund after age 60?

Senator SHERRY—Correct. There are two components to that: one is the income tax-free treatment, and the other is the removal of the exit tax.

Mr Callaghan—From a pension as opposed to a lump sum. Is that what you are referring to?

Senator SHERRY—Yes. I was not going to go to that level of detail with you but, yes, you are right. That is what I am asking about. Am I correct in assuming that the revenue forecasts about income tax collected have been reduced as a consequence of that in the forward estimates?

Mr Callaghan—As was announced in the plan that the government released, provision has been made within the forward estimates for the cost of the plan.

Senator SHERRY—So the reduction in income tax that flows and the reduction in exit tax collected that flows—the two heads, the revenue income tax and the superannuation tax, have been reduced as a consequence?

Mr Callaghan—A general allowance has been made within the forward estimates.

Senator SHERRY—Can you tell me what the general allowance is?

Mr Callaghan—No, because what the government has published is that provision has been made within the forward estimates in the plan that has been released. It has not published a breakdown. It is up to the government what it wants to publish.

Senator SHERRY—But it has published an aggregate cost, hasn't it?

Mr Callaghan—It has published a provision over the forward estimates up to—I think it was—\$6.2 million over the forward estimates. That is what it has announced.

Senator SHERRY—Correct. Therefore a component cost estimate would have been made in order to come up with an aggregate cost over the forward estimates?

Mr Callaghan—Yes.

Senator SHERRY—Thank you. I have some questions on the impact of the personal income tax cuts announced in the budget with respect to revenue. Can you provide me with the details of the number of taxpayers in each marginal tax rate band from 2006-07 as a consequence of the personal income tax cuts?

Mr Callaghan—Let me just check.

Senator SHERRY—Is there anyone who can help me?

Mr Callaghan—The only thing that is published is in the taxation statistics, and that is backward looking. There is not up-to-date published information on income breakdown.

Senator SHERRY—That is why I am asking: it is not in the budget papers.

Mr Callaghan—That is right. It is not published.

Senator SHERRY—Has the work been done?

Mr Callaghan—What work is this?

Senator SHERRY—The number of taxpayers in each marginal tax rate band from 2006-07 through to the last year of the forward estimates. Frankly, I would be very surprised if it had not been done.

Mr Callaghan—That nature of work is available, yes.

Senator SHERRY—Is it here today? Is there an officer who can give me the figures?

Mr Callaghan—Sorry, we cannot. It is not published.

Senator SHERRY—I know that. That is why I am asking.

Mr Callaghan—Again, it is the government's decision as to what it chooses to publish. We would have to take it on notice to refer it to the government.

Senator SHERRY—Was there any modelling done of the impact of the tax cuts announced in the budget on effective marginal tax rates?

Mr Callaghan—Yes, there was work done on estimating effective marginal tax rates.

Senator SHERRY—Given you have answered that, I do not see why you could not answer Senator Fielding's earlier question.

Mr Callaghan—I do not think that goes to policy.

ACTING CHAIR—Stick to your question. No observations.

Senator SHERRY—Was the modelling of the effective marginal tax rates done before or after the budget? My assumption would be that it would have been done before the budget announcement. Can you confirm when it was done?

Mr Callaghan—After the decisions are taken, work is done on that. Before that, a variety of work is always undertaken in looking at various aspects of these things.

Senator SHERRY—So both before and after?

Mr Callaghan—Yes.

Senator SHERRY—Following the budget, how many individuals have an effective marginal tax rate greater than 90, 80, 60 and 50 per cent?

Mr Callaghan—I would not know. We will have to take it on notice. We have not got anyone here.

Senator SHERRY—Why?

Mr Callaghan—I am not sure what is available.

Senator SHERRY—You are not an official that I would expect—and it is not a criticism—to be across the detail of the sorts of questions that I am asking now. Is there any officer who is?

Mr Callaghan—The advice I have received is that we are not sure and we would have to take it on notice. We will take it on notice.

Senator SHERRY—In respect of that question, yes. I have some more questions.

Mr Callaghan—It might be easier if we could take them on notice. It is going to be very hard to go through it point by point.

Senator SHERRY—Yes, but you are not the officer I would expect to know this sort of detail.

Mr Callaghan—I know, yes.

Senator SHERRY—You are getting prompting from behind you. Presumably that officer is here to answer questions.

Mr Callaghan—He is giving me advice. If he believed he could contribute, certainly he would.

Senator SHERRY—Could we have a contribution? At least can I pose these questions directly to the officer?

Mr Callaghan—Perhaps if you run through the questions we will see what we can do to help.

Senator SHERRY—Come on: that is not reasonable, Chair. There is an officer here who clearly has knowledge of these issues.

Mr Callaghan—He can come forward.

Senator SHERRY—Thank you. At least he can say yes, no or maybe or take it on notice. That would be a little easier. Mr Ray, was modelling done on effective marginal tax rates?

Mr Ray—Yes.

Senator SHERRY—Before the budget, afterwards or both?

Mr Ray—I think Mr Callaghan has already answered that question.

Senator SHERRY—Both?

Mr Ray—Both.

Senator SHERRY—And the outcome of this modelling?

Mr Ray—In general terms, the budget tax cuts reduce effective marginal tax rates.

Senator SHERRY—What do you mean by ‘general terms’?

Mr Ray—It is difficult for me to answer in specifics off the top of my head.

Senator SHERRY—I have got considerable confidence in your abilities. You know how reasonable I am. If a ballpark figure is given, I do not come back and slam the public servant the following year for giving me an estimate that might be a little bit out. You know how reasonable I am, don’t you?

Mr Ray—Yes, Senator. Quite clearly, those taxpayers who have had a reduction in their marginal tax rates, have had reductions in their effective marginal tax rates, other things being equal.

Senator SHERRY—But that would be contained in the specific modelling, wouldn’t it?

Mr Ray—That is contained in the specific modelling.

Senator SHERRY—Do you have a copy of that modelling here?

Mr Ray—No.

Senator SHERRY—Has an audit been undertaken of household types that still face higher EMTRs? There are some who face higher EMTRs as a result of the budget.

Mr Ray—That is correct. There will be some households which will face higher EMTRs as a result of the changes in the budget. As part of the analysis, obviously, we would look at

those who have lower EMTRs and those who have higher EMTRs. In general terms, the magnitude of the reductions are greater than the rises. So, if you like, there has been a flattening of the profile of EMTRs.

Senator SHERRY—Yes. But there are some who face higher EMTRs—or effective marginal tax rates, for Hansard’s benefit. Let me give you an example: single income families with children, earning between \$25,000 and \$35,000, face an EMTR of at least 80 per cent and up to 98.5 per cent. Does that sound reasonable?

Mr Ray—From memory, that does sound reasonable, yes.

Senator SHERRY—Thank you. I think you would need to take this on notice: can you calculate for the committee the increase in disposable income for such a family where private income increases from \$25,000 to \$35,000 per annum? You may have done a calculation already. You may have it here, which would be fantastic.

Mr Ray—A single income family with two children?

Senator SHERRY—Do you have a figure there for a family with two children?

Mr Ray—If you look at appendix B in the budget overview, there is a cameo analysis of a single-income couple with two children aged three and eight. The rise in disposable income as a result of the budget at \$30,000 is \$910.

Senator SHERRY—Was any modelling undertaken using the MITTS? And I cannot tell Hansard what the acronym stands for; you may be able to help us.

Mr Ray—I can tell Hansard that. It is the Melbourne Institute Tax and Transfer Simulator model.

Senator SHERRY—Was any modelling undertaken using the MITTS-B model to examine behavioural impacts of these budget changes?

Mr Ray—You are aware that we have been building capacity on assessing participation effects?

Senator SHERRY—Yes.

Mr Ray—That project is at an early stage, but as part of that project we have assessed the MITTS-B model. At this stage, we would still have some reservations about using that model to produce precise numbers, but after the budget the Melbourne Institute provided us with a draft run that it had done, and we did some analysis of that to see whether we would get similar results using our version of the model.

Senator SHERRY—So Treasury has its version of the MITTS model?

Mr Ray—Correct.

Senator SHERRY—You have been provided with figures by the Melbourne Institute?

Mr Ray—Correct.

Senator SHERRY—Having received those results, you are running it through your own model as well?

Mr Ray—Yes, our version of the model has different base data in it than the Melbourne Institute used.

Senator MURRAY—How would you know that?

Mr Ray—Because we know what data they use. We have engaged the Melbourne Institute to help us in this work at various stages in the project.

Senator SHERRY—I recall a discussion we had about modelling development at a previous estimates hearing.

Mr Ray—Correct.

Senator MURRAY—Sorry to interrupt your flow, but just let me know in what significant respects the data is different?

Mr Ray—It is more up to date, Senator .

Senator MURRAY—Yours is?

Mr Ray—Yes.

Senator SHERRY—So that modelling has been received, you are also doing your own modelling with your own model. Do you have that here?

Mr Ray—No, Senator.

Senator SHERRY—Could you take that on notice, please?

Mr Ray—Sure. I presume you are asking me to take on notice what the results are?

Senator SHERRY—Correct. Just to clarify, did Treasury do any modelling or do any through the Melbourne Institute prior to the budget announcements in order to see what different impacts would be, given different approaches on tax?

Mr Ray—I think the best way to answer that question is to say that we constantly would examine what different policy options might do. It is an ongoing function of ours.

Senator SHERRY—It is ongoing. Can I take that as a yes, that in the last financial year leading up to the budget announcements modelling was done?

Mr Ray—Modelling was done, but I would not want to mislead you that modelling was done using MITTS-B. MITTS-B is something which we have only got up and running in recent times.

Senator SHERRY—This is with respect to Treasury's internal modelling?

Mr Ray—That is correct.

Senator SHERRY—You say recent times. How recent?

Mr Ray—We have had it functioning in some form or another I guess since before Christmas. I would need to take on notice the exact time.

Senator SHERRY—You know how reasonable I am, Mr Ray. You have given me an approximate time. I asked about the modelling options and outcomes to those options. You mentioned just prior to December, Christmas, internally. What about externally, contracted out to the Melbourne Institute, for example, in the last year?

Mr Ray—We have not contracted out any modelling in the last year in the sense of actually running a model. What we have contracted out is assistance with programming skills, understanding MITTS-B—doing code walk-throughs and those sorts of things.

Senator SHERRY—So there has been no contracting out to MITTS-B. Any other modellers in this area?

Mr Ray—No, Senator.

Senator SHERRY—How many taxpayers are currently eligible for the low-income tax offset?

Mr Ray—I would need to take that on notice.

Senator SHERRY—Could you also take on notice how many will be eligible from 2006-07?

Mr Ray—Sure.

Senator SHERRY—Is the benefit of the low-income tax offset incorporated in the withholding schedules?

Mr Ray—The low-income tax offset is not incorporated in withholding schedules. It is provided on assessment.

Senator SHERRY—Have you examined the incorporation and its impact within the withholding schedules?

Mr Ray—I think that goes to a specific policy matter.

Senator SHERRY—I am just asking whether the work has been done, the examination has been carried out. I am not asking for the results; you know how reasonable I am.

Mr Ray—I think Senator Fielding went through a long discussion on this question with Mr Callaghan earlier today.

Senator SHERRY—What does low-income tax offset have to do with petrol?

Mr Ray—It is the same principle.

Senator SHERRY—Has an examination been made of the behavioural impact of the low-income tax offset being paid through the PAYG withholding system?

Mr Ray—I think that is again going close to the same sorts of questions of whether we have analysed a particular alternative option. I might be able to help you in the sense that, within MITTS-B, the effect of the way that is modelled is reasonably similar to if it were in the withholding system.

Senator SHERRY—What do you mean by reasonably similar?

Mr Ray—I would need to check whether it would be absolutely the same, that is all. As you know, if it is done in the withholding system there would be the issue of debts and those sorts of things. I am not sure that MITTS-B encompasses all that detail.

Senator SHERRY—That would be one of the different outcomes.

Mr Ray—That would be one of the different outcomes.

Senator SHERRY—Can you think of any others?

Mr Ray—Clearly, if it were in the withholding schedule, it would be withheld on a fortnightly or whatever basis.

Senator SHERRY—Thanks for that.

Senator MURRAY—I want to switch direction shortly, and I have a series of questions that you can take on notice if you want to. I want to ask a series of questions about the revenue consequences of Work Choices. I am aware of both Treasury and other agency remarks about the possible effects of Work Choices, and of course I am aware of ministerial remarks about that. My question is with specific reference to the budget papers. Were any estimates derived with respect to wages, income or tax raised as a result of the implementation of the Work Choices legislation?

Mr Callaghan—I think it is really looking at what is the general scope of factors that would be driving the parameters influencing personal income tax, for example—what would be affecting wages, employment growth et cetera. That is done at a broad macro level that then feeds through. It is not the type of element of the policy in Work Choices where, in my understanding, you could identify specific elements about which you would be able to say, ‘Here is the connection of what might be the impact on a particular outcome on the macro level.’

Senator MURRAY—Yes. In my mind is the question of whether going backwards, once the data is in, Treasury and the tax office will be able to assess the impact of Work Choices. Let me explain to you why I am interested. The statements and the analyses provided by many of those who oppose the Work Choices legislation indicate that they believe that wages will fall in key sectors where workers are without market bargaining power. Obviously, if wages fall, in an individual sense, then tax revenue will fall. From your perspective, if the economic consequence of a fall in wages is a rise in employment, you may not see an aggregate change in the overall tax revenue that comes in. So it is trying to disaggregate it to the individual or the industry effect. Those sectors which are regarded as having less bargaining power and high numbers in employment include those of retail, hospitality and services rather than, say, mining or construction, where there is high demand and therefore wages are likely to be maintained at a high level. Having tried to describe to you what my interest is—

Mr Callaghan—I understand.

Senator MURRAY—I really want to know—and I can appreciate that you cannot forecast or would find difficulty in forecasting it—whether, once the effects of Work Choices have flowed through, you would be able to see whether those effects had occurred. Is there a way in which you will be able to do that?

Mr Callaghan—I think the nature of what you are talking about is beyond the activities of Revenue Group. As you described it, you are looking at what might be the impact of the policy outcome on the overall performance of the economy. You are not looking at it solely, as you specifically noted, as a static analysis of what might be particular activities but at the more overall impact it may have on performance, on employment, more generally. Assessments have to be made on that. As I say, that is really beyond the scope of the work we do within this outcome. I would make the general comment, though, that certainly from what

we would be looking at—where particular revenue and particular performance in the economy is—it is very hard to dissect specifically what might be particular drivers against everything else that may be occurring: the broader developments in the world economy, particular activities that are happening across all the scope of policy, of macro policy and individual sectoral policies. To be able to identify it out is always going to be a hard task. But I should say that this is outside our activities.

Senator MURRAY—I will give you a specific example of why I thought it might concern revenue. There has been publicity this week about the Spotlight Group having altered its work arrangements with its workforce under the new Work Choices legislation. The union concerned, the ACTU and others have calculated that the effect of that will be a \$90 reduction per week in earnings for the workers affected. I do not know what their marginal tax rate is, but let us assume for the purposes of this discussion that it is the 30 per cent tax rate. Then, if they lose \$90, you as revenue calculators lose \$30. That is the crude calculation. So, if this were an economy-wide effect in large employment sectors, there would be revenue consequences of this occurrence. I really do appreciate that there are many other factors to take into account and I really do appreciate the complexity of it, but, if the effect were significant enough, would you notice it or have the means to pick it up or the data sets to be able to discover that that was occurring?

Mr Callaghan—No, not within the activities of Revenue Group. As you say, you are looking at what might be the performances across the whole economy. We are looking at the performance of the whole economy in terms of how it flows through into the revenue that we are forecasting, that the tax office is collecting. What are the particular drivers behind particular performances? That is something that needs to be done in assessing the performance of the economy more generally. As I say, there is not much we could do to help you in this type of questioning at all.

Senator MURRAY—I would assume the tax statistics are not disaggregated sufficiently to pick that up either?

Mr Callaghan—No, I do not believe that they are, down the line that you are trying to look at. It is very difficult. The chain of reasoning you are talking about would require a very—

Senator MURRAY—The other effect of this, of course, is that—in a straight economists' argument—if you reduce the wage share and there is no other change in the business, it just flows on to the profit share, which means that you pick up the tax at the corporate level, especially if we use the marginal tax rate of 30 per cent. If that \$90 example occurred, you would just see it shift to the corporate tax, wouldn't you?

Mr Callaghan—Again, you are looking at it in a very static sense. As you commented earlier, there are many other factors influencing it. Academics may well try to break it down to the particular impact of particular policies, but if we look at a range of policies, and we are looking at the overall performance of the economy, we see very strong growth in performance, employment, wages and profits. What are the particular components across that? A combination of components would be driving it. Similarly if you saw some downturn occurring in the economy that may have come from a variety of factors, how could you

identify the counterfactual? To try to segment and identify particular areas within that—particularly approaching it from the tax revenue point of view—and to try to feed back from looking at the tax statistics, is not, I believe, profitable.

Senator MURRAY—I did not hear you say, so I want to hear you confirm, that, in your estimates of increasing corporate tax revenue in the forward years, you were not factoring in a shift from the wage share to the profit share.

Mr Callaghan—No. In the forward years, they are just projections; just a heading out on long-run averages. So there is no forecasting; there is no assumption of changes. The one assumption that has gone into the projection years is of commodity prices. But they are not forecasts. They are just putting it at long-run rates of growth of the economy going forward, just to give a baseline from which to do the forward estimates.

Senator MURRAY—So you have not calculated a shift in wage share to profit share?

Mr Callaghan—They are not forecasts looking at what might be happening. It is not a forecast, in the projection years.

Senator MURRAY—Chair, I have a series of questions, which I advised to Mr Callaghan in advance, on the budget superannuation package. Are you happy for me to go through those five questions?

Senator SHERRY—I was going to go through it in a fair amount of detail.

Senator MURRAY—These might set the scene then. I do not have a lot of questions of detail. These are five questions I have set in advance.

Senator SHERRY—I do not think Mr Callaghan is the appropriate person to answer detailed questions.

Mr Callaghan—I am, Senator, with the help of other colleagues—Revenue Group is responsible for retirement incomes and superannuation.

Senator SHERRY—So we will not ask those questions under retirement incomes and saving policy, Output 3.1.2?

Mr Callaghan—It is all part of it.

Senator SHERRY—Okay; I am happy if you and other officers are going to take those questions.

Mr Callaghan—Yes, Senator.

Senator MURRAY—I was content for these questions to be answered on notice, but I have been advised that Mr Callaghan will provide an oral response. I would just like to proceed with those, if I could.

Mr Callaghan, the first question was—and I know you have it in front of you, but I had better record it for *Hansard*—has the Treasury estimated the projected cost of the proposal to abolish taxes on most superannuation benefits for people aged 60 and over on federal budget revenues over the longer term—say, to 2030? You will appreciate, with that intergenerational view, why I have done that. If Treasury has done so, could you provide the information?

Mr Callaghan—The Treasury has undertaken some general work on the long-term implications of the government's plan to simplify and streamline superannuation, but it is impossible to provide a definitive estimate of the long-run cost of the proposals on the federal budget. The government has made provision in the 2006-07 budget for the cost of the plan over the forward estimates period.

You specifically asked about the long-term cost to federal budget revenues, but I would point out that there are two components of the cost of the government's plan. Firstly, on the revenue side, there is the cost associated with the abolition of taxes on superannuation benefits paid from a tax fund for people aged 60 and over. Secondly, there is an expense component. The halving of the pension asset test rate from 20 September 2007 would increase expenses through increased age pension payments. The extension of the co-contribution to the self-employed is another expense component of the plan.

The long-run costs of the government's plan are dependent on the effects of first- and second-round behavioural changes—in particular, the impact of the incentives on the plan to increase saving and to increase workforce participation. The government has also indicated that it anticipates behavioural and efficiency changes from significantly reducing complexity in the area of superannuation. Given the uncertainty around estimating behavioural responses, the second-round effects of tax changes are not normally incorporated into estimates of the budgetary impact of tax policy measures. In addition, it has not been the practice of Treasury to prepare long-term costings of tax measures, including changes in tax rates and tax thresholds.

The assumption in the *Intergenerational report*, released in 2002, was that Commonwealth revenue would stay at a constant proportion of GDP. As noted in the 2002 *Intergenerational report*, this assumption was consistent with that in the international long-term budget reports and it reflected the fact that government revenue growth and GDP have the same drivers. The 2002 *Intergenerational report* did contain long-run projections of the impact of demographic changes on components of government spending. The second intergenerational report, which is scheduled to be published in May 2007 and is as yet to be produced, will reflect the impact on age pension and public health outlays of all changes, including the proposed changes to the pension assets test.

Senator MURRAY—That is good. I was one of those who were impressed with the *Intergenerational report* initiative. I thought it was a good contribution to long-term policy. Am I to understand the substance of your remarks to mean that, given the consultation that is under way at present, which will result in an announcement by the Treasurer, because he is consulting on the effects of this, we will get some kind of statistical forecast, either pre-empted in that announcement or expressed more fully in the 2007 update of the *Intergenerational report*?

Mr Callaghan—It is not up to me to pre-empt what might be announced by the Treasurer, but as I said, in the 2002 *Intergenerational report*, yes, there were projections of the impacts of demographic changes on government outlays and that included the age pension. In the next version of the *Intergenerational report* we would expect that it would have the same look at projections of government outlays, including pensions. The fact that there has been a change

in the assets test taper rate for pensions would be a factor that would be included in making those projections.

Senator MURRAY—And the analytical and modelling work that you are doing now will enable the Treasurer to make the decision as to what information he can release with respect to long-term forecasts?

Mr Callaghan—Again, I cannot pre-empt what the Treasury might release; I am just commenting on what was done in 2002 and what we would expect to be included in the update of the *Intergenerational report*, if it is prepared on the same basis.

Senator MURRAY—But if you wanted the data you would be able to produce it on that estimated basis?

Mr Callaghan—We would be. It is looking at projections of what may be happening to pensions. So we would be looking the range of factors that may be influencing the growth in pension outlays.

Senator MURRAY—The Productivity Commission projects that, in the absence of policy change, an increase in government expenditure for all levels of government of the order of four per cent of GDP, which is \$36 billion in current dollars, would be needed by 2030 to meet the high costs of an ageing population. That was from the *Economic implications of an ageing Australia* report by the Productivity Commission in 2005. Has the federal government considered how future governments will meet these costs in the absence of growing revenues from taxes on superannuation benefits?

Mr Callaghan—Your question is to what the federal government has considered. I can only refer to the discussion paper that was released in 2004 by the government entitled *Australia's demographic challenges*. In that the government outlined that its preferred solution to address the challenges of an ageing population was to implement policies designed to grow the economy more quickly. The government noted in that report that the best way to achieve higher economic growth was via increases in labour force participation and productivity.

Senator MURRAY—The 2004 announcement and the 2005 Productivity Commission report were both made without the advantage of the changes that have been put through the budget and which will presumably be introduced later in the next financial year. Can you take that question, on notice, to the Treasurer for a response?

Mr Callaghan—Yes.

Senator MURRAY—I move to question 4 on my sheet. How many people currently pay tax on superannuation benefits? What proportion of benefits attract tax? And, in respect of taxes on lump sum retirement benefits only, what is the average lump sum received by these taxpayers and the average level of tax paid? What is the average lump sum retirement benefit for all recipients of these payments? You can see why I gave this to you in advance.

Mr Callaghan—Yes. In the 2003-04 edition of the taxation statistics, personal income tax is detailed in table 5. It gives the numbers receiving eligible termination payments and other Australian pensions—that is, other than the Commonwealth age and other social security pensions—by taxable income. Taxation statistics are, of course, available on the ATO website.

The data published in taxation statistics covers all eligible termination payments and pensions and does not provide a breakdown for superannuation payments. It is normal for individuals to receive several eligible termination payments during the course of their working lives. As such, the data necessary to provide the information requested is not published.

Senator MURRAY—I would assume too that you cannot answer those questions prospectively until the final government legislation and package goes through, because, without knowing that detail, you would not be able to assess the proportion of benefits that would attract tax or the average lump sum that you might forecast would be received, because you do not know the final shape of legislation. Is that right?

Mr Callaghan—More broadly, in the sense that the government has announced the plan and is consulting on it—particularly on aspects of implementation—generally we wait to see the decisions by the government as to the components of the plan. Yes, that covers more generally any aspects—

Senator SHERRY—You are obviously not going to disclose those figures today, even though you have got a costing, but will the cost of the components be released at that point in time?

Mr Callaghan—These are always matters for government. Really, it is a matter for government as to what is going to be released.

Senator SHERRY—Is it not the norm that when a measure becomes policy, we are provided with a costing?

Mr Callaghan—Yes.

Senator SHERRY—That is the norm, I cannot think of any—

Mr Callaghan—If the decisions are taken, it would normally be included, for example, in the budget.

Senator SHERRY—And is it not the fact that we have a \$6.2 billion cost in this budget? That is factually correct, isn't it?

Mr Callaghan—I can only quote what is on the record. The government announced a plan in the context of this budget, and they stated that provision had been made within the budget for up to \$6.2 billion to cover the cost of the plan.

Senator SHERRY—I do not see the words 'up to' in mine.

Mr Callaghan—Sorry; it is my loose wording, Senator; it says 'provision of 6.2'.

Senator SHERRY—Yes, over three years.

Mr Callaghan—Yes.

Senator SHERRY—Estimated impact on underlying fiscal balance of proposed plan. Let me get this straight: you will not answer questions about the component costs of that \$6.2 billion?

Mr Callaghan—I would take it on notice. What the government chooses to publish is a matter for the government. I would have to take any question about the components on notice.

Senator SHERRY—Could I have this from the minister? We have a \$6.2 billion costing. I have a series of questions about the costings and how they are derived. There are a range of proposals. Obviously, you would accept that in order to come up with an aggregate figure, they have been costed. You would accept that, wouldn't you, Minister?

Senator Minchin—Yes.

Senator SHERRY—And we are not going to be given details about the breakdown of the aggregate cost of this plan at this estimates?

Senator Minchin—No, not at this estimates.

Senator SHERRY—That is what has been signalled.

Senator Minchin—Yes, the question of what, if any, breakdown is given at the time that these measures ultimately come into effect is a matter that the government will consider, I guess.

Senator SHERRY—You are not going to provide the breakdown of those cost estimates now. This is what is being indicated. Are there going to be any answers given on the measures themselves, when I put questions? Put aside the cost issue, are we going to get answers to any questions, or has that been ruled out as well?

Senator Minchin—No, it has not been ruled out. We will receive your questions and answer them to the best of our ability.

Senator SHERRY—Good.

Senator Minchin—Noting that the plan is a plan and it is out there for consultation.

Senator SHERRY—Yes, but with regard to the costing of each component, no. That is the attitude you are taking at the moment.

Senator Minchin—That is correct.

Senator SHERRY—Why?

Senator Minchin—We have published an estimate of the total impact.

Senator SHERRY—Yes, \$6.2 billion.

Senator Minchin—We are not, at this stage, proposing to publish details of that, but, at the time that plan is finalised and becomes legislation and we bring it to the parliament, then I leave open the possibility that we may give further information on the costings. I will refer that obviously—

Senator SHERRY—Come off it. You are not going to present a bill to parliament with a number of proposed changes without providing the details and the impact.

Senator Minchin—I am just not in a position to answer that question here and now on behalf of the Treasurer.

Senator SHERRY—Could you take that on notice?

Senator Minchin—I would be happy to.

Senator SHERRY—Frankly, I find it extraordinary you cannot answer questions today.

Senator Minchin—I am inferring that I would expect that, at the time we actually bring this in, there would be greater detail, but I am not in a position to commit to that. I think it is reasonable for you to expect further detail on that when we bring it into the parliament.

Senator SHERRY—There is a budget announcement that the exit tax will be abolished, isn't there?

Senator Minchin—There is an announcement of the government's proposal to do so as of 1 July next year.

Senator SHERRY—And there is an announcement to abolish—

Senator Minchin—And the budget figures reflect that. This is in the contingency reserve.

Senator SHERRY—Yes. That is exactly my point: the budget figures reflect this. Why can't we be told the loss to revenue and, therefore, the benefit to taxpayers of the abolition of the exit tax? Why can't we be told that?

Senator Minchin—The public and you are being told the current estimated impact of the plan on government revenue of \$6.2 billion over the first three years of this proposal.

Senator SHERRY—But why deny us, and deny the Australian community, particularly the taxpayers, knowledge of what the level of benefit is going to be? Take the exit tax, for example.

Senator MINCHIN—The public is being told what the estimated fiscal consequence will be of the proposal to effectively remove the exit tax on superannuation.

Senator SHERRY—Are you suggesting the \$6.2 billion cost of this package is the exit tax?

Senator Minchin—That is the broad plan, but obviously there are additional components of this and additional consequences of it that go to make up that figure. As I said, I imagine that, at the time we seek to legislate this and bring it into parliament, further detail on the costings will be made available. But that is a matter to be developed. I cannot commit to that here and now, but it is reasonable for you to assume that is likely to be the case.

Senator MURRAY—You see, Minister, one of the reasons why I phrased my questions as I did is that I do not believe that the \$6.2 billion is anything like a firm figure. Firstly, if you are still consulting, it will be subject to adjustment. Secondly, in the examination process, it is already apparent that the Assistant Treasurer, Mr Dutton, and the Treasurer have been amplifying on what was announced, which means there is going to be change. And, thirdly, I had the impression that the whole exercise has to be fully worked through. It was not fully worked through in time for the budget, otherwise it would not be a proposal, it would be an announced measure. My assumption the whole time is that the \$6.2 billion is not the final figure, and it could be less or it could be more. Would you agree that the \$6.2 billion is not the final figure?

Senator Minchin—Treasury may want to answer that in more detail, but I think to say that this is just some vague idea that we put out into the ether is wrong.

Senator MURRAY—No, I am not saying that it is.

Senator Minchin—The Treasurer made it clear that this is the detailed policy package which we propose for 1 July next year, but, given the complexity of superannuation—and I think this is prudent and sensible as a government—we want to ensure that, through a process of consultation with the industry and others, we identify any possible unintended consequences or refinements.

Senator MURRAY—Exactly.

Senator Minchin—We are not going into this expecting that there will be those things, but we do want to ensure that we have a process whereby, if any of those exist, they are identified, and we make sure that we introduce legislation that is workable and sensible. But again, subject to what Treasury want to say, I suspect we are confident in the robustness of that figure and the robustness of the plan.

Senator MURRAY—If I were to ask you, Minister, if you could guarantee that the cost would be \$6.2 billion, you would answer, ‘Of course not,’ and I would accept that. You cannot. The proposal is not at the stage where that figure is a final estimation. It cannot be a final estimation if you are still in the process of consultation and if ministers, the Treasurer and the Assistant Treasurer are still foreshadowing adjustments to what was proposed in the budget.

Mr Callaghan—Can I just add that the \$6.2 billion that is included is our best estimate of the plan that has been announced now.

Senator MURRAY—I accept that.

Mr Callaghan—With the elements that have been indicated for consultation, in one sense if there is an unintended consequence or something that has not been foreshadowed, particularly at the transitional side of it, then, as we understand it, the government has indicated that these are the matters we are consulting on. In the sense that they are unanticipated now, by definition there are things that we could not cost on because we do not know what they are. But I think that for some of the transitional elements of it, if we are looking at just such things as how it is going to be impacting on those now—in terms of making undeducted contributions, what should be some averaging components et cetera—they are around the edges, to some extent, of the broader plan that has been introduced. So I think that, in trying to explain it, the \$6.2 billion is our best robust estimate of all the components of the plan that have been announced. To the extent that there are consultations that may see some variations of that, yes, they would have to be taken into account. But, without knowing what those variations might be, particularly if they are transitional, in some respects they may not be particularly major. It all depends on what they are going to be. But certainly what has been announced, the \$6.2 billion, is our robust estimate.

Senator MURRAY—Senator Sherry can speak for himself, Mr Callaghan, but I would expect him to take a view similar to mine: if variations to the \$6.2 billion are a few hundred million dollars either side, it is not of great concern when you are trying to work through a proposition like this—

Senator SHERRY—In fact, that is not unusual.

Senator MURRAY—but if there are billions either side then it becomes an issue. Of course, once you take my view that a few hundred million either side does not matter that much when you are at this stage of the process, then you come back to Senator Sherry's point: surely you can give us, in a broad, reasonable sense, the aggregations which lead up to that \$6.2 billion. Your answer to us to date is that you cannot because, I gather, you have not been authorised to do so. That is correct, isn't it?

Mr Callaghan—It goes back to the earlier answer that this is what the government has published: the allowance for \$6.2 billion over the three years of forward estimates.

Senator MURRAY—Perhaps I should deal with my last question. In this question I want to go to the effects rather than to costings. I advised you of this question in advance. It is No. 5. If the proposed superannuation changes are fully implemented, are there any provisions that would prevent the recipient of a large, tax-free, lump sum benefit—say \$1 million—from passing a substantial part of their savings, say half a million dollars, on to a non-dependent family member such as an adult son or daughter on or before their own death instead of using it to finance their retirement? What tax would be paid on a death benefit to a nondependent, in this example, of half a million dollars?

Mr Callaghan—Under the proposed reforms, there would be no restriction on how benefits, including lump sum benefits, could be spent. A person could withdraw a superannuation lump sum and gift the entire proceeds. This is also true of the current system, so there is no change. However, people who are in receipt of the age pension or other income support payments that are subject to an assets test could be subject to the social security deprivation provisions if they gift a large amount of superannuation. Gifts greater than \$10,000 in a financial year or exceeding \$30,000 in a five-year period can be deemed as deprived assets. In relation to how—

Senator MURRAY—They do have to declare that gift?

Mr Callaghan—Yes, they have to declare that gift. There is no change in that situation. It applies now, and that would still apply. In relation to how a \$500,000 death benefit paid to a nondependent would be taxed under the proposed reforms, this would depend on the components of the superannuation benefit and whether it is paid from a taxed or an untaxed source. To take a typical case of a death benefit paid to a nondependent from a taxed source, under the government's plan the taxable component would be taxed at 15 per cent and the exempt component would be paid tax-free. In table 2.1 of the detailed outline of the plan, it has the description of the components which would be in the taxable and the exempt categories. While the exact tax paid on a \$500,000 death benefit paid to a nondependent from a taxed fund will depend, under the government's plan, on the individual circumstances—just as it also depends on the individual circumstances under the current arrangements—in most cases there would not be a significant difference in tax paid.

Senator MURRAY—So they would still have to pay their marginal tax on that \$500,000?

Mr Callaghan—It is not the marginal tax. In terms of how you derive the components of it—what the taxed amount would be—as I say, table 2.1 of the detailed outline has the breakdown of deriving what the various components are that you have to take into account. Under the plan, there is some simplification in determining what the exempt categories are,

but overall, on a \$500,000 lump sum paid to a nondependant from a taxed fund, under the current system and under the proposed plan, while the individual taxes will depend on the circumstances, you would generally expect that there will not be a significant difference in the tax paid.

Senator MURRAY—You would be well aware of the concern behind that question. This is a benefit designed for one effect, which is to make retirement taxes and income simpler and of greater benefit to the retiree. The concern is that those policies designed for that purpose would be diverted or perverted to provide a benefit to somebody who was not a retiree.

Mr Callaghan—The easiest way to answer that is that in paying to the nondependant that principle is not changing, in the sense that, yes, there would be tax. There is some simplification in how you derive that tax under the proposed plan, but the principle remains the same and the amount of tax that would be paid would be broadly comparable, when it is being paid to a nondependant.

Senator MURRAY—But if that principle which already applies was in fact a negative principle—in other words, it needs to be addressed as an integrity measure; and you might not agree—and if you increase the opportunities for this to occur, in that, simply, more people have more money to do this sort of thing, you actually enlarge the negative effect, if you like. You might or might not agree, but that is the concern.

Mr Callaghan—As you say, you are raising issues beyond just looking at the application of the proposed plan to the current arrangements. You are raising whether you believe that this should be—

Senator MURRAY—Except that it is your job to look at unintended consequences, so I think it is right for me to raise it if I think it is an unintended consequence.

Senator SHERRY—I do not think it is, except that—just on the specific response that Mr Callaghan has given to Senator Murray—under the current arrangements, isn't it true that, if you convert a lump sum to an annuity pension, to the extent that happens, you pay income tax on it at whatever the appropriate income tax rate is after the seniors rebate and the rebate of the 15 per cent? You pay income tax at the moment.

Mr Callaghan—Yes, after the rebates. That is to a dependant.

Senator SHERRY—Yes.

Mr Callaghan—We are talking about a nondependant in Senator Murray's situation.

Senator SHERRY—The point I am getting it is that the individual, if they put it into an annuity or a pension, pays income tax themselves.

Senator MURRAY—The retiree.

Senator SHERRY—The retiree pays it. Under this proposal, the retiree pays no income tax on the lump sum or the annuity pension—full stop—after age 60. No income tax.

Mr Callaghan—That is the plan, yes.

ACTING CHAIR—In relation to the answer that you gave to Senator Murray, my understanding is a little bit different, so I require further clarification. Where a nondependant is in receipt of a benefit after July 2007, my understanding is that it will be taxed at 16.7 per

cent rather than the build-up of the various components, as suggested in the answer to Senator Murray. If a payment is made to a dependant, it will be tax free under the new rules—I think we are fairly clear on the payment to a dependant being tax free. In terms of a nondependant, I would ask you to look again at that 16.7 per cent.

Mr Callaghan—What did you say, Senator? The nondependant at 16 per cent?

ACTING CHAIR—Payable to a nondependant.

Mr Callaghan—At what rate?

ACTING CHAIR—16.7 per cent, isn't it? 15 per cent plus the add-on, which is about 16.7 per cent, isn't it?

Mr Callaghan—Again, it is going to depend on the circumstances. The current arrangements are outlined in the detailed outline.

ACTING CHAIR—I know what the current arrangements are.

Mr Callaghan—It will depend on the circumstances of the individual in the sense of the breakdown of the components. Under the current arrangements it is going to depend on whether it is pre-July 1983, if it concessional, the amount undeducted, the post-June 1994 invalidity—those types of components will need to be factored into it to determine what will be the exact rate.

Senator SHERRY—We have the officers from the area within the Treasury. Presumably they are here to respond to detailed questions such as this. It is not an area I would expect Mr Callaghan to have full knowledge of.

ACTING CHAIR—You have a taxed fund to get away from that detailed breakdown, except in circumstances where the payment is made from a non-taxed fund, such as the Tasmanian Retirement Benefit Fund or Commonwealth pension scheme or the Commonwealth arrangements. I thought the whole idea under a taxed fund was to get away from that detailed component build-up, where you might have up to seven different levels of calculation. But you are suggesting that that is not the case?

Mr Callaghan—As I said, there is a simplification outlined a page 14 of the detailed outline, showing the simplification of the various components under the proposed plan. I will hand over to Mr Lonsdale to go into the details.

Mr Lonsdale—What Mr Callaghan said is correct. For a taxed fund a nondependant in receipt of a death benefit would under the plan be taxed at 15 per cent on the taxable component. The exempt component would be exempt. That is outlined in—

ACTING CHAIR—That is what I said. Mr Callaghan suggested that we revert back to the old formula of looking at the various components as is required under current situation.

Mr Callaghan—That is not what I said. If you look at page 14 it has the old system of all the components, and under the proposal—

Senator SHERRY—Just to clarify, when you say page 14, what document are you referring to?

Mr Callaghan—It is the detailed outline: *A plan to simplify and streamline superannuation—detailed outline.*

Senator SHERRY—I have that. There are two documents. I just wanted to clarify which document you were referring to.

Mr Callaghan—As I said and as Mr Lonsdale said, under the proposed plan, it is going to depend on how much is in the exempt component and how much is in the taxable component. In the exempt component there has been an amalgamation of the various categories under the current system. That is part of the simplification. You will still have an exempt component, as I said in my answer, and tax paid on the taxable component.

ACTING CHAIR—And that taxable component will not necessarily be this rate of 15 per cent or will it be flat?

Mr Callaghan—I will repeat what I said to Senator Murray: the taxable component would be taxed at 15 per cent. The exempt component would be paid tax free. That was what I said.

ACTING CHAIR—Sorry, there is some confusion.

Mr Callaghan—What I was trying to explain to Senator Murray was to work out how much the tax paid on \$50,000 would be. It will depend on how much is in the tax component, being 15 per cent, and how much is in the exempt component for the individual circumstances of the person.

Senator MURRAY—I was asking a two-part question: what is the effect on the retiree and what is the effect on the nondependant who is gifted a benefit?

Mr Callaghan—Sorry, I was answering what would be the tax paid if it were being given to a nondependant.

Senator MURRAY—That is right.

Senator SHERRY—Is that in all cases? What about public servants?

Mr Callaghan—No, taxed funds are different.

Senator SHERRY—Yes, that is what I thought. I think Senator Watson referred to a public servant.

Mr Callaghan—Sorry, I did not pick that up. I was just talking about untaxed funds.

Mr Lonsdale—So for untaxed funds it would be different, that is correct, Senator. If the death benefit is passed to a nondependant, it would be taxed at 30 per cent up to \$700,000, then 45 per cent above that. So, again, as Mr Callaghan said, the tax treatment does very much depend on what form the benefit is taken in, whether it is a lump sum, whether it is a pension, whether it is passed to a dependant or a nondependant and whether it comes from a taxed or a non-taxed fund.

ACTING CHAIR—In relation to this new arrangement, can you also confirm in relation to the roll-over concession that, where a small business man retires and rolls their money over into a superannuation fund, the previous \$500,000 roll-over limit will continue to apply despite the new arrangements of limitation to \$150,000?

Mr Lonsdale—Are you referring to the undeducted contributions cap of \$150,000 per year?

ACTING CHAIR—Yes.

Mr Lonsdale—On page 31 of the detailed outline there is a description of certain exemptions to the cap that would apply. The outline says that scope would be provided for certain exemptions to the cap, such as the CGT exempt component from the sale of a small business.

ACTING CHAIR—Thank you. Senator Sherry?

Senator SHERRY—We have jumped ahead a bit. Does that exemption apply to sale of a family farm?

Mr Lonsdale—If a family farm were classified as a small business, that would be the case.

Senator SHERRY—Where it is not?

Mr Lonsdale—Those issues are part of the consultation process.

Senator SHERRY—I thought they might be. I have had a lot of complaints about that. I want to get to that in more detail later. I want to come back to you, Mr Callaghan. You referred to changes around the edges in terms of costing impact. What do you mean by ‘changes around the edges’?

Mr Callaghan—It is saying how significant the changes are. If they were not significant changes to the fundamental basis of the plan, then they would not have significant costing.

Senator SHERRY—Is it not true that, on many occasions, we get budget measures that are announced, costed and detailed in the budget and there are changes around the edges later on? But we still get the costing. That has happened, has it not?

Mr Callaghan—If you say so, Senator, I am sure it has happened, yes.

Senator SHERRY—Can you recall any examples?

Mr Callaghan—Again, there have been announcements, yes, where there have been costings, yes, and there have been changes, yes.

Senator SHERRY—We have got the costings and, later on, it is not infrequent—you must be aware of that, we have talked about them quite often—that there is a change around the edges, to use your terminology, then we get a revised costing. But we do get an original costing, don't we?

Mr Callaghan—In the particular circumstances, I am sure that that has been the situation a lot.

Senator SHERRY—But we have not got the costings here, have we?

Mr Callaghan—As we have just said before and as you have also quoted, that provision has been made in the forward estimates figure.

Senator SHERRY—We have got the aggregate but not the component costs?

Mr Callaghan—No, the component costs have not been published, Senator.

Senator SHERRY—And they are not intended to be published at the moment; is that is correct?

Mr Callaghan—It is not for me to decide, Senator.

Senator SHERRY—It is not for you to decide—

Mr Callaghan—It is for the government, Senator.

Senator SHERRY—Yes, of course. Let me ask you this, then. Was there any instruction given that the costings of the components were not to be provided by an officer?

Mr Callaghan—No. No specific instructions were given, but we work on the basic principle that the government decides: it makes its announcements, it makes the decisions as to what is published. It is not for us to decide what is published.

Senator SHERRY—I can recall asking about the details of measures and their components, and receiving that information, on previous occasions. We have had a budget measure announced—in this case, \$6.2 billion dollars; that is the money the government wants from the budget—and you drill down and you get breakdowns in costs. We have done that, not infrequently, on previous occasions, but it is not going to happen on this occasion.

Mr Callaghan—I can only repeat what I said before.

Senator SHERRY—Let me go back to my question: was there any instruction given, as a matter of fact, to the Treasury officials—a clear instruction not to provide the details of the costings of the \$6.2 billion? Did that happen?

Mr Callaghan—No, there has been no instruction given. But, as I said, we were working on the basis—and there have been many occasions in the past where we say—that we can only comment on what the published information is and what the published costings are.

Senator SHERRY—I am asking you to drill down to that \$6.2 billion. I have done that on previous occasions on measures where we have gone down to the detail, the components costs, et cetera. We have done that on previous occasions.

Senator Minchin—Senator Sherry, the officials cannot do more than they are. There is a published figure. They cannot go beyond that at these estimates. I have noted your question. I will refer it to the Treasurer and see if he wants to give any further information at this stage. As I say, I doubt it—

Senator SHERRY—So do I.

Senator Minchin—but as this plan develops, and as we get to the point of legislation, I suspect we will be able to provide more detail.

Senator SHERRY—Let me go to one issue. Mr Lonsdale has alluded to it. It is an area where I would expect there to be changes ‘around the edges’. Let me go to one issue where the cost has obviously been calculated, and I cannot see how there would be changes around the edges, and that is the extension of the co-contribution to the self-employed. We have had that costed on previous occasions. We have had the original announcement to employees, and a figure given, and then its extension, and now it is being extended to the self-employed. And obviously it has been costed. Why can’t we have the cost of that? Mr Lonsdale?

Mr Lonsdale—It is difficult for me to elaborate further on Mr Callaghan's remarks. There is a part of the costing that relates to that proposal, clearly. And that is part of the aggregate allowance that has been published in the plan. Part of the \$6.2 billion over the forward—

Senator SHERRY—You would accept that, in respect of the co-contribution, we had a government announcement that there was going to be a co-contribution, and a costing of that. Would you accept that that has happened at the past?

Mr Lonsdale—Where there has been a measure?

Senator SHERRY—Yes.

Mr Lonsdale—Yes.

Senator SHERRY—Secondly, it was then extended. Was it extended?

Mr Lonsdale—As a measure?

Senator SHERRY—As a measure.

Mr Lonsdale—Yes.

Senator SHERRY—And we got the costing of that. And now there is another announced extension. Has it been announced or not? Has an announcement been made that it is going to be extended to the self-employed?

Mr Callaghan—Senator, can I just—

Senator SHERRY—No, hang on—has an announcement been made, Mr Lonsdale, that the co-contribution is going to be extended to the self-employed? Is there any doubt about it?

Mr Lonsdale—The Treasurer has announced a plan that contains a number of changes, and extending the co-contribution for the self-employed is one of those proposals.

Senator SHERRY—Correct. Is there any doubt that it will be extended?

Mr Lonsdale—It is a plan.

Senator SHERRY—He has announced it, hasn't he?

Mr Lonsdale—It is a plan, Senator.

Senator SHERRY—'It is a plan.' So can you indicate to me whether it will go into law or not? Will it appear in legislation? It has been announced as a plan; is it going to pass into law? Are we going to see legislation on it? Will we see legislation or not?

Mr Lonsdale—The Treasurer has indicated that he has released a plan that contains a number of proposals. The proposals have been consulted on. Following that consultation, the government will take final decisions on the plan, and legislation will follow. I think the Treasurer has said that.

Senator SHERRY—So the plan may change?

Mr Lonsdale—That is an issue for government. They are policy issues for government.

Senator SHERRY—Okay. The plan may change, Minister?

Senator Minchin—As I said before, this is the government's proposal. It will be implemented subject to the consultative phase we are now going through where, sensibly and

reasonably, we are going to consult the industry and any other interested parties as to any flaws they see in it and any improvements they think we can make to it to make it more effective. We have announced our objectives and the way in which we want to achieve those objectives, the detail of the plan, but in a proper spirit of consultation we are seeing whether there are any improvements that could be made to it. So we are leaving open the possibility that it could change, but we are not forecasting any changes or saying that it will change. We are being sensible in opening it up for contributions from the community.

Senator SHERRY—But you could make every budget announcement on this basis: ‘The whole budget is a plan; therefore we will put it out to consultation and it may change; therefore we are not going to provide the costings.’

Senator Minchin—No, that is not what we do. But in the case of—

Senator SHERRY—Why do it on this occasion, when in the past you have made announcements in the budget, you have published the costings and they have changed? Why so different on this occasion?

Senator Minchin—Normally you would announce the actual measure: ‘This is what the government will do.’ It is immediately brought forward in legislation to take effect, and there are detailed costings. This is different in that it is described as a plan subject to consultation with the community over a period of some months, with a view to it being presumably legislated in the context of next year’s budget, I assume, for operative effect on 1 July next year. It is not unusual for us, with matters as complex and dramatic as this, to do it by way of almost a white paper, in a sense, to put it out there as a white paper—

Senator SHERRY—A white paper?

Senator Minchin—That is a colloquial term, a loose term, but I suppose it is a reasonable description of what this is. It is out there for community consultation. Subject to the outcome of that consultation, we will implement this. At the time of implementation, as I said before, I imagine we will be in a position to give more detail on the costings.

Senator SHERRY—I have been asking the officer, Mr Lonsdale, about a specific part of the plan which is a consequent flow-on of two previous budget measures—that is, the co-contribution. When the co-contribution was announced, Minister, it was included as a budget measure, wasn’t it?

Senator Minchin—Yes.

Senator SHERRY—With a costing. When it was extended, quite rightly—I am sure, because I asked Mr Gallagher and some of the other officers a lot of questions—there was a budget measure and it was costed, it was released, before it passed into legislation. That is correct, isn’t it?

Senator Minchin—Yes. But this is not a budget measure yet.

Senator SHERRY—I understand that. But with respect to the co-contribution—we are dealing with that one specifically—

Senator Minchin—Yes, but it is part of this plan.

Senator SHERRY—there is a further extension of the co-contribution announced here.

Senator Minchin—As part of this plan—

Senator SHERRY—Yes, for the self-employed.

Senator Minchin—so it does not have the status of a budget measure.

Senator SHERRY—But it has been costed, presumably?

Senator Minchin—Presumably, as part of this overall plan.

Senator SHERRY—I hope it has been costed.

Senator Minchin—I am sure it has, but—

Senator SHERRY—Can Mr Lonsdale tell me that it has been costed?

Mr Lonsdale—Correct. It has been costed.

Senator SHERRY—So why haven't we got the cost in front of us to see?

Senator Minchin—I have already explained to you ad nauseam that this is a comprehensive plan—of which that is one element—the total impact of which is estimated to be \$6.2 billion over the first three years of its operation. It is out there for consultation. It will be modified if necessary or improved if necessary. Then, as we get to the point of legislating these as measures, details of their costings are likely to be announced at that time.

Senator SHERRY—Could I just deal with one issue for which I cannot find costings and which is not part of this package. Again, it was announced in the budget, and there is no costing. I just want to clear this one up. There was an announcement in the budget to extend the seniors tax offset for singles from, I think, \$21,968 to \$24,867 and for couples from \$36,400 to \$41,360. What is the costing on that?

Mr Ray—It is part of the costing of the personal income tax cuts.

Senator SHERRY—What is the costing on it?

Mr Ray—It is part of the costing of the personal income tax cuts.

Senator SHERRY—That is not what I asked. What is the costing of the extension of the seniors tax offset? It must have been costed. It has been costed, presumably—can we ascertain that?

Mr Ray—It is included in the costing of the personal income tax cuts.

Senator SHERRY—And what is the cost?

Mr Ray—I can take that on notice.

Senator SHERRY—Do you have a cost?

Mr Ray—I do not have a cost with me.

Senator SHERRY—Why wasn't it published in the budget papers?

Mr Ray—It was published in the budget papers. It was published as part of—

Senator SHERRY—As an aggregate again?

Mr Ray—That also goes for the extension of the low-income tax offset—the lift in the \$21,600 threshold, the reduction in the 42c rate to 40c and the reduction of the top rate to 45c.

Senator SHERRY—But when the seniors tax offset was introduced—it is a bit like the co-contribution—and I would expect you would remember this, we got a costing on that measure, did we not?

Mr Ray—My recollection is that it was a separate measure.

Senator SHERRY—Correct. And it was costed separately, wasn't it?

Mr Ray—That is my recollection.

Senator SHERRY—Yes. Now it is being extended—there is no argument about that—

Mr Ray—It is being extended as part of the personal income tax cuts.

Senator SHERRY—But why haven't we got a costing of the extension?

Mr Ray—It is included in the costing of the personal income tax cuts, as are all the other components of those cuts.

Senator SHERRY—Given we got a costing of the original seniors tax offset, why is there not a detail of the costing? Was that a government decision? If the government said that that is the way it is going to be done, then that is the way it is going to be done. Why haven't we got it in the budget papers?

Mr Ray—Senator, the standard practice for costing of personal income tax packages that has been followed for some time is to cost them in aggregate.

Senator SHERRY—Is that going to be applied to the extension of the co-contribution? Are we never going to find out how much the cost of the co-contribution is to the self-employed? Is that principle going to be applied to that measure?

Senator Minchin—As part of this plan, do you mean? I have already indicated that we cannot give you a firm answer on that, but it may well be that when we come to implement all the details of this plan there may be further information available on the individual costings.

Senator SHERRY—It is outrageous that we do not get the costs of the components given that there is a \$6.2 billion figure in the budget. It is outrageous that you will not provide us the costings—and you have got them! And you will not give an undertaking to give us the costing components when you do finalise the plan either.

Senator Minchin—I am not in a position to give that undertaking, but I have told you I will refer that to the Treasurer and inform him of your interest.

Senator SHERRY—That is contrary to every budget costing practice of every bloomin' government in the last 100 years, Senator Minchin.

Senator Minchin—I have not said they will not be available. I have noted your interest and will refer that to the Treasurer. As I have indicated, I suspect we will be in a position to give more information at the time they are implemented as measures, but that remains to be seen.

Senator SHERRY—Senator Minchin, can you recall an occasion when the government is announcing the abolition of a tax—in this case the exist tax and income tax on super for lump sum annuities for people over 60—and is indeed boasting about it, that we do not get a figure

of benefit to the taxpayer. We do not get figures for how much revenue is lost and how much tax the taxpayer will again? Can you recall such an occasion?

Senator Minchin—We have announced a \$6.2 billion figure. Most governments of both persuasions when announcing tax packages give comprehensive costings—in other words, global costings.

Senator SHERRY—Of the loss to revenue and the benefit to taxpayers. So the \$6.2 billion is the exit tax and the income tax abolition, is it?

Senator Minchin—The \$6.2 billion is the cost to revenue of this plan: There is no point asking the same question time and time again. We note your interest—

Senator SHERRY—Senator Minchin, what I am asking you is: can you ever recall a previous occasion under this government where a tax is going to be abolished—the exit tax and income tax for people over 60—where we do not know what the loss of revenue is and what the gain to taxpayers is and that that is not announced at the same time as the proposal to abolish the tax? Can you ever recall—

Senator Minchin—I think the comprehensive nature of this plan is unprecedented in the history of our government.

Senator SHERRY—It is not unprecedented, but that is another issue.

Senator Minchin—I am sure it is unprecedented. It is such a wonderful plan and one I am sure you wish you had thought of yourself. I am sure you will support it in the parliament. Indeed, I think you have already said so. I suspect, as I say, when we get closer to the day, when it is actually legislated, we may well be in a position to give more detail. But we are not at this stage.

Senator SHERRY—But my question, Senator Minchin, was: can you recall when a government—yours or ours or anyone for that matter, any government for the last 100 years—has announced the abolition of a tax, is going to get rid of the exit tax and income tax for people over the age of 60, and you have boasted about it, and we have not been provided with the loss to revenue and the benefit to taxpayers that flows as a consequence?

Senator Minchin—We have announced the impact on the fiscal balance. It is estimated at this stage at \$6.2 billion. But this package is unprecedented; I cannot think of a precedent for the comprehensive nature of this package.

Senator SHERRY—What is the specific benefit to taxpayers from the abolition of the exit tax and income tax on super for people over 60? What is it, Senator Minchin?

Senator Minchin—That would depend on the individual taxpayer and his or her particular status.

Senator SHERRY—What is the aggregate loss to revenue and the aggregate gain to taxpayers?

Senator Minchin—You are asking the same question—you are asking for a breakdown of the \$6.2 billion.

Senator SHERRY—Yes, and you refuse to answer it.

Senator Minchin—That is right.

Senator SHERRY—You refuse to answer it. You boast about a tax being abolished and you will not tell us what the cost to revenue is and what the gain to taxpayers is.

Senator Minchin—I have noted your interest in further details on how that \$6.2 billion is made up and I will refer it to the Treasurer.

Senator SHERRY—It is time for lunch, and we will resume after lunch.

ACTING CHAIR—Just a minute; I am in the chair, Senator Sherry.

Senator SHERRY—I was just telling him it was time for lunch, Acting Chair. Sorry.

ACTING CHAIR—A point of clarification: the information in relation to the \$6.2 billion does not have an impact on the budget this year, as I understand it. Is that right?

Senator Minchin—That is right.

ACTING CHAIR—And therefore my understanding of the responses is that when it does have a budgetary impact some of that information will become available.

Senator SHERRY—But it is in the forward estimates, isn't it? The impact is in the forward estimates.

Senator Minchin—There was an allowance in the contingency reserve for the impact—

Senator SHERRY—For the \$6.2 billion.

Senator Minchin—in the last three years of the four forward years. It has no impact in this coming budget year.

Senator SHERRY—But we are not just examining this budget year, are we, Senator Minchin? We are examining the estimates too.

Senator Minchin—For the forwards, yes.

Senator SHERRY—Turn it up!

Senator Minchin—But these are not yet measures being legislated. It is a plan announced in this budget—

Senator SHERRY—So there is no guarantee it will go into law; it is just a plan which may not see the light of day.

Senator Minchin—The government has announced an intention to implement this plan—

Senator SHERRY—Oh!

Senator Minchin—subject to consultation with the community. We have budgeted for it. The whole budget is based on this occurring—

Senator SHERRY—Good. No argument about that.

Senator Minchin—based on the \$6.2 billion impact in the last three years of these forward years.

Senator SHERRY—You have got \$6.2 billion there but you are not going to tell us the costs. You are not going to tell us the detail of the cost break-up for the \$6.2 billion.

Senator Minchin—All you want is further details. I know that you are interested in detail and we will give that to you in due course if we can.

Senator SHERRY—You are not going to tell it to us.

ACTING CHAIR—Could I make one correction to the *Hansard*? I think I referred to a figure of 16.7. It should have been 15 per cent plus 1.5 Medicare levy. The tax officers have been very patient. When is it likely that we will need the tax office?

Senator SHERRY—I have a lot more questions on this superannuation plan.

ACTING CHAIR—So you will not need the tax office for how long?

Senator SHERRY—We are breaking for lunch now; maybe we will just give it a bit of thought.

ACTING CHAIR—It would be better if they did not have to come back until three or four o'clock.

Senator SHERRY—I do not know how long. One of the difficulties is that we are getting a lot of stonewalling on the super plan, so I may not get any answers to the many questions I have. It is the government putting us in that position. So I am not in a position to indicate—it may be I get five minutes because I get no answers on the super plan and therefore we go straight to the tax office. So I cannot indicate, Acting Chair.

ACTING CHAIR—If there is a high probability of only five minutes, I think we have to ask the tax office to come back at 1.30.

Senator SHERRY—It could be two hours. If I get answers to all my questions on the super plan, we could be here for two hours. It depends on the degree to which the government is going to stop being secret about this plan.

Senator Minchin—There is no secret about the plan.

ACTING CHAIR—All right, then, Senator Sherry. I just wanted to make sure that we are assisting the tax office personnel in the discharge of some of their other responsibilities.

Proceedings suspended from 12.33 pm to 1.32 pm

CHAIR—Senator O'Brien.

Senator O'BRIEN—I have just a couple of quick matters. I am sure you are aware that, under item 5, subsection 38-185(1) of the GST act, when a ship bunkers—that is, takes on fuel—in Australia and is on a voyage that has a destination outside of Australia, the bunker fuel for the ship is considered as ship's stores and thus is GST free. The effect of that provision is that foreign registered ships that are granted a single voyage permit pursuant to section 286 of the Navigation Act, which are competing with Australian registered or licensed ships in the coastal trade, have that tax advantage over Australian registered or licensed ships. What is the government's policy about this lack of competitive neutrality with regard to the tax act?

Mr Callaghan—That is a question of government policy.

Senator O'BRIEN—Perhaps I will rephrase my question. Isn't that position contrary to the government's policy of competitive neutrality?

Mr Callaghan—I am sorry; it is difficult to respond to that question about whether it is contrary or not to government policy.

Senator O'BRIEN—It is factual, isn't it, that a ship taking fuel in those circumstances will not pay GST? It may use fuel taken on outside of Australia to complete—

Mr Callaghan—I am afraid we do not have our GST experts with us today. I will take your word that that is—

Senator O'BRIEN—I am pretty sure that is right. Do you need to check it?

Mr Callaghan—What specific aspect? We can confirm whether that is correct.

Senator O'BRIEN—I want to know how that fits with the government's policy of competitive neutrality. How can it be competitive neutrality, when a foreign vessel can have the fuel tax free, but an Australian coastal trade vessel must pay the tax?

Mr Callaghan—Again, I think you are asking questions of government policy. We can confirm whether they are the actual facts.

Senator Minchin—I am happy to take, on notice, on behalf of the government, that question and seek to get you an answer as to the extent to which, if any, there is an apparent or real contribution, but I cannot answer that on the run.

Senator O'BRIEN—I am happy for you to take it on notice. My understanding is that it is the fact. Given that we are talking about Australian-flagged vessels—Australian companies operating vessels on the Australian coast which on some voyages must compete with vessels not paying Australian excise or GST—I just wonder how the government views that situation. Does it endorse it?

Senator Minchin—I do not want to give an answer on the run. We will confirm the facts and I will give you an answer as to our view on whether or not, if those facts are borne out, there is any contradiction with our competitive neutrality approach.

Senator O'BRIEN—And can you find out, if they are the facts, whether the government proposes to take any action to correct the anomaly?

Senator Minchin—Sure.

Senator SHERRY—I want to go to some specific questions about assumptions or claims made in the superannuation plan. Firstly, go to page 3 of the abridged document of 9 May. If we look at the little chart—'current' and then the lump sum treatments that are possible, we see that there are eight there, and I think there has been general comment that lump sums can be taxed in up to eight different ways. Are you looking at the chart, Mr Lonsdale?

Mr Lonsdale—Yes.

Senator SHERRY—If we look at the variable tax treatments there, what is the position of a person who has had superannuation since it was compulsory in 1988, which is six out of 10 Australians who were first brought into the compulsory superannuation system after 1988? Are they all subject to these tax treatments within the lump sum?

Mr Lonsdale—Could I just clarify: when you say 'subject to superannuation', are you talking about under the SG?

Senator SHERRY—Yes.

Mr Lonsdale—So 1992?

Senator SHERRY—Yes; but the three per cent component commenced before 1992.

Mr Lonsdale—Correct.

Senator SHERRY—Do you have an answer to my question?

Mr Lonsdale—I am sorry; do you mind just restating it?

Senator SHERRY—Let us take the group—and it is the majority of Australians; it is about 60 per cent of people—who did not have superannuation prior to the three per cent productivity, which started in 1998, and subsequently that was the three per cent included within the nine per cent SG that was phased in by 1 July 2002. What are the circumstances of those people in respect of the various categories of eight tax treatments?

Mr Lonsdale—It is difficult to say. It is true that superannuation coverage increased significantly post 1992 with the SG, so a large number of those contributions would be post-June 1983 contributions, which are currently taxable.

Senator SHERRY—My question went to when super became compulsory, which was not in 1992; it was in 1998, the first three per cent. Let us take the introduction of compulsory superannuation for employees in 1998 as the start point for when the majority of Australians came into the system. Do you accept that as fact?

Mr Lonsdale—Yes.

Senator SHERRY—Let us just go through. They would not be subject to the pre-July 1983 lump sum treatment for obvious reasons, would they?

Mr Lonsdale—I am advised that they could have been, if they had the same employer before 1983.

Senator SHERRY—Even if they had not been brought into compulsory super?

Mr Lonsdale—Correct.

Senator SHERRY—Can the officer who is briefing you explain how? He obviously has some knowledge of it.

Mr Boneham—The distinctions between the pre- and post-1983 component is determined by eligible service period, not contributions made. Let us say that the person was in employment in 1980—they would have a pre-1983 component.

Senator SHERRY—But if they were new to the superannuation system that was brought in in 1998 as a consequence of the SG and had not been in the system before?

Mr Boneham—If they commenced employment after 1988, they would not have a 1983 component. But if they had not, they would have a pre-1983 component.

Mr Lonsdale—I think what we are saying is that it will depend on the individual circumstances.

Senator SHERRY—So to varying degrees, varying numbers of people are affected. It is not everyone who is currently in the superannuation system who is affected by this lump sum treatment.

Mr Lonsdale—Affected in what way?

Senator SHERRY—By the eight tax treatments in respect of lump sum payment.

Mr Lonsdale—Correct. Some people are affected more than others.

Senator SHERRY—And some people are not affected at all, other than by the exit tax.

Mr Lonsdale—And your example is?

Senator SHERRY—A person who came into the system as a new employee in 1998 has made no undeducted contributions.

Mr Lonsdale—And they would have a post-June 1983—

Senator SHERRY—And they do not have an excessive component.

Mr Lonsdale—They would have a post-June 1983 component, so they would have an ETP component.

Senator SHERRY—Yes, in respect of one of these categories of treatment.

Mr Lonsdale—In that particular example, yes.

Senator SHERRY—Did you examine the numbers of people who have varying degrees of treatment to any degree?

Mr Lonsdale—Is the question: do we know how many people have how many different ETP components?

Senator SHERRY—Yes, to any degree.

Mr Lonsdale—I would have to take advice on that. It was certainly part of the costing exercise to understand which groups of people were subject to which ETP components, because it did go very much to the cost of the plan.

Senator SHERRY—I am not going to ask you for the cost again, because I know I will not get it. Mr Gallagher is here; presumably he assisted in the costings. Is he able to give us any information on this?

Mr Lonsdale—I will check.

Mr Gallagher—The costings that we have done do not look at what people who are currently working have as components. The costings have regard to what is the expected stream of retirement incomes for people over the age of 60 as opposed to the stock of components in the current workforce. Table 5 of *Taxation statistics 2003-04*, in particular table 5B, will give you a breakdown of the different components in eligible termination payments. As Mr Ray has previously told you, both employer ETPs and superannuation ETPs are reported in that table.

Senator SHERRY—Mr Lonsdale has referred to calculating the costing of the components of the plan. Did this make it difficult to cost the components?

Mr Gallagher—Not particularly. The major components are the income streams by age and the eligible termination payments by age where we have the amounts of superannuation separately identified in our unit record tax file. So it is an issue of how we take that file forward in time in order to look at the costing of the components.

Senator SHERRY—When you say ‘take that file forward in time’, is that the three years of the forward estimates?

Mr Gallagher—It is that period, but it is also the fact that, for these purposes, we were working from 2002-03 data and so we had to get it up to 2007-08 before we could take it forward through the forward estimates. We have regard to revenue estimates and age distributions in doing that.

Senator SHERRY—What is the approximate number of people over that forward estimates period? Let us take it from 1 July 2007, which is the start-up date. What is the approximately number of people who you were able to identify would be subject to the exit tax?

Mr Gallagher—I do not have that number on the top of my mind. I would have to take that question on notice.

Senator SHERRY—Do you have any idea of what the number would be? You know how reasonable I am, Mr Gallagher.

Mr Gallagher—I would not want to suggest one number and find that it was wrong. I would not want to mislead the Senate.

Senator SHERRY—There is a figure in the paper that refers to, I think, 100,000 people.

Mr Gallagher—That is an estimated number of people retiring in a single year, so it is a flow number. That is a labour force flow number which is taken from our labour force model; it is not taken from our superannuation model.

Senator SHERRY—So it is not correct to assume that 100,000 people are the people who are not going to pay the exit tax. It would be considerably less.

Mr Gallagher—The categories have overlaps. It is quite possible that people who are taking ETPs may decide to take a sequence of ETPs over a number of years because they get the money in a rollover fund. Those people may have retired in a previous year and still be taking money out, or they may be not in the labour force and taking money out. There are a number of labour force statuses which can be associated with the taking of an eligible termination payment and taking a lump sum out of a superannuation fund.

Senator SHERRY—Were you able to identify, in financial year 2007-08, the approximate average superannuation lump sum accrual, putting aside defined benefit funds in a defined contribution scheme? Were you able to identify what that figure is approximately?

Mr Gallagher—I do not recall the number as a feature of the costing. One of the issues when you are dealing with a microsimulation model of a costing is that your outputs tend to be the costing rather than necessarily all the components of the costing. Table 5 of *Taxation statistics* is some help in that it effectively allows you to calculate the averages for each type

of payment. We have published averages in the past. If you look at RIM conference paper 98/1, you will see there are averages published in that paper.

Senator SHERRY—I am sorry; I do not have that on me.

Mr Gallagher—It is on our website, which is http—

Senator SHERRY—Just before I dash to the website, do you recall the figure approximately?

Mr Gallagher—It varies significantly by age and gender, and that is the distribution that is shown in the publication.

Senator SHERRY—I was going to go into that detail that you obviously have ready to give me, but do you know the average figure?

Mr Gallagher—I think it depends on the components. Another issue is that these numbers are normally published according to the type of component they are, but then there is the issue of how the components are allocated across people. One individual, as we have discussed earlier, may receive many components.

Senator SHERRY—Would it be correct to say that the majority of people in Australia do not have \$130,000 in superannuation?

Mr Gallagher—I think that is the case. Essentially, back in 1987, with the introduction of award superannuation, we had 40 per cent of employees covered with superannuation. The coverage grew from the introduction of award superannuation up until the point where we had—it depends which source you use—sort of 92 to 94 per cent of employees covered. That means that the majority of people in the workforce, some 52 per cent of employees, in actual fact have only had superannuation since 1987. Of course there have been a number of new employees who have entered and do not have a significant period of accumulation. So the average balance in an industry fund—you probably know this better than I do—will not be of the order of \$129,000.

Senator SHERRY—Seven hundred and fifty-one? We will use \$130,000 as the round figure—751 or 754, I cannot remember the precise figure, but it is about \$130,000, isn't it?

Mr Gallagher—Yes. You are talking about the post-1983 ETP taxation thresholds.

Senator SHERRY—Yes, which is the majority of the workforce.

Mr Gallagher—Yes.

Senator SHERRY—What about the number of people who do not pay the exit tax, effectively because it is rebated back to them if they are in a complying annuity or pension? Did you examine that issue?

Mr Gallagher—There will be that issue because there are a number of rebates which are active for people who are still working and taking their pension. They may well be entitled to the mature age workers tax offset, so there will be a variety of rebates in operation.

Senator SHERRY—I want to get to the exit tax rebate—the 15 per cent that is rebated. I know there are other rebates.

Mr Gallagher—Yes, but I am saying the effective use of the rebate. This will have been taken into account in the costings.

Senator SHERRY—That is what I am asking. It is why I am asking, actually, because I just wanted to see.

Mr Gallagher—Of course the rebate cannot offset the Medicare levy, and that will have been taken into account in the costing.

Senator SHERRY—I am talking about the 15 per cent exit tax which is rebated back to a group of people. There are a group of people who effectively do not pay it as a consequence of the measure.

Mr Gallagher—Yes, there is also the senior Australians tax offset. So there is a combination of rebates which may see people not paying gross tax. They may still be eligible for the Medicare levy.

Senator SHERRY—I am just focusing on the exit tax that has been abolished. There is a group of people who have it rebated back to them, isn't there?

Mr Gallagher—Effectively, yes. When the details are done on assessment in their personal taxation return their entire taxable income will be looked at.

Senator SHERRY—How will they be affected by the abolition of the exit tax? Would there just be no rebate—they are not going to pay it, so there is no rebate back to them presumably?

Mr Gallagher—There will be no need for a rebate where it is no longer taxable income.

Mr Lonsdale—For a person over 60.

Senator SHERRY—Yes, I understand that. But the senior Australians tax offset does not come in at age 60, does it?

Mr Gallagher—It comes in at age pension age, which is currently 65 for males and probably 63 for women..

Senator SHERRY—So for a group of people who do get to \$130,000—that group of people, whatever the number is, who have it paid back to them as a rebate—the abolition of the exit tax is a simplification, but in terms of a money outcome it has no impact, does it? I am talking about the abolition of the exit tax by itself.

Mr Gallagher—If we are talking about lump sums as opposed to a pension—

Senator SHERRY—Yes.

Mr Gallagher—the rebate for the lump sums is paid when they would have a taxation liability. To have a taxation liability those people would be over \$129,000. If we are talking about superannuation pension or annuity, which is rebated, in that case where they have taken a superannuation pension or annuity, if that were sufficient to ensure perhaps with some imputation credits that they did not pay tax, it would still be the case that they do not have a tax liability. But those people, typically, if they have annuitised will have—well, there is an issue about what amounts you would annuitise—or would probably have a larger payout in order to annuitise in order to make it worthwhile to annuitise.

Senator SHERRY—The issue I am getting at is that, with the abolition of the exit tax, there is a simplification for this group of people who have annuitised, but the net outcome is that they do not gain from it. They may gain financially from other aspects of the plan.

Mr Gallagher—But there will be people who have significant annuities who do gain.

Senator SHERRY—Yes, I accept that. You might give me the numbers, then—what do you define as a ‘significant’ annuity?

Mr Gallagher—Significant for the costing would be one that leads to a cost to revenue.

Senator SHERRY—Which would be?

Mr Gallagher—I do not have that number readily available.

Senator SHERRY—You say ‘significant’. Therefore it is useful to know what you mean by ‘significant’. What is the approximate number of people who receive a rebate of the 15 per cent contributions tax?

Mr Gallagher—Those numbers are shown in the taxed concessionally component in table 5 of *Taxation statistics*. I can get that number. I would have the number for 2002-03.

Senator SHERRY—Are we talking about people in the hundreds of thousands or millions?

Mr Gallagher—Not millions, no.

Senator SHERRY—Hundreds of thousands?

Mr Gallagher—Generally ETPs depend on people who are retiring in a year, except for those who have decided to take their lump sums in a number of portions. So it is more the flow than the stock.

Senator SHERRY—So all of the factors that we have talked about—and there are others—are factors that you would have been taking into account when calculating the loss to revenue of the abolition of the exit tax?

Mr Gallagher—Yes.

Senator SHERRY—So you have calculated a figure of the cost to revenue and the benefit to taxpayers of the abolition of the exit tax as a component within this plan?

Mr Gallagher—By ‘exit tax’ I take it you mean the tax on superannuation ETPs?

Senator SHERRY—Correct.

Mr Gallagher—Yes.

Senator SHERRY—You have calculated that figure?

Mr Gallagher—Yes, we have an estimate.

Senator SHERRY—Turning to the income tax free treatment of lump sums or income streams at age 60, you have calculated or have assisted in calculating, I assume—because there would have been other people involved, but knowing of your expertise I am that sure you would have been a mainstay of the costings—the loss to revenue from income tax of proposed changes to the income tax free treatment at 60?

Mr Gallagher—Yes. The change to ETPs is also a change to personal income tax. The superannuation funds withhold on behalf of the individual, but the wash-up is done on the individual's tax returns.

Senator SHERRY—I just want to clarify that. The exit tax itself, when it is paid—which tax revenue area is that included in at the moment?

Mr Gallagher—The withholding, I would imagine, is counted in ITW. Further consequences—

Senator SHERRY—Sorry, ITW for the purpose of—

Mr Gallagher—Income tax withholding, but it is also the case that some of the income will probably be collected on assessment with other individuals.

Senator SHERRY—None of it would be collected from the fund and classified as superannuation?

Mr Gallagher—It is not income of the fund.

Senator SHERRY—So it is not within the budget revenue figure for the general category of superannuation fund tax?

Mr Gallagher—Not on my understanding, no.

Senator SHERRY—That is not what I was told at a previous estimates. I am not suggesting that anyone misled me, but I will come back to that.

Mr Gallagher—We have discussed contributions and earnings at a number of estimates.

Senator SHERRY—Yes, we have. The application of exit tax via rebate is seen, isn't it, as an incentive to convert at least part of a lump sum, if you have sufficient, into an annuity pension?

Mr Gallagher—The 15 per cent rebate has been described as an incentive. It depends on how much you have.

Senator SHERRY—For some people it is an incentive to do that.

Mr Gallagher—If you are under your post-1983 threshold, you would have to—

Senator SHERRY—I have seen industry people promote it on that basis—annuitised pension, therefore rebated 15 per cent of the exit tax. It is promoted on that basis, isn't it, by some?

Mr Gallagher—Yes.

Senator SHERRY—Perhaps a question for you, Mr Lonsdale. In removing the incentive for some people to convert to a pension annuity—and whatever the final rules are in terms of the new pension annuity product, and there are no final rules yet; I accept that—what is the incentive to annuitise?

Mr Lonsdale—We think that the plan contains significant incentives for people to annuitise or take out pensions. There are probably three key ones. The first one is that the earnings tax exemption on capital that underpins a pension will remain under the plan. It is a very significant incentive to take out a pension. The second is that, under the plan, pension

streams for those people aged over 60 will be tax free and, because of that, their other income from other sources one would expect to be taxed at lower rates of tax.

Senator MURRAY—At a lower marginal rate.

Mr Lonsdale—Correct.

Senator SHERRY—No tax.

Mr Lonsdale—The superannuation pension would be no tax. But if they had other income—say, other work income perhaps—that would be taxed at a lower rate of tax than would otherwise be the case.

Senator SHERRY—In this case it is zero, isn't it?

Mr Callaghan—No, there is no evaluation.

Senator SHERRY—That is what I am referring to. Their superannuation income at age 60 is zero.

Mr Lonsdale—The point I am making is that their superannuation pension income under the plan would have no tax applied. But if they had other income outside the superannuation system—for example, from working—that would be taxed at a lower rate than would otherwise be the case.

Senator SHERRY—Other income could tomorrow from dividends or rentals or whatever?

Mr Lonsdale—Correct. The third significant incentive is that, by simplifying the system by removing complying and non-complying asset test exemptions, non-asset test exemptions—the myriad of regulatory issues that surround pensions—and replacing them with one streamlined pension system, it would make it easier for people to understand what a pension is about. It follows from that that, if people understand pensions better, they are more likely to take one out.

Senator SHERRY—If it is tax free, they certainly will. Isn't it also true that a lump sum will be income tax free?

Mr Lonsdale—Correct. For those people over the age of 60 who take a lump sum, that will also be tax free.

Senator SHERRY—Let us take a person who at age 60, by way of example, puts \$200,000 into the new pension product. My understanding is that they can then at age 60 spend any of that \$200,000 over what period of time they want income tax free.

Mr Lonsdale—Correct.

Senator SHERRY—Let us take the example of a person on a \$200,000 lump sum, which is in the pension product. They are aged 60. They could spend it tax free over five years up to age 65, couldn't they.

Mr Lonsdale—Correct.

Senator SHERRY—Then they would still be eligible for the age pension if they had no other assets or income, depending on the interaction of assets and incomes test?

Mr Gallagher—Depending on the interaction of those tests.

Senator SHERRY—But they could do that, couldn't they?

Mr Gallagher—You are asking whether they could spend their \$200,000—

Senator SHERRY—Yes, tax free.

Mr Gallagher—and go to the pension?

Senator SHERRY—Yes. There is nothing to stop them doing that.

Mr Lonsdale—That is correct, as is the case under the current system as well.

Senator SHERRY—Yes, if they do not annuitise?

Mr Lonsdale—That is right. People can spend their lump sums and move to the pension.

Senator SHERRY—But they cannot do that if they are in a complying annuity or income stream, because there are minimum and maximum draw down factors in the existing system?

Mr Lonsdale—Where they are non-commutable, that is correct.

Senator SHERRY—I am interested in the more detailed discussion document where you are proposing minimum draw-down factors by way of an example. I am not suggesting that those minimum factors are locked in yet. That is correct, isn't it?

Mr Lonsdale—That is correct. We would have a standard definition of what a pension is over a life expectancy and a series of minimum draw downs, not maximum draw downs.

Senator SHERRY—In fact, no maximum at all.

Mr Lonsdale—That is correct.

Senator SHERRY—Which allows a person to spend it all in one year income tax free if they so wish; that is their decision.

Mr Lonsdale—That would be their choice. Could I add one caveat to that. The data that we have examined, particularly from FaCS, and I am referring to published data, indicates that that situation you outlined is very rare. It is more likely to be the case that the majority of people after receiving their retirement benefit draw down on that benefit very slowly. I think the FaCS data indicated that for nearly three-quarters of people who received a retirement benefit, about 70 per cent of that benefit was still intact after four years of draw down.

Mr Gallagher—The ABS data on this issue was examined in the RIM conference paper 96/6, where we looked at the draw-down behaviour of people who had sufficient superannuation benefit to affect their pension. To have enough to affect your pension then, essentially it was about \$80,000 if you were a couple, under the three areas of deeming rules that applied. We found that, for something like 95 per cent of people, the major use of their lump sum was in actual fact investments or paying off debt; it was not used for straight-out consumption purposes. So the FaCS data and the ABS data from their retirement survey complement each other in this respect.

Senator SHERRY—I think it is a reasonable conclusion that over time superannuation balances will grow because of the phase-in impact of the SG. Do you agree that that is a reasonable assumption?

Mr Lonsdale—I agree.

Senator SHERRY—Have you examined what the possible behaviour or change would be as a consequence of growing superannuation balances in this area?

Mr Lonsdale—Behavioural in the sense of whether people take lump sums or pensions, or whether people use their lump sums for consumption?

Senator SHERRY—The consequence of the package is that you can spend any or all you like income tax free at any time you like, subject to the minimum draw-down factors, whatever they may be. Have you taken into account the growing superannuation savings of individuals and what the behavioural change may be? Has there been any work done on that?

Mr Gallagher—The work underlying the cameos—because we needed to do a pre- and post-comparison which was fair—assumes allocated pension minimum withdrawals, both before and after, for the purposes of making a comparison of the extent to which people are financially better off. So, in appendix A of the document, that is the assumption underlying the tables.

Senator SHERRY—Are the minimum withdrawal factors that are published as the proposal—because they are not finalised yet—the withdrawal factors over time that are applied?

Mr Gallagher—No. I am saying that, because we needed to do current policy and new policy—and allocated pensions are by far the most popular income stream products—we have used the current minimum factors for allocated pensions. We have not varied that for the purposes of making comparisons, because we could have been misleading—

Senator SHERRY—I want to be clear on this because I do not think we are actually disagreeing.

Mr Gallagher—No, we are not.

Senator SHERRY—You have existing allocated pension factors. Have you used that draw-down figure for the purposes of modelling?

Mr Gallagher—Yes.

Senator SHERRY—So you have not assumed any greater draw-down figures for the purposes of the modelling coverage?

Mr Gallagher—Correct.

Senator SHERRY—Is the removal of income tax payable as distinct from the other issues associated with the lump sum, which we touched on earlier, a simplification in itself?

Mr Lonsdale—This is for pension streams?

Senator SHERRY—Yes, where you pay no income tax.

Mr Lonsdale—We believe it is.

Senator SHERRY—If we followed that logic, why wouldn't we abolish income tax for everyone? It would be a simpler system, wouldn't it, for everyone?

Mr Lonsdale—Are you asking me for my view on a policy matter?

Senator SHERRY—Perhaps the minister could respond. If the policy rationale is that we are simplifying the tax treatment for people over the age of 60, and at least one of the arguments is that they pay no income tax because it is simple, why don't we abolish income tax for everyone under 60, Senator Minchin? Why are you laughing?

Senator Minchin—I have often dreamed of that, Senator Sherry, but then I am confronted every day with demands upon the Treasury and the finance department for spending in a whole range of areas that require some source of revenue. I think most nations have come to the view that income tax is probably the best source of that revenue to meet our needs, to defend the country and provide welfare and so on.

Senator SHERRY—But you have come to the conclusion that people over the age of 60, at least with respect to their superannuation income, do not need to pay income tax. That is the policy conclusion you have come to.

Senator Minchin—Your party supports this, as I understand it. If you are now telling us that we can go further, I will be interested in—

Senator SHERRY—When we get the costings, Senator Minchin!

Senator Minchin—I thought you supported this plan.

Senator SHERRY—We are being positive and generally supportive—

Senator Minchin—You said you think we should now abolish all income tax.

Senator SHERRY—but we want the costings.

CHAIR—I think there is too much badinage!

Senator SHERRY—Yes, back to my question.

CHAIR—Senator Minchin has not been a pure Robert Nozick libertarian since he was an undergraduate!

Senator SHERRY—Back to my question, Senator Minchin.

Senator Minchin—It is a rather fatuous question, really.

Senator SHERRY—No, it is not.

Senator Minchin—Come on. As you know, as well as anyone, superannuation in this country, as a result of what your predecessors in the Labor Party did, is taxed thrice. That has been an issue of concern to a number of us, and probably you, and the government is—

Senator SHERRY—Certainly for you too.

Senator Minchin—Yes, I have been quite honest and open about my concern about that. That is an issue we have all wrestled with. It was a function effectively of Mr Keating bringing forward the 15 per cent so that it hit contributions rather than being at what I think was originally 30 per cent on earnings. Was that it? Where was the 30 per cent?

Senator SHERRY—Thirty per cent exit; 15 per cent was brought forward.

Senator Minchin—Exit, yes. So you had a three-stage tax. Now, we know why Mr Keating did it—

Senator SHERRY—Plus income tax, whatever their age.

Senator Minchin—Yes. Having examined this question, as you know, I publicly floated removing one element of that three-stage tax. The government has on balance decided to terminate the end tax, and I think that has been extremely well received. It remains the case that superannuation is taxed twice and will continue to be taxed twice. But, in recognition of the fact that superannuation is taxed when it goes in and while it is earning funds, our decision is to therefore not tax it coming out. I think that has been widely well received.

Senator SHERRY—I accept that. My question went to the issue—you have two sets of tax removal. You have the removal of the components within the lump sum and the exit tax. That is one set. And now we have the proposal to remove income tax from revenue taken from the lump sum, which is a separate but obviously related proposal, for people at the age of 60. That is the effective cut-in date, isn't it?

Senator Minchin—Yes.

Senator SHERRY—One of the arguments is that this is part of simplification. We have simplified income tax, because no-one over the age of 60 is going to pay it from their super!

Senator Minchin—Not from their superannuation account.

Senator SHERRY—So why don't we get rid of income tax for people below age 60 and simplify it for them as well?

Senator Minchin—That would be very simple, but, as you know, we would then have to abolish the defence department, the family and community services department and a few other things as well, so I do not think we are going down that path. But we have decided on balance that, given the genuine public policy concern about the way superannuation has been taxed since Mr Keating's changes to the system and given that superannuation will continue to be taxed on both contributions and earnings, therefore pension income streams will not be taxed after 60. This has the advantage of providing some incentive to stay in the workforce until you are 60, which is a good thing. It provides some incentive to invest in superannuation and to increase national savings thereby. And, as I recall, your party has welcomed it. It has been very widely welcomed as a very genuine and important reform.

Senator SHERRY—And we would like to see the costings on it.

Senator Minchin—You have the costings. It will cost \$6.2 billion all up.

Senator SHERRY—No, we do not. I am asking about this measure in particular. Let me ask about this measure in particular. Have the long-term costs—that is, beyond the forward estimates period—of the removal of income tax from a superannuation income stream or lump sum at age 60 been modelled?

Mr Callaghan—That was the thrust of Senator Murray's question. As we said, we have done general work on these long-term implications, but we do not provide or have not provided long-term costings of tax measures—'long-term' meaning over the 30 years that Senator Murray was talking about. In the *Intergenerational report*, looking at the revenue side, as we said, the assumption was that revenue would stay as a constant proportion of GDP. It is the same question to say, if we go—

Senator SHERRY—Before you go on: I heard that, but I am asking this specifically with respect to the loss to revenue—income tax revenue in this case—of this measure, which is the

abolition of income tax. I know there are other components to it. You say some work has been done. What do you mean exactly?

Mr Callaghan—Looking at the matters you referred to already and some of the potential behavioural responses. But can I come back to your specific question—

Senator SHERRY—It is not the behaviour; it is the loss to revenue going forward.

Mr Callaghan—You are saying the loss to revenue. For everything you have to have a benchmark, so, if you are going to look at the long-term costs, the question I would have to ask you is: what is the benchmark? When we do the costing over the forward estimates, we have a benchmark for what is in the forward estimates based on projections of what is going to happen to the economy. Coming back, that is what I was saying. In terms of any revenue measure, when you are looking at it long term—over an *Intergenerational report* basis, 30 years—you have to have some benchmarks.

The benchmark that has been used in the *Intergenerational report* is to assume that revenue is constant as a proportion of GDP. It is the same as you do not do a long-run costing of a particular change in an income tax rate or a particular change in an income tax threshold, because, when you look at the wash, the drivers that are likely to be behind the revenue that you are receiving are the drivers that are going to be behind your GDP. You assume, and this has been the accepted approach, that your revenue is constant to GDP. You do not do a long-run costing of a particular revenue measure against a benchmark that includes assumptions of what is happening with all the other components of tax.

Senator SHERRY—Mr Gallagher, you may be aware of these figures: in the context of the ageing population, as at 1 July 2004—these figures are from the ABS—there are approximately four million Australians over the age of 60 out of a total population of 20.5 million, or approximately 19 per cent.

Mr Gallagher—Yes, that is about right. There are about 3.9 million people not in the labour force over age 60. By the year 2040, the ABS projects there will be eight million Australians over 60 out of an approximate total population of 27 million—or 37 per cent approximately. It is not just the raw number; it is the percentage increase of Australians over the age of 60. Does that sound about right?

Mr Gallagher—The numbers I remember are the numbers that are in the *Intergenerational report* of people over the age of 65, and that went from approximately 12 per cent to 24.6 per cent.

Senator SHERRY—So these figures of people over 60 sound about right.

Mr Gallagher—Yes. It depends very much on your migration assumption, because after 40 years the people that came in in their 20s are now in their 60s.

Senator SHERRY—So we will have, at age 60, an increasing number of people—both as a total number and as a percentage of the population—not paying income tax from their superannuation income. It seems to me to be a reasonable conclusion.

Mr Gallagher—The issue is how many of them would have paid tax under what tax regime. Mr Callaghan has described the difficulties in talking about the tax regime in a long-term and distant future, including setting inappropriate benchmarks.

Senator SHERRY—Are you saying, Mr Gallagher, it is very difficult to cost this measure over the long term?

Mr Gallagher—I think there are many uncertainties associated with costing this measure in the long term. There are many uncertainties in setting a baseline and there are many uncertainties associated with looking at the likely disposition of income and assets into the future.

Senator SHERRY—But we are faced with the situation where we have a greater raw number and percentage of the population over 60. That is fact. We know it is fact that there are increasing superannuation balances, because of the phase-in of the SG. Whatever the behavioural impact may be of increasing saving, we know that is going to happen. What other issues would we need to take into account that would not lead a reasonable person to conclude that there would be an increasing loss to income tax revenue as a result of this change? I am not going to the question of whether it is sustainable not, but it seems to me pretty obvious there will be an increase in loss to revenue.

Mr Gallagher—There will also be issues associated with higher participation at older ages. The package may well encourage participation.

Senator SHERRY—If there is increased participation in the work force, that would offset an increase in costs. We do not know by how much, but that can offset it.

Mr Gallagher—Yes.

Senator SHERRY—And these factors—I know there are other issues as well—will all be inputted into the intergenerational model before its publication in May 2007?

Mr Gallagher—Mr Callaghan has already indicated that the impact of the package, which will presumably be a measure by then, if it was May 2007, would be taken into account in the *IGR* projections of the age pension amounts. That would be both age pension and service pension, because of the change in the assets test. And there are two changes in the assets test.

Senator SHERRY—Yes. I understand that. So it will be taken into account with respect to age pension costs, but not income tax collection over the long term, which is not published, is it?

Mr Gallagher—No.

Senator SHERRY—It is assumed as a constant.

Mr Gallagher—It is assumed as a constant of revenue. The assumption here is that it will continue to be assumed as a constant, that the approach taken in *IGR 1* will be the approach in *IGR 2*.

Senator SHERRY—So we are not going to know, over the long term, through the intergenerational model, what the modelled loss to income tax revenue will be as a consequence of this measure, because it is assumed as a constant.

Mr Gallagher—On current plans for the *Intergenerational report*, it would not be shown because we are doing it the same way as we did the last one.

Senator SHERRY—I will switch back to you, Minister. Don't you think it would be reasonable, if we are to remove income tax from a group of people—in this case, people over

the age of 60 receiving their money through super—to model over the long term the loss to income tax revenue as a consequence of making a significant and growing number of people income tax free? Don't you think it would be reasonable to include that in a model?

Senator Minchin—I am not going to get into a debate here about what should or should not be in particular models. The *IGR* is a pretty sophisticated look at revenue and expenditure forecasts or projections for the Commonwealth government over a long period of time. I do not think the last *IGR* has been seriously questioned by anyone of any repute. It is obviously a consolidated assessment of the impact of changing demographics on the government budget, and I am sure the next one will be as authoritative as the last one.

Senator SHERRY—Yes, but, given what has been outlined to us, we have a measure where there will be a growing number of people treated as income tax free from their super at age 60, increasing quantum of super savings and a loss to income tax revenue—that is clear—from that measure, whatever the total net loss or gain is, and we do not know that. And we are not going to know what the long-term cost impact is going to be on our revenue base.

Mr Callaghan—What we talked about was the approach to doing any tax measure, and this applies to income tax. To use an analogy: if we went back to 1975, when there was a top marginal tax rate of 69 per cent, cutting in at \$40,000, and a very small proportion of the population were paying that \$40,000 rate. Then we could say, 'We need to do projections,' assuming that the number of people would be growing and would be coming into that \$40,000 bracket. If we looked at the total cost of that going out, we would come with a very large cost to revenue if we assumed that nothing else, no other components of tax, were changing in those long-term projections. Do you get a realistic assessment? Do you get a realistic baseline to be able to measure the cost to revenue? As I said, it goes back to the fact that there are many other drivers that influence the total revenue take that we can get.

Over the longer term, the best assumption looking at that which has been used in the past is not to say, 'Well, we're going to focus on just one tax component and assume that all others stay constant and then try and assess the impact of that over the longer term and draw some conclusions out of that.' The best is to look at it and say, 'What are going to be the various sources, regardless of where they come from, in terms of influencing the total revenue—that is, what drives the growth in the economy?' It is the same difficulty. You can do whatever you like, but really we are asking, 'What is meaningful to be able to make some assumptions on this?' Across all the various revenue measures, tax measures, there has not been an attempt to look at what this long-term cost because of these factors is. What is the realistic baseline? What is the realistic benchmark that you are looking at?

Senator SHERRY—I understand your explanation. I understand the way in which it was applied last time and will be applied next time. But my point was—in the minister's own words and the government's own words—the major, sweeping changes to superannuation in Australia, including the introduction of the income tax-free treatment of superannuation for people over the age of 60, a not insignificant change. I do not suggest that it is insignificant; it is certainly not. It is a significant change. I am just a little taken aback that there will not be modelling of the impact of this on income collections over time, given the circumstances we have discussed earlier. But apparently that is what will happen. There will be no modelling of it.

Mr Callaghan—To start with, I think the most important thing is to go down even the elements that you have been looking at: what may be the behavioural responses that come from this? In any modelling, the results are going to be dependent on the assumptions that you put in. As you indicated and as the minister had indicated, this is looking at some significant behavioural changes that may take place. It is a significant package that has a number of components to it. It is not really the case that we would have the available data to draw on to say, ‘This is giving you a very good guide about what will be the likely behavioural responses to this.’ So when we say—and I go back to the original answer to Senator Murray—that we have been doing some general work in this area, it is in the nature of the elements that you have been commenting on: what is likely to be the impact on participation? What is likely to be the impact on saving? What are likely to be some of the efficiency gains from a substantial reduction in complexity?

As I say, there are many components of it. It is a very large package, in the sense of being very different. What might be the ramifications of that? The first thing that is always necessary is to try and have an understanding of what those behavioural assumptions may be, rather than to essentially jump into them and try and say, ‘This is going to be the outcome, and this is going to be the cost.’ Any point estimate cost is just going to be as good as whatever assumptions go into it.

Senator SHERRY—Yes, of course. And the assumptions you make change the assumptions that are fed into the model.

Mr Callaghan—That is the element we have been thinking about.

Senator SHERRY—I am glad you are thinking about it. You might care to outline some of the thinking to me. On the claimed increase in saving that results from these changes: has it been modelled, and is there an increase in saving as a consequence?

Mr Callaghan—There is a difference to the work we have done in looking at what is in the forward estimates. That is the element we can focus on. Within that, I believe—and Mr Gallagher can elaborate—that, yes, in doing that, assumptions are made of likely increased flow into superannuation and likely changes in the composition of individual assets. I do not believe that we, particularly over the short period, have drawn any conclusions that there is going to be an overall increase in private savings within the period of the forward estimates.

Senator SHERRY—Just coming back to the flow, it seems to me logical—and Mr Gallagher may comment—that there would be a flow, within the parameters of whatever the maximum contribution limits are to be, of non-super assets into super because of the tax preferment. That seems to me to be, rationally, what a lot of people who are in that position will do.

Mr Gallagher—A number of analysts have commented on the likelihood that there will be that flow, for people over the age of 60.

Senator SHERRY—Over 60, and for people coming up to 60, transferring assets in, because of the income tax-free treatment. Would you agree with that observation, Mr Gallagher?

Mr Gallagher—I think that obviously if people have money outside of superannuation that is being subject to taxation and there is a mechanism for getting it in, within the contribution limits that have been set by the package, then people will look at how they could get it inside their superannuation.

Mr Lonsdale—That is an important caveat. It is a key reason why we have contribution limits in the package.

Senator SHERRY—I am going to get to the contribution limits issue shortly, but I accept the caveat—within the contribution limits. It is logical that people would do that. So it is a switching effect; there would at least be some behaviour of switching.

Mr Gallagher—There will also be some private saving increase for the retired, because the amount of money which they will get in their superannuation payouts will be higher because there will be no tax withheld. So the money that would normally have come back to public saving—

Senator SHERRY—Yes. That is the tax treatment.

Mr Gallagher—So there will be an effect there, and there will be a change in portfolio composition.

Senator SHERRY—What about the long-term behavioural impact? Let us take a person under 50, because 50 is the change where the yearly limit, for example, is increased to \$50,000; I think that is the proposal. That is an increase for people under the age of 50. What is the behavioural impact, in terms of increased saving from people under the age of 50, of increasing the yearly savings limit to \$50,000?

Mr Gallagher—I am not sure that we have fully quantified the extent to which that would make a change, because there is an extent to which people are already salary sacrificing as much as they can afford, and that would depend on their own budget constraints in terms of their ability to be getting more.

Senator SHERRY—So, effectively, the limit is not so much the \$50,000—or whatever the existing age limits are; I think I have them here somewhere—it is effectively discretionary income. How much they have got to put in is a limit, overwhelmingly, on what people can save in super.

Mr Gallagher—Yes. We think that there would be some constraints.

Mr Lonsdale—There will be constraints, Senator. People have other consumption needs. But, as part of the proposal, the limits have been significantly increased. For people under 35, the deductible limit goes from around \$15,000 to \$50,000.

Senator SHERRY—Yes, but that in itself does not mean that people under 35 will increase super contributions—including SG, which I know is included—from that \$15,000 up to \$50,000, does it?

Mr Gallagher—Some may. There would be a number of sportsmen and others who would see the advantage in doing that, and they will be able to do so.

Mr Lonsdale—They have the opportunity to do it.

Senator SHERRY—I love that word ‘opportunity’. It is ‘opportunity’, or ‘choice’.

Mr Callaghan—But some may put in more. The whole idea of trying to encourage people to make provision for their own retirement is to entice them to save. They would lock it away into superannuation if they could see the benefits of it.

Senator SHERRY—But there is no analysis of what the behavioural pattern will be for those under-50s as a consequence of these changes to date?

Mr Gallagher—I do not know that it is separated out. There is an allowance in the package for increased contributions to superannuants. It was in the forward estimates costing. We have looked at a number of behavioural issues—the first-round effects of the behaviour. By ‘first round’ I mean we look at what will happen to the people who are directly impacted by the policy change, in terms of the decisions that they can make about their own behaviour.

Senator MURRAY—And, when you are looking at these behavioural issues, are you looking not just at individual retirees but also at families and their behavioural responses?

Mr Gallagher—Our retirement models are largely on an individual basis and we have done a lot on individual cases. It is the case that a number of issues, such as superannuation splitting, which we have examined in the past on a family basis, would be less attractive on the basis of the package. So there will be an interaction between the family aspects and the individual aspects.

Senator MURRAY—The point I made to Mr Callaghan earlier was that this new package opens up opportunities for larger numbers of people, particularly within families, to share the super benefits. Dependants and nondependants can in fact get a referred benefit if the retiree structures their affairs accordingly. That is why I ask: are you are going to be looking at the broader family in terms of behavioural modelling?

Mr Gallagher—The existence of arrangements which allow families to have greater access to retirement benefits is indirectly factored in. They are already features of the super system. As Mr Lonsdale has already said, it is already the case that superannuation can be passed to dependants and nondependants.

Senator MURRAY—Yes, but more opportunities are now there—more not less.

Mr Gallagher—There are more. But certainly post-1983 and under \$129,000 families can do what they will with that money because there is no tax being imposed on it. Once it becomes after-tax money and the other undeducted contributions are returned there is no particular limit, if there was a family business that it needed to be applied to. So there is an existing situation in which superannuation can be used to achieve family objectives rather than individual objectives.

Senator SHERRY—You gave an answer a little earlier about the behavioural impact on saving. What was the assumption behind that?

Mr Gallagher—I cannot recall the exact assumption; I just know that we have taken it into account.

Senator SHERRY—Have you taken it into account because that would presumably divert some moneys from income tax to superannuation, which is taxed at a concessional rate, and therefore, for example, the contributions tax category would go up?

Mr Gallagher—That is right.

Senator SHERRY—You were going to continue. Go on—you are always very informative.

Mr Gallagher—Yes.

Senator MURRAY—Famously so, I remember.

Senator SHERRY—Not on this occasion. I am about to see how informative you are. I hate to remind the minister of this, but he gave a speech calling for the abolition of the contributions tax earlier in the year, which I note has not eventuated.

Senator Minchin—It was a fine speech.

Senator SHERRY—The minister gave a figure of \$3.3 billion. I know where he got that from. You gave evidence to the House of Representatives committee inquiry and were actually asked about this. You made some remarks about you believing—

Mr Gallagher—I think I said it was ‘appreciably more’.

Senator SHERRY—‘Appreciably more’—that is right. How appreciably more?

Mr Gallagher—As we have discussed previously, the numbers on contributions tax are not published separately. Both contributions and earnings are income of superannuation funds. The total taxation of superannuation funds is shown in the budget papers. But in addition to superannuation funds you have got to consider the statutory funds of life insurance companies, which are collected under the company tax head of revenue. I am not aware of anywhere where those numbers have been separately identified, except to the extent they underlie the TESS estimates.

Senator SHERRY—So you have not been able to identify a figure, Mr Gallagher?

Mr Gallagher—I have not been able to identify a published figure which would help you.

Senator SHERRY—That is not what I asked. That is not what you were alluding to at the House of Representatives committee. Have you identified a figure for the contributions tax? I am not talking about published figures. Have you calculated one?

Mr Gallagher—We need to have a working estimate of contributions tax to assess proposals, yes.

Senator SHERRY—Obviously in terms of the previous discussion we had, you would need to have that. What is that figure, Mr Gallagher?

Mr Gallagher—I will take the question on notice.

Senator SHERRY—You will not give me an answer. Sorry, it is not your call, anyway; it is the minister’s call. You use the term ‘appreciably higher’ in response to whoever asked the question in the House of Representatives committee. I was keeping an eye on the evidence you were giving there, Mr Gallagher.

Mr Gallagher—It is a worry. I had hoped you would have had other things to do.

Senator SHERRY—In the context of general costing approaches, what is the range of ‘appreciable’?

Mr Gallagher—I think this may be an idiosyncratic term. I do not know that I would want to—

Senator SHERRY—You are not idiosyncratic; you are highly knowledgeable, with a good grasp of figures and detail. So, whether it is idiosyncratic or not, the definition of ‘appreciable’—is it 10 per cent? 20 per cent? 30 per cent?

Mr Gallagher—I think these are the numbers that Dr Emerson tried to get a response on, and I do not recall responding at that stage, either.

Senator SHERRY—But you came tantalisingly close.

Mr Gallagher—Well, you may have been tantalised, Senator Sherry—

Senator SHERRY—I will be tantalised even more when I get the figure.

Senator Minchin—I think you could be waiting for a while, Senator Sherry.

Senator MURRAY—Be beguiling—go on.

Senator SHERRY—So the minister obviously got it wrong.

Mr Gallagher—If it is more than the 3.3, the point is that, obviously, from the costing of the package, the contributions tax measure would cost more than the package over the forward estimates period, in terms of comparisons. The comparison is the pertinent one to your current inquiries.

Senator SHERRY—Yes. But as far as you know—and I know we have discussed this before—it is the source of the contributions tax from the insurance sector that is, you think, the major component that is not published; that we cannot get? Well, you can make an estimate.

Mr Gallagher—There are also important issues with where you apply the deductions and which component you apply the deductions to, and those can make a very significant difference. If you look at tax stats on superannuation funds, you can see that the deduction amounts are considerable. And whether you allocate them against earnings or contributions makes a very substantial difference to the number that you report.

Senator SHERRY—There have been a number of issues raised with me on the issue of the proposed new limits on contributions to superannuation. I want to deal with one issue, which we have already touched on, and that is the undeducted contribution. On the sale of a small business, there is a \$500,000 capital gains tax exemption. That is correct, isn’t it? And that will be allowed, whatever the new rules on contribution limits.

Mr Lonsdale—It is an exemption to the cap, and it refers to the CGT-exempt component from the sale of small business.

Senator SHERRY—So, whatever the other caps, that cap will be exempt?

Mr Lonsdale—In addition, yes.

Senator SHERRY—In addition to?

Mr Lonsdale—A person would be allowed \$150,000 of an undeducted contribution and, in addition to that, if there was a CGT-exempt component from the sale of the small business in a year, that would be in addition to the \$150,000.

Senator SHERRY—So it is \$650,000 if, in fact, the \$150,000 per year continues, as is proposed?

Mr Lonsdale—For your particular example.

Senator SHERRY—What about a person who is part-way through a transaction on budget night? I have had a lot of inquiries about this. Let us take an individual who has sold an asset—a person who had sold an asset, and had not yet paid the money into a superannuation fund. My understanding is that the application of the undeducted contribution limit applies from budget night. That is what is stated in the budget document, isn't it? That is what is proposed.

Mr Lonsdale—Correct.

Senator SHERRY—What about a person who has sold an asset and is in fact over the limit? What do they do with it? I have had this raised with me practically.

Mr Lonsdale—This issue has come up. We are aware of it. The example is someone who has indicated an intention to make a deposit into their super fund whether they have sold an asset or not. We are aware of those issues. They are issues that we think go to the transition that the government will be considering as part of the consultation process.

Senator SHERRY—Sure. But let us take the category of people who are part way through a transaction—who have either sold assets or are proposing to sell an asset—and had not yet placed the moneys as an undeducted contribution amount into a super fund. What are they to do in the meantime while the rules are finalised?

Mr Lonsdale—I am not able to give financial advice to those people.

Senator SHERRY—I am not suggesting you are or should.

Mr Lonsdale—I thought what you were asking was: what are those people who are intending to make a deposit into a super fund meant to do if they have sold an asset or are part way through a transaction?

Senator SHERRY—Yes, I am asking that.

Mr Lonsdale—What I can outline is what has been outlined in the detailed plan, and that is that an undeducted cap of \$150,000 per year will apply from budget night. If there are transitional issues then they are issues that the government will be consulting on.

Senator SHERRY—But they do not know yet what the transitional rule will be, do they, because it has not been finalised?

Mr Lonsdale—The rule as stated in the plan is that there is a \$150,000 undeducted cap.

Senator SHERRY—I accept that, but it may change, mightn't it, because there may be transitional rules?

Mr Lonsdale—The Treasurer has said that this is a plan and it is open for consultation. There might be people who raise special transitional issues. To those the government would be considering its response.

Senator SHERRY—But what are they to do in the meantime till a response is finalised?

Mr Lonsdale—Are you asking me: what is the individual meant to do the meantime?

Senator SHERRY—Yes. Let us assume that they had sold the asset but had not placed the undeducted contribution into a superannuation fund by budget night. What are they to do with that money? How should they treat it? There is no certainty at the moment until the rules are finalised, is there?

Mr Lonsdale—Under the current law as it stands people can put in the undeducted contributions, but, if the plan goes ahead, the government has indicated from budget night a cap of \$150,000 a year will apply.

Senator SHERRY—Okay. What is the tax penalty if they put in more than \$150,000 in those circumstances? Isn't it the top marginal tax rate?

Mr Lonsdale—That is correct. It is effectively taxed at the top marginal rate. Contributions in excess of the cap would be returned to the individual.

Senator SHERRY—In some cases those individuals may have already paid capital gains tax. They have sold an asset and they have paid capital gains tax, whatever that comes to. Some people—and I am aware of this and I would be surprised if you were not—had paid capital gains tax on the sale of the asset and were ready to put into the super fund, but had not put it in. Could they on over \$150,000, having paid capital gains tax, also pay the top marginal tax rate as a consequence?

Mr Lonsdale—Only on the earnings; not on the undeducted contribution. The top rate would be applied to the earnings that accrue on the contribution that is made.

Senator SHERRY—What is the individual to do when, under 'the old rules', they have initiated an action that they cannot reverse—if they have made a decision to sell a property or an asset? This is mainly farmers and small business people I am talking about. This is the central group of people who are concerned about this. They are part way through a transaction. Are you aware that some superannuation funds have refused to accept undeducted contributions over \$150,000, even though the rules are not finalised?

Mr Lonsdale—We are aware, Senator.

Senator SHERRY—Are you aware that some funds are accepting moneys over \$150,000?

Mr Lonsdale—We are aware, Senator.

Senator SHERRY—So who is right—the funds that are accepting the undeducted contribution over \$150,000 or the funds that are not accepting it?

Mr Lonsdale—These are issues for government. As I have said, this is a plan and the government have said that where there are transitional issues they will consider them and they will make a decision in due course.

Senator SHERRY—Do you believe it would be in the best interests of these individuals so affected if it were a decision made urgently and quickly so that they know what the circumstances will be?

Mr Lonsdale—We are aware of the particular cases or cases like the ones you have put forward and we have brought those to the attention of government. The government is aware of the issues surrounding those and will make a decision in due course.

Senator SHERRY—But as yet we have no indication of a date other than it would be a date after Wednesday, 9 August, which is the close of submissions.

Mr Lonsdale—When you say a date that the government might—

Senator SHERRY—Yes. The government is seeking comments from the community on this plan by Wednesday, 9 August 2006.

Mr Lonsdale—That is correct. That is the publicly stated position.

Senator SHERRY—Back to you, Minister, do you understand the urgency of this issue for people who have been caught out in the circumstances?

Senator Minchin—This is the difficulty in public policy, isn't it? You seek to reform an area that badly needed reform and you want to do so by way of a comprehensive well thought through proposal. We are often criticised for not engaging in sufficient consultation in these things. I think that the government has very sensibly put out a pretty comprehensive plan that says how it will operate if it is to proceed and people are thereby forewarned of the government's intent but subject reasonably and sensibly to submissions from the general public. You have to give a reasonable time for that to occur. We have said what the start date would be. Obviously subject to balancing the need for proper consultation and consideration of the submissions we would want to get a final position together I assume as soon after that as we reasonably can.

Senator SHERRY—The fact that the plan is obviously not going to be finalised until after Wednesday, 9 August means that there is no certainty for this particular group of people who are caught part way through a transaction. The proposal is to apply the rule from budget night.

Senator Minchin—I appreciate that. We expressly talk about the possibility of averaging that cap and things like that and we entertained and invited comment on transitional issues. But as is always the case when changes in policy are made they often come into effect on the night or the day of their announcement. It is often the case that changes are made and take immediate effect on budget night and, yes, the fact is they will affect people who might be in the middle of some sort of transaction. That can happen every budget.

Senator SHERRY—Sure, but the difficulty is that this particular change dates from budget night and I think it is accepted that it is an issue that comes under the head of transitional issues and they will not receive finality on the current schedule until 9 August. In the meantime they are in limbo because they are part way through a transaction.

Senator Minchin—It is not for us to give financial advice to people—

Senator SHERRY—That is not an issue—

Senator Minchin—Whenever a change is made in tax arrangements some people can, in a sense, be caught out because the changes come into effect straightaway. It is often the case that tax changes come into effect immediately and obviously often they need to otherwise the system can be gained. You know why this measure needs to be done in this way otherwise you know what the consequences could be.

We have said, assuming the plan proceeds—and we want it to proceed—that this measure will come into effect as of 9 May and people should act accordingly. We have said that we

will consider whether the cap, which we intend to legislate and which would take effect from that night, might be averaged. People need to plan on that basis. As always, you cannot allow gaining of the system.

Senator SHERRY—But, Minister, they planned on the basis of the rules up to budget night. You do not seem to be particularly concerned about this. These are overwhelmingly farmers and small business people who have gone to a planner and have received a legal statement of advice to do certain things to make undeducted contributions—selling an asset. They have received that advice. There are a group of people, some of whom are part way through selling the asset and some of whom had sold the asset but had not yet put the money in as an undeducted contribution into a superannuation fund. As I mentioned earlier, some super funds are saying, ‘No, we can’t take it, because it is over the proposed new limit of \$150,000.’ Some super funds are saying, ‘Yes, we will take it, but you may have to pay the top marginal tax rate.’ These individuals would like some finality, and hopefully before 9 August. That is all I am suggesting, Minister.

Senator Minchin—I think the Treasurer did indicate his understanding that there could be people in that transitional phase and that one of the things to be considered in this consultation phase is transitional arrangements for people. If the case is made about certain individuals or classes of individuals being adversely affected in some way, then that would be considered as part of the consultation on this matter. But it is not at all unusual—indeed, it is elementary—

Senator SHERRY—They need to know as soon as possible.

Senator Minchin—You would know that certain changes in taxation arrangements just have to take effect immediately if the system is not to be gained.

Senator SHERRY—I recall seeing in the more detailed outline a reference to this group of people—people who are in these circumstances of undeducted contributions not made—as being a relatively small number.

Mr Lonsdale—That is correct.

Senator SHERRY—What is the approximate number?

Mr Lonsdale—I do not have those figures with me.

Senator SHERRY—Presumably you identified a number to come to the conclusion that they are a relatively small number?

Mr Lonsdale—Correct. There is a pool of people who make undeducted contributions each year. In terms of the number above the cap, what the outline says is that the expectation is that very few people would be affected by that cap.

Senator SHERRY—Are we dealing here in tens of thousands or less than a thousand?

Mr Lonsdale—I do not have those figures with me.

Senator SHERRY—I am surprised you are not aware of a figure, given the concern from the individuals affected.

Mr Lonsdale—As Mr Gallagher has said, I would not want to provide a figure and find that it was the wrong figure.

Senator SHERRY—Yes, but you know how reasonable I am. I am just seeking an indication. If you say approximately a thousand and you come back and say, ‘Look, it’s 5,000. Sorry.’ I am not going to complain. Mr Gallagher knows how reasonable I am. So does Mr Ray.

Mr Lonsdale—Yes. Your reasonableness is not the issue. I would just like to be sure about the number.

Senator SHERRY—The issue for me is getting a ballpark figure of what you base that statement about a small number of people on. Anyway, I come to the issue of people in existing pension annuity products who are currently part or wholly retired. Did you do any analysis of the number of people who are over the age of 60 in existing pension annuity products?

Mr Lonsdale—That would be part of the costing.

Mr Gallagher—Obviously we had a look at the information that we had on people with other Australian pensions. We looked at whether or not they were receiving a superannuation rebate so that we could determine, as best we could with the data, the extent to which they were receiving a taxed or an untaxed pension.

Senator SHERRY—And those receiving a taxed pension?

Mr Gallagher—Form part of the costing, yes.

Senator SHERRY—But in terms of the number of people in the existing pension product who may or may not transfer out of it into the new pension product, do you have any approximate number for those in the existing pension annuity product? I have seen a figure of 300,000.

Mr Gallagher—It would depend very much on the extent to which those products are non-commutable.

Senator SHERRY—Yes.

Mr Gallagher—And the arrangements that companies choose to make for non-commutable pensions.

Senator SHERRY—That brings me to the issue I was going to raise.

Mr Gallagher—I do not have those numbers with me and I am not exactly sure.

Senator SHERRY—I would suggest that it is in the hundreds of thousands but, anyway, if you do not have the numbers you do not have the numbers. The intention of the plan is that it would be allowable for an individual to transfer out of an existing pension annuity product into the new pension product. That is the intention, is it not?

Mr Lonsdale—If the existing pension product is commutable.

Senator SHERRY—Yes.

Mr Lonsdale—That would be correct.

Senator SHERRY—Have you looked at the practical issues that flow as a consequence of people moving out of a commutable pension product into the new one?

Mr Lonsdale—Which consequences? When you say ‘practical’, you are not talking about revenue?

Senator SHERRY—No, not lost revenue but the practical everyday issues that flow for industry and for those individuals perhaps.

Mr Lonsdale—These would be issues that we would be consulting on over the period ahead.

Senator SHERRY—Is it not reasonable to assume that these people will go to a financial planner? Some of them would do, wouldn’t they?

Mr Lonsdale—That would be up to the individual.

Senator SHERRY—Does it surprise you that financial planners have had a lot of calls from this group of people seeking advice?

Mr Lonsdale—Nothing surprises me.

Senator SHERRY—I am glad nothing surprises you. I thought the intent of the package, at least in part, was to reduce the use of financial planning in this area.

Mr Lonsdale—What the plan indicates is that people over the age of 60 who receive a tax-free lump sum or a tax-free pension would no longer need to seek financial advice on the tax implications of that choice.

Senator SHERRY—On the tax implications?

Mr Lonsdale—Correct.

Senator SHERRY—As a consequence of this announcement, a significant number of people in existing pension and annuity products have gone off to see their financial planner. That does not surprise you, obviously. We have already been through that. And they will pay for it. The thrust of the budget announcement is that this will minimise advice around tax arrangements at age 60, not other advice?

Mr Lonsdale—When we are talking about superannuation, pensions and long-dated products, these are financial decisions that people do not take lightly. To the extent that they would seek financial advice at present on the non-tax implications that would continue to be the case. The plan is saying that at the moment the tax implications are so complicated as to whether you take a lump sum or a pension and what sort of pension you might take that many people seek financial advice purely driven by the tax implications of that choice.

Senator SHERRY—It is around that concern that the issue of simplification arises in tax and it is related to tax advice?

Mr Lonsdale—The plan, we would expect, would significantly reduce the need to get tax advice for those people aged 60 and over.

Senator SHERRY—For the existing group of people aged over 60 who are in a complying annuity pension, who have already received the tax advice by the way, the plan has led to an increase in inquiries and their costs of financial planners. That has been the result.

Mr Lonsdale—You are asserting that?

Senator SHERRY—No, it is fact. I have seen the inquiry notices from planners who have shown me. Are you saying that you have not heard about this and you do not accept that it is fact that, as a consequence of the plan and the announcements, there has been an increase in inquiries from people in existing pension annuities to financial planners?

Mr Lonsdale—Before I would call anything a fact I would want to have a look at the calls and the responses over a period to work out whether or not it has happened as a consequence of the package. I think it is premature to draw that conclusion on what we have seen.

Senator SHERRY—Have you not had any consultation with financial planning—

Senator PARRY—Mr Chairman, I appreciate Senator Sherry's passion for this area, but I understand that he has been going since this morning and a solid hour this afternoon. There are a number of other senators here who, I believe, have questions. I am just wondering if Senator Sherry could give an indication as to how much longer he will be so that the rest of us could have a turn at questions.

Senator SHERRY—Till 6 o'clock—but on this area probably another half-hour.

ACTING CHAIR (Senator Chapman)—No, you cannot. I am sorry, you cannot dominate.

Senator SHERRY—I am being asked, that is all.

ACTING CHAIR—That is the total of your questions?

Senator SHERRY—Yes. I would almost certainly finish this area by 3.30. This is the major government plan that I am asking about. It is your plan; if you do not want to ask any questions about it, that is up to you.

Senator PARRY—I am suggesting that we do want to ask questions, not necessarily about this issue, but I know three other senators have questions.

Senator SHERRY—If we are dealing with this issue now, I am happy for people to come in and ask questions about this. We have a program, an order, and I am just following that.

Senator PARRY—I think, Mr Chairman, if Senator Sherry has indicated that 3.30 should just about pull him up, maybe after the afternoon tea break we can move to other senators for questions of the ATO.

Senator SHERRY—On this area by 3.30—I have a lot of questions for Tax as well.

Senator MURRAY—I have not understood. Are we going to Tax at half past three? Is that what you are saying?

Senator SHERRY—This is one of the few opportunities that oppositions actually get to ask anything, including the cross-benchers.

ACTING CHAIR—We are generally on tax now.

Senator MURRAY—Is there a suggestion that, after tea, we will go to the Taxation Office?

Senator Minchin—Yes, the tax office.

Senator PARRY—As against Treasury on tax?

Senator Minchin—The Australian Taxation Office is on the list and, reasonably, they want to know when we are going to get to them.

ACTING CHAIR—I just want to clarify with the government senators and Senator Fielding: are your questions to the tax office on tax or to the Treasury on tax?

Senator FIELDING—Tax office on tax.

Senator PARRY—Tax office on tax.

Senator WATSON—I have questions to both.

Senator Minchin—Could we put the tax office on at a quarter to four, and if you want come back to Treasury perhaps you can.

Senator SHERRY—In fact, we started off on the tax office, but I did not lead into this package, do not forget. There were questions from Senator Murray and Senator Watson; I am not criticising them for it. They got us into this area.

Senator Minchin—I was not attributing blame to anybody.

ACTING CHAIR—It is agreed that we will move to the Taxation Office after the break.

Senator SHERRY—Dealing with the behavioural response to the plan from people who have existing pension annuities, does it surprise or concern you that they have sought new and additional advice?

Mr Lonsdale—I would expect people to be looking at the plan, making their own assessments about what it means for them and, if they thought that there was a need to seek professional advice, then they would do so.

Senator SHERRY—Yes, and pay for it?

Mr Lonsdale—That would ordinarily be the case, yes.

Senator SHERRY—The plan, at least in respect of this category of people, has had the opposite effect to what was intended?

Mr Lonsdale—No, I do not see that at all. What the plan has said is that, if it is implemented from 1 July 2007, tax will not apply on lump sums and pension streams for those people over age 60, which will remove the need for people to seek tax advice on that choice.

Senator SHERRY—In the plan it refers to people saving an estimated \$3,000 to \$10,000. Where does that figure range come from?

Mr Lonsdale—I think those figures were presented—

Senator SHERRY—Yes, to a House of Representatives committee, but it is not sourced.

Mr Lonsdale—It was from the Rice Walker submission.

Senator SHERRY—Is it asserted or claimed that people will save \$3,000 to \$10,000 on their plan at age 60? That is the impression that it is given.

Mr Lonsdale—That sentence was included to give a sense that fees can be significant. It is not a Treasury figure.

Senator SHERRY—But you have used it as an authority figure on which to base a claim, haven't you?

Mr Lonsdale—We have presented it as something that has been raised in a House of Representatives committee hearing as an illustration of the significant nature that fees can be when someone is seeking advice.

Senator SHERRY—A saving of the magnitude of \$3,000 to \$10,000 is what is indicated?

Mr Lonsdale—Correct, that is what the sentence says.

Senator SHERRY—For at least some people there is still a need to go to a financial adviser with respect to superannuation?

Mr Lonsdale—As I mentioned before, superannuation and retirement savings are long-term decisions. People will seek financial advice, particularly if they are under 60, for example, where tax will still apply under the package.

Senator SHERRY—Let us take it at the end of the chain, so to speak, at 60. The reference with respect to possible reduction in financial advice and possible financial cost relates to tax matters, not to other matters?

Mr Lonsdale—What the plan is saying is that, from 1 July 2007, tax will not apply to lump sums and pension streams for people over 60, so the need to seek financial advice would possibly not be necessary on tax matters; that is correct.

Mr Gallagher—It is also the case that the removal of 50 per cent asset test exempt pensions may mean that some people may not need to seek advice on pension matters.

Senator SHERRY—They would initially need to seek advice to see whether they were covered in the first place, wouldn't they, and then the consequences that flow? They would need an assessment of their asset value to start with, wouldn't they, Mr Gallagher, and then the way it is treated?

Mr Gallagher—It is quite possible that people would seek advice on those issues.

Senator SHERRY—I turn to page 61 of the larger document. I suspect you will be able to help me on this. I am referring to appendix A, and there is a number of other subsequent tables. What is the assumed real rate of return and the fees charged in the calculation of the benefits?

Mr Gallagher—Investment return is seven per cent per annum after fees and charges. Wages growth is four per cent per annum and CPI is 2.5 per cent per year.

Senator SHERRY—Before inflation or after inflation?

Mr Gallagher—That is nominal, as before. Normally we take a return of about 4.5 per cent real.

Senator SHERRY—Just going to the table A1 on page 61, 'Lump sum payment'. In the right-hand column it states 'Change in after tax benefit as a result of the package'. For a lump sum of \$100,000—and I understand that at the moment the majority of Australians have under \$100,000—there is no benefit from the package. Why is that?

Mr Gallagher—In this case it is because that would not exceed their post-‘83 threshold. There would be issues about whether that entire amount of \$100,000 would in actual fact be post-‘83 contributions, but that is what has effectively been done here, as opposed to looking at the five per cent assessable amount.

Senator SHERRY—They are not benefiting from the exit tax removal, presumably, or the income tax changes?

Mr Gallagher—They would not have been caught by the post-‘83 lump sum tax.

Senator SHERRY—That is a reasonable assumption. I am just interested that they do not get any benefit, and that is the majority of Australians at the moment. If we go up the chain of lump sum, why does a person on a \$400,000 lump sum get a net benefit of 12.2 per cent? Why is it so much greater than that for a person on \$250,000?

Mr Gallagher—That is the application of the tax rate above the threshold.

Senator SHERRY—Did you do any data on the number of people this year who have a benefit of more than \$400,000 in a lump sum?

Mr Gallagher—I do not recall a breakdown in that fashion. It would have been taken into account in the costing.

Senator SHERRY—Table A1 shows that people under \$100,000 get no benefit. Just use the figures of \$150,000 and a 1.5 per cent benefit, \$200,000, \$250,000, \$400,000 and above. If you could take it on notice to provide the numbers for people with super. I appreciate it is an approximation. It seems to me that the higher your super balance—\$400,000-plus—the greater the percentage benefit. It is not just the monetary nominal benefit; the percentage benefit goes up as super goes up.

Mr Gallagher—That is correct. That is because it is above a threshold.

Senator SHERRY—If we go down to the next section, ‘Age 45 super guarantee,’ we see a similar pattern emerging. Usefully, you have got income per week. A person who earns an income of less than \$600 a week SG gets no benefit from these changes, presumably at age 60; whereas a person on \$2,000 a week gets a net benefit of 11.7 per cent. Is that correct?

Mr Gallagher—At the assumed contribution rates.

Senator SHERRY—Yes, I accept that.

Mr Gallagher—Obviously, the person at \$600,000 might salary sacrifice a large portion of their money into superannuation and get a higher benefit at retirement than the ones shown, but at the assumed contribution rate.

Senator SHERRY—At the assumed contribution rate. The majority of people do not put additional contributions over the SG at the moment, do they, at that salary wage level, as I understand it?

Mr Gallagher—No. It is very likely to be SG only.

Senator SHERRY—A person who is very likely to be SG only earning \$600 a week gets no benefit from this package at age 60, whereas a person on \$2,000 a week, SG only, gets a \$51,389 monetary benefit, or an 11.7 per cent increase in income.

Mr Gallagher—That is what the table shows, yes.

Senator SHERRY—Yes. I assume you did this, but did you assume the indexation of the \$130,000?

Mr Gallagher—Yes, it is indexed.

Senator SHERRY—I knew it was indexed, but I was not sure whether that was included in this. Could you take on notice the number of people, in the case of the SG, in the workforce who are on less than \$400 a week, between \$400 and \$600, between \$600 and \$800, and between \$800 and \$1,000—those wage income levels that I assume you presented?

Mr Gallagher—Yes.

Senator SHERRY—Could you go to the tables, which are presented in a similar way, in respect of untaxed super funds? I was a little surprised in the presentation to see that in fact there is a higher percentage benefit—I appreciate there is the rebate proposal and it is not income tax free, as it is for taxed funds—a higher level of benefit for a higher income earner than there is for an untaxed fund. Can you explain to me why that is the case? Take \$2,000 a week—

Mr Gallagher—I do not know that you can readily compare the two sets of numbers in terms of the tables. In one case we have wage and salary income and in the other table you have their actual superannuation pension, not their wage and salary income. It is very difficult to readily compare the numbers because you have to look at the putative accumulation and then look at the pension factor that has been applied to generate that superannuation pension.

Senator SHERRY—As a general observation on the tables for both taxed and untaxed funds: a person with a higher income and a higher level of superannuation savings would receive the highest percentage in net outcome.

Mr Gallagher—That is what the tables are showing. That reflects a number of features of the taxation system, such that people on low incomes, because of the action of SATO, the senior Australians tax offset, and the low income tax offset, have very low taxation liabilities.

Senator SHERRY—I notice in the document, in the section on untaxed schemes on page 45, it says that only 10 per cent of all superannuation fund members are members of such schemes, and they are nearly all public servants. How did you get that figure? I could not find a definitive figure for the number of people in defined benefit funds, let alone public sector defined benefit funds. Can you point me to the source? It is at the bottom of page 45.

Mr Gallagher—There are two potential sources of a number such as that. One is the APRA superannuation statistic on member retirement benefits structure in the APRA tables. The other potential source is the surcharge data, which will identify that a surcharge debt is being accumulated for someone in an untaxed fund.

Senator SHERRY—You still have access to that?

Mr Gallagher—Yes, for historical reasons.

Senator SHERRY—But the surcharge would give that to you for both private sector and public sector DB funds. Private sector DB would be paying a surcharge. There is a surcharge assessment.

Mr Gallagher—Private sector DB would have a contribution, and the surcharge could be taken from the contributions.

Senator SHERRY—Is the number of people in a private sector DB relevant for these calculations or is it only the public sector? The document says they are nearly all public servants. What about in private sector defined benefit funds?

Mr Gallagher—Many of them would be untaxed.

Senator SHERRY—What about Telstra DB? How is that classified at the moment?

Mr Lonsdale—We think it is fully funded.

Senator SHERRY—I know it is fully funded. But there must have been a component untaxed, even if it is taxed now. I am wondering how you treat that. That is a pretty big fund. The other ones would be the university funds. Are they taxed or untaxed funds?

Mr Lonsdale—We do not have the data with us on which funds are taxed and which are untaxed.

Senator SHERRY—I accept you would not, but in the case of Telstra and the university funds, we are dealing with very big funds in terms of numbers, which can impact on the figures, which is why I am interested in the way they were treated, because it is a little unusual. They are not mainstream public sector super funds anymore.

Mr Lonsdale—No. We understand that.

Senator SHERRY—Would you take on notice to ascertain whether the Telstra and university funds, which at least some time in the past have been, and may well still be, treated as public sector funds, fall into these categories?

Mr Gallagher—Subject to issues about individual taxpayers.

Senator SHERRY—Of course. I am not asking for individual taxpayer information. Is that what you are getting at, Mr Gallagher?

Senator SHERRY—I am just interested in—

Mr Gallagher—The fund, in a way, is a single taxpayer. That is my concern. Are you asking about the activity in one fund?

Senator SHERRY—Yes. There is a high likelihood that there would be groups of people by a certain period, a cut-off date, where the rules may have changed. I am not interested in the individual people. I am just interested to know whether you have taken it into account when calculating your 10 per cent.

Mr Lonsdale—We will take it on notice.

Senator SHERRY—You referred, Mr Gallagher, to the ABS data. There is a significant category of hybrid, which are both DB and defined contribution. How did you—

Mr Gallagher—Many funds are defined benefit on the employer side and defined contribution on the member side, so they put in post-tax contributions—undeducted contributions.

Senator SHERRY—Not many funds, did you say?

Mr Gallagher—I said a number of funds will have that so-called hybrid design.

Senator SHERRY—I cannot remember the number off the top of my head, but it is a big number. You refer to defined benefits statistics, and they are certainly there. For public sector super funds it is there. But there is this group called hybrid which is very difficult to get a breakdown for. Did you go to APRA to get a breakdown from it directly or did you just look at the statistics that were published?

Mr Gallagher—I will take on notice the exact source. I listed the two potential sources.

Senator SHERRY—I am interested in the way you were able to come to a conclusion on that basis. I might ask APRA about a breakdown. I have asked for it before; they never seem to be able to give it to me, though. In the calculation of the tables we have been having a look at in appendix A, the seniors tax offset, which we had a brief discussion about earlier, cuts in at age 65 for men and 63 for women. Under the plan, you can take your super at age 60 tax free. How did you go about calculating those tables? It seems to me quite complex in terms of outcomes. At age 60, when you take into account the seniors tax offset, for example, which cuts in at 63 for women and 65 for men, and then calculating a net outcome—

Mr Gallagher—A number of years ago we set up RIMHYPO to do extremely complex and tedious calculations on a routine basis and we have been publishing cameos in a number of documents, probably since 1993, when the Retirement Income Modelling Unit was set up.

Senator SHERRY—You have amended it for the impact of the senior Australians tax offset?

Mr Gallagher—Yes, that is kept up to date in terms of the modelling. The other thing is that, as we note, some of the calculations have been done in a spreadsheet rather than in RIMHYPO. In 8.6.1 we talk about general assumptions.

Senator SHERRY—I will conclude on this point about the senior Australians tax offset. Let us take a single person. It will increase from \$21,960 to \$24,867.

Mr Gallagher—That reflects the low income tax offset change. The government changed that amount from \$235 to \$600, and we set the threshold at the point where the income tax liability would be equal to the sum of the two offsets.

Senator SHERRY—Does that effectively mean that a single man of age 65 pays no tax on income—and this would include non-super income presumably—below the level of \$24,867?

Mr Gallagher—From 2006-07, yes.

Senator SHERRY—I have seen advertisements that refer to a higher figure.

Mr Gallagher—Those advertisements often include the 15 per cent annuity rebate. In terms of a tax strategy, the rebates themselves do not offset the Medicare Levy above the highest seniors Medicare Levy threshold, and therefore you would need imputation credits to offset the Medicare Levy.

Senator SHERRY—It is broadly correct that, if you are 65 years of age, you are not paying tax on an income below \$24,867?

Mr Gallagher—Correct, if you meet the normal requirements—the residence requirements.

Proceedings suspended from 3.32 pm to 3.52 pm

Senator FIELDING—I have some questions about the tax office change. I asked some questions last time on this area, too, and I want to follow those up. Thank you for the Cap Gemini reports. I appreciate that; they were quite useful. The executive summary showed the four overall work streams. There were two red flags and the other two were amber, which is of some concern. Can you walk me through where that change program is at currently and how it is tracking along according to the schedule?

Mr Farr—Yes, there were some red flags and so on, and I will cover that. At the end of the day, that is what they are there to report to us about. You may recall that we have three major phases to the program. The weekend before last, we implemented the major systems release for phase 2. That is now in production and operating. Last week, our 3,000-odd contact centre staff were using the enhanced technology as a result of that release. We have begun this week bringing on people to reduce the number of case management systems in the tax office down to that single case management system. Possibly last time I mentioned that we had some relatively short delays early on with some of the technology. It did not affect the overall length of the program, but the first release was a bit late. Since then, we have been tracking pretty well to schedule and to budget. We are still tracking to schedule and to budget. We were certainly aware of the issues raised by Cap Gemini in the January report. Cap Gemini works with us so, in a sense, the report is stuff we already know. It gives us feedback as we go along. We made a lot of changes to the way we were doing things, concentrating particularly on the change management aspects. I am very happy that we are well on track and going, I believe, very strongly.

Senator FIELDING—I certainly appreciate the reports, too, by the way. To start with, with respect to the tax system, I got into the changes to make sure we have flexibility. Originally, it started along the lines that there was some talk about how the tax reform would help families. That is the reason I started on this issue, to make sure it was flexible. I was a bit concerned about some of the programming language, the COBOL, so I have decided to keep a bit of an eye on that. That was the reason. I thought it would be wrong not to, actually. I come back down to a question, generically, again: in terms of the percentage fit, have you found out anymore about the off-the-shelf-type system, the TAS system, and do you still think it is the same percentage fit as it was originally?

Mr Farr—There is nothing to change that significantly. It is also important to understand that the TAS component is only a small proportion of the total solution that we are talking about from our IT platform. In fact, if I look at COBOL generally—and I know that was a concern that you raised previously—within our current set of systems we have in the order of 40 million lines of COBOL. We would expect at the end of the program something in the order of three million to four million lines of COBOL. It is a much lower percentage. The COBOL that we would be using is largely the most modern version. As you mentioned, COBOL has been around for a long while. But COBOL 2002, which is the version we will be using, is much more modern and allows us to do a lot of the things that modern languages do. We would also be looking to implement some productivity tools, like Micro Focus COBOL,

which would allow our developers a much better interface and much better productivity editing. There are number of things we are doing to modernise it. But even within that main processing system—the integrated core processing system, which was the TAS system—we have developed quite a lot of it. For example, the entire user interface has been redeveloped in Microsoft.NET, to give it a browser-type interface as opposed to the old-fashioned interface that came with it. But the back end, the core part of the big processing engine, is still very much a transfer from TAS.

Senator FIELDING—So the schedule is on track. Is that the original schedule or is it a revised one? I understand that projects do chop and change and I am just trying to work out whether the budget has changed at all.

Mr Farr—We were due to finish in the final part of the release in June 2008. That is still when we are planning to do that; nothing has changed. The big change of our processing systems will be in December 2007. That has not changed, either. As I mentioned, the first release moved back a little bit within that program, and that pushed the second release back but, overall, the program is on track. In terms of the budget, we are within about 1.5 per cent of budget. That is not causing any concern, either. We have done a couple of software upgrades and a few things like that which we did not count on but which will benefit us in the long run. The contract we have with Accenture is a fixed-price contract. If there have been cost overruns—and I suspect there may have been in some aspects—they have been borne by Accenture.

Senator FIELDING—I would be interested in getting, probably between now and the next estimates, another progress report, if I can, just to keep on eye on it, if that is okay.

Mr Farr—Progress reports on?

Senator FIELDING—Cap Gemini.

Mr Farr—The independent—

Senator FIELDING—Yes.

Mr Farr—Yes, one came out last week.

Senator FIELDING—I fully understand that with big projects like this there are ups and downs. My original concerns still exist; I just want to keep on eye on it, if I can.

Mr Farr—There are some other documents that, if you wished, I could table to give you an idea of what the total solution looks like in very simple architecture terms, and also some of the change management approaches that we are bringing in.

Senator FIELDING—That would be useful, thank you.

Senator PARRY—Commissioner D’Ascenzo, I have furnished you with some *Hansard* pages. I am wondering who to direct questions to concerning those questions from the last hearings in February.

Mr D’Ascenzo—Mr Konza is here and he can help.

Senator PARRY—I do not know whether you have had a chance to study the *Hansard* pages but, on page 73, I asked some questions about the benchmark interest rate that was used for sections 109E and 109M of the Income Assessment Act. My main concern last time was

the rate not being published on the website. I have a printout of the website as of 19 May. I have also checked today. It is still not on the website for the 2005-06 year, the current financial year. My questioning, which was answered on pages 98 and 99 of *Hansard* from that day, 15 February last year, indicated that the rate was published in advance so that companies could utilise that benchmark rate for setting the loan fee. I have two questions. First, has anything changed? Secondly, if nothing has changed, why is the rate not published on the internet?

Mr Konza—I have only just received these extracts from you. Thank you very much for them. Like last time, if you give me a few minutes, I think we have the technology so that we can actually go and check what is going on. We would hope to have an answer this evening.

Senator PARRY—The rate is 7.3 per cent. I found that rate as a result of a phone call, rather than just accessing it off the Internet, which is a useful tool. As I also mentioned in *Hansard*, I commended the Taxation Office for the website. It is a great website. It is just missing that one vital figure

Mr Konza—As I advised you last time, we publish a tax determination each year, so there certainly should be written evidence of it on the website, and I will track that down.

Senator PARRY—I am happy to provide you with a printout of 19 May for the website, if you would like to have that as well.

Mr Konza—Thank you.

Senator WATSON—I understand there was a further examination into the deductibility of subscription payments, and that review was conducted by the tax office, in circumstances where retired professionals wish to continue their association with their professional associations, by continuing the payment of subscription and being involved in voluntary activities with their professional association. Could you tell me the status of that deductibility?

Mr D'Ascenzo—I am not personally aware of that review. It sounds to me like it is a question that would be in connection with the earning of assessable income. Other than that, I am not sure where it is at. Perhaps I can take that on notice and provide a report, unless any of my colleagues have any better knowledge of that?

Senator WATSON—It might have been a Treasury review; it might have been asked to look at it?

Mr D'Ascenzo—I can go back and see whether anything is happening in that area and report back.

Senator WATSON—The accounting profession continues to face problems with division 7A, despite relatively recent amendments in this area. In terms of equity and tax justice, how can we have a credible tax system in circumstances where we have a situation of no mischief, no loss of tax revenue, no benefit to an individual, and yet the Commissioner for Taxation has no discretion in imposing tax penalties as harsh as those imposed on the most blatant tax evaders? I remind the committee that, while discretions are not necessarily consistent with the self-assessment environment—and that is the reason—late last session there was a corporate

tax amendment involving discretions. Are you happy with your tax auditors having to enforce such legislation?

Mr D'Ascenzo—Ultimately the responsibility of the tax office is to apply the law. Where the law applies in a way that is seemingly unfair or has consequences over and above the underlying policy intent, our normal operation is to advise Treasury and through Treasury advise government of those consequences and allow government to see what they can do to fix up those unintended consequences.

Senator WATSON—Given that the tax office is increasing its audit activities in relation to superannuation funds under its jurisdiction, can you give the SMEs an idea of the Taxation Office's audit expectations in conducting audits for the 300,000-plus SMSFs?

Mr D'Ascenzo—This is for the self-managed super funds?

Senator WATSON—Yes.

Mr D'Ascenzo—Last year we did 3,600 audits, and we are planning to do another 3,600 audits this year. A lot of those audits are follow-ups from contravention notices provided by the auditors for the self-managed super funds. In that sort of area, it is questions of the requirements of the SI(S) Act and whether or not they are being complied with. Those requirements include a sole purpose test to ensure that self-managed superannuation funds buy investments for the purpose of retirement benefits, questions of whether or not you can deal with associates of the self-managed super fund other than on an arm's-length basis. There is a range of rules of that nature and that is where our focus has been. Raelene Vivian is the Deputy Commissioner in charge of that area and she might be able to elaborate.

Ms Vivian—I am happy to go into more detail, but I think the commissioner gave a very good overview of what we are doing with self-managed super funds. In addition, we have spent quite a bit of effort on raising the education profile of trustees and auditors about their responsibilities in terms of self-managed super funds.

Senator WATSON—My question was largely directed to the provision of a checklist prior to an audit for trustees to look at so that they know what essential features you will be looking at to see whether they comply with those benchmarks, as it were. That is the reason for the question. I understand there is quite a lot of default. If we could get that checklist and distribute it, that would be very handy.

Mr D'Ascenzo—I thought that we would have had that checklist in the marketplace. Earlier this year, both Raelene and I gave speeches to the superannuation professionals association of Australia, which is one of the peak bodies in relation to self-managed super funds. In those presentations we gave a checklist of what people should be looking at. That information, I would also imagine, would be in a lot of our educational material and our website. Just from practical experience, from 1 July 2004, we have had 7,300 auditor contravention reports. The top six reported contraventions from those reports are assets not in the name of the fund. You might say, 'Why is that a concern?' If the asset is in the name of someone else and that other person goes into liquidation or bankruptcy, then the fund is out of pocket. The other contraventions included loans made to members or a relative, particularly where those loans are on non-arm's-length terms; in-house asset breaches, in other words, assets are used for purposes other than superannuation benefits or retirement benefits in the

long term; documentation problems—some self-managed super funds do not maintain their documentation requirements; borrowings by the self-managed super funds for purposes not allowed by the legislation, in other words, the fund borrows to buy something that is not within the specified classes of assets that funds can buy; and breach of the sole purpose test, where the asset acquired is not acquired by the fund for genuine retirement income purposes. That is very consistent with what we see through our audit activity.

Senator WATSON—Speaking of contraventions, approved auditors and actuaries must report all SMSF contraventions. How many contraventions were advised in the last financial year, both for auditors and actuaries?

Mr D'Ascenzo—My statistics are from 1 July 2004. The total number of auditor contravention reports was 7,300.

Senator WATSON—Actuary contraventions?

Ms Vivian—We do not split it that way.

Senator WATSON—It is auditors and actuaries?

Ms Vivian—Yes. Mainly what we find is that most of the contravention reports do come in from the auditors.

Senator WATSON—It is over 7,000 for both categories?

Ms Vivian—That is since 1 July 2004.

Senator WATSON—From 5 June 2005?

Ms Vivian—That is since 1 July 2004 to about 16 May this year.

Senator WATSON—So it is more than 12 months?

Ms Vivian—Yes. So that is about 23 months. Probably in the last financial year we have received about 2,500.

Senator WATSON—Why is it that risk management statements for SMSFs are not required to be audited each year under your regime? Are you moving towards that situation?

Ms Vivian—Under the SI(S) Act the self-managed super fund is required to have a risk management strategy.

Senator WATSON—That is right.

Ms Vivian—They need to advise us either verbally or in writing, but under the SI(S) Act that is all we can actually check.

Senator WATSON—Are you going to insist on them being audited?

Ms Vivian—No. In terms of the soundness of the risk strategy, that is actually the responsibility between the members and the trustees.

Senator WATSON—Is there any benchmarking required for these small funds in terms of risk managing strategies?

Ms Vivian—No, certainly not from us as a regulator.

Senator WATSON—Do you intend to move in that area?

Ms Vivian—No. Again, our responsibility under this act is to determine that they have a risk strategy in place but not in terms of the content of the risk strategy.

Senator SHERRY—Where you have a risk strategy it would be acceptable?

Ms Vivian—Yes. Under the SI(S) Act they do not actually need to formally keep it for a self-managed super fund in writing. They can advise us, although we do actually suggest to the trustees that they should have a risk management strategy in place.

Mr D'Ascenzo—In fact, the tenor of the presentations which we gave earlier this year was to stress to trustees the responsibilities and obligations of running a self-managed super fund. The concept that we put was that it may be good for some but not necessarily for all and that there were risks and responsibilities. Ultimately it was their responsibility primarily to ensure that the risk profiles that they undertook were such that guaranteed a reasonable retirement income. What the SI(S) Act provides is categories of assets and investments that are appropriate for self-managed funds to invest into. Our role as regulators in that area is to ensure that those rules are met but not to ensure or to in any way evaluate or analyse the risk choices made by the self-managed super fund.

Senator WATSON—Commissioner, last year the government introduced a \$100 million turnover test, whether people could satisfy the same business test, and at the same time commenced a review into improving the same business test. Submissions were called and had to be put in by the end of January but as yet there has been no outcome. I remind you that the Warburton Hendy report stated that when it comes to lost recruitments we did not compare so well with other OECD countries. What has happened to lost recruitments?

Mr D'Ascenzo—I am not quite sure of the question. In terms of the same business tests, those proposals are mainly matters for Treasury and the development of policy, so the review of the same business test would be under Treasury control.

Senator WATSON—Could the minister respond?

Mr Gallagher—As you outlined, yes, the announcement was made and it was subject to review of the \$100 million on the same business test. The government has not made an announcement of the outcome of that review yet; so no announcement has been made yet.

Senator WATSON—You might also be able to help with the next question. In relation to capital gains tax and non-residents—perhaps by way of the following background: two particular budget announcements commenced last year regarding international taxation. Where are we at in relation to capital gains tax and non-residents and foreign tax credits?

Mr Callaghan—Consultation has been under way on these issues and draft legislation is being prepared.

Senator WATSON—As to revision of the general interest charge and the shortfall interest charge, while the general interest charge and the shortfall interest charge have a statutory seven per cent and three per cent uplift respectively, the commissioner has a discretion to remit the relevant interest charge where the circumstances warrant it. There have been numbers of reports where it appears there is some reluctance in the operations area to exercise the discretion to further remit the GIC or the SIC, even though the taxation people in the audit area—coincidentally, I thought—who would be far better across the particular circumstances

of the case, may well be inclined to make further remission if it was their decision to make. What I am worried about is almost the development of a turf war. My question to Mr D'Ascenzo is whether he is satisfied it is a good idea to have decisions about interest remissions made by personnel who are almost invariably unfamiliar with the particular circumstances of the case, rather than the audit person who would have a pretty thorough knowledge of that background.

Mr D'Ascenzo—I am not necessarily accepting that there are those internecine disputes within my office; so, based on that proposition, I am not necessarily saying that there has been any failure on the part of my officers to apply the discretion in a fair way, having regard to the practice statements and guidelines we have issued to them about how they should do that. Having said that, we have been looking at ways of trying to ensure that processes are demonstrably fair and appropriate, with the appropriate levels of checks and balances for the community, and we have revised our guidelines and practice statements both on the remission of general interest charge and the shortfall interest charge and they are due to be issued shortly. We have also decided to move the remission of the shortfall interest charge to the compliance area from our operations area—

Senator WATSON—That is good, yes.

Mr D'Ascenzo—but to leave the general interest charge, which is a non-payment issue, to the operations area, that should have regard to the facts and circumstances of the non-payment rather than the merits of the case itself.

Senator WATSON—I referred to the Burgess report. Mr Kevin Burgess was a former senior legal practitioner. He undertook a review of the tax office's audited advice procedures in relation to some of the other larger companies. I just report several of his important findings:

Some executives reported that after having truthfully explained certain facts and circumstances in detail to ATO officers, their explanations were treated with cynical disbelief and the ATO officers continued to deal with the matter on the basis of their earlier incorrect assumptions.

That was at paragraph 10.3. A second one from the Burgess report:

Hence it appears that there is both some evidence and a strong perception that a seriously inappropriate cultural attitude exists with at least some group of ATO officers.

That is the Burgess report, paragraph 11.4. Given that these are quite serious findings, what steps is the tax office taking to address these issues outlined in the Burgess report, and I just raised two of them?

Mr D'Ascenzo—The preface to the report was by Mr Burgess. He actually did not go into the truthfulness of the claims but just reported what was said. He is not making a comment that those allegations are true; he is making a comment that those allegations were made. I do not think you can start from there with a proposition or an assumption that they are necessarily true allegations. In fact, if you take the first quote that you provided there and you take away the 'incorrect' from that quote, that is possibly the case in some situations. Whether or not the assumptions were correct or incorrect, nobody knows. In terms of cultural attitudes, that runs counter to your previous questions. Your previous question would probably belie any such cultural concern. Having said that, our tax administration has to be able to demonstrate

to the community that its processes are fair and reasonable, in accordance with the law and that in the way that it operates it allows and facilitates the utmost amount of procedural fairness in its processes. You will see that part of the Burgess report, and our response to that report, is to review our end-to-end processes for how we go about doing our audit work, the range of checks and balances and the expectations. Organisationally, if you look at our strategic statement, you will see the very significant focus we have on values that we think are organisationally sound, and those values start from things like the application of the law. They start from being fair to people. They start from trying to ensure that we put ourselves in the shoes of taxpayers. For an organisation that embraces those sorts of values, that is the best way to demonstrate or overcome perceptions, be they real or not real, of any cultural issue.

Senator WATSON—My next question concerns what I call ‘dividend tainting rules’. By way of background, I remind the committee that, when the dividend imputation rules were replaced with the simplified imputation system in July 2002, the new rules did not replicate the share capital tainting, or dividend tainting, rules that were a feature of the previous regime. As we all know, the tainting rules are designed to prevent companies from inappropriately shifting amounts from their capital account into retained earnings and then distributing to their shareholders in tax effective ways. At the time, business was told that these issues would be dealt with later. When we look at the recently introduced Tax Laws Amendment (2006 Measures No. 3) Bill 2006, on 25 May, the dividend-tainting rules have not surfaced. I understand the Treasury has not finalised these for inclusion in that bill, so we have a bill to deal with part of the problem but not the other part. Do we acknowledge that we have been left with a legislative vacuum for the past four years. This affects many corporate taxpayers, who have been concerned about the absence of any legislation in this area. Tainting, for example, with shares a capital account can result in a company having no franking credits, and this could be disastrous. How is Treasury progressing with the dividend-tainting rules, assuming it is proposing to recommend to government that such rules be introduced? We have tainting rules in relation to capital but not in relation to dividends?

Mr Callaghan—My understanding is that those matters are still being looked at and work is still progressing on those. I would have to check with the experts. I am not sure.

Senator WATSON—Can you take the question on notice?

Mr Callaghan—I will take the question on notice.

Senator WATSON—That does not give us much guidance as to whether there is going to be movement on this or whether the vacuum will continue for another four years.

Mr Callaghan—Yes.

Senator WATSON—Again, I express a frustration from business about too few experienced personnel in Treasury actually dealing with tax issues. This is not a criticism of their competency. They are very competent people. They are committed. They are dreadfully overworked. Given the extra revenue that is coming in, particularly through company tax, are you satisfied the business tax area is sufficiently resourced, given the work that is still to be done in clarifying a significant number of technical consolidation issues, for example, as well as other business reform issues, including tainting, usage of company losses and the operation of the same business test? The question is: given the extra revenue that is coming in from the

corporate area, and the corporate belief that you have a lot of very talented people but not enough for the complexities of tax law to be able to assist them in the discharge of their responsibilities—

Mr Callaghan—We believe that the resources we have are appropriate to the task that we are performing. There will always be a case of prioritising in terms of what activities are being done. I believe the comment has been made by business that they are concerned about the turnover of staff. Yes, that is a natural consequence of any workplace; we do see a natural turnover of staff. There is always the challenge, working in this area, of ensuring that we have appropriately qualified people, and that remains, as in any workplace, an ongoing challenge. As I say, yes, we have the appropriate resourcing. We do have to prioritise. We do focus on particular issues. Some of our prioritisation is done in consultation with the external sector, with the taxpayers, the business community and in particular in the corporate tax areas. In short, yes, we have the appropriate staff but we do have to prioritise. That is a fact of life.

Senator WATSON—This morning you indicated that three additional people were added to a particular department, so the priority in the business area is not deemed to be so great if you are putting on additional staff?

Mr Callaghan—No. The decisions always have to be taken across the entire group as to where resources are being deployed. As we see some projects being completed, they will be deployed elsewhere. We have maintained our resources working on corporate tax/business tax. At times we have increased these resources. Across all the activities of the group there will be changing priorities and the resources will be deployed depending on those changing priorities. For example, right now, in terms of working on superannuation, we have deployed more resources within the revenue group working on superannuation matters, but this has not come at the expense of working on business tax issues.

Senator WATSON—I turn to the timing of the completion of the plain English rewrite of the Income Tax Assessment Act 1936 and the introduction of an annual or periodical technical clarification bill to expedite early resolution of legislative anomalies. What sort of progress has been made in this area? We have a tax act that, in terms of plain English, has not been completely rewritten.

Mr Callaghan—A tax law improvement program was started. I forget the exact year. That led to the introduction of the 1987 act. The continuation of that tax law improvement program ceased with the review of business tax, the Ralph review. We are taking opportunities as we go forward to see how we can improve the drafting of the law as particular changes continue. Where there are significant policy changes, we would be looking to see whether we can improve the whole drafting of particular sections taking that program forward.

In terms of the second part of your question about an annual tax law technical amendment bill, there is always work on tax law clarification matters. You will see that, attached to many of the tax bills that go forward over the course of the year, there will be a large number of what could be classified as technical amendments. Some of them could be classified as clarifications, small issues that require resolution. You see that as an ongoing process that is attached to each of the tax bills that go through in the course of the year. The maintenance of the law is under way now. It is occurring. In essence, an annual tax law bill is not required,

because we do attach it to the tax bills that are presented to parliament over the course of the year. We attach those clarification issues to the bills.

Senator WATSON—Thank you. On self-assessment—Mr D’Ascenzo’s specialty—I understand that a review might have been conducted by Mr Voss. There was some independent oversight in relation to self-assessment. What suggestions have been made in relation to a modified self-assessment system for most individuals and small business taxpayers to give them greater certainty and reduce compliance cost? Has there been any progress in relation to that report?

Mr D’Ascenzo—I am not sure what report you are referring to. There was a review of self-assessment. That was done by Treasury.

Senator WATSON—It was either the Board of Taxation or, alternatively, the Voss report. There was a review into self-assessment.

Mr D’Ascenzo—That was a Treasury report.

Mr Callaghan—There was a review of self-assessment. We have seen a number of pieces of legislation flow out of that. A number of other reviews that were recommended in the course of that review of self-assessment are under way.

Senator WATSON—Pardon?

Mr Callaghan—We have seen some measures already enacted from the recommendations from that review. There are other recommendations that call for additional reviews, and they are under way.

Senator WATSON—Can you give us more detail?

Mr Callaghan—For example, one of the measures that came out was a reduction in the period for amendments. I forget the exact details now. I would have to look them up. It was going down from four years to two years for uncomplicated tax affairs, except for areas of avoidance, for example. Those pieces of legislation that came out of the review of self-assessment have gone forward. There were a whole series of recommendations. Some of them pointed to the administrative practices of the Australian Taxation Office. I believe those have been implemented or are under way. There were others that called for particular reviews in some of the applications of the shortened amendment periods to other aspects of the tax law beyond income tax. Those are being looked at. There were a large number of recommendations within that report of the review of self-assessment. Those were accepted by the government and they are being progressed.

Mr D’Ascenzo—The *Report on aspects of income tax self assessment* was released on 16 December 2004. It made 54 recommendations. Thirty of these required legislative responses and 24 were administrative in nature. Of the 24 administrative recommendations, 17 are being implemented by the tax office, four by Treasury, two by the inspector-general and one by the Board of Taxation in conjunction with Treasury. Of the recommendations requiring legislation, 29 of those 30 called for consequential administrative changes by the tax office. Legislation to enable the shortfall interest charge and penalties recommendations received royal assent on 29 June 2005. For the advice and period of review legislative recommendations, royal assent was received on 19 December 2005. In relation to the

administrative recommendations that are within the bailiwick of the tax office, nine of these have now been completed, with a further recommendation scheduled for finalisation by the end of June 2006. Tax office follow-up on recommendations requiring legislative response has been completed for 22 recommendations, with work relating to a further seven scheduled for finalisation by the end of December 2007. That supports Mr Callaghan's conclusion that progress has been made in terms of implementing those recommendations.

Senator WATSON—I now refer to enhancing the tax office's advice services. I understand that you are in the process of upgrading your technical advice services to tax agents to assist them in dealing with the more complex technical issues on behalf of their clients, particularly SME clients. Could you advise the committee what has been achieved to date and what you hope to be able to deliver?

Mr D'Ascenzo—I think it is a broader issue. Our focus in relation to the tax profession was to provide a heightened level of assistance and support to the profession, bearing in mind the pivotal role that they play under our system. That takes many forms and, rather than running into solutions, one of the processes that we have through the many consultative forums we have with tax professional bodies is to try to rework the way we provide them with substantial support. Some examples of what has already occurred include a lot of transactional information and facilities being available to tax agents through the tax agent portal. That is the main level of information now on a day-to-day basis between ourselves and tax agents. We have put in place a premium telephone service that allows them to have quick access to our people through quick-dial facilities and the like and then referral to more specialist areas where that is appropriate. We are reviewing whether or not that one-plus-one approach is the best way of dealing with that and we will be talking with professional bodies to see whether or not different approaches might produce a better outcome. We make public to the tax profession, as we do to the public more generally, our own research materials, our databases, our precedents, anything that we use to make our own technical decisions. We provide a free private ruling service to the public generally but also to tax agents on behalf of their clients, and basically the proposition is one of trying to work with the tax profession to ensure that they are capable and well regulated. If we do that, I think they will then help their clients in understanding their rights and obligations and interacting with the tax office and the tax system more generally.

Senator WATSON—I now have a question in relation to current age based salary sacrificing. In the pre-budget situation, which I will refer to as the current age based salary sacrifice limits, what happens where that limit is exceeded? Is there a penalty and, if so, who pays it—the employer, the employee—and who is responsible for supervising that?

Mr D'Ascenzo—Ms Vivian might provide more details on that. Just before she answers that question, I want to go back to the earlier question that you put to me, about the deductibility of subscriptions for retired professionals. I made inquiries into the area in my office that might be relevant to that. They are not aware of any such review. Unless Mr Callaghan knows anything in that area, my suggestion is that you provide us with more details and we will certainly follow it up for you.

Senator WATSON—Just to clarify that: does that mean that you are disallowing subscriptions because there is no connection with the payment and the current income or lack of income?

Mr Konza—Yes, that would be the general situation. Where someone is receiving, say, a superannuation payment, then the fact that they contributed to the superannuation fund—

Senator WATSON—No, this is the subscription deductions?

Mr Konza—Yes. As a working accountant, I have contributed to a super fund, I retire, I then get a superannuation pension, but there is no nexus between my continuing professional membership and the derivation of the annuity. We would not generally allow it, no.

Senator WATSON—It was an issue that raised its head in the weekend press almost 12 months ago. I have checked this. There was an undertaking that it would be looked at, because there was a lot of voluntary activity that could be lost as a result of the contribution that people can make in their retirement years to their profession. If they are denied any deductibility, there would be less inclination. Some of these subscriptions are quite expensive.

Mr Konza—Yes. Such a review would have to be at policy level.

Senator WATSON—You have clarified your position. I will now have to find out who gave that undertaking and we can follow that through.

Mr D'Ascenzo—We will follow that up further from our end as well to see what we can find.

Ms Vivian—In terms of salary sacrifice arrangements, employers can claim a deduction up to the age based limits for their employee. That is where the deduction would occur. In terms of compliance, it would be us in terms of following up with the employers the claims that they have made against their income.

Senator WATSON—Do you check with the employer to make sure that they are not exceeded?

Ms Vivian—In terms of checking, it would be part of our overall compliance program with employers and where we are following up.

Senator WATSON—The same regime would apply of checking this responsibility when the new age based regime comes—\$50,000 or, if you are over 65, \$100,000?

Ms Vivian—That is probably an issue for my Treasury colleagues if they wanted to answer that from the discussion paper.

Mr Callaghan—Under the plan for exceeding the \$50,000 limit for the deductible contributions to salary sacrificing, exceeding that limit would then be subject to a 45 per cent tax rate. That would be fully deductible for the employer, even though they exceeded the limit. Under the plan, it would be the Australian Taxation Office. The plan proposes that the Australian Taxation Office would do the follow-up as to imposing the higher tax for any contributions above the \$50,000 limit.

Senator WATSON—Does the tax penalty that you refer to apply under the current regime or will that apply only under the new regime?

Mr Callaghan—No, that is under the new regime under the proposed plan.

Senator WATSON—Thank you very much.

Senator MURRAY—In late April, Liam Bartlett, a well-known journalist in the *Sunday Times* in Perth, on page 15, raised an issue concerning the proper payment, both in time and in quantum, of superannuation under the superannuation guarantee legislation by employers. Although he did not mention it specifically in his article, in the background was no doubt the knowledge that a former Labor minister had been alleged to have failed to pay up for young people in his employ at all and certainly in time. Without going into the specifics of a particular individual, as a result of that I investigated the problem generally and am fairly well convinced that the tax office would have no idea at all as to how many employers are not paying superannuation on time or if they are under paying and, I suppose with some, whether they are paying at all. I do not think that is a consequence of a tax office attitudinal issue. I suspect you neither have the resources nor the people to do that job. But perhaps you could explain to the committee to what extent you think the tax office is able to ensure that the superannuation guarantee is being paid by all employers and is being paid on time?

Mr D'Ascenzo—Again, this is a question that Raelene Vivian might elaborate on, but I will preface her comments. I note in the budget the government has given the tax office funding to better allow us to follow up complaints by employees as to Super Guarantee obligations of an employer, including a greater facility to provide employees with information about our progress in that area. It is an area where we have had backlogs in relation to following up employee complaints. The budget announcement foreshadowed a heightened appreciation of that risk by the organisation. Within our current forward looking compliance plan we are certainly looking to do more in trying to follow up superannuation guarantee obligations.

Ms Vivian—In overall compliance, one of the questions that you are asking is how satisfied we were. We do follow up all complaint cases that we get where employees come to us and advise us that they feel their employer has not been taking out superannuation. We get somewhere between 14,000 to 20,000 complaints a year. At one level, if you took that out of the number of employees out there in the community, you could probably say there is certainly some level of compliance, but there are certain sectors that we do have some concerns about, particularly the micro market.

Senator MURRAY—What do you mean by the 'micro market'?

Ms Vivian—Probably our area of most non-compliance is in the small business area.

Senator MURRAY—'Micro' to me means five employees and less; is that what you mean?

Ms Vivian—Our definition is a bit broader than that, but it is probably small business.

Senator MURRAY—My 'small business' definition is 20 employees or less. Is that what you would suggest?

Ms Vivian—Under \$2 million turnover is where we focus on. That is probably the area that we find is most non-compliant. One of the issues that we do find, without commenting on any specific cases, is our inability to advise employees of the action that we are taking. Maybe

to assist here, if I were to run through what I would call a good case for us, in terms of follow-up work, it can take somewhere between nine to 12 months. By then you are into action. If an employer refuses to pay, then you are into some form of debt collection activity. During that time under our current law we cannot advise the employee as well in terms of any progress on their case. That adds to some of the complaints that you will see coming through Liam Bartlett.

Senator MURRAY—Let me stress that I think the tax office is caught by both law and resources. I am not overly critical of tax office efforts, but I do think the first obligation of the tax office is to try to assess the likely quantum of non-compliance, even if it is just in a designated industry as opposed to the whole employer community, and I would have thought that might be possible if you selected a sample. Let us just say you chose a particular retail sector. If you select a sample and identify the range of non-compliance, which might give you an indication, in a crude sense, of the percentage of non-compliance. Also, before you reply, I always thought that the basic thought behind the broken windows philosophy is right, that if someone is non-compliant in this area you will probably catch them out for being non-compliant in workers compensation or insurance or any other tax area; it will exhibit an attitude which will reflect in other areas which you are concerned about from an integrity point of view.

Ms Vivian—When I talked about our most non-compliant area it was a micro market. It was based on a small benchmarking exercise we took about two years ago. We are actually looking at undertaking a further one. In that benchmarking exercise it was based on 100 or so cases and that identified the micro market as the key area of non-compliance. What we found there was that roughly in that very small benchmarking exercise there was about 40 per cent non-compliance in some of these businesses but we found, of that non-compliance, 50 per cent was partial compliance—in other words the employer had probably tried to do the right thing but got some of the calculations wrong—and the other 50 per cent was non-compliance.

Senator MURRAY—I would break up non-compliance into a timing issue, which is not as bad, in my view, as under payment or non-payment. To pay the full nine per cent late is better than not at all. Did you break up your benchmark into timing issues, under payment and non-payment?

Ms Vivian—No. When I talk about partial compliance, that would have been some areas ranging from not paying the full amount to probably some timing issues, but we did not break it up any further than that. As I said, it is a very small benchmarking sample to help us with our compliance work and it is something that we are looking at doing some more of over the next year or so.

Mr D'Ascenzo—Just stepping back from that, all our intelligence including that benchmark study confirms your initial assumption that there is a level of non-compliance in this area which would warrant further attention by the tax office and it is part of that intelligence that we were able to feed through due processes and which the government responded to and provided the tax office with \$19.2 million over four years to improve responsiveness to taxpayer inquiries regarding the superannuation contribution by employers as part of a wider package of compliance work that we plan to do in this area. The summation of all that is, yes, we think that more work needs to be done there; there is a risk; we have had

extra funding from government and we have also highlighted that as an area of focus in our compliance planning.

Senator MURRAY—Record keeping by many small businesses, as you know, is not their strong suit. If you found somebody was a serial offender, are you able to go back as far as you want, if necessary, all the way back to the original introduction of the superannuation guarantee? Can you do that?

Ms Vivian—With the super guarantee there is no time limit.

Senator MURRAY—You can go back, providing the records allow you to?

Ms Vivian—Certainly we can go back in terms of both records. We also have the ability to raise default assessments. The issue more is whether they have the ability to pay.

Senator MURRAY—As you would probably follow in the general press, there has been a lot of discussion about fees and percentages with respect to superannuation products, and the parliament and the government have been at pains to have discussions and eventually arrived at a situation where they believe the new disclosure regime should be in dollars as well as in percentages, and that comes in on 1 July. I tell you that story because it is apparent to me that many people who will be affected by this are not percentage minded, so they would not know whether they were paid nine per cent, eight and a half per cent, eight per cent or seven and a half per cent. They just do not know. I suspect rather than non-compliance—I just suspect it, I do not know it—that in fact under payment is likely to be the biggest of all problems. This is simply because they recognise that the recipient would not have any idea as to what they are entitled to. Is that instinct of mine accurate or you would not know at this stage?

Ms Vivian—Certainly in the non-compliance cases under payment is certainly an issue. I suppose one of our issues is that, when employees come in to us to complain, it is often at the point of time that the relationship between the employee and the employer has broken down and sometimes the timing also makes it difficult in following up some of these cases.

Senator MURRAY—I made the remark I made earlier about my instinct because the vast number will never complain because they just will not know and what I am afraid of, and no doubt the tax office will have its own views, is that we might be dealing not just with hundreds of thousands of employees but millions of employees who have been underpaid either inadvertently by genuine error, by people who have made mistakes in their returns, or by deliberate malfeasance?

Ms Vivian—There is certainly an element. As I said in our benchmarking exercise 50 per cent was what I call non-compliance, in other words not paying. The only other comment I would make though is, in terms of the complaints that we do get in from employees, there is a considerable amount—it varies a bit, but somewhere about 30 per cent—that when we actually follow up with the employer they have done the right thing. It has sometimes been a timing issue or a misunderstanding by the employee, too. In commenting, with the introduction of choice, there has been a lot of attention in the community about superannuation and we certainly have not seen any sudden growth rate in terms of the complaints that we are getting in, but where we are trying to move our compliance is not focus—certainly deal with the employee complaints as they come in, but there are a few industries that we have concerns in and we would rather move our compliance so that we are

more proactive out there, rather than waiting for the employee to come in. That will really be the attention of our focus over the next couple of years.

Senator MURRAY—I cannot recall the exact figures for the number of small business employees but we know that it is many millions. It might well be six or seven million or maybe more but let us, for argument sake, say 10 per cent had been duded, you would end up with six to seven hundred thousand people who are owed a substantial sum of money. I am just using that for illustrative purposes, but the point of that illustration is a question: when you have reviewed this area again are you likely to release your findings, because I would assume if the Australian population were told that large numbers of them might have been duded, they would then go and check their books, whereas I do not think they are doing that now? That is the question that I am asking you. Will you be releasing the results of your review of this area once you have gone a little deeper?

Mr D'Ascenzo—As a general approach, we have tried over recent years particularly, but progressively over a longer period of time, to be a much more open and transparent organisation and the release of our compliance plan a few years back is an indication of that. What we do with the compliance plan is we actually provide some tracking back of our promises or our commitments to see how well we fared and whether or not our choices in terms of risks have been well placed. So that is one avenue where we will be making our activities more public, but the way I see our active compliance work is not as an after-the-event glut again. It is all about trying to have prevention rather than cure in the process. Therefore, I think publication of what we are doing, why we are doing it and what we are seeing, very similar to the question that Senator Watson asked in relation to self-managed super funds, is very much part of our deterrence, supporting honest taxpayers by signalling the risk areas. Your suggestion of making public what we do in this area and thereby perhaps alerting more employees to their rights and obligations is something that we will pick up.

Senator MURRAY—One of the suggestions I would make to you is that you consider the sort of ready reckoner you have for other areas—and I know ASIC does this—to assist people to check their own superannuation returns to see that the right amount was paid. That is not done at present. That might be a useful assistance.

Mr D'Ascenzo—We will certainly consider that.

Senator SHERRY—What is the money you have indicated in the budget for? How do you intend to use it?

Mr D'Ascenzo—Firstly, as I mentioned, there are two aspects of the changes proposed in the budget. One aspect was in relation to changing the law to allow us to give more information to employees. Part of the funding will be to clear some backlogs that are currently in place with employees who have already complained to us, and yet we have not had sufficient resources to follow up all those complaints.

Senator SHERRY—Is that the super plan provision to issue standard form lost superannuation rollover statements or forms to individuals or is it something different?

Mr D'Ascenzo—No, this is an additional element of the budget announcements under the heading 'Improving the responsiveness of the tax office to employees'.

Senator SHERRY—Yes, I saw that.

Mr D'Ascenzo—Basically, there are two components to this announcement. The first one is to change the level of information provided to employees with regard to their complaint cases. What we are faced now with is a situation where an employee might complain to us, we might be following this up, as Ms Vivian said, but the employee does not know that and we are not able to tell them what we are doing in relation to a third party. It is that level of not knowing what the tax office is doing that is a serious angst to people. They have made a genuine complain and they just do not know how that is progressing or if it is progressing at all.

Senator SHERRY—We have discussed this before. You cannot inform them at the moment, as I understand it?

Mr D'Ascenzo—That is right.

Senator SHERRY—I have raised the issue with Mr Carmody—

Mr D'Ascenzo—That is right.

Senator SHERRY—who stated that that should be removed. Is that what is proposed to be done, is it?

Mr D'Ascenzo—That is right. I think that is a positive announcement. The second side of it is addressing the current backlog. The funding for this backlog is for two years only, 2006-07 and 2007-08. Some of that money is to clear up existing complaints and then to add that extra funding to our already current plans to do more in this area. As I mentioned to Senator Murray, we had identified this as a risk area that we wanted to focus more attention on over a three-year period.

Senator SHERRY—Can I bring to your attention a truly shocking case. I can give you the name, because I have authorised to do so. It concerns a Ms Sue Underwood, of 39 Binalong Road, Mornington. Let me give you a brief summation of what is an incredible saga. Six years ago, in July 2001, she was employed by a firm known as Ridler & Walker, and Ms Underwood notified of insufficient employer contributions and lodged it with the Australian Taxation Office. On 8 August 2001 she received a confirmation letter from the ATO, case number MPOSPR8553/0118, received by a Mr Wilson. On 13 August the superannuation audit from the ATO was received by Ridler & Walker. In August 2001 the audit was completed and sent to the ATO. On 30 August 2001 employee notification of insufficient employer contributions was lodged with the Australian Taxation Office re Ridler & Walker for the period 1 August 1996 to 3 July 1998 by Ms Underwood. There were some other employees as well involved in this. A confirmation letter from the ATO, case number, was received by Ms Underwood on 3 September 2001. From 1 March 2002 to 11 June 2004, 10 phone calls were made by Ms Underwood to the ATO to see how the case was going. No news, no response. She was advised on the last phone call to go to her member of parliament or to the local ombudsman. On 11 June she rang my good friend Mr Harry Quick's office and was advised that the ombudsman would handle it. On 23 July 2004, the ombudsman, Mr Farley, rang—no news yet. On 7 December 2004, she rang Mr Farley, call back. On 17 December 2004, she rang Mr Farley—waiting on the ATO. On 18 January 2005, faxed Mr Farley copies of initial ATO letter confirming notification and case numbers. On 8 February

2005, Mr Farley rang—still waiting on the ATO. On 7 March 2005, Mr Farley rang—still waiting on the ATO. On 16 of May 2005, Mr Farley sending case to a senior tax officer in Canberra. On 9 June 2005, rang Mr Farley, who was asking the ATO more questions, awaiting response. On 18 August 2005, Mr Farley going away for six months, will pass the case on. On 23 August 2005, contacted the ombudsman's office. Someone to ring back from the tax office. No-one rang back. On 24 August 2005, Mr Anderson, principal investigation officer for the Commonwealth Ombudsman, will be finally conducting talks with the ATO. On 2 September 2005, a letter from Mr Anderson, satisfied with the ATO taking appropriate action, told to wait another six months. On 4 April 2006, emailed Mr Rohan requesting him to reopen the case. Email from Mr Snoxall, the senior investigation officer, Commonwealth Ombudsman, taking over the case and making further enquiries with the ATO. It just goes on and on, and she still has not got her money.

Mr D'Ascenzo—I do not know what that sort of situation is.

Senator SHERRY—Five years with the ATO, two years with the ombudsman and she is still waiting for unpaid contributions for the period between 4 July 1998 to 31 August 2001. On top of that, this fellow Ridler is still in business, still employing other people. In addition, I am told he was a trustee of the Quadrant Superannuation Fund, which covers local government employees in Tasmania. This fellow, an employer, has evaded paying his responsibilities for more than five years, and you still have not got him; he is still in business.

Mr D'Ascenzo—I do not have knowledge of the case.

Senator SHERRY—That is why I am outlining the details to you, because this is truly outrageous.

Mr D'Ascenzo—We do not know the background to it.

Senator SHERRY—I have given you the background and I am asking you to look at it.

Mr D'Ascenzo—I am sure we will.

Senator SHERRY—Under the current law, you cannot come back to me or to her, can you?

Mr D'Ascenzo—No. But that is why we probably suggested that people approach the ombudsman. They may have a different opportunity to provide information on our processes.

Senator SHERRY—I have the letter from the ombudsman here. I think there is a reference here that the ATO could not provide him with anything beyond general information and could not provide him with specifics of the case.

Mr D'Ascenzo—The ombudsman has an opportunity to check on our process and has access to all of our information, files, procedures and the lot. I do not know what is behind that case. These are situations where the proposed changes to the law should enable—

Senator SHERRY—Why have you not instituted legal action for recovery?

CHAIR—Let him finish. Mr D'Ascenzo, you finish your answer.

Mr D'Ascenzo—You mentioned about the 10 phone calls between 2002 and 2004. With the change in the law we are able to provide a progress report to the taxpayer, and that will be helpful because I think the concern here is that nobody at the moment, including myself,

knows exactly what has happened within that period of time and what the facts and circumstances are. I think that is going to be helpful in terms of trying to ensure that there is communication, and that will help ensure that things are not delayed any longer than they need to be.

Senator SHERRY—I accept that and I have long argued for that change, but the fact is that at this point in time no recovery action in terms of legal action has been taken against Mr Ridley five years on.

Mr D'Ascenzo—Again, I do not know the case and I do not know whether or not the claim is substantiated.

Senator SHERRY—You will assure me you will follow this one up?

Mr D'Ascenzo—Yes.

Senator SHERRY—In respect to moneys that are recovered and are credited to the superannuation account of an employee who has complained, after you have recovered the money is the employee then notified of the payment to their superannuation fund?

Ms Vivian—Yes, the employee is notified. One of the issues at the moment is that when we receive the money from the employer we then pass the money through to the nominated superannuation fund and we then have to wait about 30 days for the fund to confirm that they have either accepted the money or else they have sent it back to us. It is at that point of time that we notify the employee that we have now received the money.

Senator SHERRY—Is there any backlog of notifications at the moment?

Ms Vivian—Not to my knowledge in terms of notifications, no.

Senator SHERRY—In the previous estimates this time last year, I think it was, there was a discussion about moneys that had been recovered but there was a delay in payment due to a systems problem.

Ms Vivian—Yes.

Senator SHERRY—Where are we with that? Has that systems problem been cleared up?

Ms Vivian—In the most part I would say yes. There are a few outstanding cases that have some quite complex problems with them that we are clearing up over the next couple of months. We have about 1,027 accounts that we are clearing up over the next two to three months. Those are the only issues that were still held up from that problem.

Senator SHERRY—As to those individuals, for what period has the money been outstanding? The tax office has collected it.

Ms Vivian—Yes.

Senator SHERRY—When was the money collected?

Ms Vivian—It would vary considerably amongst those individuals. I think one of the issues is that these are quite complex cases with quite a number of different problems but certainly, as you are aware, in some of the cases where we held money for an undue period of time we were then paying compensation for the lost interest. If it applied to these cases then we will be paying that as well.

Senator SHERRY—Going back to my earlier question, when you notify an employee that moneys that you recover are placed in the fund, do you notify them of the period for which money has been recovered, because it may not be the totality of the amount owed?

Ms Vivian—I would have to confirm that but I would surmise that we would notify them of the period of time, for what period and for what money, but I can actually take that on notice and get the actual wording that we use.

Senator SHERRY—I am informed that at least up until now you have not been able to pay money—let us take a person who is over 65 and, the way Ms Underwood is going, she will be over 65 by the time she gets her money. So it is not an unusual situation. You turn 65, you have retired, you have collected your super and you no longer have a superannuation account. What do you do in those circumstances?

Ms Vivian—In those cases, if they reach the preservation age and are eligible, then we would pay the money directly to the person. Sometimes in those cases the money comes in from the employer. Let us say we pass it through to the super fund. For some reason the employee is either, as you said, no longer with fund, they have retired, the fund—

Senator SHERRY—Probably, the way things are going, some are dead.

Ms Vivian—In some cases the fund would pass the money back to us. We would then contact the employee. In those cases then we would remit the money to the employee.

Senator SHERRY—So that is what occurs. If there is no fund because the employee is no longer in a fund—

Ms Vivian—If they have effectively retired because—there may be another issue where, if there is no fund but they are working somewhere else or they have rolled their money over to another fund, it just varies on the circumstances.

Senator SHERRY—So you will pay it direct to them in those circumstances?

Ms Vivian—That is my understanding, yes.

Senator SHERRY—You did provide some figures on notice about the amounts of money unpaid that are being wiped off, for want of a better word, that cannot be collected. You provided me with the figures that, for example, in the 2000-01 financial year there was \$3.8 million in super guarantee contributions that could not be collected presumably because the employer has gone bankrupt or whatever. To what period did those moneys relate? So, for example, 2000-01, did that relate to the previous financial year or is it just an amalgam of moneys over a number of previous years that you have just come to the conclusion you could not collect?

Ms Vivian—It would be an amalgam of money over a variety of different years.

Senator SHERRY—I notice from those stats that the amount of money that was being wiped off, if you like, and just not collectable, increased significantly. For the period December 2003 to June 2005, \$84 million was wiped off. Over what time period was that money owed, over a couple of years? Do we have any period it relates to?

Ms Vivian—No. Again, it would vary. It would be an amalgam over a number of years. I would surmise it is probably fairly old debt and that we will find that it was both irrecoverable and uneconomical to pursue to collect.

Senator SHERRY—What is the level of debt at the present time, or the last time for which you have figures that you have checked?

Ms Vivian—I would need to take that one on notice.

Senator MURRAY—Just before we resume this topic, I have a question I meant to ask you, Ms Vivian, but maybe Mr D'Ascenzo is better for it. It is obviously in the interests of the super fund institutions and so on to maximise the funds coming in. Do they blow the whistle or raise issues with you that they suspect certain employers are not complying, or are they used at all as allies in trying to get compliance? Is there any cooperative way in which you can use their systems and so on?

Ms Vivian—We do work quite closely with the professional bodies. We have a consultative forum that meets four times a year. That is a forum where they raise a number of issues with us. There are some other different forums that flow from that in terms of either technical issues through to compliance issues. We also work closely with them about education as well in terms of getting messages out and working jointly on that as well.

Mr D'Ascenzo—We have not seen funds specifically coming in to provide the information that you mentioned.

Senator MURRAY—I would hope that they would be active partners. There are two sides to that question: one is whether they do it voluntarily or, secondly, whether they need to be either incentivised, to use that new word, or legislated to assist.

Ms Vivian—At a broad level they will raise with us that they might see an area of risk across the industry, they might ask us for our view or might indicate that scenario which we would be looking for compliance. What I have had raised with me is more at an individual level where it might range from a financial planner, an agent or someone will come in with some concerns where they might be what we would classically call a dob-in, where there would come in and talk to us about some specific areas of non-compliance.

Senator MURRAY—A simple systems process would be an age analysis, for instance, because they know when they are being paid. A simple age analysis would determine whether payments are coming in on time, for instance, which is one element of compliance. Do they just keep quiet about that or do they raise it with you?

Ms Vivian—They have raised that with us in some discussions. It can be an interesting dilemma for them in that they follow up debt collection for, say, some non-payment of superannuation. The issue is, of course, as well that the employer becomes potentially applicable for superannuation guarantee charge.

Senator MURRAY—Sorry?

Ms Vivian—They may be following up where an employer has not paid its superannuation. They have debt collection activity that follows up with that employer to get the superannuation paid. I suspect one of the dilemmas they have is that they get the money that is paid through to their fund late and it also means that that employer is—

Senator MURRAY—Potentially liable for penalties?

Ms Vivian—Potentially liable for superannuation guarantee charge. If it is paid within the 28 days after, they can apply the amount of money they have paid against the superannuation guarantee. That is one of the issues that they face.

Senator MURRAY—Are there substantial numbers of complaints that do not come to the tax office and that go direct to the super funds. Do the super funds then pursue those debts and not advise you of the failure to comply?

Ms Vivian—I am certainly not aware of what complaints go into the super funds, but I am aware that some of the funds, particularly industry funds, certainly follow up closely with the debts. One of our compliance activities that we are starting to look at is how we might be able to work more closely with them in the future to work together in terms of non-compliance in this area.

Senator MURRAY—Perhaps you can correct me, but it would seem to me that, under the law, there is at least a moral obligation—I would be surprised if there is not a stronger obligation—for the fund to tell you, because of your responsibilities under the act, that an employer has failed to comply with the superannuation guarantee legislation.

Ms Vivian—What you see is that the funds generally have, effectively, a contract with the employer, and they are following up with the employer in terms of the lack of superannuation payments into their fund under their contract.

Senator MURRAY—I am not satisfied with your responses. The reason I am not is that my understanding of the legislation is that the penalties for non-compliance are deliberately set by the government at a very stringent level.

Ms Vivian—That is right.

Senator MURRAY—Therefore, where someone knows that an employer is not complying and they are part of the triangle—I do not mean a busybody, but as part of their function—they should be telling you. Has this matter been discussed as a policy issue?

Ms Vivian—I am not aware that it has at a policy level, but in terms of our present and future compliance action we are looking at where we can work more closely with the funds in that area to improve our compliance.

Senator SHERRY—Where an individual complains and the tax officer visits the employer and puts them through an audit process to identify the figure, the ATO would then issue an assessment notice, would it not?

Ms Vivian—Firstly, when an employee complains, we look generally at all of the employees of that employer. When we go in to talk to the employer, we may look at offering them voluntary compliance. They then fill out a superannuation guarantee form and we issue an assessment based on that. But if they do not assist us with that process, we would raise an assessment on them.

Senator SHERRY—What is the average time that it takes to issue the assessment notice?

Ms Vivian—At the moment, on average we do about 46 per cent of the cases in eight months.

Senator SHERRY—Sorry?

Ms Vivian—In eight months.

Senator SHERRY—So it takes eight months to issue the assessment notice from the point at which the conversation or inspection has taken place with the employer?

Ms Vivian—Yes.

Senator SHERRY—Could I suggest that that is not good enough?

Ms Vivian—No, and that is one of the things, in terms of the additional funding from government, we are trying to improve. I will use a case to show you the difficulty. On day one, an employee might contact the tax office and say, ‘Look, I do not think my employer has taken out the money.’ We have a chat, talk to them and get the details. At the moment, it may be somewhere between two and three months before we might actually commence a more formal audit investigation; we are looking to close that gap. Let us say, at three months we contact the employer. At that time, often the employer may not want to give us the information over the phone and may ask for us to send them out the questionnaire. If we send them out the questionnaire, they normally have 21 days to fill that out. Often, they will ring up after 21 days and say, ‘Can we have an extension of time?’ All of a sudden, you are into another two or three-month delay just in terms of determining the information from the employer. Whether we can then raise an assessment is dependent on the quality of the information that comes back. If the employer has been compliant, has gone to the fund and has good records, that helps us. If they have not, then it may take us another month or two in terms of working with both the employer and the fund to obtain that information.

Senator SHERRY—I do appreciate the difficulties you could run into, which you have outlined, with some employers. There would be some, I can appreciate, given what you have outlined, where it might take longer than eight months. It is the average time of eight months that concerns me.

Ms Vivian—That is where we are looking to try and change some of our processes. Firstly, we are trying to move more to phoning and working with the employers. In terms of what I call low-risk employers who do not have a history of non-compliance with us, we will get on the phone and offer voluntary compliance with them. I am also looking for how we can assist the employers in getting the relevant information that they need as well, so that we can try and reduce the time it is taking us.

Senator SHERRY—So far this financial year—you may not have the data, but for the previous financial year—against how many employers has legal action been taken for the collection of unpaid superannuation contributions?

Ms Vivian—I would need to take that on notice, because I think it would be combination. In some cases, we do take prosecution action against employers. That is in terms of providing us with the information.

Senator SHERRY—Yes.

Ms Vivian—The other part of your question is legal action in terms of debt collection.

Senator SHERRY—To collect the money.

Ms Vivian—Yes.

Senator SHERRY—Debt recovery.

Senator MURRAY—But you do not have to take legal action to apply the penalty, do you?

Ms Vivian—No. But to raise an assessment you need a certain level of information. If an employer—and, fortunately, this is the smaller group—refuses to respond to our questions, sometimes we need to take legal action to obtain just the basic information so that we can raise the default assessment.

Senator MURRAY—I understand that. But there are people who pay up, where you apply the legal penalty and no legal action is involved.

Ms Vivian—That is correct, yes. We aim to move more to that, because it is a much quicker process and a better outcome for the employee.

Mr D'Ascenzo—In terms of the comment about not being totally satisfied, I read that to be that this is an important area and that there is a genuine belief that more can be done in that area. We agree with that. In fact, what we are trying to do is to strengthen our processes and improve them. We, too, believe that if we can shorten those time frames and also perhaps take up some different ideas—and Senator Murray gave us the idea of doing more work with the funds themselves, looking at this issue afresh, with the funding that we have now been provided—we can make improvements in that area.

Senator SHERRY—Just going quickly back to this issue—

Mr D'Ascenzo—Would Senator Parry like an answer to his question now?

Senator SHERRY—Can I just conclude this area of superannuation?

Mr D'Ascenzo—By all means.

Senator SHERRY—I have a bit more to go through, as well as on general tax. In terms of the figures that you have provided on notice about moneys wiped off and that you cannot collect, could you take on notice what is an average figure that is wiped off per year as uncollectible? The figures that you have provided vary so much. I appreciate what you did provide. There is no relationship with the period where the debt is outstanding. In one sense, your figures were a bit misleading, but not deliberately so. It gave the impression that, as I say, in 2000-01, there was \$3.8 million, and it jumped to \$84 million in December 2003 to June 2005. It looked like there was a massive increase in moneys wiped off. Could you work out an average figure for me that is wiped off per year?

Mr D'Ascenzo—And some explanation of why the differential?

Senator SHERRY—Yes. I suspect that the amount is going up, but it seems to me that the figures that were provided gave a somewhat skewed picture.

Mr D'Ascenzo—It may be that it is just a backlog of write-offs all in one year for prior periods.

Senator SHERRY—Yes, that is right.

Ms Vivian—In terms of that increase, there are two elements that might help to explain it. Firstly, in 2003 the actual amounts we started recording started to include both the penalties and the GIC involved. Prior to that, the amounts had not. Secondly, from about July 2003 we started putting a lot more resources into quite specifically looking at superannuation guarantee debt and cleaning up the old debt. Up to that point, the focus on the debt had been more where the superannuation guarantee was part of a composite debt. That is another reason why you are seeing such a major increase in terms of debt write-off; cases are being cleaned up.

Senator SHERRY—In taking that on notice, you might indicate for the periods the number of employers approximately—you know how reasonable I am; I would not hold you to the nearest employer—and the approximate number of employees for whom a debt has been uncollectible.

Mr Konza—Earlier this afternoon Senator Parry asked some questions and I was wondering if I could take the opportunity to answer those. Thank you for your questions. From the work you have done, it was apparent that I had some sort of problem but I was also bemused because it had not been raised with me before now and so I had my people do some checking. The way the system works for the benchmark interest rate for deemed dividend provisions is that, as we discussed last time, the bank variable housing loan rate published by the Reserve Bank is taken to be the rate. In that respect, the rate is set without any action by the ATO. But as I indicated last time as well, each year we publish a tax determination to inform the community of what that rate is. In fact, we did publish that tax determination on 29 June 2005. It was tax determination 2005/31. The publication of that tax determination was not notified on the website and that is why you were unable to find it. That is our error and I will have it corrected. However, the publication of the tax determination would have been picked up by the professional associations and tax writers, and so that is why I had not heard before now from the community that they could not find the rate; it would have been picked up on the other information services. Those who could not find it, obviously as yourself, were able to ring up as well. As you said, the website is generally comprehensive but, due to an oversight, the figure for the 2006 year was missing. I apologise and thank you very much for bringing it to our attention.

Senator PARRY—Thank you, Mr Konza. I appreciate that. Especially when the page is headed ‘Benchmark interest rates’, that is the easiest way to find it. It is only a minor issue, but I am sure that will solve some problems for some constituents.

Mr Konza—We will make sure we do not miss it again.

Senator MURRAY—I move to the next topic. This might be a difficult one. You might have to take it on notice. I do not think it is a major issue but it alarmed me as an inconsistency. The Tax Laws Amendment (2006 Measures No. 1) Bill 2006 was passed at the end of March this year. One of the schedules was to provide exemptions from Australian tax on non-Australian source income for individuals who are temporarily residents of Australia for tax purposes. The bill defined a ‘temporary resident’ as the ‘holder of a temporary visa, not previously being an Australian resident within the meaning of the Social Security Act 1991’ and, thirdly—and this is the one I want to draw to your attention—‘is not married to an Australian resident’. The difficulty I have is that I think it means that you are not exempted if you are married to an Australian resident but if you are in a de facto relationship you would

be. The intention of this exemption is to make it that people who are absolutely temporary are the ones affected. What I would like to ask you, and I do suspect it will have to be on notice, is: would you be able to pick up that people are getting this exemption who are in fact in a de facto relationship with an Australian resident? Because to my mind, if you cannot get it when you are married to an Australian resident you certainly should not get it if you are in a de facto relationship.

Mr D'Ascenzo—It is a bill that Mr Callaghan might be—

Senator MURRAY—It has been passed. It is an act now.

Mr D'Ascenzo—I am not sure how as a matter of compliance we would follow that up. It would be very hard to administratively follow up those issues, but there are other areas in the law where that is the requirement.

Senator MURRAY—The easiest way would have been for the law to be amended so that it applied to someone whether they were married or in a de facto relationship and then that is easy. I do not know how large the mischief will be.

Mr D'Ascenzo—If the government were to make a change, we would put an extra box in our application form that says, 'Are you in a de facto relationship?', as we would in other areas.

Senator MURRAY—You probably would need to identify to the government that there is an inconsistency and a problem and that there is some revenue loss as a result. It just struck me as an odd one.

Senator PARRY—The taxation department does not set as to who—

Senator MURRAY—If you are raising a point of order, you can raise it. But it is for the chair to rule, not you.

Senator SHERRY—The minister can intervene.

Senator MURRAY—And the minister can intervene. I am going to move on to another issue, if I can, Operation Wickenby. I do not want any operational details or anything you should not give me that might upset the apple cart, because it all sounds very exciting, the progress you are making, particularly with the latest court case. What I am interested in is how long you think it will be before the stages of investigation are likely to be concluded so that the prosecutor could examine the issues? That is, of course, predicated on two things: firstly, any legal impediments that may be put in your way; and, secondly, the difficulty of the pursuit itself.

Mr D'Ascenzo—It is a good example of collaboration and cooperation by the five government agencies that have been working together on that project, including the Australian Crime Commission, the Director of Public Prosecutions, the Australian Federal Police, ASIC and the ATO. A lot of work has been done and is being done, and I am advised by the ACC that they are hopeful that in the second half of this year they will be in a position to lay charges. That is not to pre-empt further investigations and further work done under that approach. We have a regular meeting of senior people from those organisations. I have the privilege of chairing those meetings. Certainly we are very conscious of the need, in accordance with the law and the facts and evidence that are provided, to send clear signals

about behaviour that we think is contrary to the law and about the fact that the Commonwealth, as the Commonwealth, will take firm action in relation to fraudulent behaviour. We are very keen for that to occur and to occur quickly. It is pleasing that the latest legal hurdle to the ACC, in terms of the use of its powers to get information, was disallowed by the courts, giving the ACC a clearer run to pursue the ultimate goal. So I, too, am quite excited that in the second half of this year we will see some charges.

Senator MURRAY—The federal government announced in January—in fact, it has happened, as far as I am aware—that it would be injecting \$300 million into Operation Wickenby. That is obviously over and above those funds that are already available to the agencies for investigations. That is a substantial amount of money. That was not just for the tax office, was it, that was for all the agencies involved?

Mr D'Ascenzo—That is right, that is for all the agencies. I think the tax office did get the major share of that to provide basically more investigators on the ground, including an increase in our legal capability and also an increase in our debt collection capability. Operation Wickenby is not just looking at one approach to solving these problems but trying to use the whole arsenal within the Commonwealth powers, including proceeds of crime, which have already been used in one case, and our own tax powers, which have been used in other cases, as well as criminal charges laid by the police and the ACC. I might have a breakdown of that. I will check my papers.

Senator MURRAY—There was no additional money put into the budget for this, was there? I do not recall any.

Mr D'Ascenzo—I am not sure.

Senator MURRAY—There was that January injection, which I think was sufficient.

Mr Callaghan—Yes.

Senator MURRAY—You were going to give me a breakdown, Ms Martin?

Ms Martin—I do not have a current breakdown between agencies. I can confirm it was mentioned in the budget, but it was the same amount that was announced in January, about \$305 million, for the agencies over six years.

Senator MURRAY—This is my last question with respect to Operation Wickenby. An article by Michael McKenna and Michael McKinnon in the *Australian* on 29 March 2006 stated that documents filed in the courts alleged widespread criminal behaviour. In other words, it was not just an issue of tax, and that is why those other agencies were concerned. They were said to be investigating illegal activities, including tax evasion, money laundering, drug importation and so on. I do not want to go into those details with you; I do not think that is necessary. Is it your expectation that this operation will indicate where there might be still some integrity issues to address—in other words, loopholes and mechanisms in the law that have been utilised to allow people to behave in a corrupt or criminal way?

Mr D'Ascenzo—What we are seeing in this area is not so much a clever use of the law but the use of the overseas leg to conceal and hide or to dress up things as something other than what they are. It does get to a range of fraudulent or evasive practices in some of the cases that we have seen. The use of back-to-back loan arrangements, the use of repatriating money

that is earned by an Australian resident overseas into Australia through some sort of gift or other non-taxable form—these are not things that affect the legislative base. It is really a level of behaviour that is contrary to the law, if those are proven to be the facts. I am positing the allegations that we are currently pursuing. There may be other things coming out of that exercise. The fact that we have had a range of legal challenges on the powers of the ACC that the courts have said are not viable has confirmed the powers of one of the Commonwealth agencies in dealing with these sorts of matters. The fact that we are working together in a cross-agency group is a new way of doing things that helps Australia's capability to respond to these sorts of practices.

There may be things that could feed into legislative change. If that were the case, we would certainly refer it through Treasury or through the Attorney-General's Department, depending on the nature of the change, as appropriate. But at this stage, within the narrow confine of the Operation Wickenby exercise, the allegations are more rudimentary than some sophisticated use of overseas elements. Operation Wickenby is not the extent of the scope of the work both by the Australian Taxation Office or by other law enforcement agencies in relation to the use by taxpayers or promoters of jurisdictions outside Australia. Some of those other areas may have questions of deficiencies in relation to our tax law. In fact, those deficiencies can be contrary to the policy intent against taxpayers or contrary to the policy intent against the revenue. Either way, our process is to advise Treasury of those to put them into possible consideration for legislative amendment.

Senator MURRAY—I asked you the question deliberately because, as you are aware, the justice minister is consulting presently with a view to finalising anti-money-laundering legislation by, I think, August. I just wanted to be assured that you have a process whereby, if there were any things you found that mattered with respect to that legislation, there was a process of feeding it through. You have assured me that that is happening.

Mr D'Ascenzo—Yes. And that is not just on this. The way I see the tax office role is that, as we do our work, we will find situations where on the ground either there are practices or laws that do not reflect the underlying policy, and that can be for taxpayers or against taxpayers. Either way, in an even-handed way we try to provide that advice to Treasury in terms of what might be done to provide a more coherent fabric of law to reflect the government's policy intent.

ACTING CHAIR—My question concerns what constitutes retirement for purposes of the superannuation contribution splitting, often referred to by the acronym SCS. I am conscious that eligible fund members can begin splitting on or after 1 July 2006. I draw attention to the fact that there is a different interpretation offered by APRA to the Australian Taxation Office and I am conscious that it would be helpful if this difference could be resolved before 30 June. We have recently had separate documentation produced by both APRA and the tax office and there appears to be a different interpretation on what constitutes retirement for the super contribution splitting purposes. On initial reading it would appear that the ATO's Nat 15237 has a much narrower view than the APRA interpretation. My understanding is the tax office views on retirement for those aged 60 and over would appear to be a lot stricter in that once you have ceased a gainful employment relationship once you are over 60 you have retired for

SIS A93 purposes and cannot therefore be a superannuation contribution splitter recipient. APRA's view is a lot wider. I refer to their circular LA.1, where they state:

Eligible superannuation contribution splitter recipients include: a spouse who is (1) under the age of 55; (2) aged between 55 and 64 and currently gainfully employed for 10 or more hours per week; (3) aged between 55 and 64 not currently gainfully employed for 10 or more hours per week but has not yet decided that they will never resume gainful employment for 10 or more hours per week; or (4) aged between 55 and 64 and has never been gainfully employed for 10 or more hours per week.

I believe that as such, on a reading of those two definitions, there does appear to be a quite significant and fundamental difference between the Taxation Office and APRA in terms of their treatment of retirement for superannuation contribution splitting. I presume the tax office is aware of these differences. But in view of the need to treat all splitters the same, whether they are under APRA jurisdiction or under ATO jurisdiction, I think it is in the interests of equity, fairness and good legislation to ensure that there is that complete harmony. Could I have a comment, please?

Ms Vivian—I am aware that we are discussing with APRA about that issue and we have raised it with Treasury. I can take it on notice to provide where we are at with it. Our aim would be to reach a consistent definition with APRA on that issue. My understanding is it is still under discussion, but we simply need to resolve it fairly quickly.

ACTING CHAIR—Yes. Will that resolution be well before 30 June?

Ms Vivian—I would hope so, but I need to check where we are with those discussions in reaching it. We need to have it before 30 June because it is after 30 June that people need to make their decisions about what amounts they split. Our intention would be to have a consistent definition with APRA.

ACTING CHAIR—Before then?

Ms Vivian—We are working towards that.

ACTING CHAIR—Within the next few weeks?

Ms Vivian—I would hope so. My only issue is that there does seem to be a bit of discussion here and we are raising it with Treasury. I will certainly be following up on it to make sure that we follow through on it.

Senator MURRAY—There is a serial emailer to senators—and I try not to pay too much attention to them because once they become serial you get a little less responsive. But she did raise a serious issue about TFN withholding taxes being debited from a youth's account, in other words, somebody below 18 who did not have a TFN and was in full-time study. Is that an issue? Is that something to be concerned about? It struck me as strange that somebody who did not have a tax file number because they were in full-time study would still have a withholding tax taken from them by the bank.

Mr Callaghan—Well, if that is the application of the law. I am not sure what the law is, if there is any deviation in terms of its application to students.

Mr D'Ascenzo—I do not think there is. I think students can apply for a TFN if they think they are going to derive income that could be subject to withholding. In fact, you have a lot of people who do odd jobs and they will get a TFN to ensure that there is no withholding.

Senator MURRAY—So the remedy is for the student to apply for a TFN and then get the rebate?

Mr D'Ascenzo—That is right.

Senator MURRAY—It is as simple as that. There is no onus on the bank to actually say: 'Look, we have no record of a TFN from you. If you do not have one, you should apply for one'?

Mr D'Ascenzo—I do not think there is any onus. That would be the remedy.

Senator MURRAY—I should address the issue to the bank ombudsman to raise with the banks?

Mr D'Ascenzo—Yes.

Senator MURRAY—Mr Konza, you answered a question that was taken on notice from the additional estimates on 15 February, topic AT83 *Hansard* page E61-62, on tax return lodgment benchmarks and the new business area lodgment compliance and so on. You gave quite a full answer, for which I thank you. You outlined the pilot project and the compliance records you are reviewing. Do you have an update as to progress in this area or anything to add to your previous answer?

Mr Konza—On that particular occasion, I was pinch-hitting for a colleague. That colleague is here tonight, so Mr Reardon can answer the question himself.

Mr Reardon—The answer that Mr Konza gave last time went to a number of projects and some of our approaches in detecting the people who do not lodge. You asked about whether we had benchmarks of non-lodgers. As Mr Konza said last time, one of the difficulties we have is that the commissioner prescribes by legislative instrument the categories of taxpayers that are required to lodge a return. So, by definition, the people who do not meet those requirements are not required to lodge a return. The difficulty we have is establishing who has a requirement to lodge and following up those who have those requirements. As Mr Konza said last time, we look to sources of information from outside the ATO to give us an indication of activity or an indication of income, and the response that we provided to you in the question on notice went through some of those activities. As the response said, in the large market segment we continue our work there, following up all entities. When I talk about large market I talk about entities with a turnover of over \$100 million. To date, as at 30 April, we have secured lodgment of over 2,500 activity statements and 770 income tax returns. The liabilities that we have established as a result of those lodgments is just over \$46 million. So that is one area.

We also have an aspiration to follow up all entities in the small-medium enterprise market—that is enterprises with a turnover of between \$2 million and \$100 million. We have had quite a significant impact in that market, following up income tax returns and activity statements. Just in the period February to April we have raised over \$94 million in liabilities associated with lodgments in that market.

Some of the other areas we have looked at are income tax returns who have a significant liability, over \$20,000, and we continue to follow up those activities. We have looked at our high-profile taxpayers across a range of occupations and professions, including the legal

profession. We have updated all our information from outside the ATO in terms of the legal profession—the solicitors, barristers, judges and magistrates. We will look further at their 2005 lodgment patterns. We have looked at information from mortgage providers around low documentation loan recipients and followed up people who have not lodged who have received those sorts of loans, on a priority basis.

We are also looking at entities in the microbusiness area who are working in the cash economy. To date, we have secured over 2,500 income tax returns and raised liabilities over \$6 million from entities that we have got lodgment out of in the micro business area. So that is just some of the activities. There are other things we are doing as well, but that goes some way towards answering your question.

Senator MURRAY—It sounds like impressive progress. In your answer you said in your last paragraph:

Non-lodgers are followed up according to risk and more information on those individuals and businesses we are examining are identified in the tax office's compliance program 2005-06. We expect more of our successes will be highlighted in the commissioner's annual report for this year.

When you do your annual report, rather than just being illustrative, which is what is implied by saying 'more of our successes will be highlighted', could you be more analytical? I will give you an example. You refer to obtaining information on approximately 350 recipients of low documentation loans. You have found that around 50 per cent of these people had outstanding income tax returns so you extended the work and, to date, a further 20,000 taxpayers were selected for compliance action. What I would like to see in the annual report, if you are going to report on it, is a detailed tabulated response: you went after 20,000, you found that 4,000 had to put in income tax returns and the money generated was so many million. Will you take that on board? I know your annual reports are very demanding documents.

Mr Reardon—Certainly. The commissioner has made clear he wants us to be transparent and share our results, I think as you have described, in an analytical way to show our detection methods as well as our successes in obtaining lodgments.

Mr D'Ascenzo—I have some information here. Mr Reardon spoke about activity statement lodgment performance, and indicated a whole range of things that we are doing to improve on that. It goes to the prevention rather than cure concept. Lodgment in 2001-02 on time was around the 70 per cent mark and, over time, we have now raised it to around the 80 per cent mark. So that is a 10 per cent increase over a four- or five-year period, which I think is very significant in tax terms. That to me is a better indicator than '100 of these and 200 of those'. They can be efficiency measures and an indication that we are active in this area, but it is all about trying to ensure that those people that want to do the right thing are able, advised, equipped and find it easy enough to do it, and to encourage and deter others so that you have a higher rate of voluntary compliance at the end of the day.

Senator MURRAY—That is true. I think it is to be commended. That is a very significant improvement. My concern has been those who sit outside the tax system. As you know, when the ABN system and the GST system were introduced there was hope that people would be pulled into the system. But that actually seemed to result in a decision by some to try and

remain completely outside of the system. Therefore, non-lodgment activity is very important to closing that cash economy or non-compliance sector.

Mr D'Ascenzo—I understand and I agree.

Senator MURRAY—That is why I raised it on that basis. I just want to return to a previous issue. You may like to think about these answers, as to whether you want to give them now or would like to think about it and come back later. I will give you four questions on the Wickenby matter which we raised earlier. I am very sensitive to the issue of not intruding upon the operational side of things. I will put them to you and you can see how or whether you would respond. The first question is: do you anticipate further proceeds of crime action shortly and, if that happens, is there any fear that it could jeopardise any criminal actions by telegraphing the case? The second question is: are any settlements likely to be reached in the near future and have any been reached?

Mr D'Ascenzo—The whole idea was to try to use a whole range of weapons in the arsenal available to the Commonwealth. I suspect that there will be more situations where we will use proceeds of crime. That will be done in conjunction with the other agencies to ensure it is a coordinated approach that does not cause any strife or harm to other approaches that are being taken. So it will be coordinated. I do expect us to be very active in that area. Your second question—

Senator MURRAY—Are settlements part of the range of options you are considering?

Mr D'Ascenzo—We have already had 18 voluntary disclosure approaches. We have had two settlement offers. We have made 250 requests or demands for information. We have demanded 2,400 lodgments. So there is a range of people, and that will work its way through, depending on the facts, on how we will proceed with these matters.

Senator MURRAY—The rough figure was that about 500 individuals were involved. Is that still the rough number?

Mr D'Ascenzo—You have to remember this is a project that has its own confines but, in a sense, it is not the whole picture. In relation to this particular project, I am not sure about the numbers involved.

Ms Martin—Just as a general scale, it is still anticipated the total could be up to 500 Australian residents. As the commissioner has said, it has a broad range of scope. In the potential criminal range there are nine groupings which involve about 38 individuals.

Mr D'Ascenzo—This is allegedly; it depends on the facts, ultimately.

Ms Martin—That is right—that are being looked at under that guise. Then there are high risk for revenue issues, and there are 32 groups there that are being looked at, involving 65 individuals. There is a further grouping where additional information has been sought. There are about 120 individuals there. There have been a number of letters and calls received, as the commissioner said. There have been 18 voluntary disclosures. There was also the identification of a large group of noncompliant through the process, where 2,400 demands for returns have been made. We are also aware of other international promoters as well. That gives a sense of scale and that it is part of a wider range of issues.

Senator MURRAY—You mentioned revenue. I see two aspects to this. One is punishing people for breaking the law, but the other one is recouping revenue if you can. Are you anticipating substantial revenue recoupment?

Ms Martin—I am not sure if I have the revenue figures here. I can check on those for you. In some of the settlement offers there have already been voluntary disclosures, usually including payment arrangements, so there would be some revenue implications. I will just have to check on the final figure. I have a figure but I am not sure of it.

Mr D'Ascenzo—Just as an example, in the two settlement offers that have been received we estimate that the tax involved could be in the order in total of about \$30 million, just on those two alone. The dollars will ultimately start to add up in relation to this project, but we do see it very much as sending a clear signal to the community that where people undertake these sorts of activities—and they are alleged at this stage, but assume that those allegations prove to be true—that sort of behaviour will face the full force of the Commonwealth working together to properly apply the law to those actions.

Senator MURRAY—That is why I put it into two compartments, one criminal and one revenue recoupment. As you know, I am a money man and I would like to see us get back our \$300 million if we could—and more. Revenue recoupment is definitely a part of the action.

Mr D'Ascenzo—It is. It is interesting in the sense of the proceeds of crime legislation. I have indicated to the other agencies that the tax office are not concerned whether that is raised by the tax office or by another law enforcement agency. As far as we are concerned, we are there to try to apply the full force of the Commonwealth powers to bring accountability to these actions.

Senator SHERRY—On the same matter, Ms Martin, you made a reference to possible criminal activities—what sorts of criminal activities are we talking about?

Ms Martin—They are the same range of issues the commissioner referred to before, about potential fraudulent activities such as false invoices and arrangements that purport return of income to be something that it is not. They are basically fraud related activities.

Senator SHERRY—Does this include money that is obtained from illegal sources—drug money and such?

Mr D'Ascenzo—The Operation Wickenby focus is not necessarily in that area, but those sorts of issues do crop up in the wider range of work that we and other government agencies are doing in this area.

Senator PARRY—Ms Martin, you indicated figures of 65 individuals and 32 groups in one of your analyses. Please do not answer if this is sensitive. Are the individuals groupings such as married couples and company directors? How do you end up with the variance?

Ms Martin—When you see arrangements like this—and I am speaking very generally here—it may be business partnerships, sometimes it may be related people.

Senator PARRY—So it is legal entities more than—

Ms Martin—Yes. So you might have one arrangement but several parties in various relationships involved.

Mr D'Ascenzo—It comes down to two sorts of things that allegedly we are seeing. One is the creation of deductions or having income hidden offshore that should be taxed in Australia, and that can happen through false or inflated invoices. In other words, the international promoters provide Australian businesses with a false or largely inflated invoice so that tax deductions can be overclaimed. Sham loans I mentioned, where you pretend to have a loan to somebody that is then loaned back to you. Asset disposals—an international entity that is beneficially owned by the vendor; in other words, you provide it to yourself, so to speak, but nobody knows who beneficially owns the overseas entity. And where the beneficial ownership of the Australian resident is concealed—so money is going somewhere else and it looks like a bona fide transaction but actually it is still owned by the person, who is able to use it for their own purposes.

There are other situations where, rather than having income that should come to Australia as income, you have the use of debit or credit cards held offshore and then used to spend money offshore without it being disclosed in Australia. You have funds returned to Australia as a gift or inheritance from a relative offshore or a deceased relative, whereas it is really money that should be taxable in Australia but is siphoned through those sorts of channels. This is where the promoter pays for expenses incurred by the Australian resident taxpayer and he gets a fee for that. Sham leases repatriate taxpayers' funds or allow tax deductions for the holding costs of holiday homes and, again, borrowings and the interest rates when they are back to back. That is the range of activities that allegedly we are seeing.

Senator SHERRY—If we can come back to a couple of superannuation issues, there is a revenue measure in the budget, a super measure, to which a figure of \$150 million per year is attached. I think this is mainly for state superannuation funds. I will just double check that. It concerns the appropriate use of pre-1 July 1988 funding credits. I notice the measure says it is state but not Commonwealth or local government funds. Are we dealing here with only state public sector funds?

Mr Lonsdale—We think that is the case.

Senator SHERRY—How many funds have you identified?

Mr Lonsdale—I do not have those figures.

Senator SHERRY—It says state based funds. It may or may not be all of them but the implication is that it is all state based; you do not name any.

Mr Lonsdale—We expect that they are state based funds based on historical practice. We have been in discussions with the tax office about particular superannuation funds that have been accessing pre-July 1988 credits. So the basis of the measure is historical practice.

Senator SHERRY—How has this been identified? How was it picked up? Was it picked up by the tax office?

Mr Lonsdale—How has the issue come to light?

Senator SHERRY—Yes.

Mr Lonsdale—I understand that is the case. Over a period of time the inappropriate use of pre-1988 funding credits has come to light. It has arisen as a policy issue and has culminated in the budget decision.

Senator SHERRY—Has the tax office been able to identify the superannuation funds to date?

Mr D'Ascenzo—We provided all the information we could to Treasury to indicate that the way we saw it was that there was some inappropriate use of the pre-July 1988 funding credits. We provided that information to Treasury and we have been working very closely with Treasury to develop proposals.

Senator SHERRY—Presumably that would be a list of the superannuation funds as well. You must have identified some of the funds.

Mr D'Ascenzo—Yes. To do this you need to look very carefully at the funds to work out whether or not they are appropriately or inappropriately using those credits.

Senator SHERRY—Is it the tax office that has been examining the internal practices of the funds to identify the size of the issue, the size of the moneys involved?

Mr D'Ascenzo—I would say that was the case.

Senator SHERRY—It gives the impression it is all state based public service funds. Is that correct or not?

Mr D'Ascenzo—I do not know. I do not know what the coverage is. It really depends on whether or not there is an abuse or apparent abuse of those systems. It really depends on the funds and how they operate and how much—

Senator SHERRY—It seemed to me pretty definitive that there was going to be \$150 million a year from this area, that you had identified abuses.

Mr D'Ascenzo—That is what our research suggests.

Senator SHERRY—They are constitutionally protected, aren't they?

Mr D'Ascenzo—I do not know.

Mr Lonsdale—I think we are talking here about separate funds from the constitutionally protected ones.

Senator SHERRY—So there is no legal impediment to collecting the revenue, if need be?

Mr Lonsdale—Under the measure?

Senator SHERRY—Yes.

Mr Lonsdale—No.

Senator SHERRY—Would it require legislation?

Mr Lonsdale—Yes, it would.

Senator SHERRY—Why would it require legislation?

Mr Lonsdale—The genesis of the issue is that the legislation that is currently in place does not fully reflect the policy intent that was in place at the time and because of that the legislation needs to be changed under the measure.

Senator SHERRY—How is that the fault of the funds then? If they are complying with the current law and you have to change the law to reflect the policy intent, how is that the fault of the fund? Seemingly they are paying the correct tax, as the law has been written.

Mr Lonsdale—The measure is to ensure that pre-1988 funding credits are used for contributions in respect of pre-1988 amounts, and that is what the measure is seeking to do.

Senator SHERRY—Was this an oversight when the initial legislation was passed?

Mr Lonsdale—I do not think it was an oversight.

Senator SHERRY—Why are they not paying the money then?

Mr Lonsdale—I think what has happened over a long period is that the way that states, for example, fund public sector schemes has changed from a situation where funds were placed into superannuation schemes and paid out very quickly thereafter—and in those cases the legislation appears to work—to, over time, a situation where funding amounts are put in that may not correlate with the benefit that is actually paid in a particular year. Because of that mismatch, the legislation does not work in the way that it is meant to fulfil the policy intent.

Senator SHERRY—Have all of the state based funds been checked now to determine how many there are and the quantum of revenue that will be raised?

Mr Lonsdale—The quantum of revenue here is, as the commissioner outlined, following the investigation of funds. It is based on what data we know is out there at the moment and extrapolating that forward in terms of what we would collect under the measure.

Senator SHERRY—Has the checking of the state based funds now concluded?

Mr D'Ascenzo—From my memory in this area, we calculated a percentage of the pre-1988 funding credits and we extrapolated that across the holdings of the particular funds that we looked at, and I think that was the basis of some of the calculations.

Senator SHERRY—I am still not clear. Have all the state based funds been checked now for this issue?

Mr Lonsdale—In what way? I am not sure I follow the question.

Senator SHERRY—Have you checked every state based superannuation fund to see how widespread the practice is in terms of the funds that are doing this? Are we talking about every state and territory government?

Mr Lonsdale—I would have to take that on notice.

Senator SHERRY—How have we then got a figure in the budget of \$150 million a year?

Mr Lonsdale—The costing is based on investigations that have taken place in respect of the use of pre-1988 funding credits.

Senator SHERRY—This is a pretty big figure, isn't it? Is there someone here who has been involved in this checking?

Mr D'Ascenzo—Not that I have on my team. But, just from memory, we worked out the amount that we think has been used inappropriately or contrary to the policy intent, we know the base of total state based amounts and we extrapolated forward.

Senator SHERRY—Yes, but it is not local government, it is not Commonwealth government; it says it is states. You cannot name the funds and you cannot name the states. Therefore, the assumption would reasonably be that it is all of them. Is it all of the states or are there some that have not been doing it? At the moment it clearly implies that it is every state.

Mr D'Ascenzo—I understand.

ACTING CHAIR—You might like to consider that over the dinner break, as it is past 6.30. It would appear that the tax office is going to be required until we finish tonight, so questions to the Takeovers Panel, the Office of Financial Management and the National Competition Council will be dealt with tomorrow.

Senator Minchin—What happens to the Inspector-General of Taxation?

ACTING CHAIR—His questions have been placed on notice.

Proceedings suspended from 6.33 pm to 8.01 pm

CHAIR—Ms Vivian, it has been alleged that, once a compliant fund becomes non-compliant, the ATO ceases its regulatory jurisdiction; is that correct?

Ms Vivian—It refers to a bit of the case study that you gave me. I have just been having an interesting discussion on this matter back in the office. At one level what I am being informed is that, in terms of our powers under the SI(S) Act, if a self-managed super fund does something to make them non-complying, such as bringing in an extra member or having a member that is not a trustee, there is a question about whether we have powers under the SI(S) Act to do something further. However, in looking at that, it would seem to me there is a gap between what APRA would deal with and what we deal with. We do have a joint regulators meeting. At one level I am going to have a look and see whether we can do a bit more in that area. Also, I will raise it with APRA to work out so that we do not have these people falling in the middle between the ATO and APRA as regulators.

CHAIR—My concern, in raising that issue, was that, if you had a disaffected party who had been taken advantage of by the dominant trustee, that person did not appear to have any rights, or was advised that she did not have any rights in appealing for justice through the regulator, in this case the ATO.

Ms Vivian—In terms of this case study, we are doing some work on it. Even though the names were changed, I could recognise it as one where we are in contact with the person. In reading through it and talking to my staff, it would seem to me that there is a potential gap and that we need to talk to APRA and make sure that we do not have people here falling between us as the regulator or APRA. Whilst at one level I think they were advised that we could not do anything at a very early stage, I will have a look at our procedures, because I think it should have been escalated up for some further examination at that point, and the person—

CHAIR—Yes, because the situation went from bad to worse.

Ms Vivian—Yes, that is right. When I look at this case, there are three areas. Firstly, in terms of the person entering into this arrangement, I think it is a very good example of the sorts of issues that people need to be aware of when they are becoming part of a self-managed

super fund. The sort of arrangement they entered into then made some of the further action a little more difficult. Secondly, in terms of the escalation processes when they raised it with our office, I will have a look at them, because I think that should have been escalated to a more senior point to do something about it. Thirdly, it does seem, in some quick discussions back in the office, that this is an area where there is a bit of a gap. It so happens we have a joint regulators meeting in a couple of weeks, and I will raise it there so that we sort out with APRA a process so that we make it clear who would deal with issues like this.

CHAIR—So you can assure us that, in terms of that regulatory gap when they become non-compliant, particularly through no fault of the victim, she will not suffer consequences and will have a regulator to look to?

Ms Vivian—That is right. We need to either look at whether we can do something under the tax office powers under the SI(S) Act, so we will have a further examination of that, or find a better process to work with APRA, if it ends up that it has to be referred to APRA, for how we can actually work with them so that we can sort them out fairly quickly.

CHAIR—That sound a reasonable resolution. Will you keep us informed?

Ms Vivian—Certainly.

Senator SHERRY—I would like to go back to a couple of super matters, but there are a couple of other issues I will touch on first. I do not know whether you are aware, Mr D'Ascenzo, that recently there have been a number of articles in the *Australian* newspaper concerning Virgin Blue, the destruction of documents and a tax scheme to minimise GST through transfers of aeroplane leases overseas. Are you aware of those articles?

Mr D'Ascenzo—Yes, I have seen the articles.

Senator SHERRY—Are you able to comment publicly about any aspect of this investigation?

Mr D'Ascenzo—It is difficult having regard to the ground rules that I understand this committee works under in terms of getting into individual cases and the like. But if there are some specific questions, I am open to see what we can answer without going into specifics.

Senator SHERRY—Is there any activity by the tax office concerning lease arrangements on aeroplanes?

Mr D'Ascenzo—Both at the GST and the income tax areas, we have a level of focus on industries, including the transport industry and the airline industry.

Senator SHERRY—Does that include aeroplane transactions?

Mr D'Ascenzo—Not necessarily every transaction, but we are looking in that scope.

Senator SHERRY—Some transactions?

Mr D'Ascenzo—Yes.

Senator SHERRY—I understand the degree to which you can comment publicly. There have not been any legal proceedings that have become public through those legal proceedings commencing as yet, have there, in respect of aeroplane leases?

Mr D'Ascenzo—Mr Jackson might know more about that.

Mr Jackson—There have been some legal proceedings in relation to some matters and, whilst I do not have it on any authority, I understand that some of the information that was attributed to those articles was obtained from legal proceedings.

Senator SHERRY—So there have been legal proceedings involving aeroplane leasing arrangements and GST that should have been paid or may be owed?

Mr Jackson—There were legal proceedings to do with the nature of the administrative action that we were taking, which referenced back on some particular matters. In relation to a comment you made earlier, I understand that we issued a taxpayer alert on leasing arrangements about 12 months ago, maybe a little bit more, which referenced certain types of arrangements and made our position fairly clear.

Senator SHERRY—Was that alert in respect of aeroplane leases or did it make reference to them?

Mr Jackson—I believe it made reference to aeroplane leases, yes. I do not have it with me so I cannot tell you for certain, but I believe it did.

Senator SHERRY—The legal action you refer to was to obtain documents, was it?

Mr Jackson—No, there was legal action involving continuance of our administrative activities, and the court held ultimately that those activities could continue.

Senator SHERRY—Against whom was the court ruling?

Mr Jackson—Against other parties.

Senator SHERRY—You do not recall the parties?

Mr Jackson—I do recall the parties but, as is the practice, we do not talk about individual cases here.

Senator SHERRY—I am only going to things that are in the public domain apparently.

Mr Jackson—I understand that but, irrespective of the information, there is information in the public domain. If you would like to access that, you are able to. We are getting into that territory of talking about individual cases and particular circumstances, and that is not an area that I would like to traverse.

Senator SHERRY—I do know where to draw the line. Has there been a tax office communication/media release on this matter at all, on the proceedings that were initiated to obtain documents?

Mr Jackson—No.

Senator SHERRY—What was the nature of the action—to continue your administrative work or investigation, to check the documentation and contain it?

Mr Jackson—To continue administrative work, but again I would rather not comment on the particular activities.

Senator SHERRY—At least some of those details are obtainable from the court documents?

Mr Jackson—That is correct.

Senator SHERRY—Do you deal with the High Wealth Individuals Taskforce?

Mr Jackson—Alas, no. There may be another officer here who can help.

Senator SHERRY—I missed some of the questions earlier while I was out of the room. Some of them may have been asked. The \$82 million allocated for the High Wealth Individuals Taskforce in the 2006-07 budget: that is extra funding, is it not?

Mr Konza—Yes, it is.

Senator SHERRY—How is a high wealth individual defined?

Mr Konza—It has control of assets in excess of \$30 million.

Senator SHERRY—Do you have an approximate number of high wealth taxpayers that you are monitoring?

Mr Konza—We are monitoring about 1,000.

Senator SHERRY—Why are you monitoring these 1,000 persons?

Mr Konza—The 1,000 people that we have in mind are about 900 people who we have identified as having assets in excess of \$30 million, and we are simply checking whether their tax performance equates to their economic performance, which is our standard practice. The other 100 that I included in the 1,000 figure are people who may not meet the \$30 million test, but might have a very high profile or may have control of assets that have not been counted in the \$30 million.

Senator SHERRY—When you say ‘high profile’, you can be high profile and not have any money.

Mr Konza—Yes. We are talking about people who have wealth.

Senator SHERRY—Such as senators.

Senator MURRAY—And tax officers.

Senator SHERRY—Yes, hardworking tax officers; I agree with that one. I am just not clear on this. You have got the high profile person, but there has to be some sort of prima facie evidence that they have got money, and substantial amounts of it?

Mr Konza—Yes. The reason that I say that we are concentrating on 1,000 people is that there are still cases from time to time which come to light where the person may have control of many millions of dollars—\$20 to \$25 million would not normally fall into the taskforce area—but we may identify that they are engaged in activities which are very similar to that undertaken by high wealth individuals.

Senator SHERRY—Technically the wealth may not be in their name but they are able to influence it in some significant way?

Mr Konza—That is one of the instances, yes.

Senator SHERRY—How many high wealth individuals have been prosecuted? Let us take this financial year to date and the previous financial year.

Mr Konza—I would have to take that question on notice. I do not know.

Senator SHERRY—What about high wealth individuals in the same periods that I have asked about who were not prosecuted but agreed to pay a sum settlement?

Mr Konza—Again, I do not know. I would have to take that on notice.

Senator SHERRY—If you could take both questions on notice and perhaps give us a total figure for those categories.

Mr Konza—This is in the last year that you are referring to?

Senator SHERRY—This financial year and the last full financial year.

Mr Konza—Thank you.

Senator SHERRY—The extra funding of \$82 million is a fairly substantial amount of money. Why did you need extra funding?

Mr Konza—Basically when the High Wealth Individuals Taskforce was established some years ago we chose at that time a figure of about \$20 million assets and, over the years, we have steadily lifted that threshold to the \$30 million that it is today but, nevertheless, even with the lifting of that threshold we have found that the numbers of people who exceed that threshold have grown quite steadily and the task force needed more resources to be able to effectively cover the population.

Senator SHERRY—‘More resources’—that is, more staff to oversee the area, because of the growth in numbers. Is that basically the central issue?

Mr Konza—Yes, it is.

Senator SHERRY—You will be employing additional staff obviously?

Mr Konza—Yes.

Senator SHERRY—How many approximately?

Mr Konza—In this coming year we are looking to add about 100 staff to the task force and rising to about 180 over a four-year period.

Senator SHERRY—How many are in there at the moment?

Mr Konza—There are 93.

Senator SHERRY—That is 93 and another 100, which will take you to 193?

Mr Konza—Yes.

Senator SHERRY—Another 80? That is almost going to triple in size?

Mr Konza—Yes.

Senator SHERRY—That is a fair sized unit. Are the people being recruited from outside, internally or both?

Mr Konza—We will be advertising our jobs in the outside world.

Senator SHERRY—The outside world—it almost seems as though it is another country.

Mr Konza—Very Freudian, isn't it? Sorry.

Senator SHERRY—Do not apologise. They are slogging away in the tax office just like they are slogging away at estimates. I can understand your feeling.

Mr Konza—Yes. We will be advertising at large and, while I would anticipate that a percentage of people will come into the ATO, nevertheless our experience is that most of the staff are likely to be recruited from within the ATO because of the specialised skills and experience that are required. We have also in our plans made provision to contract specialist services if they are needed as well.

Senator SHERRY—When you say ‘contract specialist services’, you would have to be a bit careful of that, wouldn’t you, given the sensitivity of information? It would not be easy to do, I would not have thought.

Mr Konza—That is right. You have to be very careful, but the High Wealth Individuals Taskforce has used external legal advice and even external accounting advice from time to time over the past 10 years.

Senator SHERRY—The anticipated additional revenue that is estimated to flow from this?

Mr Konza—The estimates were that there would be about \$600 million over the four years that were covered by the measure.

Senator SHERRY—Just on the recruitment of staff, while I am thinking about it—and I do raise this issue with APRA and ASIC—do you have any observations to make about the difficulty of the recruitment of specialist staff ?

Mr D’Ascenzo—It depends on the market in the particular area. We have a lot of specialisations in the tax office. I know that, for instance, in terms of doing our financial accounts, just the accounting expertise in that area is hard. The auditors in our internal audit area we find difficult to get. The cost profile of top-flight technical people is expensive. With IT, there is a drain in terms of skills shortages for competing products, so there are difficulties in getting appropriate skills. That is why we have, over the last 10 years, invested quite heavily in graduate programs and cadetships, as an opportunity of growing some expertise ourselves and trying to mix that with whatever specialist expertise we can get from outside the tax office.

Senator SHERRY—Senator Murray, do you have another question?

Senator MURRAY—No. I think you have covered the high wealth thing. That has been running now for eight years—the High Wealth Individuals Taskforce?

Senator SHERRY—Yes. It is eight years, isn’t it?

Mr Konza—No, actually, it is 10.

Senator MURRAY—Is it 10? I thought it was introduced in 1997 or 1998. It was after the Howard government came into power.

Mr Konza—I worked on it in 1996 in a previous life, so that is how I know it has been going at least 10 years.

Senator SHERRY—Up until last year, how much revenue has been raised as a consequence of the activities?

Mr Konza—I do not know off the top of my head, but it is covered in the annual report each year. There is a specific table provided for it.

Senator MURRAY—I remember it being a very high figure. It was well over \$1 billion over the 10 years.

Mr Konza—Yes, it has been.

Senator MURRAY—With respect to recruitment, it would pay a high wealth individual to have someone inside telling him what is going on. I assume you have very good screening techniques to make sure you do not get a mole in amongst your recruits?

Mr Konza—We do have serious security arrangements regarding the task force. When you get into areas or activities such as project Wickenby and that sort of thing, that can be very sensitive. Generally, when we monitor a high wealth individual's activities, so far as them and us, it is not a particularly secret activity. We are going out and asking them questions and so forth. There can be sensitivities if we have inside information. We would have to watch things like that. The whole of the task force is very careful with the information it receives, because it is very sensitive information. But I would not say that, generally speaking, its activities are greatly susceptible to mole activities.

Senator MURRAY—What about with respect to high wealth criminal figures?

Mr Konza—High wealth criminal figures within the tax office are handled generally by the serious non-compliance branch. They have the types of security arrangements that are applicable to project Wickenby and things of that nature. That is a much more serious issue.

Senator MURRAY—It is not unknown for the two sectors to cross over, is it?

Mr Konza—It is not unknown.

Senator MURRAY—I am not suggesting that it is common.

Mr Konza—No.

Senator MURRAY—I am certainly not suggesting that. But it is not unknown.

Senator SHERRY—I just wanted to return to some superannuation issues. Perhaps I will deal with the matter that flows from the superannuation plan. There are some other matters, but they do not relate to that. It deals with this issue of lost superannuation. Mr D'Ascenzo, have there been evaluations of the proposals outlined in the plan in respect of consolidation of lost superannuation accounts?

Mr D'Ascenzo—We have had some consultation in the process and we are heavily involved in providing our expertise to Treasury in the further development of the proposals.

Senator SHERRY—I assume that there will be a cost to this, Mr Lonsdale?

Mr Lonsdale—There will some administrative costs.

Senator SHERRY—Is that contained within the \$6.2 billion?

Mr Lonsdale—No. At the bottom of the table there is a footnote, which says that admin costs—let me just find it—

Senator SHERRY—It says, 'Does not include admin costs'.

Mr Lonsdale—Yes, ‘Does not include admin costs’.

Senator SHERRY—So this proposal falls within that category?

Mr Lonsdale—Correct.

Senator SHERRY—Are there any other proposals that fall within the footnote of administrative costs?

Mr Lonsdale—There are several streams within the proposal that will require the tax office to do some things that they are not doing at the moment. Those issues need to be worked through, with associated admin costs.

Senator SHERRY—I notice that it is proposed to have a simple standard form. I think I have read those words somewhere before—existing Labor policy. Obviously, this is the ATO’s form. Is it envisaged that there would be a simple standard form for superannuation funds of the same type, so that they are all using the one transfer form?

Mr Lonsdale—The idea would be that there would be a standard form that would be used across the industry. We need to have further discussions during the consultation period with industry on that.

Senator SHERRY—I note it says that the ATO would contact people with lost accounts and provide them with a simple standard form to complete. Is one of the bases for a declaration of a lost account not if mail is returned ‘address unknown’? That is one of the bases, as I understand it. So there have been two years of no contributions, the fund makes best efforts to contact the member, and mail is returned ‘address unknown’?

Mr Lonsdale—I think that is correct.

Senator SHERRY—Then they notify the register. That is correct, Ms Vivian, is it not?

Ms Vivian—Yes, that is correct.

Senator SHERRY—The tax office has its lost account register and notification, but a proportion of these people—a proportion unknown; you may know, but I do not—have no address. Where would you send the form to if it is ‘address unknown’?

Mr Lonsdale—As part of the proposal, which is separate from this but relates to the tracking of contributions, TFN reporting would be required for people making a contribution. We think that that would assist the tax office to identify accounts going forward and enable it to better match accounts with people.

Senator SHERRY—‘Accounts going forward’—we have just over five million accounts on the register of lost members at the moment. There would be a proportion of those where there is no address and no TFN number. So it is going forward—

Mr Lonsdale—There is a going forward aspect and, as you point out, there is also a stock aspect. It is my understanding that the tax office are going through a program now of matching people with their accounts. Where that cannot be done in a hard-matching way with TFN, there are soft-matching techniques that are being used to reunite members with their accounts.

Senator SHERRY—Could you give me some detail on that, Ms Vivian?

Ms Vivian—Of approximately 5.4 million accounts, we can match to probably 4.5 million accounts and in that process there is some—

Senator SHERRY—When you say ‘match about 4.5 million’, matching with what?

Ms Vivian—What I mean by that is that we have a good sense of who they are and their current address, from our records.

Senator SHERRY—So even though there is not a current address you are able to data match, compare that number with—

Ms Vivian—We run a data matching—

Senator SHERRY—another address on another record database?

Ms Vivian—Yes, through their record. Effectively, what we are using is the tax file number. What we say there is that, from about 5.4 million, we can identify tax file numbers of about 4.5 million, although in saying that, there is a proportion of those 4.5 million where we call it a ‘soft match’, where we think it is who the person is but there is a bit of doubt. Those 4.5 million are actually accounts. That actually relates to about 3.1 million people. As you are probably aware, we are in the midst of writing out to three million people across the country telling them that they have potentially some lost superannuation and suggesting they take some action.

Senator SHERRY—On that issue for the moment, I know you are sending out letters, because I have had a few people comment to me about it. What has been the response? Are you able to ascertain a response? They will be going to the fund at the moment with the transfer details, presumably?

Ms Vivian—No, all we can do is write to the individual. To date, we have sent out 1.47 million letters. But for the ones in 2004-05, we sent out 500,000 letters and, since then, in terms of looking at what the response has been, I think there has been enough time for the funds to come in and take them off the register, if they have basically gone back in. Interestingly, of the 500,000 people we wrote to in 2004-05, 30 per cent have come in and actually been removed from the register by the funds.

Senator SHERRY—By the funds?

Ms Vivian—By the funds.

Senator SHERRY—Yes. We will see the results of the lost members register and the number of accounts and moneys—what the total impact will be. Presumably, that will be in the annual report for this financial year.

Ms Vivian—It should be reflected in that.

Senator SHERRY—Where you have a tax file number for someone who is overseas, who has left the country, how do you deal with that? Do you still write to them?

Ms Vivian—We write to the most current address that we have. For those people, I think it would vary a bit between whether the address we have is an Australian address or an overseas address.

Senator SHERRY—Yes, you could have a person who has left the country who may have given a forwarding address that is overseas, or it may be an Australian address. Presumably you would not get much response in that case.

Ms Vivian—That is right. At the moment, we are focusing on Australian addresses, but I think that is something we will then have a look at.

Senator SHERRY—Has the issue of exit fees been raised with the tax office as a consequence of this process?

Ms Vivian—Not to my knowledge.

Senator SHERRY—It would more than likely be raised with the fund, would it not?

Ms Vivian—What we advise is that they need to check with their funds and look at things like that.

Senator SHERRY—But under this new process, you are to send out a standard form, presumably with the details. Would it have the fund detail in the standard form that goes to the individual?

Ms Vivian—We ask them to contact the fund.

Senator SHERRY—No, I know the current process. I am referring to this new process which says that the ATO would contact people with lost accounts and provide them with a simple standard form to complete. So they have still got to fill in the form themselves.

Mr Lonsdale—Those issues are being gone through at the moment. We need to work through that, not only with the tax office but also with industry.

Senator SHERRY—Yes. Most funds I know actually include their own form in their mail-outs. It is a constant all the time. You are aware of that, aren't you, Mr Lonsdale?

Mr Lonsdale—Yes.

Senator SHERRY—So the funds are doing it. We are going to have a standardised form and then the ATO is going to send out a form as well. They are already getting a form. You are just adding the ATO's form to the form the funds send them, albeit a standard form.

Mr Lonsdale—As I said, these are issues that we are working through with industry now. We will be working out what the form looks like and what is in the form to get the simplest transfer possible for individuals who want to make the choice to amalgamate.

Senator SHERRY—Yes. There will be a standard form—that is a simplicity, in my view—and there is a 30-day period and standard identification required, but it just seems to me that it is the ATO providing a form which the funds already provide, albeit that it will be a standard form.

Mr Lonsdale—As I said, we are working through that and there need to be discussions with industry on it.

Senator SHERRY—What about the issue of exit fees? Is there going to be discussion with industry on that?

Mr Lonsdale—I am sure there will be.

Senator SHERRY—You are aware, there are, I think, about half a million legacy products with exit fees which penalise to varying degrees people who transfer their money out?

Mr Lonsdale—We are aware of the exit fee issue.

CHAIR—Are you aware, Mr Lonsdale, of a speech that the head of MLC gave to CEDA, stating that now 30 per cent of their revenue actually comes not from commissions but from advice—holistic advice? Obviously, there are some positive signs on the horizon of some leadership in this area. Earlier tonight I sent a little note to Mr Callaghan in relation to reforms in relation to self-assessment. I was just a little uncertain as to whether, in talking about the general interest charge and a few other little changes, I really asked the lead question, which was: were those changes related to income tax going to be extended to a range of other taxes which the tax office administers, for example, the GST, the fringe benefits tax and other tax? The whole point of the question was extending the review of the income tax self-assessment, ROSA, measures to other taxes. I think I have pointed out that there have been since 2005 a number of very positive changes to the income tax self-assessment system which strike a very appropriate balance between the rights of the taxpayers and the duty of the ATO to collect the revenue. I do not think I got a response to that. I know I was talking about the general interest charge, but whether I focused in on that I cannot quite recall.

Mr Callaghan—I thought we did try to cover that. Yes, one of the recommendations that was in the ROSA was to consider the application of these recommendations, as they were applying to income tax, to other taxes administered by the Commonwealth. The same principles underlying all the ROSA recommendations are there. It is: to what extent could greater certainty be given to taxpayers? It is looking at such issues. It still has to be progressed, I should say, but the issues that would need to be looked at, for example: can there be one approach to a ruling system; can there be some commonality in amendment periods as applying to other taxes? As you say, in the FBT area, there are different amendment periods now. The issue that needs to be looked at is: could there be a more common approach? It is the same in terms of penalties, for example. These are all issues that still have to be progressed. They are matters that have not been addressed yet in terms of the application.

CHAIR—They have not been?

Mr Callaghan—They have not been progressed yet. It is still essentially on the forward work program.

CHAIR—Right, and when do we expect some finality in relation to any of them, like fringe benefits tax, the GST—if we could get a common approach?

Mr Callaghan—It is impossible to give any indication as to the timing. The government accepted the recommendations. On this one we would still have to give advice to the government on how to progress this recommendation. It may go forward, for example, by initially issuing a discussion paper to canvass the views of taxpayers as to how they see this could operate but, as I say, it is still work in progress or on the forward work agenda.

CHAIR—That covers the penalty regime, does it? It appears that perhaps some aspects of that in relation to the GST are out of kilter with income tax.

Mr Callaghan—These are all matters that would need to be considered. It is not possible to say what would be covered in it, because it still has to be progressed, but they are the types of things that I would believe we would be going out first to consult on to see about the application of the principles to other taxes.

CHAIR—How long would that take, about 12 months—within 12 months?

Mr Callaghan—I do not know, is the honest answer. It would be impossible to give a specific time frame as to it all, because it is all forward work.

CHAIR—Thank you.

Senator SHERRY—I will try and finish the superannuation issues now. There was a recent article in the *Daily Telegraph* headed ‘Tax office targets rail super scam’. Apparently there were some persons working in the railway industry who had been subject to a scam involving the use of, I think, self-managed superannuation funds or, alternatively, a purported fund into which moneys from the superannuation fund, First State Super, were transferred. Is there activity going on in respect of this matter?

Ms Vivian—We are taking some action against some promoters that have been targeting early access to their superannuation.

Senator SHERRY—Is the rail industry one that is being examined?

Ms Vivian—There is one of the super funds in the rail industry, yes.

Senator SHERRY—Did I read correctly yesterday that a promoter who had been promoting an early access scheme was jailed for two years?

Ms Vivian—That article was more about where someone had been effectively fraudulently acting as a financial planner, and it was through ASIC that that action was taken.

Senator SHERRY—It was not the tax office in that one?

Ms Vivian—No. We have actually disqualified and gazetted two promoters from being formal trustees of a self-managed super fund.

Senator SHERRY—Is this in respect of self-managed super funds where you have the jurisdiction, whereas ASIC has—

Ms Vivian—In this case, it was in terms of where there were promoters that were acting as self-managed super fund trustees and rolling money through the self-managed super fund to give early access.

Senator SHERRY—They set up a self-managed super fund as trustees and used that vehicle to effect transfer?

Ms Vivian—To effectively target people for early access.

Senator SHERRY—I turn to the surcharge. I understand there has been a delay in issuing updates of surcharge debts to taxpayers who owe a debt ongoing? Is that correct?

Ms Vivian—We did have a problem. Normally we do surcharge runs at various times during the year. With our February run there was an error. We have recently issued all of those surcharge assessments in May. We had a problem with the calculation that we used.

Senator SHERRY—You had not actually issued them?

Ms Vivian—No, we had not actually sent them out. We then worked with the funds just to work out the best way to correct this error. The best way seemed to be to effectively reissue them all again with new dates. Because the systems are complex, that took us till May. A number of my colleagues have remarked that they have received their surcharge assessments, so I would say they are out the door.

Senator SHERRY—I have not received mine yet.

Mr D'Ascenzo—It is in the mail!

Senator SHERRY—Can I respond by saying that the cheque to pay it is in the mail! What were the approximate number that were not distributed in February as a consequence of this?

Ms Vivian—Just bear with me.

Senator SHERRY—While you are looking, too, if the figures are available, what is the total approximate number of ongoing assessment notifications for the financial year that have been issued with respect to surcharge?

Ms Vivian—That broader question I would have to take on notice. In terms of the ones that were delayed from February through to March, there were about 280,000 for current year, plus another 130,000 held up, so that comes to about 410,000 assessments.

Senator SHERRY—It is still that many?

Ms Vivian—It is still flowing through from 2004-05. The February run is probably one of the larger runs, too, because it is one of the ones most recently after the funds have lodged the members' contributions statements that allows us to calculate it. Plus you have also got a lot more tax returns in the door as well.

Senator SHERRY—These are people who were assessed in the last financial year when the tax still applied?

Ms Vivian—That is correct.

Senator SHERRY—Do you have an estimated number of those where it will be ongoing? I am thinking here about defined benefit fund members, who generally do not pay it until they retire.

Ms Vivian—That is a fairly difficult number for us to estimate. As a very broad approximation, so we can get a sense of what the workloads might be, it seems to be somewhere in the vicinity of about 110,000. But I would also say that I think it will be a while, because funds often re-report their members' contribution statements or there are amendments to tax returns that can then therefore affect the surcharge assessments. I think there will be some back-year amendments as well for a period.

Senator SHERRY—So the ongoing revenue shown in the budget papers is effectively the moneys that are being paid under the surcharge as people reach retirement. Is that correct? Can someone tell me?

Mr Ray—On an accrual or a cash basis?

Senator SHERRY—Both.

Mr Ray—On an accrual basis there is interest accruing.

Senator SHERRY—That is the interest accruing. Cash basis?

Mr Ray—Cash basis is when it is paid.

Senator SHERRY—That is only the interest figure that is showing up?

Mr Ray—There is ongoing compliance activity, too, which is tailing off.

Senator SHERRY—Do we have a total debt figure? I am sure you have one.

Mr Ray—We have estimates of what is going to be returned through the forward estimates, published in the budget papers.

Senator SHERRY—Presumably that is based on a total figure of a total surcharge debt that is accrued and will accrue interest?

Mr Ray—The problem is that the surcharge debt is going to be sitting there for a long time. Rather than work off the debt, what we work off is the flow. We do not have an estimate of the net present value of the debt.

Senator SHERRY—Just remind me: what is the debt accruing at? What is the interest? Is it the bond rate?

Mr Ray—It is the long-term bond rate.

Senator SHERRY—I have a couple of questions in respect of the choice of fund and its implementation. We have discussed this at previous estimates. I do not recall the number, but there was an increase in staffing as a consequence of increased inspection levels of superannuation generally. Can you give me an update on the increased staffing and whether it has been implemented? Are many more staff going to be employed? What is the total number at the moment?

Ms Vivian—For this year we were funded to undertake compliance work in a range of operations and the design work, and those staff have been in place during the year and undertaking the work.

Senator SHERRY—How many people are on the ground actually checking to see whether the forms are being handed out and processed by the employer?

Ms Vivian—We were funded for approximately 90 people to do that work, but the way that we did it in the organisation is that we used some of our integrated field that are across there. It was equivalent to about 35 FT doing that work, and they are certainly still running through some of those checks. By the end of the year we are hoping that they will have done about 7,500 visits. In addition, we made about 30,000 calls to particularly microemployers to see if they had offered choice or had heard about choice.

Senator SHERRY—Is that 7,500 visits to separate employers or more than one visit in some cases?

Ms Vivian—That would be visits to separate employers.

Senator SHERRY—Were the officers who were carrying out the visits able to ascertain what industrial provision the employers were under—state or federal? There is a different activation date.

Ms Vivian—That is true. What we try to do is target them where we think we want to check in terms of ensuring compliance. They are some of the issues that they may look at in the firm. But what we are finding in most cases is that, when they talk to the employer, they are certainly in most cases aware of their obligations under choice.

Senator SHERRY—In respect of those who are legally covered at the moment, and that would be extended on July 1 to state awards—

Ms Vivian—In terms of choice, which is probably another indicator, to date we have had about 850 people contact the office to complain that choice has not been offered. The bulk of the complaints were ‘not offered choice’; the next level was ‘not paid to a correct fund’. There were some who said that the employer had charged for choice. We are working through those complaints. Of about 60 that have been finalised, we have found only one case where the employer had only verbally offered choice.

Senator SHERRY—What do you mean by ‘employers had charged for choice’?

Ms Vivian—There were only five complaints. For the ones where we have called and talked to the employer it seems that there is sometimes a bit of a misunderstanding between choice and the concept of super guarantee. Those are just some broader issues that were talked through. What I am saying is that was what the original complaint logged with us was about. However, to date, when we have contacted the employers we have not found any evidence of that.

Senator SHERRY—In terms of compliance with the form being passed out, of the employers checked were there any identified who had not provided the standard forms to their employees?

Ms Vivian—Of the employers checked, we found only one case. But we are still working through the complaints on that basis.

Senator SHERRY—That is as a response to a complaint. What about the field officers out visiting?

Ms Vivian—It is a little difficult to give something specific. What I am hearing back is that in most cases employers are aware of it. Certainly, what the officers do is give the employer the information or even tell them where they can access the information.

Senator SHERRY—But are they doing it?

Ms Vivian—To our knowledge and from quite a bit of external research, the feedback is that that is happening. As I mentioned, we also made about 30,000 calls. Again, that has strongly indicated that the employers were aware of choice.

Senator SHERRY—I know they would be aware of it. There has been massive advertising. It is the process that they have got to go through.

Ms Vivian—Yes. They knew about the process.

Senator SHERRY—I did have some self-managed super fund issues that I wanted to raise briefly. I am aware that there was some discussion with Senator Watson earlier. You will recall that in the previous estimates I raised the issue of Westpoint. I was a little surprised that you had apparently not taken any investigative action in respect of self-managed super funds that

were apparently caught up in the Westpoint exercise. Has anything changed since we last discussed this matter?

Ms Vivian—We have been working closely with ASIC in terms of either assisting it or looking at what action we can take. One of the difficulties that we have is that the information that we get from self-managed super funds when they lodge their annual returns is that specific investments are not identified. All we can do is look at trends about where major investments are, which is one of the reasons that we have not taken any action.

Senator SHERRY—I understand that. Have ASIC or individuals named the self-managed super fund—you are regulating this area—and have you then gone to examine them? Have you received the names of any of the self-managed super funds in order to examine them?

Ms Vivian—Not to my knowledge at this stage, although we are still working with ASIC on that. The other issue is that most of those funds would not have lodged this year.

Senator SHERRY—You do not have the names yet. I understand why they would not have lodged, because they would be new. Once you have received the names and they have lodged, what would you be proposing to do?

Ms Vivian—We might have a look at some of the auditors involved in auditing these and looking at whether they are lodging contravention reports and where they are at, but that is probably about the limit at this point of what we can do in terms of looking at those self-managed super funds.

Senator SHERRY—I recall in the previous conversation with Senator Watson mention was made of your activity in issuing information with respect to self-managed super funds. Is there a legal requirement for a disclosure document to be issued, as there is with other financial services products, in respect of self-managed super funds?

Ms Vivian—No, not to my knowledge.

Senator SHERRY—To issue guidelines, if you like, is a bit difficult, isn't it, because you do not know about these funds until after they are established?

Ms Vivian—Self-managed super funds need to come to us to register to say that they are going to be a complying self-managed super fund. We send out to all new registrants information about the responsibilities of a trustee and what they need to do.

Senator SHERRY—This is after they are established, presumably, because they have registered?

Ms Vivian—They register. It depends a bit. Once they are established, they are meant to come in within a certain period to us. We send out that information to them as soon as we can. That is generally before they lodge their first return. We have also been trialling ringing up some of the trustees, probably in some of the self-managed super funds that we see, from our knowledge, as being more at risk, to check that they are aware of some of their obligations.

Senator SHERRY—How do you ascertain from your knowledge or your observations that they are more at risk? What are the characteristics?

Ms Vivian—I would have to take that on notice. We look at a couple of things—the information they provide us and the number of members coming forward—and we have a risk-profiling tool that looks at other areas where we have had concerns.

Senator SHERRY—This would be essentially after they have got some advice from goodness-knows-who, because they are not covered by FSR in respect of disclosure, and set it up?

Ms Vivian—It varies. With self-managed super funds you have, from observation, a whole range, from people who have sought financial planning advice and advice from accountants, to other people who might be trying to do it themselves. You do get a range of those people coming forward.

Senator SHERRY—People doing it themselves can effectively take advice from anyone. There is nothing legally to stop them.

Ms Vivian—In our material and the joint education document we have put out with ASIC we have said, ‘If you are setting up a self-managed super fund, these are four questions you need to think about.’ We have been urging people to seek financial advice and advising that they will need to have the funds audited—along those lines.

Mr D’Ascenzo—We do provide that information once they are registered, but all that information is readily available in publications or on our website. If people wanted to do some research, all that we said there is—

Senator SHERRY—I understand that. Have you ever done any surveys to see how many people do that before they establish them?

Mr D’Ascenzo—Not that I know of.

Senator SHERRY—In the Westpoint case it would be interesting to see how many were aware of their obligations in respect of self-managed super funds, would it not? Wouldn’t it be interesting to know this via some sort of survey?

Mr D’Ascenzo—There are a lot of things that would be interesting to know, but ultimately one of the responsibilities, as you know, for trustees is that they need to judge the level of risk of their investment.

Senator SHERRY—That is another issue, too. I am not one to suggest work just for the sake of it, but this is an area of risk, isn’t it?

Mr D’Ascenzo—You asked, ‘Where would they get the advice?’ We do a lot of work with tax agents and financial planners, and we provide that information to them as well. If they are advising their clients to get involved in these areas, they have the information available that we provide. We are using intermediaries as a means of providing that information to the clients.

Senator SHERRY—But it is true, isn’t it, that other financial products have a requirement for the issuing of a standard statement of advice document? This area does not, does it?

Mr D’Ascenzo—That is right.

Senator SHERRY—You referred earlier to your SPAA conference speech back on 1 March. Would a total investment from a self-managed super fund in the same parent company cause concern for the ATO if it were identified?

Mr D'Ascenzo—A parent company of?

Senator SHERRY—Of the person who has created the entity, the self-managed super fund, and they actually placed the money in the entity with which they are employed?

Mr D'Ascenzo—I think that starts to get into the in-house asset—

Senator SHERRY—So, it would cause concern?

Mr D'Ascenzo—That is right.

Senator SHERRY—How would you pick that up—from the auditor; you would be reliant on the auditor?

Mr D'Ascenzo—That is some of the work that our auditors do, to check those specific rules that the SI(S) Act provides, and to ensure that there is compliance. The other one, of course, is the auditor, and the auditor contravention reports. In other words, they must have these signed off by the auditors, and they should be checking that they are compliant.

Senator SHERRY—They are signed off by the auditor at the end of the financial year when they have to provide their report?

Mr D'Ascenzo—That is right.

Senator SHERRY—There is an information pack, *DIY super: It's your money ... but not yet!* Do you issue those?

Ms Vivian—Yes, we have them available for people to call up and get them from us. We have the information on the web. As soon as new trustees register, we also send them out, although I think in that one, we probably send out the *The obligations of a trustee* booklet, which covers a lot of the same information.

Senator SHERRY—I notice in your speech, Mr D'Ascenzo, that you said the tax office has:

... a dedicated team of 35 officers whose role is to contact, by phone or mail, those funds that are behind on lodgement. During 2005-06 their focus will be on 30,000 high risk APRA and Self Managed Superannuation funds with outstanding income tax/regulatory returns and or member contribution statements.

I think we have over 300,000 self-managed super funds. That is 35 staff for over 300,000 funds; it is about 8,800 self-managed super funds per officer.

Mr D'Ascenzo—All they are required to do though is to seek lodgement, so that starts off with an outbound call approach, for instance.

Senator SHERRY—Have you increased the staff in the last year in this area?

Mr D'Ascenzo—I think the fact that we have 35 is an increase from what we had.

Senator SHERRY—But is it sufficient, given the number?

Mr D'Ascenzo—Only for the task of trying to pursue lodgment—that is basically the choice we made in the allocation of our resources. If we find that that is not taking us forward, then we need to relook at our resource allocations.

Senator SHERRY—Are the resources that you have available in this area solely or largely as a consequence of the regulation levy? Is that what you are mainly dependent on?

Ms Vivian—No. I think we gave you a response to a question on notice that we spend about \$18.3 million in the self-managed super fund area.

Senator SHERRY—You did.

Ms Vivian—The levy is not as much as \$18.3 million. Whilst we collect the levy, it is effectively put into consolidated revenue.

Senator SHERRY—What is the levy at the moment?

Ms Vivian—It is \$45.

Senator SHERRY—Once only or ongoing?

Ms Vivian—It is \$45 on an annual basis. We send out statements for that at the time the return is lodged.

Senator SHERRY—That raises about \$13.5 million? But you have informed me that you are spending \$18.3 million on the regulation.

Ms Vivian—We certainly are spending more than what would be attributable to any levy coming through. I think that is recognition of some of the risks that we see in this area.

Senator SHERRY—I did not see anything in the budget to increase that allocation, Mr D'Ascenzo, beyond the \$18.3 million.

Mr D'Ascenzo—Is that a matter for Treasury?

Senator SHERRY—It is just as a matter of fact, but it is also a matter for the tax office, because you can get allocated internal resources without asking for additional resources, can't you?

Mr D'Ascenzo—That is right. That is what I meant about the choices. Basically, if you look at our compliance plan, which is one of our public representations of the choices we make in terms of administration, that is all about trying to say to the community, 'Hey, here are the choices we have made across a whole range of different things.' Because the reality is that tax administration is all about making informed choices about where you think you can improve voluntary compliance or you can address risks to the revenue or risks to taxpayers in terms of the law not operating as intended, or risks to taxpayers who do not know their rights and obligations.

Senator SHERRY—Sure, but are you aware that APRA has been going through and is just about to complete a licensing of other superannuation funds? Are you aware that that process is going on?

Mr D'Ascenzo—We know that, yes.

Senator SHERRY—These areas are a lower risk than self-managed super funds, but they have been spending—they have told me the number of people in the funds, but it is

considerably more in a lower risk area that they are spending in terms of licensing and regulation than you are in this area at the present time. Would you accept that?

Mr D'Ascenzo—Well, I have not compared the APRA budget, but what I can say is that we have made our choices transparent, and it is a question of where I take it from to put where. That is what is public, and that is what I am inviting comment on and I welcome your input.

Senator SHERRY—I think you should be doing more. It is a higher risk area—

Mr D'Ascenzo—From where? What do I do less of?

Senator SHERRY—Well, you sort out the internal resources, and, when I am in government, I give you a personal assurance, you will get more money from a Labor government. I give you that assurance. This is a high-risk area in which there is considerably less money being spent on resources—and I understand your constraints—in a higher risk area than APRA are spending with respect to other super funds which are lower risk. I have to ask them for the latest figures anyway, when I see them tomorrow. It just seems to me to be an observation. We are dealing with people's retirement incomes; there is a very high-profile scandal at the moment involving a significant amount of moneys that were primarily, not exclusively, invested through self-managed super funds.

Mr D'Ascenzo—Yes, and I think it is up to us to make sure that we are well on top of any emergent or increasing risk in this area, and that is where we make the choices of allocating resources from somewhere else to this area and vice versa. What we have currently is already a ramp up of what we had.

Senator SHERRY—Yes, I understand that, and I note, too, that you are spending more than the levy, which means the cost recovery principle is not being applied, is it? At the moment, you are not fully recovering costs to regulate the area. Is there to be an increase in the levy for regulation in this area? Have you heard of anything?

Mr D'Ascenzo—I am not aware of that.

Senator SHERRY—At the moment, on those figures supplied to me, you are looking at about \$13½ million that goes into consolidated revenue, and you are spending about \$18.3 million. Frankly, I think you are struggling in terms of the regulation in this area, but you are spending \$5 million more. In that speech, you said:

To date, all of our compliance activities for self managed superannuation funds planned for 2005-06 are on track.

To which compliance activities were you referring when you said they were on track?

Mr D'Ascenzo—The estimate of doing 3,600 audits, so for that period of time in the year, we had the number of audits that we expected to have at that time.

Senator SHERRY—As to the other issue in that speech, you identified the investments held by asset class. There is a little pie graph; do you recall that?

Mr D'Ascenzo—Vaguely.

Senator SHERRY—It showed that 30 per cent of the assets were held as cash and term deposits; is that correct?

Mr D'Ascenzo—That is the information I have.

Senator SHERRY—It seems to me to be a very high figure.

Ms Vivian—That is based on the information that the funds returned to us in their income tax returns and how they classified the information.

Senator SHERRY—What about the prudent person principle test here and its application? With respect to the application of that to other superannuation funds, I am not aware of any super funds that carry 30 per cent cash and term deposits. Did you examine the prudent person test?

Ms Vivian—What we were just pulling out there is that some people were interested in where and what self-managed super funds were investing in. People indicated the different areas of their investment as information provided in their income tax returns, so it was really more just giving some information back to the industry.

Senator SHERRY—Okay, so you do not proactively do a representative survey, for example, on this issue or the level of fees or things like that?

Ms Vivian—No.

Senator SHERRY—I do recall us discussing this on a previous occasion. You seemed to indicate that you were going to do some work in this area.

Ms Vivian—What you might be referring to is that during the last estimates you asked us about providing more statistical information from what we collected. Firstly, this year's tax statistics that are currently available on our internet site have a bit more information; secondly, we have a consultative paper out with the super consultative committee regarding what would be the areas in which they thought we could provide further information. I am expecting them to come back in about mid-June, although I will be checking with it because I think a number of them may have some other priorities at the moment in terms of responding to government. Once we get that back in, we were then looking to see what we could do to provide the information. I mentioned before that we would then look to either both improve tax statistics or to see if we could put some further information up on our website.

Senator SHERRY—Are you liaising with APRA on this?

Ms Vivian—APRA is on our super consultative committee, yes.

Senator SHERRY—APRA publish data which I think is useful.

Ms Vivian—We provide some of that data to them, I think.

Senator SHERRY—That is right, but it is limited. You get good data—I think it could be better—on other super funds across a range of the indicators and information, but you do not get anywhere near the same consistency when you come to self-managed super funds. Will you be endeavouring to get a greater level of consistent data? I am not saying it would be identical in terms of its presentation.

Ms Vivian—I think that is something we would have a look at and certainly discuss with APRA.

Senator SHERRY—Some 25 to 30 per cent of superannuation assets are now held through self-managed super funds. I cannot recall the latest figure, but it is certainly a very substantial proportion.

Mr D'Ascenzo—I think it is in my presentation.

Senator SHERRY—In your speech?

Mr D'Ascenzo—In one of those charts. It is actually quite a large proportion.

Ms Vivian—It is \$165 billion.

Senator SHERRY—Don't you think it is useful to have consistent data across types of super funds?

Ms Vivian—We will certainly be looking at it. I am just not sure of the level of information that we collect versus APRA; that is why I need to check it. At one level, with 300,000 funds, we are effectively looking at what is actually passed through to us.

Senator SHERRY—They are down in the hundreds now, and even then they are having trouble getting these commission details out of some of these retail funds. There are not many of them, but that is an issue I will pursue with them. There needs to be some issue of representative survey—I would not suggest that you do it for all 300,000; you know how reasonable I am about these things—covering asset types, fees, charges, that sort of thing, along the lines of the APRA data or consistent with that. I think it would be in everyone's interests, frankly.

Mr D'Ascenzo—Wouldn't the return form information be more accurate?

Senator SHERRY—Sorry?

Mr D'Ascenzo—Why wouldn't we use the return form information?

Senator SHERRY—If you want to.

Mr D'Ascenzo—That is how we gather that sort of information.

Senator SHERRY—My concern is: is it representative? The other funds are required to complete a form. I do not know whether you would be going that far; it is just representative data. Trying to get it from all 300,000 self-managed super funds I think would be a pretty tall order.

Ms Vivian—We are proposing to provide the statistics based on the return information that they lodge with us. Whilst I am a little hesitant, but happy, to look at what we can do to provide some sort of similarity with the APRA data, I think they might actually do a separate survey to the funds to get some of that information.

Senator SHERRY—Yes, they do; there is a separate form.

Ms Vivian—So the basis for our looking to provide more data at this stage is certainly only on the basis of the information that is lodged on their income tax return.

Senator SHERRY—Yes. It would just be useful to try to get a greater consistency of data across all sectors.

Ms Vivian—We are happy to look at that.

Senator SHERRY—And which is representative, because, as I say, 30 per cent cash and term deposits in self-managed super funds I think is a cause of concern in terms of both diversification and maximisation of return.

Senator MURRAY—You can contest that. It shows signs of a very conservative approach and a non-risk approach. It is the safest of all investments.

Senator SHERRY—And the lowest rate of return.

Senator MURRAY—That is right; that is why it is the safest.

Senator SHERRY—I am not sure it is unsafe. If you do a balance—it is a discussion about portfolio investment theory which I do not think is appropriate for here.

Senator MURRAY—Yes, it is probably not the right time to debate it.

Senator SHERRY—It is the theft and fraud and the activities of Westpoint that I am more concerned about when it comes to safety.

Senator MURRAY—Yes.

Senator SHERRY—A very important issue—and I hope there is someone who can help me; I think I have finished the super issues—is the paper that the tax office is using.

Mr D'Ascenzo—That our printer is using?

Senator SHERRY—It is your printer, yes, but you buy it.

Mr D'Ascenzo—No, the printer buys it. We have contracted the printer.

Senator SHERRY—Well, you are obviously forewarned, Mr D'Ascenzo.

Senator Minchin—It had better be made from Tasmanian trees, mate!

Senator SHERRY—That is right; I have a vested interest in those Tasmanian trees being cut down. I have never made any apology for it, either.

Senator Minchin—No, that is fair enough.

Senator SHERRY—Let us take the *TaxPack*: where is the paper coming from?

Mr D'Ascenzo—We have information on that. Again, our contract is with the printer. The printing has gone to a tender process, and I understand that the majority of the paper is coming from an overseas source.

Senator SHERRY—Oh dear, look—

Mr D'Ascenzo—I think the Australian content is in the order of 16 per cent.

Senator SHERRY—Sixteen per cent; you are remarkably well informed, given it is a question about paper. What is the size of the contract, approximately?

Mr Konza—I would have to take that on notice. It is a printing contract, so there is the paper content but the bigger part is the actual—

Senator SHERRY—What is the printing contract, approximately?

Mr Konza—I do not know. I will have to take that on notice.

Senator SHERRY—Well, Mr D'Ascenzo is remarkably well informed. Sixteen per cent is Australian paper. Do we know what countries the foreign paper is coming from?

Mr D'Ascenzo—No, I have not got that information.

Senator SHERRY—Can you take it on notice?

Mr D'Ascenzo—Sure.

Senator SHERRY—Can you give me some indication—and I will not hold you to the nearest million—of whether we are looking at tens of millions of dollars for the *TaxPack* contract?

Mr D'Ascenzo—I would have thought it would be a large contract.

Senator SHERRY—How many copies of the *TaxPack* do you have printed each year, approximately?

Mr D'Ascenzo—It varies because we are reducing the number of *TaxPacks* because of the success of our e-tax. As well as the *TaxPack* there are a range of associated forms, there are short forms—

Senator SHERRY—Is that all part of the contract?

Mr D'Ascenzo—I think it is but I could not guarantee that.

Mr Konza—In very approximate terms, three million *TaxPacks* might be printed.

Senator SHERRY—The approximate cost?

Mr Konza—I do not know the cost.

Senator SHERRY—So it is in the millions, and unfortunately most of the paper is coming from overseas. You did not place any tender requirements to use domestic Australian paper?

Mr D'Ascenzo—No.

Senator SHERRY—Why not?

Mr D'Ascenzo—I would have to check with our procurement area but it could have to do with the trade agreements.

Mr Konza—The overriding requirement under the financial management act, I am advised, is value for money. A requirement that we use only Australian paper could contravene certain of our trade agreements. But, so far as the commissioner's role as head of a government organisation is concerned, the value for money principle is paramount and the cost savings that were able to be made by using the overseas sourced paper has swung that contract.

Senator SHERRY—Do you know what the cost savings were?

Mr Konza—No. I did not bring any pricing details. I do not even have any approximate figures in my head.

Mr D'Ascenzo—My chief finance officer was keen to advise me that the procurement guidelines were closely followed.

Senator SHERRY—Presumably there are no guidelines about use, non-use, limited use of overseas paper in these procurement guidelines?

Mr D'Ascenzo—If there had been we would have put it in.

Mr Konza—I am advised that the procurement guidelines prohibit those sorts of restrictions because of the potential for it to contravene trade agreements.

Senator SHERRY—When we are looking at approximately 16 per cent Australian paper—I hope it is coming from Tasmania—can you advise me where the 16 per cent Australian content is coming from?

Mr D'Ascenzo—I think the 16 per cent is recycled paper that had been available from Australian sources.

Mr Konza—No. The 16 per cent is about one-third made up of the paper that goes into the cover, which of course is a higher grade paper than the actual contents pages, and the other two-thirds is paper left over from last year's print run. New paper that has been purchased for this year's *TaxPack* is restricted to the cover of the *TaxPack*. I might note that, in this context, I would estimate that the tax office prints about 25 per cent of the number of tax packs that it once printed. We had about 1.5 million tax returns lodged on *TaxPack* last year and we had 1.3-odd million tax returns lodged using e-tax. Following the trend lines that have been going for several years now, it would seem almost inevitable that this year e-tax will outstrip *TaxPack*.

Senator SHERRY—For the first time?

Mr Konza—For the first time as the primary self-lodgment vehicle.

Senator SHERRY—Do I recall a discussion last time about a problem with storing the tax returns?

Mr Konza—That was the odour—

Senator SHERRY—Chemical odour or something.

Mr Konza—The odour at our Penrith storage bays, yes.

Senator SHERRY—Is that because of the paper or the printing on the paper?

Mr Konza—I recall the interrogation that occurred here on that topic last time but I do not actually recall—we had chemical testing done. There were staff complaints that the paper, when stored in such quantities, was emitting some sort of odour. I do not know how it was resolved in the end.

Senator SHERRY—It did get a bit of a run in the media, as I recall. There was some great concern and interest amongst journalists and the public about poisoned tax staff. Could you follow that up, take it on notice and see what has resulted from that?

Mr Konza—Sure.

Senator SHERRY—That is a side issue to this use of foreign paper. Is the *TaxPack* the biggest contract that the tax office has each year in terms of a printing job?

Mr Konza—I would be speculating so I think it might be best if I take it on notice along with the cost information that you have already asked for.

Senator SHERRY—What other major printing jobs would be carried out by the ATO?

Mr Konza—New initiatives from one year to the next can be very large—for example, there were a great many pamphlets produced on Choice. Although *TaxPack*, being 140 pages or so, is pretty big.

Senator SHERRY—What printing contracts have you got coming up of a reasonable size?

Mr Konza—I would not know. I do not know that anyone would know.

Mr D'Ascenzo—This contract is an annual contract, at about tax time. Tax time is coming up and that is why it is a big—

Senator SHERRY—And obviously you vary it to a degree each year.

Mr D'Ascenzo—That is right.

Senator SHERRY—So it is an annual print job. Let us take the Choice material that was produced. What paper was that printed on, Australian sourced or foreign sourced?

Mr Konza—I certainly do not know. I do not know whether our superannuation line representative knows.

Senator SHERRY—Could you take this on notice: could you look at your top 10 print jobs for this financial year and the last financial year, and provide me with an analysis of the paper that was used, the cost of the print job, the proportion of paper that was sourced from Australia, the proportion of the paper that was sourced from overseas and which countries overseas.

Mr Konza—We may not know that data.

Senator SHERRY—You could go to the printer, surely.

Mr Konza—Yes, we could, but it depends on how many printers there are. There could be a great deal of work involved.

Senator SHERRY—I have to say that Mr Evans, the Clerk of the Senate, was asked about this issue at the estimates for the Senate and he got back a letter to us—it was not to me; I did not ask about it—the next day, I think. The letter included details of the components of foreign paper and where it was sourced from.

Mr D'Ascenzo—We will see what we can provide to you.

Senator SHERRY—This is an important issue for the people that I represent in Tasmania, because, rightly, there is very strong concern about the increasing quantities of foreign paper being used in this country. It is a serious matter, certainly for people who live on the north-west coast of Tasmania, where part of our paper industry is located. I want to talk about some issues relating to prosecutions. We had a discussion on the last occasion about the relationship with the ATO and the DPP involving prosecution guidelines. Mr D'Ascenzo, you indicated at the last estimates hearing that whether or not to prosecute a particular case was ultimately a matter for the DPP.

Mr D'Ascenzo—That is correct.

Senator SHERRY—That is what you said. But you said that the DPP is a partner with you in the process.

Mr D'Ascenzo—In that it normally has referrals from us on matters either investigated by ourselves or by ourselves and the Australian Federal Police or by the Australian Federal Police on our behalf. In that sense they are part of that process. In Operation Wickenby, the Director of Public Prosecutions is part of the joint task force.

Senator SHERRY—Are you aware of the evidence that Mr Bugg, the Commonwealth DPP, gave at the February estimates to Senator Ludwig?

Mr D'Ascenzo—No, I am not aware of it.

Senator SHERRY—I thought you might have been made aware of it. Senator Ludwig asked Mr Bugg:

In terms of a good working relationship with ASIC, ATO and the ACCC, do you contact them to ask them if they are sitting on any work or any briefs that should come across or if they are working on something that is coming across?

Mr Bugg replied:

Pretty much as I said a moment ago, at a regional liaison meeting the regional commissioner if it is ASIC or the deputy commissioner if it is the ATO might say, 'We've got this big matter and we are just about ready to start talking to you about where it should go to from here. We think half of it should be prosecuted, the other half should be dealt with by way of civil penalty, but we will need to sit down and talk to you about it. That will probably be in a couple of months.' That is the sort of exercise that goes on. Rarely these days is the truck parked in our backyard without reasonable notice.

Senator Ludwig asked:

Given what you have said about it being unusual that the truck would turn up without someone phoning you beforehand, is the Gerard case one where they would talk to you beforehand?

Mr Bugg responded:

No, I think the then commissioner made a public statement. The matter was never referred to my office, so that did not ever come our way. If I could just pause to make a comment about that, it is quite interesting how, in a sense, I think some commentators believe that we are the gatekeeper on what gets prosecuted and what does not. That is certainly true on the application of the prosecution policy of the Commonwealth, which I was outlining earlier. We are totally dependent on what is referred to us by the 40-odd agencies who refer matters to us following their investigation or examination of matters over which they have regulatory responsibility.

Senator Ludwig asked:

But you could ask for a brief if you wanted one?

Mr Bugg replied:

I have no power to direct an agency to refer a matter to me.

If Mr Bugg, the DPP, is totally dependent, to use his words, on what is referred to them by the ATO, in what sense is the DPP a partner of the ATO in the process of deciding whether or not to prosecute?

Mr D'Ascenzo—Again, I am not sure I put 'partner' in the context of the decision to prosecute because the decision to prosecute ultimately is a matter for the DPP. In terms of the partnership arrangement, we have a memorandum of understanding with the DPP that indicates that we will refer to them matters that fall within the referral guidelines which they

think are appropriate. They are worked out together and we then comply with the guidelines that are worked out mutually amongst ourselves.

Senator SHERRY—If you decided—not you necessarily personally, but if the tax office decides—not to refer a matter or not to discuss it with the DPP, not to brief them, in effect you make the call, don't you?

Mr D'Ascenzo—I think there is a practical reality to that point. I think this is very important: you work it out with the DPP by saying, 'Which cases do you want referred to you that you think are appropriate for prosecution action?' and you outline the sort of matters that warrant that exercise. You then comply with those agreed guidelines in referring matters to the DPP. In doing that, quite properly, you need to make choices about whether or not a matter falls within those referral guidelines. If they do and if you come to the conclusion that they should, then they are referred. If you properly conclude that no, you do not think they fall within the referral guidelines then you do not normally refer it.

Now you might say, 'How do you know that works; that is the theory, how do you know it works?' It works this way: there are a whole range of processes that we in the tax office have to take when we go about questions of referrals or questions of settlement or otherwise. There are a whole range of checks and balances, there are documentation requirements, there is signing and countersigning at various levels. There are specific delegations. Ultimately, it is put in to the pile for quality assurance by another group of people. So there are checks and balances in the system to make sure that it works appropriately. On top of all that there are external scrutineers like the Australian National Audit Office that can look at those matters. There are a range of checks and balances so that the system should work in accordance with the ultimate or underlying policy intent as worked out with the DPP.

Senator SHERRY—Regarding the partnership guidelines for investigation and prosecution, Mr Bugg gave a speech on 15 May called 'DPP Partnerships with the ATO' in which he summarised the DPP-ATO guidelines. I assume they are what you referred to earlier.

Mr D'Ascenzo—Yes, they are.

Senator SHERRY—He described the guidelines as follows:

The responsibility for investigating tax offences rests with the ATO and AFP with the DPP role at the investigation stage limited to providing legal advice;

The primary responsibility for prosecuting such offences rests with the DPP, with the DPP agreeing that ATO officers may conduct certain prosecutions for offences against taxation laws;

Offences involving taxation matters should be prosecuted by the DPP under the Crimes Act or the Crimes (Taxation Offences) Act where: serious fraud on the revenue was involved; and cases in which there is a circumstance of aggravation (eg bribery or corruption involving ATO officers);

DPP agreed that ATO officers may conduct summary prosecutions for offences against the TAA and other taxation laws so long as certain listed matters were referred to the DPP such as (and this list is by no means exhaustive): effectively all matters where there is a plea of not guilty; matters involving "high profile persons" appeals from summary taxation prosecutions.

Is that a correct summary of the relationships and the guidelines that you follow?

Mr D'Ascenzo—I think it is, generally. There are other guidelines, including the guidelines we provide to our people, and there is a recent memorandum of understanding that Mr Bugg and I recently signed.

Senator SHERRY—Mr Bugg's reference to high-profile persons: what characterises a high-profile person for these purposes?

Mr D'Ascenzo—I think it takes its ordinary meaning of someone who is in the public eye. We talked about high-profile people previously in the high-wealth individual space.

Senator SHERRY—It could be a sporting, media, political identity?

Mr D'Ascenzo—It could be. I think anything that is likely to attract a lot of public attention is something that we would refer on to the DPP for decision, provided it falls within the guidelines that we think that there is a reasonable case to answer.

Senator SHERRY—I asked you questions at the last estimates about the ATO-DPP prosecution policy. There was a reasonably limited discussion about it. In response to questions about prosecution policy, you said:

... there is a responsibility for all government departments to determine whether the expenditure of more funds on a certain matter is likely to provide a commensurate benefit to the Commonwealth.

How is the notion of 'commensurate benefit' relevant to the question of whether or not to prosecute? Isn't prosecution about something other than just recovering the revenue?

Mr D'Ascenzo—I thought that comment might have been in the context of settlements—whether or not you would settle a matter—and the question was, 'What are the chances of recovering more for the Commonwealth in some other way?'

Senator SHERRY—What matters do you take into account when considering whether or not to prosecute?

Mr D'Ascenzo—The first situation is whether the facts provide a prima facie or a reasonable case that could found a prosecution in court. Then, if the case falls within the referral guidelines you mentioned, we would refer those to the DPP to make their choice. On the other hand, if we thought that, on the face of it, it was not such that it would be a reasonable case to take to court then we would not refer it.

Senator SHERRY—Do you take into account matters such as the accused person's finances or their level of legal representation in considering whether or not to proceed?

Mr D'Ascenzo—I think the question comes up this way: is the matter, on the facts, one that warrants prosecution based on a reasonable likelihood that, if we were to refer this matter, the evidence available to us and further evidence the AFP or others could ascertain would lead to a successful prosecution? That is then provided to the DPP and they make the ultimate choice if it falls within those guidelines.

Senator SHERRY—Where you are able to ascertain intentional disregard of the tax law and evasion of millions of dollars in tax, doesn't that usually warrant prosecution?

Mr D'Ascenzo—If you have evidence of that, that is the sort of case that would warrant prosecution.

Senator SHERRY—According to the DPP, there is a three-stage test when considering whether or not to prosecute. This is what he said on 27 February when he appeared before the Legal and Constitutional Legislation Committee:

... and the first stage is: is there a prima facie case? Then it is a qualitative analysis of the evidence that establishes that prima facie case: are there reasonable prospects of conviction? You are looking at the credibility of witnesses and a whole range of issues. If you determine that there are reasonable prospects of conviction then you consider whether a prosecution is warranted in the public interest, and there is a whole range of public interest factors in the published document. This is the Commonwealth policy and it applies to all agencies. It may determine that you will not prosecute but it would be a rare situation where we would say, 'It is not in the public interest that we should prosecute this matter.' We would then go back to the agency and say, 'There is a case there but it is really not in the public interest.'

Do you follow the three-stage test that the DPP has outlined here?

Mr D'Ascenzo—Yes. The DPP has outlined the prosecution policy of the Commonwealth and the guidance we provide to our people is consistent and aligned with those guidelines. In fact, my informal responses to your question reflected the same sort of concepts.

Senator SHERRY—The DPP, Mr Bugg, said at estimates that the first time he heard of the Mr Gerard matter was on the radio after the story was in the media. Is it the case that the ATO did not refer the Gerard matter to the DPP?

Mr D'Ascenzo—Do we want to get into an individual case of that nature?

Senator SHERRY—Mr Bugg was asked about this and he indicated on the record that it was not referred to him and the first time he heard about it was on the radio.

Mr D'Ascenzo—I am sure Mr Bugg would not want to say anything that is incorrect.

Senator SHERRY—If that is correct then it is correct to assume that the ATO did not refer the matter to him.

CHAIR—I think, Senator Sherry, that you are now trespassing beyond the convention of this committee which does not countenance questions about the affairs of individual taxpayers. I would ask you to move on to something else, please.

Senator SHERRY—Mr Bugg was able to comment on that and he is the DPP.

CHAIR—You have quoted Mr Bugg and what he said, you say, is on the public record. That is fine. Then you have gone further than that and asked Mr D'Ascenzo to comment on matters which you surmise arise from something Mr Bugg allegedly said on the public record. That is where I think you have gone over the line.

Senator SHERRY—I think it is a reasonable summation.

CHAIR—That is your opinion but the question is out of order.

Senator SHERRY—You know the respect in which I hold you, Chair, so I am going to conclude my questioning on this matter.

Proceedings suspended from 9.46 pm to 9.59 pm

Senator SHERRY—There was a question put on notice about prosecution and DPP referrals at additional estimates in February 2006 by Senator Ludwig to which I want to refer;

it is number AT95. According to the answers to additional estimates, the ATO has figures on the amount of briefs returned to the ATO from the DPP for 2004-05. In the answer to the series of questions relating to those 31 cases returned to the ATO in 2004-05, how many briefs were returned without action?

Mr D'Ascenzo—Without action by the DPP?

Senator SHERRY—Yes.

Mr D'Ascenzo—My reading of that was that no action was taken in 31 of them.

Senator SHERRY—Of those 31, were any prosecuted?

Mr D'Ascenzo—No. The fact that they returned the brief to us meant that they have taken no action on those briefs.

Senator SHERRY—Are the identities and penalties of those who were prosecuted a matter of public record?

Mr D'Ascenzo—Prosecutions and the outcome would be a matter of public record but that would be a matter within the DPP's knowledge and records.

Senator SHERRY—Are you able to supply the committee with those details? Surely you would have that on file.

Mr D'Ascenzo—We could work with the DPP and see what information we can provide along those lines.

Senator SHERRY—Of the almost 700 cases investigated by the ATO between 2001 and 2005, excluding the cases sent to the DPP, how many were prosecuted?

Mr D'Ascenzo—These are the ones on which we actually briefed the DPP. The other prosecutions are more in-house prosecutions which are more in terms of the non-lodgment type area. Once you have a defended action, our referral guidelines say that that has to be referred on to the DPP. The in-house ones are really the ones about nonlodgment, late lodgement—those sorts of issues. I do not think I have the figures available here but I can provide them to the committee if you wish. They are in the annual report as well.

Senator SHERRY—Could you provide how many were prosecuted and in dollar terms what was recovered?

Mr D'Ascenzo—It is not a recovery if you prosecute. It could be a sanction, it could be a court fine, it could be a good behaviour bond.

Senator SHERRY—It could be a range of things. Could you provide the detail of what moneys were obtained, if I can use that expression?

Mr D'Ascenzo—Even if it is a fine it is not to the tax office, it would be through the court processes.

Senator SHERRY—I know it is not to the tax office, but there is a money that flows from the action. What was the money that flowed from the action? I know it does not flow to the tax office. These prosecutions I am asking about, are they a matter for public record?

Mr D'Ascenzo—Yes. All prosecutions are before a court and are for public record unless the court makes an order of closed, in camera, which I do not think is normal for prosecution action.

Senator SHERRY—Could you please supply a list of the identities and penalties of those prosecuted? Will you take that on notice?

Mr D'Ascenzo—My colleague was just saying to me that we had advice from the Solicitor-General to say that, just because something is on the record, it may still come under the secrecy provisions, but I think that, if we obtained it for the purposes of helping this committee, it would be in the ordinary course of our duties.

Senator SHERRY—I did not quite catch that.

Mr D'Ascenzo—It was a question about even though something is public, we have advice from the Solicitor-General that it may still be in breach of our secrecy provisions if we recount that from our own knowledge rather than from the public record. There is a proviso in our secrecy provision that says 'in the ordinary course of our duties', and I think this would be a situation where providing that information to the committee, pursuant to request by the committee, is in the ordinary course of our duties. It will be a difficult manual exercise to do that, because we are not the ones that keep records of court actions, but we will see what we can do.

Senator SHERRY—You would record a conclusion presumably on a file?

Mr D'Ascenzo—That would be good practice. That would mean that we would have to go and dig up all the files and manually collate the information.

Senator SHERRY—I have to be, on this occasion, perhaps unreasonable. We discussed facilitation payments at the last estimates. Section 26-52(4) of the Income Tax Assessment Act describes facilitation as:

An amount is not a *bribe to a foreign public official* if it is incurred for the sole or dominant purpose of expediting or securing the performance of a routine government action of a minor nature.

In contrast, the Criminal Code Act requires:

... not only the same criteria as in the ITAA, through part B, but also two further conditions to make out a defence against bribery. It is necessary to show that, as soon as practicable after the conduct occurred, the person made a record of the conduct. More importantly, it must be proved in A, that the value of the benefit was of minor nature.

Surely, under this definition, facilitation payments could be major not minor in value, even for, say, a hypothetical \$100 million, for example. Theoretically, is it not possible that a facilitation payment could be minor in nature like a simple contract but could be significant in market value?

Mr D'Ascenzo—I am not sure that I would take that interpretation off hand. I would have thought a more ordinary reading of that would be that there might be some relativity in relation to the particular transaction. I think the whole scheme of that act talks about things of a minor nature. The sorts of examples that it gives are things of a minor nature being of low market value.

Mr Konza—I think the question overlooks subparagraph 5(d) of that. Section 26-52(5)(d) provides that such an arrangement:

does not involve encouraging a decision about:

- (i) whether to award new business; or
- (ii) whether to continue existing business with a particular person; or
- (iii) the terms of new business or existing business.

You would think that particularly sub-subparagraphs (i) and (iii)—the decision to award new business or the terms of a new or existing business—would take out most of those valuable cases that you might have been positing.

Senator SHERRY—That particular subclause, if I can refer to it, would become the sort of predominant test?

Mr Konza—The previous subparagraph talks about some of these routine government actions such as getting a licence and a permit, police protection, mail collection or delivery and so forth. The major proviso is in subparagraph (c), involving a decision, and subparagraph (d), encouraging a decision. Between those two you would think that they would cover the high-value instances you were thinking about.

Senator SHERRY—I think again we discussed this on the previous occasion. Does the tax office still hold the view that the Income Tax Assessment Act regarding facilitation payments does not need to be brought into line with the reciprocal Criminal Code sections—that they do not need to be identical?

Mr D'Ascenzo—All I can say is that the policy of this provision is that it is about allowing facilitation payments that are for the dominant purpose of expediting and securing the performance of a routine government action of a minor nature. It seems to me to apply to minor activities not major activities. I am not sure where the difference is or what difference it has.

Senator SHERRY—You do not believe there is a practical difference?

Mr D'Ascenzo—Again my reading of it is that a routine government action of a minor nature is a routine government action of a minor nature, which is not something of significantly high value—it is not major, it is not nonroutine.

Senator SHERRY—The justice minister, Mr Ellison, recently put chief executives of Australia's top 100 listed companies on notice to stamp out kickbacks involving foreign officials. Has the ATO launched a crackdown on corporate tax deductibility claims on facilitation payments made on international contracts?

Mr D'Ascenzo—We are certainly building it into our compliance program. I am not sure whether or not there are large instances of facilitation payments—

Senator SHERRY—No, I have not got to that point yet. You say you are building it in, what does that mean?

Mr D'Ascenzo—As part of our checklists for our auditors.

Senator SHERRY—It has not been on the checklist?

Mr D'Ascenzo—No, it was one of the recommendations of the OECD to put it onto our checklist.

Senator SHERRY—What does that involve?

Mr Konza—The instructions that we give our auditors are being amended to ask them to direct their attention to independent lists that are maintained of countries in which corruption can be a significant problem in doing business. We instructed them to then turn their attention to whether the taxpayer that they are reviewing has conducted any substantial amount of business in any of the countries on that list. If they have conducted any business in that country then they are to examine whether the company would have its own internal controls to ensure that section 26-52 is being complied with. In the absence of the discovery of those controls, further audit work might then be required.

Senator SHERRY—Is there any process of increasing awareness amongst corporations about the change?

Mr Konza—We are in the process of developing a revised booklet for large business. Any changes in our operations would be documented in that and provided to boards and CEOs of large public companies.

Senator SHERRY—There is a revamp of a booklet; when is that to be circulated?

Mr Konza—We are in the process of doing it in consultation with the Corporate Tax Association. We are hoping to release it some time in August as part of our symposium that we are doing with large corporates.

Senator SHERRY—Presumably you already have a booklet that has gone out on a previous occasions on this?

Mr Konza—On what we are doing in relation to our compliance activities, vis-a-vis large corporates, but it did not include specifically questions of bribery or facilitation payments.

Senator SHERRY—Will there be attention drawn to the fact that this is a new, revamped area?

Mr D'Ascenzo—Yes. I think it makes sense to alert people to this activity. We also have a range of other things, like adding some pointers on our website to our work in that area. I mentioned beforehand the task of including it in our checklist for our auditors. Basically, we are following the OECD recommendations and making it more explicit.

Senator SHERRY—Okay, you will be making it more explicit and you will be drawing attention to the fact that it is more explicit?

Mr D'Ascenzo—That is right.

Senator SHERRY—Will this also involve small to medium sized businesses?

Mr Konza—The procedures that I outlined would apply to auditors of small and medium enterprises, yes.

Senator SHERRY—Is it focused on any particular sectors? There is not a different priority accorded to particular sectors?

Mr Konza—No. One of the factors that goes into a case plan for a review of a taxpayer is the extent to which they have international dealings, for a whole lot of reasons of which you would be already aware. These processes would be a subset of the procedures that are used for reviewing any taxpayer in that situation.

Senator SHERRY—What is the penalty for a company found guilty of bribing foreign officials at the present time?

Mr D'Ascenzo—There is a question of whether or not you can claim a deduction for the amount of the bribe; the income tax law says you cannot. On the other hand, bribery itself can be a crime under the Crimes Act.

Senator SHERRY—Let us say you claim a deduction and obviously it is not a claimable deduction, what is the penalty in those circumstances?

Mr D'Ascenzo—The administrative penalty?

Senator SHERRY—Yes.

Mr D'Ascenzo—It really depends on whether it was done in intentional disregard of the law. If it was a conscious act with a purpose it could be as much as 75 per cent of the tax shortfall. If you claim a deduction of say \$100 and that meant that you paid \$30 less tax than you might otherwise have done, it could be 75 per cent of the \$30 as a penalty.

Senator SHERRY—If it was found to be disallowed as a deduction—and let us assume that you have said that it is not an allowable deduction—then there is a reassessment on the basis that it is a bribe, would it be the DPP who would deal with the issue of prosecution if it was a bribe as such and any penalties that arise from there?

Mr D'Ascenzo—It would. Then the DPP would think about whether or not the evidence was sufficient to have a prima facie case, as you mentioned in those guidelines. That would depend on perhaps the mens rea of appropriate controllers of the company. The DPP may take into account whether or not those prospects are sufficiently strong to make a charge. If not, the brief would be referred back to us.

Senator SHERRY—The DPP would make the call in respect to a bribery charge; you may probably be involved in evidence or material that would be presented to it.

Mr D'Ascenzo—That is right. We would be providing the DPP with what we had.

Senator SHERRY—Is the tax office aware of any particular—

Senator MURRAY—Before you go on from there with the same point, if I may, you can, on your own notion, decide to disallow the claim, can you?

Mr D'Ascenzo—We would disallow the claim in those circumstances.

Senator MURRAY—You would impose or not impose a penalty so either the claim would be disallowed and the cost to the company is the forgone allowance, or it is the forgone allowance plus the penalty. If the company wish to challenge that, they would then have to go to the AAT, I presume, in the first instance?

Mr D'Ascenzo—They could go straight to the Federal Court.

Senator MURRAY—They would have to prove that it was not a bribe.

Mr D'Ascenzo—They would have the onus of proof but based on a civil standard. If, ultimately, a charge were laid by the DPP in those circumstances, we would have to withdraw the penalty, because you cannot have double jeopardy on the culpability side.

Senator MURRAY—The point is, you can act without referring the matter to the DPP. You can make—

Mr D'Ascenzo—We would do all that but—

Senator MURRAY—You can act on your own appraisal.

Mr D'Ascenzo—That is right, but if it fell within our referral guidelines, we would then refer it to the DPP as well.

Senator SHERRY—I am not asking for the names, but are there any companies that are currently facing a check in respect to bribery? Are there any companies currently being checked by the tax office for claiming tax deductibility on facilitation payments?

Mr D'Ascenzo—I do not know. I cannot specifically say yes or no on that.

Senator SHERRY—I am not going to ask for the names, I am aware of that. Why can you not indicate?

Mr D'Ascenzo—I just do not know the nature of all our investigations.

Senator SHERRY—Is Mr Konza aware?

Mr Konza—I am not aware of any specific cases either. I make the observation that we are looking to put it into our procedures so at one level there will be companies that will be checked. That is stating the obvious, I think.

Senator SHERRY—According to a report in *The Age*—not that I always take reports in newspapers as gospel—there was a comment by Mr Paul Ingleby, who is the Chief Financial Officer of AWB. He said the Australian Tax Office was reviewing AWB's accounts and the company was cooperating. He said:

The ATO in its ordinary course is conducting a risk review. We are co-operating with that but all our advice is that these payments are deductible.

Are you aware of that press comment?

Mr D'Ascenzo—I did not follow that press comment. Now that you have brought it to my attention—

Senator SHERRY—On 25th May 2006. Are you aware of that, Mr Konza?

Mr Konza—No, I am not.

Senator SHERRY—As part of this upgrade, is the ATO devoting any extra resources to this focus or additional focus?

Mr D'Ascenzo—We are not treating it as an issue-specific audit topic. What we are saying is that, as you go through your risk analysis of the companies that have dealings with these sectors and countries where there is more chance of bribery or facilitation payments over and above what is intended in the law, you should look at those as part of your audit processes. It would be a risk factor that we would take into account in our selection and our examination of audit cases.

Senator SHERRY—Has the ATO taken advice that, where a bribe has been paid, if it were identified as a bribe, there would be no tax penalty even where it was found to be a bribe?

Mr D'Ascenzo—There are not guidelines of that nature that I know of. Regarding penalties, while we apply the law, the law itself sets the standards for penalty. The penalty standards are based on asking the following questions. Has someone taken reasonable care in completing their return? Have they been reckless? Has there been intentional disregard of the requirements of the law?

Senator SHERRY—In terms of cases settled in the 2004-05 financial year, how many were settled and recorded in the ATO's settlement register?

Mr D'Ascenzo—I will have to take that on notice, but I can give you that information.

Senator SHERRY—How many cases have been settled in 2005-06?

Mr D'Ascenzo—We can take that—

Senator SHERRY—Same question. How many cases in the two questions I have just asked have been subject to technical quality reviews under the ATO's Practice Statement Law Administration PS LA 2001/11 (GA)?

Mr D'Ascenzo—Again I will take that on notice, but I can make the point that they are part of our quality review processes. They are in the pool from which we do our quality reviews.

Senator SHERRY—What are the issues that have been identified by the technical quality reviews?

Mr D'Ascenzo—In relation to just general matters?

Senator SHERRY—Yes.

Mr D'Ascenzo—Generally speaking, our QA has been quite favourable. There is always room for improvement. I can list the outcomes of that review in providing you with the questions on notice that you asked.

Senator SHERRY—Who has conducted those? You say it is quite favourable, but who is one?

Mr D'Ascenzo—We have senior people from the ATO but in addition to that we also have an external representative; in other words, an external expert that is on contract to us and they are part of our review processes. So there is a level of external objectivity to our quality review processes.

Senator SHERRY—Is it one external person or is it more than one?

Mr D'Ascenzo—I think we have different teams that operate in different areas. For instance, there might be a team that works in the small business area and a team that works in the large business area. So there would be a range of different people on those different teams.

Senator SHERRY—In respect to the first two questions I asked, could you provide the names and positions of the external consultants who have sat on those reviews?

Mr D'Ascenzo—Yes.

Senator SHERRY—Thanks. How many of these cases have been settled at commissioner level? You would have to take that on notice, wouldn't you?

Mr D'Ascenzo—I do not think there would be a case that necessarily comes in or is isolated at commissioner level to say that it is settled at commissioner level. The whole beauty of these processes is that there is a process that involves a range of people, a range of checks and balances and signatories to these arrangements. It is not usual for any of those to involve the signature of the commissioner in the settlement of those cases. In fact, none strike me just from memory as having occurred that way.

Senator SHERRY—Perhaps you could check. Is the settlement register maintained on computer or is it on hard copy, or both?

Mr D'Ascenzo—I think it is on computer.

Senator SHERRY—You think—but could you check?

Mr D'Ascenzo—I will. I am sure it is on computer, but I just have not looked at it recently.

Senator SHERRY—Who puts the information onto the settlement register after the ATO has settled an audit with a taxpayer?

Mr D'Ascenzo—The case manager that is responsible for that case puts it onto the register.

Senator SHERRY—Who can access that settlement register?

Mr D'Ascenzo—They have to go through an area in the office of Chief Tax Counsel to access that register.

Senator SHERRY—What is that process?

Mr D'Ascenzo—You would need to explain what you wanted to access the register for and, if it is in the ordinary course of our duties, it would be allowed to occur.

Senator SHERRY—Has the settlement register been subject to any scrutiny by any authority outside the ATO? I am thinking here of the Inspector-General of Taxation or the Auditor-General or a parliamentary committee.

Mr Konza—The Auditor-General has done reviews of the application of our settlement guidelines in the past.

Senator SHERRY—Can you recall the last occasion?

Mr Konza—I can only recall that it occurred some years ago, but we should be able to check quite readily.

Senator SHERRY—Statistics such as the number of settlements, the amounts settled and the issues settled are recorded in the settlements register. Are there statistics in the ATO annual report on that?

Mr Konza—I am not sure that there are.

Senator SHERRY—Why are statistics not in the ATO annual report?

Mr D'Ascenzo—I do not think there is any specific reason.

Senator SHERRY—You do not have any objection if those statistics are supplied to parliament through the annual report?

Mr D'Ascenzo—No. It could be a good way of making these things more open and transparent.

Senator SHERRY—Good. In the event of a settlement arrangement of a large case audit, what would be deemed appropriate circumstances, particularly in terms of lost revenue?

Mr D'Ascenzo—It comes down very similarly to the question that was made by the DPP in prosecution, and that is, first and foremost, whether or not there is a reasonably arguable case to say that the position the ATO holds is a good one and tenable in court. The second question is not so much whether or not the argument might be tenable but whether or not the evidence is sufficiently fresh or admissible for that to go further to a court process.

To do that, usually in the large-case area you would have the case manager and they would almost invariably consult the internal tax counsel. There would finally be a sign-off to approve the settlement by an SES officer independent of that process. In large cases, almost invariably, there would also be external counsel and maybe the Australian Government Solicitor. All of them would come to a consensus that the best way of getting the best value for the Commonwealth in relation to this matter might well be a settlement. That would be documented and put on the register, and it would be available in the pool of cases that were looked at in terms of post-completion review in terms of quality control. That would be available also for external scrutineers like the ANAO.

Senator SHERRY—In accepting settlement, there is obviously a revenue that the tax office believes should be received but it may accept a lesser revenue. Are there any statistics available on that?

Mr D'Ascenzo—I do not think our register keeps that counterfactual—what might otherwise have been the case. Sometimes it is not so much a compromise of a debt in that nature; it is sometimes an acceptance of the taxpayer's argument in relation to certain aspects of a matter.

Senator SHERRY—Do you think it would be useful to have some statistics on that?

Mr D'Ascenzo—All it says is that, having reviewed all the evidence, that was what we thought the liability should be.

Senator SHERRY—It might be a useful additional oversight in terms of performance and valuation, might it not?

Mr Konza—For example, in certain valuation issues which are quite often raised there is a wide spectrum of possible results. To place on the register the upper limit might be quite misleading as to what a likely result would be.

Mr D'Ascenzo—I am putting the argument here to this committee that there is a very serious and sound process of checks and balances so that these arrangements are done ultimately in a very proper way, and in a way that ultimately benefits the Commonwealth, or is seen to be benefiting the Commonwealth. They usually involve a range of other players, including external counsel; there are signatures and delegations that differ in terms of who carries on the carriage of the matter to who can co-sign off a certain matter. There is quality control afterwards and there is also openness in terms of external scrutiny. It is very important in terms of community confidence that not only does that message get through but everything

is done that is reasonably possible to make it as open and transparent as possible. I am attuned to suggestions that can open that transparency and give that confidence to the community.

As Mr Konza said, if we try to get down to what might be a precise counterfactual we might get into difficult areas, but it can be a situation where there is a compromise to indicate what that compromise is in the order of. In those situations where it is not a compromise but where we consider that, based on the information and new information provided, we are persuaded that the amount of liability is lower than originally said, then there is no difference. Ultimately, this is because it is not really a settlement; it is an agreement with the taxpayer that, on the facts of those matters, it should be that lower amount.

Senator SHERRY—Give me a minute to consider that.

Mr D'Ascenzo—I am very keen to ensure that the very proper and rigorous processes that we would take within the organisation are recognised by the community.

Senator SHERRY—There was one matter that I meant to ask about earlier which I was going to put on notice. There is no need for Ms Vivian to come to the table; I will just put it on notice and draw your attention to it. In the answer to my question regarding the SMSFs that lodged an annual return in 2003-04, there were 96,882 that contained amounts less than \$200,000. Could I have the number that lodged an income return in 2003-04 to compare the relative number of 96,882 with the number that were lodged?

Still on enforcement, there was an article in the media recently, in the *Sydney Morning Herald*, 'Underground economy baffles Tax Office, cash operators difficult to find', of Wednesday 1 March 2006. It did cause quite a deal of radio and TV commentary. Are you aware of that? It was about flushing out cash operators in the dancing sector of the adult industry.

Mr Konza—Yes.

Senator SHERRY—Does that ring a bell? I thought it might. I got a lot of comments in the Burnie pub about this. I have this Burnie pub test. The ANAO did an audit of the ATO's efforts to control and evaluate the black economy. I have not read this audit report—I normally read them—but I am going on the press coverage. Apparently, ATO officers had made field visits to strip clubs. Is that correct?

Mr Konza—Yes, it is.

Senator SHERRY—This was part of the cash economy evaluation was it?

Mr Konza—Our approach to the cash economy involves us identifying certain high-risk industries. The adult industry, which involves not only the dancing clubs but brothels and escort services, was identified as one of those high-risk industries despite some of the significant difficulties that you encounter when improving compliance in an industry like that.

Senator SHERRY—Yes.

Mr Konza—Our officers convened groups of brothel owners and explained to them their tax obligations. Similarly with the dance clubs, they had to go to the clubs and talk to the owners. There were high rates of non-compliance.

Senator SHERRY—Non-compliance in respect to what areas of tax?

Mr Konza—Omitted income by the dancers.

Senator SHERRY—Right.

Mr Konza—Most strikingly—and I cannot give you the numbers—there was a very high rate of welfare fraud as well amongst the dancers. We worked closely with Centrelink to assist them to address those issues.

Senator SHERRY—Welfare fraud—when you talk about the non-compliance in respect to tax, what about GST? Presumably there are cover charges that are made?

Mr Konza—That is right. Certainly with the business owners there were issues about their GST liabilities as well.

Senator SHERRY—Did many of them not have an ABN number for example?

Mr Konza—I do not know that but think it unlikely as in most of these established businesses they are quite keen to claim their input tax credits.

Senator SHERRY—What about superannuation guarantee enforcement?

Mr Konza—I do not think superannuation guarantee enforcement was a particular part of this project. This project was really starting at fundamentals—registration, deduction of tax in the first place and declaration of income. We have an employer obligation workforce and they have been doing work on superannuation guarantee awareness. When they identify cases they have referred them to the superannuation workforce.

Senator SHERRY—What about tipping; I would image that tipping is significant in a place like this. What is your attitude to tips as assessable income?

Mr Konza—Clearly they are assessable income. *TaxPack* is very clear and our tax returns have always been clear that that is the case.

Senator SHERRY—Did you leave copies of the *TaxPack* there?

Mr Konza—Yes, we did leave documentation there. We created brochures for the adult industry to hand out and left them with employers, and we checked on their registration rates et cetera.

Mr D'Ascenzo—We have about 600 people that focus on cash economy high risk industries. These include building and construction, licensed hotels, motor vehicle wholesaling and retailing, tourism, low-doc loans and loan brokers, restaurants, cafes, takeaway food outlets, barter, fishing, the adult industry, nail artists, cheque cashing facilitation, horse racing and exports. There is a range of industries on which we are focused.

We are also doing a lot more in terms of data matching for micro businesses; ATO data matching plans for 2005-06 are for approximately 3 million third party transactions to be matched against taxpayer records. In addition we plan to match about 7.2 million activity statements and income tax return labels to identify businesses outside of industry norms. We have to look at it in a broad sense. It is not an easy matter to tackle. We are finding that one area of risk is business to the consumer; that is where the GST system does not provide an incentive to be in the system. Again, we are using data matching in trying to match third party information with information provided to us or lodged or not lodged with us, including things like new domestic building approvals, and matching that against our lodgment records.

Senator SHERRY—Brothels and dance clubs et cetera would be one of the more difficult cash economy areas I would imagine. Do you have a regular visitation schedule or was it just decided to do this as a one-off? Will this continue?

Mr Konza—The various industries that have been selected as high-risk industries are subject to an ongoing program. The aim of that program is to establish compliance levels and work to the stage where we have either high levels of self-imposed compliance or systemic measures put in place such as data matching to maintain compliance. We would be looking to stay involved in compliance action in the adult industry until the officers in charge of that particular industry are able to convince us that it has been brought under sustained control.

Senator SHERRY—You have officers who have specific responsibility for this area?

Mr Konza—Yes. We have officers who are responsible for this particular industry and then they use officers in our field force across Australia to do the fieldwork.

Senator SHERRY—Are there any specific selection criteria for officers working in this area? Presumably you just do not pick any of the officers that are available; I would have thought you would need some specific criteria for work?

Mr Konza—I do not know. Obviously gender mix is one of the things on which we concentrate.

Senator SHERRY—Is there a requirement that they work in pairs? Sending in individual officers may be difficult.

Mr Konza—I do not think that we have any sort of particular selection method for deciding which officers go into this but we do monitor the officers involved. We find generally with our work that some officers like the more edgy work and some people do not. Some people like to go into the serious non-compliance part of the ATO but a lot of people have no desire to mix with criminals. Similarly we have had to monitor our officers because some of them find that continued exposure to the adult industry becomes a bit disturbing for them after a time and they need to be rotated out.

Senator SHERRY—They would be open to unfair pressure or possible blackmail if they are unaccompanied?

Mr Konza—Yes.

Senator SHERRY—That is more the concern that would be possible.

Mr Konza—Yes, that is right.

Mr D'Ascenzo—When you are doing things on a project basis like this it is not the lone auditor; it is a question of a very coordinated approach through the team leader, and it is managed on that basis.

Senator SHERRY—In the case of that sector have you any revenue—I am talking about tax revenue and not the social security fraud that they would deal with—any tax revenue estimates that have flowed as a consequence?

Mr Konza—We would have direct revenue results from our work in that area. I do not have them available to me at the moment but they would be within the office.

Senator SHERRY—If you could take that on notice.

Mr Konza—Sure.

Senator SHERRY—In this sector how do you identify a person's correct name? You mentioned the issue of social security fraud, which you were able to identify as a major area. How do you get their name and their identity in these circumstances and then, flowing on from that, data match in terms of social security?

Mr Konza—I do not know that that has been a particular problem.

Senator SHERRY—I would have thought a person in these circumstances collecting social security and not declaring their income, or part of their income, would be very reluctant to provide their identity to a tax officer, particularly in this sector.

Mr Konza—Yes, but we go and ask their employers for their names.

Senator SHERRY—And they give them to you?

Mr Konza—The employers? Yes. If they do not want to we can compel them to.

Senator SHERRY—Yes.

Mr Konza—Sorry, I was thinking ahead—I thought you were saying that they would give false names to their employers.

Senator SHERRY—Well, that was going to be my next question. I am sure that there is an element of that going on.

Mr Konza—Yes, I think so. I guess there is some legwork that is required there. Auditors do a range of basic things and if they have concerns about that, they do things like write down car registration numbers, which we can check back. They get the phone numbers out of the personnel records. We can check them back, hopefully to a verified name or certainly a higher integrity name. Auditors are quite resourceful.

Senator SHERRY—I appreciate that, but people in this area would be pretty resourceful too, I would have thought.

Mr Konza—I do not know—I think you are talking about an industry where people were perhaps not generally expecting the tax office to take an interest. Indeed, our auditors in this area say that some of the resentment of our action is due to the fact that the people who work in this area—the workers I mean, not the owners—have an attitude that if you have to do what they have to do to earn a quid it is a bit much to be expected to pay tax as well. So I think it may not have been that hard to get the identity when we went in because they were not expecting us.

Senator SHERRY—Do you get claims for deductions from this sector for work related expenses?

Mr Konza—Yes. I am surprised that you have not seen some of the racier articles in the newspaper listing the things.

Senator SHERRY—Not in this article anyway.

Mr Konza—No.

Senator SHERRY—The *Sydney Morning Herald* is just a bit sort of—I suppose some counterpart newspaper would.

Mr Konza—I think they did run an article on it actually, on our ruling.

Senator SHERRY—I have only looked at this one article, and that does not have any of the so-called racier articles. They do claim tax deductible items but do not declare income?

Mr Konza—No, I think they—

Senator SHERRY—They declare some income obviously if they are claiming a deduction.

Mr Konza—Yes. When we go into an industry we say, ‘Look, we expect compliance and as part of that process we will clarify any questions that you might have.’ They did ask for a range of matters to be clarified and we have supplied them with that. That has been circulated widely, as we had hoped, and reported widely as well.

Senator SHERRY—We touched on it earlier. In this sector, I would have thought there would be a greater likelihood of criminal involvement. I would not have suggested all the operations have a criminal connection. Obviously that leads to concern by officers who are involved in the area of inspecting. Do you provide any specific training?

Mr Konza—The answer to your question I think is that the training we provide to those officers is that if they suspect any criminal activity they call in our serious noncompliance branch, and those officers are very experienced, often ex-police.

Senator SHERRY—During the course of this work, have there been any physical threats or actual physical violence on any tax officials?

Mr Konza—None of which I am aware.

Senator SHERRY—Turning now to the simplified tax system, how many small businesses have adopted the simplified tax system since its introduction in 2001?

Mr Konza—As at 31 December 2005 there were more than 620,000.

Senator SHERRY—The predictions of take-up: didn’t the ATO not give a prediction of 95 per cent?

Mr Konza—I do not have any recollection of that.

Senator SHERRY—Could you take that on notice. What is the number of small businesses? Do we have a comparison in terms of the 620,000 take-up?

Mr Konza—I am advised that that is estimated to be 28 per cent of eligible businesses.

Senator SHERRY—Is that a lower take-up than expected by the ATO?

Mr Konza—The ATO just administer the simplified tax system and we have emphasised at all times since its implementation that it is a choice for taxpayers to make.

Senator SHERRY—Yes, I understand that, but you have to do costings. So you would still attempt to estimate, I would have thought, the likely take-up just for costing purposes.

Mr Konza—There may have been estimates but I am not aware of them.

Senator SHERRY—Take it on notice. Have you undertaken any research—

Mr D'Ascenzo—Just on that, some of that information may not be in the tax office; it may be within the Treasury. But I can say, from my own memory in this area, that we did expect a higher level of take-up. It was slow. We have increased it a bit. The government has made some changes recently to try to increase it even further.

Senator SHERRY—Has there been any research undertaken to determine why the level of take-up has been lower than expected?

Mr D'Ascenzo—In the process of developing more recent changes to the law there has been extensive consultation with the tax profession, and some of the changes announced reflect the concerns raised by the profession. One element that I recall was that people wanted to use the cost basis for the receipt of income but the accruals basis for liabilities, so they wanted to bring the liabilities first. Also, a lot of tax agents use accrual systems. They are basically trained in accounting and therefore consider that the accrual system is a better accounting framework for business. So for them to change over their systems to a cash system is certainly a bugbear for them. There was also a question of how much the different pools of depreciation benefits were useful for microbusinesses. That is my memory. Mark, you might have some other thoughts.

Mr Konza—Just an additional detail to what the commissioner said is that some of the feedback that we got was that business financiers required accounts to be done on an accruals basis. The original STS required people to use a cash basis and that was one of the reasons that restriction was removed last year.

Senator SHERRY—When I asked about research that has been undertaken, there has not been a sit-down specific research project on this take-up issue and the impediments to the take-up issue?

Mr Konza—We sent officers out to see tax agents, for example, who had high numbers of eligible taxpayers but low take-up rate. We asked them why they were not doing it. We consulted with small business as well.

Senator SHERRY—So that evaluation, if you like, was to identify possible changes presumably that were announced in the budget?

Mr Konza—We just provided our observations of how the system was operating.

Senator SHERRY—There were some announcements in the budget. What is the cost of the changes that were announced in the budget?

CHAIR—Senator Sherry, while the officer is finding the answer, I see it is beyond 11 o'clock. Do you want to wind up and put the rest of your questions on notice, when you get the answer to this one?

Senator SHERRY—Yes.

Mr Callaghan—For small business, under the aligning definitions in the tax laws, the costing that is quoted is nothing in 2006-07, \$1 million in 2007-08, \$55 million in 2008-09 and \$71 million in 2009-10.

Senator SHERRY—I am finishing on this point. Why is there a reasonably rapid escalation in the cost over time?

Mr Callaghan—I think it is starting from the year 2007-08 income year. Then in 2008-09 is when you see the impact of it.

Senator SHERRY—Is it expected that the cost will continue to increase beyond the forward estimates?

Mr Brown—They will tend to build up and then peak. I think there would be a continued increase beyond the forward estimates but not indefinitely.

Senator SHERRY—Right; then a levelling off?

Mr Brown—Yes.

Senator SHERRY—I will leave it there and put the rest on notice.

CHAIR—That is the end for the tax office and Revenue Group of Treasury?

Senator SHERRY—Yes.

CHAIR—You are all excused, Mr D'Ascenzo and officers. Thank you very much for your attendance.

Committee adjourned at 11.03 pm