Minerals Council of Australia

15 June 2009

Mr John Hawkins
Committee Secretary
Senate Economics Committee
Department of the Senate
PO Box 6199
Parliament House
CANBERRA ACT 2600

Dear Mr Hawkins

Better targeting the income tax exemption for Australians working overseas

The Minerals Council of Australia (MCA) has significant concerns in relation to the changes contained in *Tax Laws* Amendment *(2009 Budget Measures No.1) Bill 2009* to narrow the scope of section 23AG *Income Tax Assessment Act ('ITAA')* 1936.

Background

The MCA is the peak industry organisation representing Australia's exploration, mining and minerals processing industry nationally and internationally in its contribution to sustainable development. The MCA's strategic objective is to advocate public policy and operational practice for a world-class industry that is safe, profitable, innovative, environmentally and socially responsible and attuned to its communities' needs and expectations. MCA member companies produce more than 85 per cent of Australia's annual minerals output, and will account for about 60 per cent of Australia's merchandise exports in the year to June 2009.

One of the significant structural shifts In Australia over recent years has been the strong growth in the level of Australian foreign direct investment (FDI) abroad. The gap between Australian FDI abroad and the level of FDI in Australia has narrowed significantly. As at December 2008 the level of Australian FDI abroad was $285 billion. At the same time FDI in Australia was $387 billion. This trend of increasing outwards investment from Australia will continue. A survey recently released by the Export Finance Insurance Corporation (EFIC), the *2009 Global Readiness Index*, found that 84 per cent of companies with offshore operations planned to expand these activities. Of survey respondents without offshore operations 44 per cent were planning to establish a presence offshore.

The importance of outwards investment for the mining industry is also under appreciated in Australia. The level of foreign assets held by Australian mining companies rose by about 30 per cent during 2008 to reach $46 billion. Over the same year the level of foreign investment in mining in Australia (as measured by the level of financial liabilities in the mining sector in Australia) rose by about 9 per cent to $137 billion. Overall in the four years from 2004 to 2008 the level of outwards investment by mining rose more than four times, while foreign investment in mining in Australia almost doubled.

The strong growth in outwards investment means that members of the MCA employ increasing numbers of Australians to work overseas on projects in various countries around the world. These projects deliver significant benefits to the Australian economy, including:

- the repatriation of foreign income earned by Australians to Australia;
- the development of specialist skills and experience of Australian residents;
- providing a profile for Australia in many developing and developed countries; and
- creating substantial opportunities for other Australian industries and service providers to win flow-on business in these overseas markets.

WALTER TURNBULL BUILDING
LEVEL THREE
44 SYDNEY AVENUE FORREST CANBERRA ACT 2603
PO BOX 4497 KINGSTON ACT 2604
TELEPHONE: + 61 2 6233 0600
FACSIMILE: + 61 2 6233 0699
WEB: www.minerals.org.au
EMAIL: info@minerals.org.au
ABN 21 191 309 229

Policy Issues

The Press Release announcing the Government's changes stated that the measures would:

- protect and increase Commonwealth revenues; and
- protect the integrity of the tax system by ensuring "that workers who earn income overseas do not have an unfair advantage over workers who earn income and pay tax in Australia."

The draft legislation contained *Tax Laws Amendment (2009 Budget Measures No.1) Bill 2009* does not address these policy issues but does significantly increase the costs for employers and the administration required to employ Australian residents.

In relation to additional Commonwealth revenue, the MCA submits that Treasury has failed to consider:

- the impact of the reduced competitiveness of the Australian companies in hiring Australian employees to work overseas;
- that many Australians working overseas are highly mobile and therefore may not choose to be resident in Australia;
- Australian companies seeking to employ workers on foreign projects may choose to employ non Australian residents to work on overseas projects due to the higher cost of an Australian worker and the additional compliance burden;
- the additional economic benefits where Australian residents working overseas repatriate their salary to Australia, to the benefit of the Australian economy;
- that Australia may well lose its position as a net exporter of resources expertise; and
- that Australia will lose the presence of a significant number of Australians working and building relationships in developing countries within Asia, Africa and South America,

In respect of the integrity of the Australian tax system, the proposed changes will create significant disparities for Australians working overseas as compared to Australian workers including:

- the Australian residents working overseas may be subject to Pay As You Go Withholding (PAYGW) (or equivalent withholding) in two jurisdictions;
- the Australian companies may be subject to Fringe Benefits Tax (or equivalent) in two jurisdictions creating a significant additional cost to employers; and
- an Australian working overseas may have committed to a contract to work overseas based on certain assumptions about the Australian tax system which under the proposed law will be detrimental to their financial position.

Furthermore, MCA submits the significant narrowing of the income tax exemption in Section 23AG of the ITAA 1936 exemption fails to consider:

- the significant financial and personal considerations that arise for Australian residents undertaking overseas based employment;
- the benefits derived by Australian companies and the Australian economy from Australian residents undertaking foreign assignments; and
- many Australians working overseas actually work in jurisdictions where the effective tax rate is similar to the Australian tax rate.

Technical issues

The MCA is aware that various submissions on technical issues have been made in the consultation process including:

- the failure to provide consequential amendments such that the proposed changes to section 23AG of the ITAA 1936 adequately interact with the PAYGW regime, the foreign tax offset rules, the Fringe Benefits Tax ('FBT') rules and the Australian double tax treaties;
- the failure to ensure that Australians working overseas are not subject to cash flow problems on the basis of being subject to PAYGW potentially in two jurisdictions and the timeliness of being able to claim foreign tax offsets;
- the double taxation of Fringe Benefits, with no ability to claim reductions for foreign taxes paid on the benefits in the foreign jurisdictions and the additional administration required by employers to extract required information on

benefits provided in the foreign locations,. This is a likely to cause a significant incremental cost to employers; and

- the compliance difficulties for Australian resident individuals working overseas associated with claiming foreign tax offsets when the foreign taxes have been paid, with the misalignment of tax years in other countries (i.e. calendar year end) opposed to a 30 June year end in Australia; and
- the amendment to Section 23AG may result in businesses looking to Section 23AF for relief. Under the current convention of 23AF, only pre-approved projects will be eligible for the exemption. It is likely companies who have developed projects in a developing country may have applied for exemption prior to construction if 23AG wasn't available at the time. With no transitional arrangements proposed, or clarification of the criteria for relief under Section 23AF, companies previously relying on Section 23AG have been left with uncertainty. Had the change been launched with transitional arrangements, pre-approval for projects would have been sought before the implementation date of 1 July 2009.

Recommended Actions

The MCA submits Treasury should undertake

- further consultation with key stakeholders to obtain industry views as to the consequences of these proposed amendments,
- further consultation on the criteria the Trade Minister is to apply in assessing projects to be in the "national interest".
- confirm its assumptions and forecasts are accurate; and
- further work on ensuring the proposed legislation interacts better with other elements of the Australian tax system.

Despite the professed objective of the changes to the tax exemption, the announced measure essentially introduces discriminatory treatment between workers engaged in the public and private sectors.

Removal of the exemption for private sector workers is a revenue measure which will affect the costs of Australian businesses investing and operating overseas and reduce Australia's international competiveness. It is counterproductive in a globalising environment where Australian industry, including the minerals industry is increasing operations offshore. The measure is also inconsistent with the Government's stated aims to encourage overseas investment and expand services exports over time.

I would be happy to discuss further any of these matters.

Yours Sincerely

Stephen Deady
Director Industry Economics & Taxation.