THE SENATE

A NEW TAX SYSTEM (CLOSELY HELD TRUSTS) BILL 1999

A NEW TAX SYSTEM (ULTIMATE BENEFICIARY NON-DISCLOSURE TAX) BILL (NO. 1) 1999

A NEW TAX SYSTEM (ULTIMATE BENEFICIARY NON-DISCLOSURE TAX) BILL (NO. 2) 1999

Second Reading

SPEECH

Monday, 28 June 1999

BY AUTHORITY OF THE SENATE
Senator COOK (WA) (8.24 pm)—I rise to speak on the A New Tax System (Closely Held Trusts) Bill 1999 and two other bills relating to non-disclosure—A New Tax System (Ultimate Beneficiary Non-disclosure Tax) Bill (No. 1) 1999 and A New Tax System (Ultimate Beneficiary Non-disclosure Tax) Bill (No. 2) 1999. The issue of tax avoidance through family trusts is one that we on the Labor side of the chamber have been concerned about for a long time. We have been calling on the government to take action and, most recently, to abide by its undertaking to provide consistent treatment of tax entities so that trusts are taxed in the same way as companies.

In announcing that it intends to do this, the government has claimed a positive budgetary impact of $1.67 billion in the year 2000-01, declining to $650 million in the year 2002-03. However, we have not yet seen those bills. We have only seen the ones that are now before the chamber. It is a small measure to deal with some of the abuses of tax structures for the purpose of tax avoidance and evasion. It requires the disclosure of the ultimate beneficiaries of income from trusts. That is so that the Commissioner of Taxation can check whether each beneficiary has properly disclosed the net income of their net assets, including the receipt of any tax preferred amounts. Failing that disclosure, the income of the trust will be taxed at the top marginal rate, plus the Medicare levy.

However, these requirements apply only to closely held trusts, which are defined in the bill—and I will not read the provision—and discretionary trusts, which are also defined in the bill. I will not read that provision either, except to say that a discretionary trust is a trust that is not a fixed trust—that is, one where persons have fixed entitlements to all the income and assets of the trust. A fixed entitlement is an indefeasible interest in a share of the income or assets of a trust.

The bills before us specifically exclude unit trusts with units listed on the Stock Exchange—complying superannuation funds, deposit funds, pooled superannuation trusts and deceased estates until the fifth anniversary of the death. The fact that it is only expected to raise an additional $30 million a year is a demonstration of how limited this measure is. There are many greater tax avoidance and evasion issues associated with trusts. The government's reluctance to come to grips with these avoidance and evasion issues shows how uninterested it is in real tax reform that protects the revenue and makes everyone pay their fair share.

There is every sign that the government wants little more than a few measures it can point to to deflect criticism about its lack of action. The lack of speed and commitment in this area has now reached the dimensions of a scandal of such proportions that, in the context of this bill, it requires a second reading amendment. I was going to apologise to the chamber for not being able to circulate this amendment because we have been moving faster than I anticipated, but the Clerk has acknowledged that it has been circulated. I move:

At the end of the motion, add:

"but the Senate is of the view that:

(a) in relation to tax avoidance:

(i) the Government has failed for three years to take adequate action to deal with major tax avoidance and evasion by high wealth individuals using complex trust structures;

(ii) lack of action is causing major ongoing losses of revenue;

(iii) at the time these aggressive tax avoidance and evasion schemes were first identified by the Australian Taxation Office in late 1995 and early 1996 an amount of $800 million was being evaded by 80 high wealth individuals;

(iv) some of the high wealth individuals participating in these schemes were manipulating their taxable incomes to declare as little as $20,000 a year and so claim various government benefits;"
(v) the legislative action required to eliminate these schemes is well understood by the Australian Taxation Office; and

(vi) the lack of adequate action on tax avoidance and evasion using trusts is an indicator of the Government's failure to provide proper and fair tax reforms; and

(b) in relation to so called taxation reform, of which this bill forms a part as a component of the New Tax System:

(i) the government has not achieved real tax reforms in Australia, it has merely agreed to introduce an unfair GST;

(ii) the new Howard/Lees GST will involve a massive tax mix switch which will hurt ordinary families, which is directly contrary to the balloted policy of the Australian Democrats;

(iii) the Howard/Lees deal will actually increase the tax on food in Australia;

(iv) ordinary people will now face a GST on top of state indirect taxes on bank accounts; and

(v) the amended tax package is still unfair and will also damage the environment".

It is obvious to anyone with a serious interest in tax policy that there is scope for tax avoidance and evasion using tax structures. Throughout 1994 and 1995 the Treasurer's office pressed Treasury for advice on the extent of the problem and the possible remedies. It was raised on an almost weekly basis in meetings with the department. Nothing was forthcoming until 9 November 1995 when the Australian Taxation Office, not the Treasury, advised that they had uncovered a significant problem using multiple trust structures. They had been using new software which was capable of finding patterns in large amounts of seemingly unrelated information. They had found that large numbers of seemingly unrelated trusts were in fact related and a range of techniques were being used by high-wealth individuals to reduce tax liabilities to low or negligible levels.

Treasury and the tax office worked on the issue over the next three months, eventually advising the Treasurer that it would be appropriate to make a public announcement that the government would act to end these practices. The press release issued by Treasurer Ralph Willis on 11 February 1996 accurately set out the issues. It was entitled, 'High-wealth individuals: taxation of trusts.' I have indicated a copy of this press release to the minister, who is not at the table but is in the chamber. I would seek leave to incorporate the text of this press release because it does set the record straight. The minister did indicate to me that that was an acceptable action.

Leave granted.

The document read as follows—

On November 9, 1995 I was informed by the Australian Taxation Office that as part of the Compliance Enforcement Strategy authorised by the Government, it had conducted analysis of the accumulation of wealth by certain individuals and the taxes paid by them. That analysis revealed that some high wealth individuals were employing strategies which allowed them to accumulate wealth, enjoy a lavish lifestyle, but pay little or no tax. The analysis was in its early stages but the ATO believed the revenue implications might amount to several hundred million dollars.

At my request, the ATO and Treasury provided more extensive advice and analysis on December 20 1995. It revealed that in the 1993 financial year, 80 individuals each with a net work of over $30 million had returned taxable incomes of $20,000 or less. This enabled some of them to qualify for low income rebates, Medicare exemptions, deferral of HECS payments and reduced child support payments. The tax minimisation techniques employed by these individuals mainly involved the use of trusts.

By January 19, 1996, the ATO and Treasury were able to advise that on the basis of the work undertaken to date in respect to 100 wealthy individuals alone, appropriate measures to deal with a range of specific tax minimisation techniques using trusts would produce additional revenue of at least $500 million. Later at a meeting on January 23, 1996, Treasury gave me verbal advice raising that estimate to $800 million. Some amount could be forthcoming in 1996-97, but the first full year effect would be in 1997-98.
The January 19, 1996 advice also included separate revenue estimates in addition to the $800 million for techniques involving thin capitalisation and abuses of the provisions for payments by trusts to foreign charities.

The ATO has identified a number of complex tax planning arrangements used by some wealthy individuals to avoid tax, these include:

- the characterisation of income as capital by the use of multiple trust structures to conceal a common controlling mind. If the activities of the various trusts and associated companies were viewed as a whole, the profits of the group could be treated as trading income. The ATO has found a number of cases of wealthy individuals operating over 100 trusts;

- the creation of artificial losses (revenue as well as capital) to neutralise otherwise taxable profits, particularly through the use of related party transactions;

- distributions to wealthy individuals and family members being disguised as loans and other benefits which are claimed to be non-taxable. In relation to companies this includes exploitation of alleged weaknesses in section 47A and 108 of the Income Tax Assessment Act 1936, of the deemed dividend provisions;

- the continued use of offshore trusts to hold significant funds which seem to be applied for the benefit of wealthy individuals and their families; and

- the use of Australian charitable trusts and overseas organisations to disguise benefits provided by family trading trusts to family members.

Obviously, these are not techniques which are practised by the overwhelming majority of trusts operated by and for Australians. Trusts provide an appropriate structure to meet a range of legitimate needs such as for charities, education and non-profit organisations, deceased estates, a variety of family purposes, and for solicitors and other professionals. The Government will not interfere with these arrangements. The Government undertakes that the measures it will adopt will ensure that activities not involving tax avoidance are not adversely affected.

No responsible government could stand back and let blatant abuse of the tax system by extremely wealthy individuals continue. The ATO is undertaking action to test the effectiveness of the existing law to deal with some of these practices. However, it is not expected that an outcome will be achieved by these means in the near future due to the long time frames involved in testing issues before the courts. The ATO has advised that it is particularly difficult to run test cases in these areas because the individuals concerned will settle at the end of the day rather than have their private affairs or practices exposed to the public.

On January 29, 1996, I wrote to the Secretary of the Treasury and the Commissioner for Taxation, asking them as a matter of urgency to develop a legislative response to cover income from the 1996-97 financial year. The new tax measures which the Government will introduce to deal with these specific areas of tax avoidance will be prospective not retrospective.

One of the most important things this Labor Government has given Australia since it was elected in 1983 is a tax system based on the principle of integrity and fairness. Maintaining that basic integrity and fairness requires stamping out tax avoidance wherever and whenever it emerges.

The reason these measures are being announced today is because the Government is seeking a mandate to deal with this area of tax avoidance. We call on the other parties in this election to support these reforms. I am offering Mr Howard a briefing this afternoon from the Commissioner of Taxation.

The Treasurer
Ralph Willis
11 February 1996

When you read that press release you will see a very clear case for reform and the proposals that the Labor government—had it been returned—would have carried through. The press release also refers to the shadow Treasurer. I understand he received a briefing the very next day.

More than three years have passed and the two substantial things that have changed are the government and the fact that Australia no longer has a government that will do anything about the scandal. If the Howard government
had any interest in the fairness and integrity of the Australian tax system, it would have legislated in its first year to put an end to this abuse. Two weeks before the 1998 election, when the government needed money to fund the tax cuts contained in its ANTS package and when it knew Labor would raise this issue, it came out with a plan to tax trusts as companies. Eight months later, we have still not seen the legislation. But it is not just eight months since the task was put in front of it; it is three years, three months and 25 days. Perhaps the Treasurer is shooting for the record on inaction on major tax fraud. Former Fraser government Attorney-General Peter Durack left the prosecution files of the bottom of the harbour schemes in his bottom drawer for seven years. If the Liberal government—surprisingly to all of the critics—were to win, for example, the next election, the Treasurer has a chance of beating the Durack record on inaction.

We are now being told that the government will produce its solution to this problem in the Ralph Review of Business Taxation. It is a bit more urgent than that. It has been a bit more urgent than that for more than three years. In the 1998 federal election, Labor indicated its preparedness to tax trusts as companies, so it is not a matter of political debate between the Labor and Liberal parties. The remedies on trusts are clearly set out in the ANTS package by the Treasurer. Labor wants them implemented as quickly as possible, but now the election is out of the way and the issue has been put off. Why has a policy which was clear enough to be included in the government's election policies been too difficult? Why is this the case when we have been hearing regularly over a year from the Prime Minister and the Treasurer about their determination to stamp out abuse in this area? On 30 September 1997 the Australian Financial Review reported:

The Prime Minister ruled out an attack on the abuse of trusts for taxation purposes on the spurious grounds that such a move would hurt small business.

The Prime Minister was sufficiently incensed by this to make a personal explanation to the House the same day. He said:

Can I say that I have done no such thing. What I have said, and I am happy to repeat it today, is that I have assured the members of the government parties that in any taxation changes we make we will not be acting in a manner that would seriously damage, or indeed damage at all, small business. But at no stage have I said that my government would never take action against the abuse of trusts. We will always take action against abuses within the tax system.

On 24 February 1998 the Treasurer was reported in the Herald Sun announcing that family and company trusts would be taxed at the same rate as company profits as part of the government's crackdown on tax loopholes. The Australian Financial Review quoted him on the same day as saying:

In an ideal tax system, taxes would relate to the economic activity that is being carried on, rather than the legal vehicle which houses that activity.

The Prime Minister and the Treasurer are very adept on this issue. They say one thing but they do nothing. Any move to stop tax evasion and avoidance always meets resistance. Someone will try to characterise the measures as draconian or claim that their activities are legitimate or essential. According to the Australian Financial Review of 30 September 1998, the coalition's policy was being undermined by the Leader of the National Party even before election day with his letter of 22 September 1998 in political doublespeak to the Australian Cane Farmers Association:

I can assure you that whilst the National Party is committed to stopping any practice of `rorts' through FBT or trusts, it will take all necessary action to ensure that genuine use of distributions of capital from family trusts to beneficiaries will not be subjected to fringe benefits tax.

This contradicted the government's tax policy which said FBT would be:

... extended to benefits in excess of $1,000 a year provided by companies to their shareholders or by trustees to trust beneficiaries, where the benefits were not taxed currently.

There was a report in the Australian Financial Review on 30 March this year, following a National Party meeting, that Senator Winston Crane was focusing his attention on preserving the rights of `legitimate' business trusts. Senator Crane claimed he had received a lot of support from his coalition colleagues. The next day AAP reported that Queensland state opposition leader Rob Borbidge had announced that the Queensland National
Party would oppose any attempts to tax trusts like companies and that both the Prime Minister and the Deputy Prime Minister had been told of the Queensland Nationals’ position.

On 25 May 1999, the *Sydney Morning Herald* reported that National Party concerns that the Review of Business Taxation proposals would reintroduce death duties on family farms by cracking down on discretionary family trusts had been given a sympathetic hearing among coalition parliamentarians. The report said it was understood the cabinet secretary, Senator Bill Heffernan, was investigating the matter further following a presentation from Queensland solicitors Cleary and Hoare—more about Senator Heffernan in a moment—who were representing more than 200 farmers. The National Party is apparently hoping the Review of Business Taxation will not pursue proposals to tax trusts as companies.

On 24 May, Glenn Milne reported in the *Australian* that the Deputy Prime Minister had said, ‘We’ll kill this in Cabinet.’ Parliament has sat for several weeks since then, but there has been no personal explanation like the Prime Minister’s. On the *Sunday* program about a month ago, the Deputy Prime Minister was again trying to characterise taxing trusts as companies as a death duty. His exact words were:

But, at the end of the day, are we about to retrospectively reintroduce death duties by a some approach to trusts? No.

And:

The Government’s made no decisions, and we still haven’t got the Ralph report, and it will be a little while yet.

This was immediately contradicted, first by Mr Ralph, reported in the *Australian Financial Review* as saying:

We can’t see where there is any negative effect arising out of proposals being considered that would give effect to an inheritance tax.

It was then contradicted by the Treasurer when he responded to a question from the Deputy Leader of the Opposition in the House, who asked him to:

...confirm that full implementation of the proposal to tax trusts as companies outlined in your original GST package had been factored into the budget surplus projections?

The Treasurer replied:

The government’s policy as announced in A New Tax System, ANTS, stands. The government is proceeding to implement that. In relation to those matters that are fully costed as part of ANTS, they have of course been taken into the budget position.

The noise was coming from the National Party even before the election was over, and it is still coming today. That explains the last eight months procrastination. The Prime Minister and the Treasurer are going to have to decide very soon whether their position is best summed up by an incisive comment made by the Minister for Sport and Tourism in her backbench days. On 2 October 1997, she was reported in the *Sydney Morning Herald* as saying:

Carmody should stop attacking Australians for not paying tax.

That sums up where the Liberal Party have been coming from for the last three years. Nor should we forget in the context of this debate that there are 20 members of the government frontbench who have trusts themselves. We saw today how this government treats conflicts of interest. We can only wait and see what the next excuse will be. Which interest groups and what misrepresentation will we see next? Meanwhile, the tax evaders and avoiders are using Australia as a tax haven and treating the rest of the community with contempt. The tax commissioner can have a good enforcement regime, but he will not be effective if the government fails to give him the tax law to do his job. Any government that lets tax avoidance and evasion of this magnitude go unchecked can never be taken seriously on tax reform.

I made a reference in my remarks to the Parliamentary Secretary to the Cabinet, Senator Bill Heffernan. We do know that about 20 out of 27 of the government frontbench have trusts. We do know that, in the last government, Senator Warwick Parer had a web of deceit that outlined his involvement in trusts.
Senator Kemp—Mr Acting Deputy President, on a point of order: to suggest that a colleague, Senator Parer, has a web of deceit is outside the standing orders and should be withdrawn. It is untrue and should not be said.

The ACTING DEPUTY PRESIDENT (Senator Sherry)—I would ask you to withdraw that comment, Senator Cook.

Senator COOK—I withdraw. We do know, however, that Senator Heffernan is the Parliamentary Secretary to the Cabinet, that he is the self-professed cardinal or the eyes and ears of the Prime Minister, John Howard, in the New South Wales Liberal Party and that he is a holder of six family trusts and one unit trust which he says he needs for succession planning in his family. If, under his proposal, he distributes $5,400 to each of 10 beneficiaries, due to the tax-free threshold no tax would be paid on $54,000. That should be compared to what a wage earner would have to pay on $54,000—$16,000—in tax. Not many ordinary Australian battlers get access to this level of tax avoidance.

The issue of the use of family trusts and the interlocking nature of family trusts to split income and to lower levels of taxation are matters of considerable concern in Australia. It is about time that the government followed what the Labor government would have done had it been re-elected in 1996 and legislated in the form that Ralph Willis had announced in, as I recall, February of that year. The fact that the government sit back, fail to act and refer to it in their ANTS package but do not carry it through in their legislation giving rise to the ANTS package—flip it off to the Ralph inquiry—indicates a degree of massive insincerity.

We will be watching very closely when the Ralph inquiry reports. We will expect the Ralph inquiry to take up the issue of tax evasion and avoidance through the use of family trusts and, if it does, we will then expect this government to act quickly. We do not hold much hope that it will. While it should, in the interests of the Australian community, we are aware of the vested interests of many members of its own frontbench. This has been one of the reasons, I believe, why it has failed to police this matter up until now.

Senator Kemp—You had 13 years.

Senator COOK—I take the interjection. I go back to the facts. It is very rare that we are able to nail the Assistant Treasurer in a debate, because he is so slippery—he trades in platitudes and argues whatever is the platitudinous version of the truth. The facts are that a former Treasurer of the Commonwealth of Australia, Ralph Willis, a highly respected Australian and a well-regarded Treasurer, sought from Treasury—and finally got from the Taxation Office—advice on what was occurring with family trusts and, upon receipt of that advice, acted promptly to do something about it.

The other fact is that the election intervened, and the advice has been sitting there for three years—unaddressed by this government and now the subject of consideration within the Ralph review. I think what says it all is that 20 members of your own frontbench are potential beneficiaries of this inaction, and that is a disgrace. However, we will wait and see what the Ralph inquiry puts, and we will be expecting the government to move promptly to end tax avoidance by the use of trusts in this manner.