
NATIVE TITLE AND TAX:

UNDERSTANDING THE ISSUES

by Miranda Stewart*

The income tax treatment of payments under native title agreements has been a matter of concern to stakeholders.¹ In May 2010, the federal Treasury Department released a Consultation Paper on *Native Title, Indigenous Economic Development and Tax* (the 'Treasury Paper').² This article summarises the key issues and discusses the three main options for reform that are canvassed in the Treasury Paper. These are:

1. An income tax exemption for payments under native title agreements;
2. A new, tax-exempt Indigenous Community Fund; and/or
3. A native title withholding tax.

The Treasury Paper is one of several important consultation papers on Indigenous issues that were released by the federal government in 2010. Others include *Leading Practice Agreements: Maximising Outcomes from Native Title Benefits*,³ the *Indigenous Economic Development Strategy*,⁴ and *Indigenous Home Ownership*.⁵

INCOME TAX EXEMPTION FOR NATIVE TITLE AGREEMENTS

UNCERTAINTY IN CURRENT TAX LAW

The Treasury Paper states, correctly, that 'applying the current rules of the income tax system, payments provided under a native title agreement may or may not be assessable income' for a native title claim group.⁶ Payments, property or other benefits received under native title agreements may be assessable if the payment (or the market value of property or other benefits) is 'ordinary income' or is taxed by a specific provision or as a capital gain.⁷

Many payments under native title agreements will not be ordinary income as they are payments for a one-off disposal ('mere realisation') or extinguishment of property rights.⁸ However, payments under agreements that share profits or enable the claim group to receive an income stream linked to commercial use of the land, for example in a mining operation, may be income.

A native title payment that is capital in nature may be taxed under the capital gains tax (CGT) rules. Native title is a unique property right recognised at common law.⁹ As such, it is likely to be a CGT asset and a taxable capital gain may arise where the payment received by a native title holder exceeds the cost of that asset.¹⁰ For example, a native title agreement may involve the 'disposal' of a CGT asset¹¹ or the 'termination' of a right which is a CGT asset.¹² If an asset is 'pre-CGT' (it was acquired or created before 20 September 1985 when CGT was introduced), gains will be exempt from tax.

TAX TREATMENT OF COMPENSATION PAYMENTS

Payments for native title are, fundamentally, compensatory in nature. Native title holders are entitled to compensation 'on just terms to compensate the native title holders for any loss, diminution, impairment or other effect of the act on their native title rights and interests'.¹³ The right to compensation arises as a result of the operation of the *Racial Discrimination Act 1975* (Cth). The *Native Title Act 1993* (Cth) ('NTA') recognises this right and introduces mechanisms for determining compensation.

The Treasury Paper states that 'compensation payments for the extinguishment or voluntary surrender of native title rights would generally be regarded as compensation for the loss of a pre-CGT capital asset' so that any gain would be exempt.¹⁴ It relies on Tax Ruling TR 95/35 issued by the Commissioner of Taxation to 'look through' a settlement agreement to the 'underlying asset' and assumes that the underlying asset (the native title or right to compensation) is pre-CGT.¹⁵ However, the analysis is complex and there is uncertainty as to whether this approach is correct. Further, TR 95/35 does not refer to native title at all.

In Goods and Services Tax Ruling GSTR 2006/9, the Commissioner confirms that compensation for native title relates to 'the loss suffered by the claimants on the extinguishment of their interest in the land'.¹⁶ However, this ruling deals only with a government authority compulsorily acquiring native title rights under a statute, with the effect that every interest in the land is extinguished

'and each person who formerly held such an interest has that holding converted into a claim for compensation'.¹⁷ It does not deal with payments from private actors and it is unclear whether payments for temporary suspension of native title or access to lands would be treated in the same way.

THE CASE FOR A SPECIFIC INCOME TAX EXEMPTION

This article argues that a legislative tax exemption is required to ensure certain, consistent and equitable outcomes for native title claimants. The legal and moral basis for an exemption is that they are, fundamentally, agreements for compensation. As Marcia Langton observes, payments under native title agreements 'are private transactions, but as substitution for crown compensation, they should not be taxable in their primary form'.¹⁸

Clarity is needed in defining a native title agreement for the exemption (the Treasury Paper does not define a 'native title agreement'). Native title agreements are very diverse, ranging from narrow agreements focused on discharge of one-off rights, to settlements relating to entire projects, regions and a suite of rights. Payments may be made under agreements 'as if' there is native title but where, ultimately, no native title determination is made, including payments made under the 'right to negotiate' under the NTA. However, most agreements are the result of negotiations that take place under processes set out in the NTA. They may be Indigenous Land Use Agreements ('ILUAs')¹⁹ (the main agreement making process); 'future act' agreements²⁰ (which compensate for future impairment of native title, even though the agreement itself may not extinguish or suspend title); or agreements which are ancillary to these main NTA agreements. Frequently, an ancillary agreement contains the real economic deal, generating payments and other benefits that are significant to economic development of a claim group. Also important are State native title settlement frameworks (not referred to by the Treasury Paper), such as those of South Australia and Victoria.²¹ These must be included in an exemption for payments under 'native title' agreements.

WHAT SHOULD A TAX EXEMPTION LOOK LIKE?

A specific exemption could be legislated in the tax law, by reference to the relevant provision in the NTA under which a 'native title agreement' is negotiated. Treasury proposes a reference to 'any agreement recognised or authorised under the NTA'.²² This may not be wide enough to encompass the diversity of native title

agreement processes summarized above. Crucially, it is the native title agreement-making *process* that should be supported by the exemption, as this process is a major form of engagement and collaboration between Indigenous people, governments and private enterprise, facilitating economic participation and governance.²³

A potential model for the exemption exists in ITAA97 s 118-37, which provides a specific tax exemption for capital gains arising in relation to compensation payments received for wrongs or injuries suffered by individuals in their occupation or that they suffer personally.

One option considered by Treasury is 'to allow an independent decision maker (such as the Commissioner of Taxation or the National Native Title Tribunal) to declare that an agreement is a native title agreement to which the income tax exemption extends'.²⁴ The question has also been posed by FaHCSIA and the Commonwealth Attorney-General departments as to whether 'any new tax treatment should be conditional on adopting ... governance measures and leading practice principles' which would be reviewed afterwards.²⁵ This article disagrees with these proposals. Participants (both claim groups and other stakeholders) need clarity at the *beginning* of a native title negotiating process that payments will be exempt. Making a tax exemption conditional on agreement outcomes, registration or surveillance at the end of agreement-making would work against providing certainty and fairness *upfront* in native title negotiations.

The Treasury Paper also considers whether there should be any restrictions on the use of tax-exempt native title payments. This article suggests that as long as an eligible agreement making process has been done, there is no warrant for restrictions on the use of payments. So, for example, the exemption should extend to a payment received by an individual under an eligible native title agreement.²⁶

The exemption should not be conditional on payments being made into a regulated tax-exempt entity (see below). The native title claim group should be entitled to determine the best short and long term use of native title payments. The communal nature of the underlying asset and the requirements of the NTA should provide sufficient safeguards.

A tax-exempt payment or property received may be invested to generate further income or gains for the claim group. These would be taxable under normal rules unless the asset was owned by a tax-exempt entity (see below).²⁷

A TAX-EXEMPT INDIGENOUS COMMUNITY FUND

Charitable trusts or other entities that have obtained tax exemption as Public Benevolent Institutions ('PBI') are commonly used for holding benefits and managing payments under native title agreements, largely to ensure tax-exempt status. However, charitable trusts are 'imperfect' for Indigenous purposes in several respects:²⁸

1. Charitable purposes are restricted and there are problems with listing multiple purposes;
2. There are difficulties relating to accumulation of funds for the long term;
3. The definition of 'public' or 'public benefit' may cause problems with benefiting native title holders 'related by blood' (by virtue of defining the group by their ancestors);
4. There may be conflict between broader community purposes and the specific obligations of native title holders in law and culture;
5. The Commissioner of Taxation's view that a purpose of commercial activity is not generally allowed, even where this is to enable a community to become economically sustainable in the longer term.²⁹

A TAX-EXEMPT INDIGENOUS COMMUNITY FUND

The Treasury Paper considers the option of establishing a new tax-exempt entity that it calls an Indigenous Community Fund ('ICF').³⁰ An ICF could be established by inserting a new category of exempt entity in the income tax law.³¹ Endorsement by the Commissioner of Taxation may be required and special conditions may be included in the statute or regulations.

This article supports the establishment of an ICF. The fundamental goal should be to support an Indigenous community in converting a communal benefit made under a collective agreement into economic development and relief of economic disadvantage for current and future generations. The purposes of an ICF should be defined in consultation with Indigenous communities; for example:

- Addressing economic and social disadvantage through direct provision of community services and payments to individuals;
- Provision for long term wellbeing, for example contributions towards individual superannuation;
- Accumulation for future generations;
- Supporting administration costs for native title Prescribed Bodies Corporate.

An important purpose, which is missed by the Treasury Paper, is to facilitate business development. This is acknowledged as central in the government's Indigenous Economic Development Framework.³² For example,

the ICF could use a portion of funds for business loans and may prioritise Indigenous business ventures in collaboration with other organizations such as Indigenous Business Australia.

ICFs of various scales could be established, ranging from a small local group to a regional or State based Fund covering a number of groups. An ICF established for a limited group of beneficiaries would likely delineate that group on the basis of Aboriginal law and custom.³³ A larger scale ICF might accommodate some pooling of resources to achieve economies of scale and better returns.

USE, INVESTMENT AND GOVERNANCE OF AN ICF

An ICF should be required to use its funds for the purposes set out above. In general, tax-exempt treatment requires that an entity be 'not for profit' in the sense that it cannot make distributions to individual members. However, there is a case for allowing an ICF to make limited cash payments to individuals, for example elders in a community, without putting at risk its tax exemption. This provides some recognition of individual claimants' interests and can contribute to the agreement-making process because they enable individuals to benefit immediately, in a small but visible way, from the native title agreement.³⁴

The Treasury Paper suggests that a particular legal form, such as a corporation established under the *Corporations (Aboriginal and Torres Strait Islander) Act 2006* (Cth) ('CATSI Act'), could be required for the ICF. However, this article suggests that the form of an ICF does not need to be limited in this way. An ICF should also be an optional alternative to other entities including charitable trusts, which remain suitable as potential vehicles for investment of native title payments for purposes such as educational scholarships.

To achieve the key purpose for the long term benefit of a community, an obligation to accumulate some funds for the long term could be required. This obligation might not apply where the annual revenue stream is below a certain amount. Bearing in mind the purpose of long-term accumulation, an appropriate regulatory authority might be the Australian Prudential Regulatory Authority ('APRA'), which regulates superannuation funds. Other limits on investment or distribution of funds, such as a cap on the proportion of capital in an ICF used to support commercial activity, would also be required because of the risk of such investments.

The decision-making processes of the ICF should reflect Indigenous law and custom, contributing to effective

participation and legitimacy. Administrative burdens must be balanced with good governance, especially for smaller funds. Possibilities include at least one director experienced in corporate and financial management; a minimum number of representatives of the community; for ICFs of a certain size, independent responsible persons on the board; audit, returns and plans to be prepared in line with good funds management. Many of these governance issues arise with respect to charitable trusts at present; they cannot be avoided but processes could be streamlined and structures made more suitable.

As many existing agreements rely on charitable trusts or PBIs, transitional rules would be required to enable “migration” of existing assets to the ICF without attracting tax consequences.

NATIVE TITLE WITHHOLDING TAX

The Treasury Paper also considers the option of a native title withholding tax.³⁵ This could be modeled on the current Mining Withholding Tax (‘MWT’) levied at four per cent on ‘mining payments’ made to Aboriginal people or a distributing body such as a Land Council, in respect to the use of Aboriginal land.³⁶ It is collected from the mining company.

The MWT is simple and generates no further tax consequences for the recipients. It operates in a well understood manner in the Northern Territory. Consequently, some have suggested that this is a good option for reform.

However, the model may not translate well to the diversity of payments and agreements in the native title context, which are summarized above. More fundamentally, the premise of this model is that tax is owed on the payment.³⁷ As is clear from the discussion above, it is a matter of principle that payments related to native title should be tax-exempt.

CONCLUSION

The link between taxation of native title payments, maximizing outcomes from native title agreement making and Indigenous economic development is strong. It is important that the government address the tax issues raised in the Treasury Paper holistically.

This article welcomes the Treasury Paper on the tax treatment of native title and supports the enactment of both a specific tax exemption for payments under native title agreements and a new tax-exempt ICF. These are complementary options that together have the potential

to improve agreement making and enhance native title outcomes. It will be crucial, to ensure the best design and full acceptance of any reforms, that there is significant further consultation with traditional owners, Native Title Representative Bodies, industry and other stakeholders.

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- 1 Workshops on tax were organised at Native Title Representative Body Conferences in Perth (2008) and Canberra (2010) and by the ATNS Project in 2007 and 2008. For an overview of the tax issues, see Lisa Strelein, ‘Taxation of Native Title Agreements’, *Native Title Research Monograph* (No1/2008) AIATSIS, available from <<http://www.aiatsis.gov.au>>.
- 2 The Treasury, Australian Government, *Native Title, Indigenous Economic Development and Tax: Consultation Paper* (20 October 2010) <<http://www.treasury.gov.au/contentitem.asp?NavId=037&ContentID=1890>>. Consultation recommenced (after the federal election) in October 2010; submissions were due 30/11/2010.
- 3 FaHCSIA and Attorney General’s Department, *Leading practice agreements: maximising outcomes from native title benefits* (July 2010) <http://www.fahcsia.gov.au/sa/indigenous/pubs/land/Pages/leading_practice_agreements.aspx>, submissions were due 30/11/2010.
- 4 FaHCSIA, *Indigenous Economic Development Strategy* (May 2010) <<http://resources.fahcsia.gov.au/IEDS/>>, submissions were due 17/12/2010.
- 5 FaHCSIA, *Indigenous Home Ownership Issues Paper* (May 2010) <http://www.fahcsia.gov.au/sa/indigenous/pubs/housing/indig_home_ownership/Pages/default.aspx>, submissions were due 17/12/2010.
- 6 The Treasury, above n 2, 5. See also Strelein, above n 1, 26.
- 7 *Income Tax Assessment Act 1997* (Cth) (ITAA97) s 6-5 (alternatively, a specific provision, eg s 15-20 which taxes royalties, could apply).
- 8 *Scottish Australian Mining v FCT* (1950) 81 CLR 188; *FCT v Myer Emporium Ltd* (1987) 163 CLR 199.
- 9 *Mabo v Queensland (No. 2)* (1992) 175 CLR 1, 51, 89, 110-112 and 194-195; *Western Australia v Ward* (2002) 191 ALR 1, 161.
- 10 ITAA97 s 104-5; divs 110, 112, 116.
- 11 CGT event A1, ITAA97 s 104-10.
- 12 CGT event C2, ITAA97 s 104.25.
- 13 *Native Title Act 1993* (Cth) (NTA) s 51(1).
- 14 The Treasury, above n 2, 4.
- 15 TR 95/35 para 70.
- 16 GSTR 2006/9 para 89.
- 17 *Ibid*, para 85.
- 18 Marcia Langton, *The Mabo Lecture: Native Title, Poverty and*

Economic Development (speech delivered at the Native Title Conference, 3 June, 2010), 17 <<http://www.atns.net.au/objects/NCUWSARNERB/Mabo%20Lecture%202010%20Langton.pdf>>.

- 19 NTA, div 3.
- 20 *Ibid*, s 31.
- 21 See *Traditional Owner Settlement Act 2010* (Vic), <<http://www.justice.vic.gov.au/wps/wcm/connect/justlib/doj+internet/home/your+rights/indigenous+victorians/native+title/justice+-+e+traditional+owner+settlement+act+2010>>; South Australian Native Title Resolution process, <<http://www.iluasa.com/>>. These are recognised under s 87, 22L and elsewhere in the NTA.
- 22 The Treasury, above n 2, 8.
- 23 See the detailed comparative research on agreement-making in Langton, Tehan, Palmer and Shain (eds) *Honour among Nations? Treaties and Agreements with Indigenous People* (Melbourne University Press, 2004).
- 24 The Treasury, above n 2, 9.
- 25 FaHCSIA/AG, above n 4, 7.
- 26 Where the individual is in receipt of a government benefit, such a payment may have an impact on that benefit under the *Social Security Act 1991* (Cth). There is not scope to address this here, but if a payment is tax-exempt, it may be appropriate that it be counted in determining entitlement for social security purposes.
- 27 For example, freehold land may be received in a settlement, see eg Mt John Valley ILUA (NNTT Number: DI2009/002, registered 6 May 2009); Broome ILUA (Yawuru Prescribed Body Corporate ILUA, NNTT Number:WI2020/003, registered 24 May 2010 & Yawuru Area Agreement ILUA, NNTT Number WI2010/004, registered 6 August 2010).
- 28 Strelein, above n 1, 33; Lisa Strelein and Tran Tran 'Taxation, trusts and the distribution of benefits under native title agreements', Native Title Research Report No 1/2007, AIATSIS, Canberra; Fiona Martin, "The legal concept of charity in the context of Australian taxation law: the public benefit and commercial activity, important issues for indigenous charities" (2010) 25 Australian Tax Forum 275; Fiona Martin and Audrey Sharp 'Taxation of Charities for the Advancement of Indigenous Peoples within the same Family: Australia and New Zealand compared' (paper presented at Australasian Tax Teachers Association conference 2010).
- 29 But see *Commissioner of Taxation v Word Investments Ltd* (2008) 236 CLR 204 (HCA).
- 30 The Treasury, above n 2, 10.
- 31 ITAA97, Div 50.
- 32 Above n 5.
- 33 Based on evidence led to establish the native title claim: see eg *Adnyamathanha No. 1 Native Title Claim Group v The State of South Australia (No.2)* [2009] FCA 359.
- 34 As noted at n 26, the social security consequences would need to be examined.
- 35 The Treasury, above n 2, s 3.3, 14: this was proposed, but not enacted, by the Howard government in 1998.
- 36 The MWT currently applies to payments under the *Aboriginal Land Rights Act 1976* (NT).
- 37 Strelein, above n 1, 46.

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