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15 October 2008

Infrastructure Australia
Level 21
Deutsche Bank Building
126 Phillip Street
SYDNEY NSW 2000

Dear Sir / Madam,

Discussion Paper 2: Public Private Partnerships – Submission on Taxation Issues

We are pleased to make the enclosed submissions in response to Discussion Paper 2: Public Private Partnerships. We would be happy to discuss with you any issues that you would like to explore further.

Yours sincerely,



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Encl

SUBMISSION COVERSHEET

Submissions may address any key issues related to the Infrastructure Australia agenda and/or in specific response to the topics raised in the discussion papers.

Please complete and submit this form with your submission. Where possible, *Infrastructure Australia* requests submissions are submitted electronically. Contact us:

Via email Write 'Submission' in subject field of the email and send to: mail@infrastructureaustralia.gov.au	Via post Address your submission to: The Infrastructure Coordinator Infrastructure Australia GPO Box 594 Canberra ACT 2601 AUSTRALIA
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Submission title: Discussion Paper 2: Public Private Partnerships – Submission on Taxation Issues

Author(s): Amrit MacIntyre

No. of pages: 3

Date: 15 October 2008

Please indicate if your submission:

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Please indicate which of the following your submission covers:

Issues Paper 1 — Australia's Future Infrastructure Requirements

Issues Paper 2 – Public Private Partnerships

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Water Infrastructure

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- Authors of submissions are responsible for securing the appropriate right to use any third party material incorporated into their submissions.
- Submissions made by individual community members should not include any personal details other than your name, suburb, state/territory or country. For submissions made by organisations contact details may be included.

Please tick to indicate that you have read and agree to the above.



Discussion Paper 2: Public Private Partnerships

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Discussion Paper 2: Public Private Partnerships (*Discussion Paper*)

Taxation Issues

The taxation costs of delivering infrastructure under a public private partnership model will be one of the important matters that a private sector partner will need to take into account when making decisions on whether to participate in such a project and in costing the project. A policy objective of the government ought to be removing taxation obstacles to the effective and cost efficient delivery of infrastructure.

Income Tax

The income tax (including capital gains tax issues) concerning infrastructure have been written on widely¹, with substantial commentary on the issues arising out of the Division 250 amendments to the *Income Tax Assessment Act* 1997. We do not propose to add further commentary in this regard. We confine our submission to stamp duty and GST issues which appear to have had little coverage.

Stamp Duty

Stamp duty is levied by all States and Territories. Pursuant to the terms of the *Intergovernmental Agreement on the Reform of Commonwealth State Financial Relations*, stamp duty in respect of transfers of land is not to be abolished but will remain in place indefinitely. Given the narrowing of the revenue base of the States and Territories over the years, particularly following the introduction of GST in 2000, stamp duty in respect of land remains an important source of revenue for the States. In the light of these circumstances, the States and Territories may have a limited appetite for any further contraction of their tax base. Nevertheless, we make the following observations on the application of stamp duty on land transactions, as regards infrastructure projects.

Typically, a significant revenue cost of the delivery of infrastructure projects will be the stamp duty cost of land acquisitions. Where the private partner must acquire land, the stamp duty payable will be a transaction cost which will form part of the overall cost of the relevant infrastructure project. Given that the effective rate will be between 4% and 6.75%, this will be a significant project cost. Unlike GST, there is no mechanism for the recovery of stamp duty by means of input tax credits. The cost therefore becomes a real embedded cost. Where the relevant land is acquired not through acquisition of the fee simple interest but through a long term lease, conveyance or transfer duty will still generally apply at the top marginal rate where the consideration for the acquisition is a premium (as opposed to periodic rental) except in Victoria.

Where the transaction requires a transfer to the Commonwealth of the land in question at the conclusion of the project, the availability of exemption depends on the legislation of the relevant State or Territory and whether the doctrine of crown immunity applies. Whether the doctrine will apply will depend on the circumstances of each case and cannot automatically be assumed. In many cases it does not. While the law of the States and Territories often allows exemptions for the benefit of the relevant State or Territory government no such exemption is generally available for the Commonwealth.

The Commonwealth's ability to escape taxation will generally depend on the Constitution which may prohibit such taxation. Section 114 imposes a prohibition on a State imposing any tax on property belonging to the Commonwealth. However, the precise scope of the provision in prohibiting stamp duty on a transfer of land to the Commonwealth is not always clear especially where stamp duty is strictly a tax on the transfer instrument in question rather than the property itself (e.g. *Superannuation Fund Investment Trust v Commissioner of Stamps* (SA)[1979] HCA34).

¹ Mackenzie, Gordon, *Infrastructure Taxation in Australia: Accessing Losses and Avoidances* [2008] UNSWLRS 30

Further stamp duty could apply where the infrastructure asset in question is held by the private partner in a special purpose vehicle (*SPV*) into which investment occurs by way of equity. While all States and Territories allow various exemptions from stamp duty for certain types of SPV, for example where the investment vehicle is listed (or in New South Wales, Victoria and Queensland investment is open only (or largely) to prescribed categories of wholesale investors), the rules are often complicated and exemption is often difficult to claim.

Stamp duty therefore could apply potentially up to three times. Once on the initial acquisition of land, again on investment into the SPV which has acquired the land and again on the final transfer of the asset into public ownership.

Where the transaction occurs by way of sale and leaseback, the prospect of double stamp duty once again applies first on the initial sale and again on the subsequent leaseback.

One approach is for relevant Commonwealth legislation to prohibit the imposition of stamp duty in the appropriate circumstances. However, such an approach is fraught with difficulty. First of all, the ability of the Commonwealth to so legislate will depend on a constitutional power to do so. It is not clear that such a power will exist in all cases. In any case, in light of the Commonwealth Government's policy of cooperative federalism, it does not appear that such an approach would be appropriate.

Where the liability lies with the Commonwealth, the Constitution may not necessarily provide relief from duty. The arguments and uncertainties that can arise as to whether a State law imposing stamp duty contravenes a Constitutional prohibition are illustrated in the cases of *Superannuation Fund Investment Trust* (concerning sec 114) and *Allders v Commissioner of State Revenue* (VIC) [1996] HCA58 (concerning sec 52(i)).

To avoid the outcome of a possible conflict with the States and the uncertainty of the Constitutional position, it is suggested that a solution should be found through the cooperation of the States. This should occur by means of the granting of appropriate exemptions by the States in respect of:

1. the initial acquisition of land by the private partner;
2. making available appropriate exemptions for investors into SPVs holding the relevant infrastructure assets where none is currently available; and
3. ensuring no duty applies on the end transfer of the relevant assets to Commonwealth ownership.

Such legislative amendments it is submitted could be dealt with on a project by project basis assuming that the issues in question arise from a limited number of high value projects. Such an approach may be more acceptable for the States rather than blanket exemptions.

The impact of stamp duty on the cost of the infrastructure project is seen in the ongoing dispute between the Commonwealth and New South Wales over the NSW government's assessment of "land rich" duty on the acquisition of the Sydney Airport by Macquarie Airports through Southern Cross Airports Corporation Holdings Ltd. The amount of duty in question is understood to be \$400 million.

Goods and Services Tax

Goods and Services Tax (*GST*) has applied in Australia since 1 July 2000. As a broad based tax covering most economic activity and applying at the rate of 10%, it could be expected that GST will apply to supplies and acquisitions at all stages of an infrastructure project. Under the mechanism that makes input tax credits available for input GST against the output GST liability of the owner and operator of the infrastructure asset, the net cost of GST should in principle be zero. To this extent, the application of GST in respect of infrastructure projects should pose less problems than the application of stamp duty.

However, on the delivery of a completed infrastructure project to the Commonwealth as envisaged in the Discussion Paper, the amount of GST that will be payable on the supply is expected to be substantial given the value of large infrastructure projects. As long as the amount of the relevant GST is collected by the infrastructure owner from the Commonwealth, no difficulty should arise. The effective cost would be borne by the Commonwealth. That is, the infrastructure owner would collect the amount of the GST from the Commonwealth and effectively return the amount to the Commonwealth.

In order to avoid unnecessary disruption to Government cash flows, consideration could be given to making the supply of relevant infrastructure projects GST free. This could be achieved for example by including a new sub-division into *A New Tax System (Goods and Services) Tax Act 1999* that allows for relevant projects to benefit from such treatment on delivery to the Commonwealth. Nominated projects could be brought within the scope of such a provision by means of regulation.

It should be noted that the European Court of Justice in the recent case of *Zweckverband zur Trinkwasserversorgung und Abwasserbeseitigung Torgau-Westelbien* (Case C 442/05, 3 April 2008) allowed the delivery of an infrastructure project in the nature of a water delivery system to occur on a GST free basis (or zero rated to use relevant European terminology).

Given that at least in economic terms, GST is supposed to operate as a tax on the end consumer, there does not appear to be any reason derived from the theory or policy underlying value added taxes, to prevent GST free treatment for the delivery of infrastructure projects into public ownership.

Where a private partner establishes an SPV to hold an infrastructure project and invites investors to acquire interests in the SPV, the SPV will typically incur intermediary fees. Such intermediary fees can be significant. Where the output of the SPV is an equity or debt interest, it would be input taxed. The consequence would be inability to obtain input tax credits on services and other things it acquires in relation to the relevant input taxed supplies. Some acquisition costs will give rise to the ability to obtain a reduced input tax credit, e.g. arranging fees and brokerage fees. Other acquisition costs, e.g. the cost of advisory services will not give rise to the ability to claim input tax credits. Where the SPV holds a relevant infrastructure asset governed by public private partnership of the kind contemplated in the Discussion Paper, consideration should be given to allowing relief on costs for a SPV holding the relevant assets. While amending the *A New Tax System (Goods and Services Tax) Regulations 1999* to provide for special rules allowing such relief may complicate the legislation, given the special circumstances governing large "one off" projects, such relief, it is submitted, would be appropriate.