

THE ECONOMIC DEVELOPMENT OF NORTHERN AUSTRALIA: A CRITICAL REVIEW OF THE TAXATION BENEFITS AND INCENTIVES BOTH PAST AND PRESENT AND THE POTENTIAL TAXATION OPTIONS FOR THE FUTURE

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ABSTRACT

In 2015, the Australian government (Commonwealth of Australia) produced a White Paper on the need to realise the full potential of northern Australia and for that region to become an economic powerhouse within Australia. The White Paper explicitly states that the government is not declaring the north a Special Economic Zone where tax concessions are provided to businesses to reside and operate in the region. This paper will examine the current government's approach to developing the north and in particular the approach to attracting economic activity and foreign investment. This paper will focus on the current tax benefits for those living and working in the north, such as zone rebates, and in particular on what more that could be done by the Australian, state and territory governments to encourage economic activity. The paper will also examine the tax concessions that existed in the past such as an exemption for income tax pursuant to the now repealed s 23(m) of the *Income Tax Assessment Act 1936* (Cth) for companies resident in the Northern Territory prior to 1947, and the Darwin Trade Development Zone that was abolished in 2003. The paper will then assess the merits of offering tax benefits in the form of tax credits for businesses operating in the north and greater tax deductions. The paper will explore the merits of a Special Economic Zone for the north as well as tax benefits that could be offered by the states of Queensland and Western Australia and the Northern Territory. The paper will also provide recommendations for a range of tax benefits that could be offered by the various governments to businesses and individuals in order to assist in developing the north. If not, the north may fail to fulfil its true potential.

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I INTRODUCTION

The 'north' of Australia encompasses parts of the Northern Territory, Western Australia and Queensland. It is generally defined as the part of Australia that is to the north of the Tropic of Capricorn.¹ This is the area that is specifically examined in this paper and in particular the taxation issues that relate to its development. This paper will examine the current government's approach to developing the north, in particular to attracting economic activity and local and foreign investment. The paper will focus on the current tax benefits for those living and working in the north, such as zone rebates, and then explore what more could be done by the Australian, state and territory governments in terms of taxation benefits. The paper will examine the tax concessions that existed in the past such as an exemption from income tax pursuant to the now repealed s 23(m) of the *Income Tax Assessment Act 1936* (Cth) for companies resident in the Northern Territory prior to 1947, and the Darwin Trade Development Zone that was abolished in 2003. The paper will then assess the merits of offering tax benefits in order to attract investment and people to develop the north, including exploring the merits of a Special Economic Zone (SEZ). The paper will conclude with recommendations for various tax benefits to be offered – otherwise the north may not succeed in fulfilling its true potential.

Prior to examining the existing taxation concessions and the past taxation concessions that applied to the north of Australia, it is important to examine the recent Australian government (Commonwealth of Australia) inquiries into recommendations for the development of the northern part of Australia. There are two main reports: the first in 2014 comprising an inquiry; and a subsequent 'Green Paper', discussed in Section A, below. The government then issued a 'White Paper' in 2015, discussed in Section B, below. Both government reports discuss the merits of an SEZ and the existing tax concessions that are relevant to the north, such as the zone offset for individuals. These reports form the basis for the introduction of this paper and put the taxation issues for the development of the north into context. A recent paper by Jeffrey Fitzpatrick and Zhang Jian provides an excellent discussion of the literature on the problems facing the development of north Australia and the creation of an SEZ.²

A Pivot North – Inquiry into the Development of Northern Australia

As the Chair of the Joint Select Committee of Northern Australia stated in their foreword to the 2014 inquiry, '[s]ince 1937 there have been numerous reports and recommendations with the aim of developing Northern Australia which are gathering dust on shelves. It is now up to us to prove the sceptics wrong and get things moving'.³ The Green Paper puts the northern part of Australia in perspective when it states that the

¹ ADC Forum, 'Northern Development: Creating the Future Australia' (Report of the ADC Forum, Northern Development Summit, June 2014) xi <<https://adcforum.org/adc-news/adc-northern-development-summit>>.

² Jeffrey Fitzpatrick and Zhang Jian, 'Using China's Experience to Speculate upon the Future Possibility of Special Economic Zones (SEZs) within the Planned Development of Northern Australia' (2016) 18 *Flinders Law Journal* 29, 35.

³ Parliamentary Joint Select Committee on Northern Australia, Parliament of Australia, *Pivot North – Inquiry into the Development of Northern Australia: Final Report* (September 2014) ix <www.aph.gov.au/~media/.../24%20Committees/.../Final%20Report/Final.pdf>.

area of land represents 40 per cent of Australia's total land mass but only has 1 per cent of the population of Australia. It is on the doorstep to Asia.⁴ The Green Paper was the first step in promoting the development of northern Australia and it was then followed by the White Paper, discussed below. The terms of reference included an additional requirement in relation to taxation matters. The committee was asked to make recommendations on taxation matters related to the regulatory and economic environment of northern Australia.

The committee examined the various submissions relating to the introduction of an SEZ. One of the strongest advocates for an SEZ was Australians for Northern Development and Economic Vision (ANDEV).⁵ Their contention was that the whole of the northern part of Australia should be an SEZ with reduced state, territory and Australian government taxation, tax concessions for investment in infrastructure and streamlined regulatory requirements.⁶ Other aspects of the ANDEV submission will be discussed in Part IV of this paper.

Recommendation 37 of the Green Paper stated that the Australian government should explore reforms to the taxation system in order to promote investment and development in the north. The recommendation considered that an SEZ be established.⁷ As discussed below, the White Paper on the north categorically ruled out the establishment of an SEZ. The committee, in its recommendation 38, contended that the zone tax offset, which provides very limited income tax relief for individuals working and living in remote areas, should be reviewed. The basis for this recommendation was that the purpose of the offset should be to promote development and that can only be achieved by individuals employed by business in the remote areas.⁸

This report formed the basis for the subsequent White Paper, published one year later.

B The White Paper on Developing the North

In 2015 the Australian government produced a White Paper on the need to realise the full potential of northern Australia and for that region to become an economic powerhouse within Australia:⁹

The north has untapped promise, abundant resources and talented people. It is also Australia's closest connection with our key trading markets and the global scale changes occurring in Asia. A strong north means a strong nation. Even though over one million people live in the north — all of the Northern Territory and those parts of Western Australia and Queensland above the Tropic of Capricorn — it accounts for over half of our sea exports (Ports Australia, 2014). Thriving and diverse exports in minerals,

⁴ Ibid.

⁵ Australians for Northern Development and Economic Vision, Submission No 147, Attachment 9 to the Parliamentary Joint Select Committee on Northern Australia, Parliament of Australia, *Pivot North – Inquiry into the Development of Northern Australia: Final Report*, 7 April 2014.

⁶ Parliamentary Joint Select Committee on Northern Australia, Parliament of Australia, above n 3, 39.

⁷ Ibid 191.

⁸ Ibid 192.

⁹ Government of Australia, 'Our North, Our Future: White Paper on Developing Northern Australia' (2015) <northernaustralia.gov.au/files/files/NAWP-FullReport.pdf>.

energy, agriculture and tourism underpin our national income. The earnings from the Pilbara alone are larger than the individual economies of 119 countries but are generated by only 60,000 people (Pilbara Development Commission, 2013).

Many previous efforts to develop the north have floundered through a lack of foresight and the absence of markets in our region for high value goods and services. Through this, the first ever White Paper on Developing Northern Australia (the White Paper), the Commonwealth Government is putting in place the right policies, at the right time, to unlock the north's vast potential. This White Paper has been developed to stand the test of time — it should be the first, and last, White Paper for the north.¹⁰

Given the optimism and encouraging assessment of the northern part of Australia you would have expected the Australian government to be engaged in a great deal of activity encouraging both people and businesses to move to the north and develop its potential. However, the only tangible sign of any activity is the announcement by the Minister for the Department of Industry, Innovation and Science that from 18 January 2017 the 'Office of Northern Australia' (ONA) will be established in Darwin, Northern Territory, with one full-time public servant.¹¹ The minister, Josh Frydenberg, made the following announcement in relation to the establishment of the ONA:

Further, the ONA will play a central key role in the implementation of the Government's \$5 billion Northern Australia Infrastructure Facility (NAIF), working closely with northern stakeholders and colleagues in the Department of Industry, Innovation and Science. The NAIF will provide concessional loans to major economic infrastructure to support the development of Australia's north.¹²

The White Paper states that the free trade agreements with China, Japan and the Republic of Korea will bring foreign investment into the area.¹³ More private investment is being encouraged by the government in order to support its ambitious plans for developing the north.¹⁴ Most of the foreign investment in the mining boom period of 2010 to 2015 was directed in the north and the government at the time of the White Paper expected it to continue. In 2012 it consisted of \$206 billion.¹⁵ As history has now shown, the mining boom is over and investment has reduced substantially as new infrastructure and plants have been constructed. However, it is contended in this paper that private investment both domestic and foreign will not be attracted to the north without some form of taxation benefit. The current company tax rate of 30 per cent is one barrier to investment.¹⁶ The government also believes that as a result of its promotional activities

¹⁰ Ibid 1.

¹¹ Department of Industry, Innovation and Science, Government of Australia, 'Office of Northern Australia Open for Business' (Press Release, 18 December 2015) <www.northernaustralia.gov.au>.

¹² Ibid.

¹³ Ibid 152.

¹⁴ Ibid 61.

¹⁵ Ibid.

¹⁶ Company tax rates have been reduced for small businesses. The *Treasury Laws Amendment (Enterprise Tax Plan) Act 2017* (Cth) reduced the income tax rate for small companies. For the year ending 2016, companies with an average turnover of less than AU\$2 million had a rate of 28.5 per cent. For the year ending 2017, companies with an average turnover of less than AU\$10 million have a rate of 27.5 per cent. For the year ending 2018, companies with an average turnover of less than AU\$25 million will have a rate

it will attract investment to the north,¹⁷ and the free trade agreements with the US, Japan, China, Republic of Korea, Singapore and Canada will support this objective.¹⁸ The Australian government also believes that investment will be increased by reducing barriers such as lengthy timeframes for regulatory approvals, high costs, and duplication of government approvals.¹⁹ The government introduced an Entrepreneurs' Infrastructure Programme whereby the government provides grants: an Early Stage Innovation Company tax credit for investors, as well as Export Development grants. It contends that these financial and tax-related benefits should assist in attracting investment in developing the north. These arrangements are discussed briefly in the Part III of this paper.

The White Paper specifically states that the creation of an SEZ in a particular region of Australia would contravene the *Commonwealth of Australia Constitution Act 1990* (the Constitution), as it would amount to discrimination in taxation pursuant to s 51(ii) and s 99.²⁰ The report goes on to state that any reduction of taxation and the streamlining of regulatory requirements should apply to the whole of Australia and not just an SEZ.²¹ The Australian constitutional issues relating to the non-discrimination provisions in respect to taxation are examined in detail in the following section of this paper.

II AUSTRALIAN CONSTITUTIONAL ISSUES

The tax and tax transfer benefits that are currently being provided to individuals and corporations operating in the north of Australia would suggest that these benefits do not contravene s 51(ii) and s 99 of the Constitution and that more extensive tax or tax transfer benefits could be offered to both individuals and corporations in the future in order to develop the north. However, this issue of the Constitution specifically prohibiting discrimination between states in relation to taxation will now be examined in detail prior to discussing the specific tax benefits that exist today.

Section 51 of the Constitution provides the specific powers that are reserved for the Australian Parliament and s 51(ii) states that Parliament has 'the power to make laws with respect to taxation; but so as not to discriminate between States or parts of States.' The Constitution then contains a further restriction on potential preferences between states with s 99:

The Commonwealth shall not, by any law or regulation of trade, commerce, or revenue, give preference to one State or part thereof over another State or any part thereof.

of 27.5 per cent. The average annual turnover figure increases to AU\$50 million and the company tax rate reduces to 25 per cent by the year ending 2027.

¹⁷ Ibid 61.

¹⁸ Ibid 63.

¹⁹ Ibid 59.

²⁰ Ibid 60.

²¹ Ibid.

These provisions should now be read on the understanding that any reference to 'states' should also include the two territories of Australia, namely the Australian Capital Territory and the Northern Territory.

The High Court in the case of *Cameron v Deputy Federal Commissioner of Taxation for Tasmania* (1923) 32 CLR 68 held that different rates at which livestock was valued in different states in Australia under the *Income Tax Assessment Act 1915–1918* amounted to discrimination between the states and was thus unconstitutional. At that time livestock values differed between states, such that cattle in Tasmania, where this case was brought by the appellant, had a value of £3 and yet in New South Wales the value was £6.²² This impacted on the taxpayer's calculation of their taxable income and the amount of income tax to be paid. His Honour Mr Justice Higgins provides the following summary of the positions of the taxpayer and the application of the law contained in the Constitution:

The position of the taxpayer is that he has to pay on his income; that his income depends on his profits; that the profits depend on the value of his stock; and that the values depend on the State in which he happens to be carrying on his business. Two pastoralists may in fact make £1 000 net profit – one in New South Wales, the other in Queensland; and yet under these Rules they may be treated as making unequal profit, and be liable to pay unequal income tax. The only reason for this result is that one is in Queensland, the other in New South Wales. This, in my opinion, is clearly a discrimination between States as to taxation.²³

The full bench of the High Court, consisting of Knox CJ, Isaacs, Higgins, Rich and Starke JJ, unanimously agreed that the specific taxation rule that attributed different values to different livestock in each state infringed s 51(ii) and s 99 of the Constitution.

The 'isolated area zone tax offsets' (in the *Income Tax Assessment Act 1936* (Cth) s 79A), which are discussed below, is arguably an example of a taxation preference being given to individuals living in parts of Western Australia, Queensland, South Australia, New South Wales, the Northern Territory and Tasmania. Victoria is the only state that is not regarded as having any remote areas. Perhaps this is one of the reasons why the taxation preference contained in the remote area offset has not been challenged as infringing the Constitution. Fullarton contends that there are two alternative reasons why s 79A has not been declared unconstitutional. The first reason he contends is that the isolated zone offset is in effect financial assistance to those individuals living in certain parts of Australia and therefore is allowed pursuant to s 96 of the Constitution.²⁴ His second contention is that the offset is not taken into account in determining the individual's taxable income and therefore is outside the scope of s 51(ii) of the Constitution.²⁵ Both contentions have merit and according to Fullarton they are the reason why the isolated zone offset has been in existence for more than 70 years.²⁶ Fitzpatrick and Jian appear to agree with Fullarton's contention that the isolated zone offset is a form of financial assistance and not taxation discrimination. They argue that this form of 'financial

²² *Cameron v Deputy Federal Commissioner of Taxation for Tasmania* (1923) 32 CLR 68, 78.

²³ *Ibid.*

²⁴ Alexander Fullarton, 'Are You Still Here, Mr Hasse? A Study of Australia's Tax Rebate for Residents in Isolated Areas' (2014) 9(1) *Journal of the Australasian Tax Teachers Association* 24, 34.

²⁵ *Ibid.*

²⁶ *Ibid.*

assistance' is permitted under the Constitution by virtue of s 96, which allows Parliament to 'grant financial assistance to any State on such terms and conditions as the Parliament thinks fit'.²⁷

It is also contended, as discussed above, that the isolated zone offset affects many individuals living in a wide area of Australia and not just one state or territory. This may be one of the reasons why neither Victoria nor the ACT have deemed it necessary to challenge the offset in the High Court of Australia as being unconstitutional pursuant to s 51(ii) and s 99 of the Constitution. Moreover, the existence of s 96 of the Constitution adds strength to the argument that the zone offset is constitutional.

III THE EXISTING TAX BENEFITS RELATED TO THE NORTH

There are a number of minor tax benefits that are provided by the Australian government that are relevant to individuals working in the north. This part of the paper will examine those tax benefits as they apply to individuals. This will also include a brief examination of the tax benefits provided to corporations in the form of export market grants and tax concessions for innovation development and research and development expenditure. Some state and territory governments provide tax benefits in the form of reduced payroll tax, land tax and stamp duty. The Northern Territory does not have a land tax so that tax relief is not relevant to individuals or corporations if operating in the Northern Territory.

A Isolated Area Zone Tax Offset

The isolated area zone tax offset is available for individual taxpayers living in remote areas classified as zone A with an offset of AU\$338; zone B with an offset of AU\$57; special area within zones A and B with an offset of AU\$1173; and an overseas forces offset of AU\$338. The offset, or rebate as it was originally known, was introduced in 1945 in recognition of individuals living in remote and harsh conditions.²⁸ The Henry Tax Review recommended that the isolated zone rebate be reviewed, and this is contained in recommendation 6(b):

The zone tax offset should be reviewed. If it is to be retained, it should be based on contemporary measures of remoteness.²⁹

Since the Henry Tax Review, which was released in December 2009, nothing has been done to review the tax offset. Fullarton provides a detailed discussion of the history of these tax offsets and contends the rebates should be increased and could be used as a means of attracting university graduates by reducing their university debt.³⁰ This would be an important incentive especially if you are trying to attract a skilled workforce to a particular area. It is an alternative to paying exorbitant wages.³¹ As discussed below,

²⁷ Fitzpatrick and Jian, above n 2, 64.

²⁸ *Income Tax Assessment Act 1936* (Cth) s 79A.

²⁹ Government of Australia, 'Australia's Future Tax System: Report to the Treasurer' (Australia's Future Tax System Review Panel, December 2009).

³⁰ Fullarton, above n 24.

³¹ Government of Australia, above n 9, 104.

medical practitioners are paid a cash incentive to work in isolated and remote areas. The White Paper states that the cost to revenue of this tax benefit is AU\$300 million per year and has been in place since 1945 to help individuals living in remote places.³² The scheme has been amended to exclude the fly-in and fly-out workers who do not 'have their usual place of residence' in the remote areas.³³ The requirement of residing in the remote area for more than 183 days was replaced with the residence test. This measure took effect from 1 July 2015.

B Remote Area Housing Exempt Fringe Benefit

Employers are exempt from paying fringe benefits tax (FBT) on the value of housing that is provided to individuals working in remote areas (*Fringe Benefits Tax Assessment Act 1986* (Cth) s 58ZC). In order for the accommodation to be exempt from FBT it must be located at least 40 kilometres from a town with a census population between 14 000 and 130 000, or 100 kilometres from a town with a census population of 130 000 or more. If the accommodation is located within zone A or B it must be at least 40 kilometres from a town with a census population between 28 000 and 130 000, or at least 100 kilometres from a town with a census population of 130 000 or more.

C Financial Incentives for Rural Doctors

The Australian government introduced financial incentives for individual medical practitioners operating in remote areas throughout Australia. They are a form of tax transfers designed to benefit remote communities by attracting medical practitioners to rural and remote locations.

From 1 July 2015, the General Practice Rural Incentives Program (GPRIP) moved to the new classification system, the Modified Monash Model (MMM), to more effectively target financial incentives to doctors working in areas that experience greater difficulty attracting and retaining general practitioners. Participants are now being assessed against the new eligibility criteria. The first payments under the new arrangements commenced in August/September 2016.³⁴ From 1 July 2017 a new flexible payment system was introduced for medical practitioners and this is set out in the Australian Government Department of Health website.

The maximum incentive payment amounts are shown in the following table. They show the maximum annual payment available to medical practitioners across each MM category at each year level.³⁵ The MM categories relate to the level of remoteness of the medical practice.

³² Ibid.

³³ *Tax and Superannuation Laws Amendment (2015 Measures No. 5) Act 2015*.

³⁴ Department of Health, Government of Australia, *General Practice Rural Incentives Program: Program Guidelines* (30 June 2017) <http://www.health.gov.au/internet/main/publishing.nsf/content/general_practice_rural_incentives_programme>.

³⁵ Ibid.

Table 1

Location (MM)	Year 1	Year 2	Year 3	Year 4	Year 5 +
MM3	\$0	\$4500	\$7500	\$7500	\$12 000
MM4	\$0	\$8000	\$13 000	\$13 000	\$18 000
MM5	\$0	\$12 000	\$17 000	\$17 000	\$23 000
MM6	\$16 000	\$16 000	\$25 000	\$25 000	\$35 000
MM7	\$25 000	\$25 000	\$35 000	\$35 000	\$60 000

These amounts are not subject to withholding tax but are part of the medical practitioner's assessable income. The Australian government is prepared to make a tax transfer payment under this scheme in recognition of the fact that medical practitioners would prefer to live and work in the urban parts of Australia and not the remote and rural areas. This approach could easily be extended to other skills that are in short supply in remote areas. There may be a scarcity of particular skills in Australia and market wages are not sufficient to attract those people to the remote areas, or there may be a compelling social need for those skills, such as teachers.

IV THE FORMER TAX CONCESSIONS

There have been attempts to attract business and people to the Northern Territory (NT) through the use of taxation concessions. On 1 July 1978 the NT attained responsible self-government. Prior to that date the NT was administered by the Australian government, having been handed back to the government by the State of South Australia on 1 January 1911. The people living in the NT lost their representation in the State Parliament of South Australia and the Australian Parliament. From the time of the first major European settlement in 1863 until 1910, the NT was the responsibility of the Government of South Australia.³⁶ The NT has a very chequered history, which has resulted in various attempts by governments to offer taxation incentives in order to encourage investment in the area. The two main schemes to provide taxation concessions for businesses in the NT are examined below.

A Exemption from Income Tax for Companies Resident in the NT

In 1923 the Australian government first granted an exemption from income tax for companies involved in primary production, mining or fisheries that operated in the NT. The exemption continued until 1 July 1947. Clause 3 of the explanatory memorandum for

³⁶ P F Donovan, *At the Other End of Australia* (University of Queensland Press, 1984) xiii.

the Bill stated that the exemption was introduced 'in order to assist and encourage the development of the Northern Territory of Australia'. This was achieved by inserting s 23(m) into the *Income Tax Assessment Act 1936* (Cth) (ITAA 36). This did not create a potential problem with s 51(ii) of the Constitution because the NT was not part of South Australia, or an independent territory, but under the administration and control of the Australian government.

P F Donovan, in his book on the history of the NT, examines the state of the pastoral industry in the 1920s at the time of the income tax exemption being introduced by the Australian government. Most of the pastoral land in the NT is held as leasehold land and many of the existing leases at that time were governed by South Australian legislation. When these leases were to be consolidated under NT legislation, 52 lessees preferred to hold their land under South Australian law.³⁷ According to Donovan, this leasehold problem and the introduction of the income tax exemption did not help to stimulate the industry and only the large pastoralists welcomed the tax benefit.³⁸ Due to a state of economic depression in the NT, large pastoralist companies came to dominate the industry as never before.³⁹ This would appear to be the case even now in the northern region of Australia.

The exemption from income tax encouraged development in growing cotton near Katherine but it was not very successful due to transport problems.⁴⁰ As a result of a 'cotton' expert from India being invited to inspect suitable land in the NT by the Australian government, 152 agricultural blocks were offered for settlement. The rent was waived for the first 21 years.⁴¹ Only 11 leases were taken up in 1923 and 47 in 1924.⁴² The cotton growing was a failure and it was contended at the time that the only reason why cotton growing started in the first place was due to the waiving of the rent on the land and the income tax exemption pursuant to ITAA 36 s 23(m).⁴³ However, the income tax exemption was successful for opening up new agricultural land in the NT.⁴⁴ It would appear from Donovan's history of the NT that isolation, lack of infrastructure and climate all acted to inhibit the NT from developing during that period.

The well-known High Court case of *North Australian Pastoral Company Limited v Federal Commissioner of Taxation* (1946) 71 CLR 623 examines the concept of residence in the NT in order for the income from primary production to be exempt from income tax.⁴⁵

B The Darwin Trade Development Zone (TDZ)

The Darwin Trade Development Zone (DTDZ) is Australia's former attempt at establishing a form of a Special Economic Zone. It commenced on 25 September 1985 as

³⁷ Ibid 62.

³⁸ Ibid.

³⁹ Ibid.

⁴⁰ Ibid.

⁴¹ Ibid 63.

⁴² Ibid.

⁴³ Ibid.

⁴⁴ Ibid.

⁴⁵ The former s 23(m), *Income Tax Assessment Act 1936* (Cth).

the *Trade Development Zone Act (NT)* (TDZ Act) and was repealed on 1 July 2003. The TDZ Act was amended on 18 June 1999 in order to establish Trade Development Zone Authority. The objective of the amended TDZ Act was to establish an authority to administer, control and encourage the development of a Trade Development Zone in the NT, to attract industry to that zone, and for other related purposes.

Each corporation wanting to operate within the DTDZ was licensed by the authority. The effect of obtaining a licence was that 'notwithstanding anything in any other Act, a licensee shall not be liable to pay a fee, tax, duty, rate or charge specified in the Regulations in relation to the business conducted by him in the Trade Development Zone in respect of the period during which his licence remains in force.' In effect the NT government exempted the businesses within the zone from payroll tax and stamp duty. The zone was similar to Export Processing Zones in other parts of the world where manufacturers are allowed to import components into a bonded warehouse without paying import duty and export finished goods without paying excise or sales tax.⁴⁶

The functions of the Authority were:

- (a) to promote and manage the Trade Zone;
- (b) to make arrangements for the provision of facilities and services to meet the requirements of persons carrying on business in the Trade Zone;
- (c) to advise persons carrying on business or proposing to carry on business in the Trade Zone on matters relating to the provision of services and facilities and privileges available, or which will be available, to them in relation to those businesses or proposed businesses and provide general assistance to facilitate the establishment and conducting of those businesses as it thinks fit;
- (d) to advise the Minister and such other persons and authorities as the Minister directs or the Authority thinks fit on –
 - (i) the development and encouragement of the use of the Trade Zone for manufacturing, entrepot and associated industries; and
 - (ii) the needs of, and the provision of government and other services to, persons carrying on business in the Trade Zone; and
- (e) such other functions as are imposed upon it by or under this or any other Act.

The DTDZ was abolished in 2003 by the *Trade Development Zone Act Repeal Act 2003 (NT)*. The second reading speech provides a very brief statement of why the first ever Australian attempt at an SEZ was now being abolished:

The bill is cognate with the repeal of the Trade Development Zone Authority Act. Australia is now party to all trade agreements which restrict government subsidies and many forms of government assistance to exporting business. Australian business and government also adhere to principles of competitive neutrality onshore. To say the least, times have changed since the concept of the Northern Territory Trade Development

⁴⁶ F D Robins, 'Darwin's Trade Development Zone (Its Appeal and Its Success)' (Occasional Paper Series No 2, University College of the Northern Territory, Faculty of Arts, 1988) 13.

Zone. The concept of a zone where businesses derive a benefit over other like businesses because they are in a particular zone is no longer appropriate in today's business world.

Government therefore does not intend that the corporation take on the activities of what is currently the Trade Development Zone Authority. The corporation becomes responsible for the land interest, assets and liabilities of the Trade Development Zone on its establishment. The current lessees will, at that point, become tenants of the Land Development Corporation. It is intended that there will be as little disruption to Trade Development Zone businesses in this change over as possible. A provision is made in the bill for the assignment of all rights, authorities, other than the exemption from payroll tax and stamp duty. These exemptions as a right of the TDZ licence will cease with the repeal of the Trade Development Zone Act. A separate arrangement is being provided by Treasury to cover payroll tax concessions over licences until the licences expire. Stamp duty concessions will cease all together.

F D Robins was given financial support by the University College of the Northern Territory to undertake a study of the DTDZ. The college was the forerunner to the establishment of Charles Darwin University. At the time he wrote the report the DTDZ had been in operation for two years. The review consisted of interviews with Asian businessmen interested in establishing a factory in Darwin. Robins commences his review with a discussion of why the DTDZ was established in the first place. He states that as far back as 1974 the people of Darwin wanted to establish a duty free port but that the Constitution would prohibit special preference being given to the NT in relation to import duties and excise.⁴⁷ However, Paul Everingham, the then Chief Minister, and the Prime Minister Bob Hawke were in support of the concept and the law was put into effect to establish the DTDZ on 25 September 1985.⁴⁸ Robins identifies the fact that the DTDZ has a number of inherent disadvantages that Special Economic Zones in other countries do not have. First, the population was at that time very small; second, while it is close to Asia it does not have 'cheap labour'; third, the DTDZ is a project of a second-tier government operating within a federal system of government.⁴⁹ This third point reinforces the fact that the taxation benefits are restricted to NT government benefits and limited customs exemptions.⁵⁰

Robins examined the DTDZ's appeal for Asian investors and observes that the motivation for Asian businessmen contemplating a factory in Darwin was their wish to migrate to Australia.⁵¹ However, the businessmen expressed concern about the prospect of 'strikes' in Australia and the high rates of income tax and the newly introduced tax on capital gains.⁵² They were also concerned that Darwin did not have an established freight link to Asia and this would create difficulties in exporting the finished products.⁵³ Robins was very circumspect when trying to assess the success of the DTDZ after two years. He found that after two full years of operation the DTDZ had its first business and a textile

⁴⁷ Ibid 4.

⁴⁸ Ibid.

⁴⁹ Ibid 2.

⁵⁰ Ibid.

⁵¹ Ibid 21.

⁵² Ibid 23.

⁵³ Ibid.

manufacturer was about to start.⁵⁴ Very little has been written about the ultimate success of the DTDZ and subsequent NT governments have not raised the prospect of re-establishing a trade zone.⁵⁵ The tax concessions that were offered by the Government of the Northern Territory were very limited. However, there are a number of successful new industries operating within the former DTDZ, especially in the area of oil and gas processing. Robins made the observation that the DTDZ was unique in Australia but that if it demonstrated its success it could be replicated elsewhere in Australia and this would occur by 1990.⁵⁶

It is important to note in the second reading speech for the repeal of the DTDZ that one of the reasons given for its abolition was the need for the Australian government to adhere to its contractual obligations under the General Agreement on Tariffs and Trade (GATT) and that a trade zone offering special taxation treatment was a possible infringement of those obligations.⁵⁷ The potential infringement related to the concept of 'national treatment'. According to John Mo, national treatment is the term in international treaties that ensures that the home country treats the nationals of the foreign country in the same way it does its own domestic nationals in commercial dealings.⁵⁸ The existence of the DTDZ could have been seen as providing favourable taxation treatment to domestic businesses, constituting discrimination of foreign businesses. The Australian government obligations under GATT must be taken into consideration whenever an SEZ is being considered for the development of the north.

V RECOMMENDATIONS

If the Australian government is serious about developing the north then tax incentives in different forms must be considered for both individuals and businesses. The following part of the paper will examine a range of taxation benefits that might be worthy of consideration in the future.

A Special Economic Zones

In order to assess the merits or disadvantages of an SEZ, it is important to briefly examine what an SEZ is and what form it would take. SEZs are all zones established by governments as a means of encouraging multinational enterprise investment in the country. They provide an 'economic sanctuary' consisting of specially demarcated areas for businesses to carry out their operations under a set of rules different to domestic businesses. While the underlying reason for establishing such zones differs for each country they all contain these basic key features:

⁵⁴ Ibid 38.

⁵⁵ A great deal of effort has been made to research this issue but it would appear that the DTDZ is to be forgotten without some form of assessment.

⁵⁶ Robins, above n 46, 39.

⁵⁷ The General Agreement on Tariffs and Trade (GATT) consists of World Trade Organization (WTO) member states agreeing on reducing trade barriers and resolving trade disputes. For more detail see John Mo, *International Commercial Law* (LexisNexus, 4th ed, 2009) 714.

⁵⁸ Ibid 720.

- Seeking foreign investment into the country;
- Requiring products and services developed in these zones to be exported out of the country (protecting the local domestic markets);
- Providing total exemption or a reduction of sales, income and other duties either for a specified or unlimited period of time;
- Employing and up-skilling the local population;
- Reducing the amount of 'red tape' and bureaucratic procedures in these zones, eg 'single window' administrative solutions;
- Providing free importation of raw materials, components and equipment; and
- Injecting foreign direct investment and capital into the country.

There are a number of different types of zones and in order to understand what is meant by an SEZ it is useful to briefly describe the other types of zone:

1. Industrial Estates or Parks, which are designated areas that mainly involve import substitution products and processing raw materials obtained by the domestic market.
2. Export Processing Zones (EPZs), which are mainly focused on processing products or services for export. This was the type of zone that the DTDZ was designed to emulate.
3. Free Trade Zones (FTZs), which have been developed to expand trade with neighbouring countries and to obtain reductions or exemptions from duties and other taxes.
4. Special Economic Zones (SEZs), which are areas engaged in a wide variety of activities that can include research and development and manufacturing and enjoy similar tax benefits provided to FTZs.
5. Investment Facilitation Establishments (IFEs), which 'entail a tract of land, with or without real estate facilities, or building development and contain certain basic infrastructure facilities such as water, electricity, road and other types of amenities for the facilitation of business or commercial activities.'⁵⁹

An EPZ is defined as:

a clearly demarcated industrial zone which constitutes a free trade enclave outside a country's normal customs and trading system where foreign enterprises produce principally for the export and benefit from certain tax and financial incentives.⁶⁰

⁵⁹ ASEAN Secretariat and United Nations Development Programme, *Industrial Estates, Export Processing Zones, Free Trade Zones, Science and Technology Parks in ASEAN* (ASEAN Secretariat/United Nations Development Programme, 2002) vii.

⁶⁰ P Arunahalam (ed), *Special Economic Zones in India: China's Way of Development* (Serials Publications, 2010) 167.

The main difference between an EPZ and an FTZ is that an FTZ 'is an integrated township with fully developed infrastructure whereas an EPZ is just an industrial enclave.'⁶¹ As stated in the introduction to this paper, for ease of understanding all types of zones are referred to as Free Trade Zones (FTZs).

The amount of land allocated for zones differs from country to country:

In some cases entire countries, such as Singapore or Hong Kong, are virtually EPZs in themselves. In others, such as China's 'special economic zones', they are on such a vast scale that they don't seem to fit the definition ... individual firms have been granted zone status, notably in Tunisia, where nearly 580 firms (1989-90 figures) in nine regions of the country fall into this category.⁶²

Similar to worldwide trends, most currently operating zones focus on labour-intensive, assembly-orientated activities such as apparel, electronics, and electrical goods, with women making up the majority of the workforce.⁶³

Incentives offered by SEZs encompass regulatory incentives, financial incentives and fiscal incentives. In the context of SEZs, regulatory incentives encompass the relaxation of regulations impacting targeted companies. Such relaxed regulation is generally the relaxation of direct investment regulations, and may also include relaxation of visa classes to attract certain employees or of trade, shipping and manufacturing regulations. Financial incentives encompass public spending to attract companies. This may consist of direct cash payments or subsidies, or increased public funding on infrastructure. Financial incentives can be designed to specifically target desired industries through tailoring the infrastructure of the geographical area to the needs of such industries. Financial incentives, for example through low land rental and utilities, are offered in countries such as Egypt, Lebanon and the United Arab Emirates.⁶⁴

Fiscal incentives consist of easing the tax burden of targeted companies or their employees. Unlike the other incentives, they are commonly legislation-based changes through the tax system. Such fiscal incentives may specifically be targeted at industries through the creation of eligible categories, or may be generally applied to all such taxpayers within the region. Targeting may also be achieved through reducing certain taxes that apply to targeted industries, such as indirect taxes on the importation and exportation of goods and services as desired. Fiscal incentives may apply for a limited period of time (eg a tax holiday).

In the context of Middle East and Northern African (MENA) countries, fiscal incentives play a large part in the policy of attracting investment in both the general economy and SEZs, with a number of SEZs providing attractive tax regimes:

⁶¹ Ibid.

⁶² Ibid.

⁶³ Richard Newfarmer, William Shaw and Peter Walkenhorst (eds), *Breaking into New Markets: Emerging Lessons for Export Diversifications* (The World Bank, 2009) 225.

⁶⁴ Nada Farid, 'Towards Best Practice Guidelines for the Development of Economic Zones: A Contribution to the Ministerial Conference by Working Group 1' (MENA-OECD Investment Programme, Marrakech, 23 November 2009) <<https://www.oecd.org/mena/competitiveness/44866585.pdf>>.

MENA countries rely in large measure on fiscal incentives to attract investors in the general economy, with financial and regulatory playing a less prominent role. For the most part fiscal incentives offered to investors in the general economy are available to companies in the FEZs as well. However, some zones go beyond this and offer additional fiscal concessions. Four countries offer a complete exemption from corporate and private income taxes in their free zones (Algeria, Egypt, Kuwait and United Arab Emirates), whereas companies located in SEZs (in Egypt – and likewise in Jordan) are requested to pay certain low income taxes. Jordan's free zones offer freedom from the taxation of corporate profits earned on manufacturing goods for imports or trading within the zones. Several countries (Lebanon, Morocco and Yemen) offer corporate tax holidays in their FZs that are more generous than what is available under their general investment incentive regimes. Some zones also offer reduced personal income taxes on expatriate staff. In Yemen, the income of non-Yemeni employees is completely exempt from taxation; in Jordan's free zones non-Jordanian employees enjoy a 12 year tax holiday, and in Tunisia's FZs a flat individual income tax rate of 20% is applied to the salaries of foreign staff.⁶⁵

MENA countries initiated the trend for economic zones to move away from Free Trade Zones and Export Processing Zones towards Special Economic Zones, with a focus on value-added services to specific industries.

The 2002 Multilateral Investment Guarantee Agency (MIGA) (a member of the World Bank Group) 'Foreign Direct Investment Survey' provided the top 20 factors cited as the main determinants affecting the decision-making process for locating overseas.⁶⁶ The top 3 by percentage of influence were market access (77 per cent), stable socio-political environment (64 per cent) and ease of doing business (54 per cent). Despite fiscal incentives playing the largest part in the design of attracting companies and investment, national taxes and local taxes were cited as 11th and 17th most influential at 29 per cent and 24 per cent respectively.

According to these statistics, tax is only one consideration for a company in deciding whether to locate a business in an SEZ jurisdiction. The factors considered most important are those that may facilitate economic activity and enable a business to generate pre-tax profits. This is obvious, because a lower rate is not going to be beneficial if a business cannot profit in the first place. Despite tax concessions being used as the main tool by governments to attract businesses to locate to an SEZ, the tax benefits may therefore not be the primary factor considered by such businesses.

Given the fact that taxation concessions are not the main focus of SEZs, it is quite strange that the Australian government has dismissed the idea of establishing an SEZ in Australia. The government is currently concerned about bringing the Budget back into surplus, but their approach to an SEZ may be short-sighted given the other benefits of an SEZ. The government's White Paper on developing the north specifically stated that they were not

⁶⁵ Ibid 9.

⁶⁶ MIGA, 'Foreign Direct Investment Survey: A Study Conducted by the Multilateral Investment Guarantee Agency with the Assistance of Deloitte & Touche LLP' (The World Bank, January 2002) <<http://documents.worldbank.org/curated/en/669281468764093551/pdf/267930Foreign0Direct0investment0survey.pdf>>.

in support for the development of an SEZ in the north of Australia. They made the following comment:

A Special Economic Zone (SEZ) is a geographically limited region in which special taxation and/or regulatory arrangements apply such as duty concessions for manufactured exports. Since the establishment of the first modern free trade zone in Ireland in 1959, it is estimated that 3 500 such zones have been established in around 130 countries (Boyenge, 2007). SEZs have been successfully used to trial reforms before being applied more broadly. More often, SEZs have been useful in attracting investors who are particularly sensitive to taxation and/or regulatory hurdles.

The creation of SEZs must be considered carefully to ensure that they attract new investment, given their ability to potentially lead to misallocation or distorted investment decisions. The World Bank found that if a SEZ is to be successful then 'the commercial case must be present' and that case 'must be based on sustainable sources of competitiveness, not on fiscal incentives' (Farloe & Akinci, 2011).

In Australia, the Constitution prohibits Commonwealth taxation that discriminates between states or parts of states as well as Commonwealth laws or regulation of trade, commerce or revenue that gives preference to one state or part of a state over another.

If the policies within SEZs (for example, lower taxation or regulatory requirements) have net advantages for an economy, there is an argument for extending the logic of these policies to the nation as a whole — and not confining the benefits of SEZs to specific regions. This principle underpins many of the measures in this White Paper, which are national in scope while being of particular significance to the north.⁶⁷

However, there are a number of individuals and organisations that do not share this view with the Australian government. For example, in August 2013, the then Prime Minister Kevin Rudd pledged to create a Special Economic Zone in the Northern Territory with a company tax rate of 20 per cent, a third lower than anywhere else in Australia. Rudd then went on to say that the Constitution would allow the creation of a special taxation zone and that he was prepared to fight such a case in the High Court. The then Opposition Party leader Tony Abbott appeared to support the notion of a special tax zone on the basis that the Coalition had already recognised the potential of northern Australia and the need for taxation concessions.⁶⁸

On 20 May 2015, the former Federal Treasurer Joe Hockey stated that a special tax zone for northern Australia was 'worthy of consideration' as part of the White Paper on northern Australia that was due to be released at the time.⁶⁹

⁶⁷ Government of Australia, above n 9, 41.

⁶⁸ Judith Ireland and Daniel Hurst, 'Prime Minister Kevin Rudd Has Announced a Special Economic Zone in Northern Australia', *Sydney Morning Herald* (online), 15 August 2013 <<http://www.smh.com.au/federal-politics/federal-election-2013/tax-cuts-economic-zone-part-of-kevin-rudds-plans-to-develop-northern-australia-20130815-2rybz.html>>.

⁶⁹ 105.7 ABC Darwin, 'Northern Australia Tax Zone Worthy of Consideration, Treasurer Joe Hockey Says', 20 May 2015 (Xavier La Canna) <<http://www.abc.net.au/news/2015-05-20/northern-australia-tax-zone-worthy-of-consideration-says-hockey/6482926>>.

ANDEV (Australians for Northern Development and Economic Vision), a think tank supported by Gina Reinhart, supports the creation of a 'Northern Economic Zone' that will offer tax advantages to attract and retain investment. They contend that SEZs have been very successful internationally in encouraging economic growth in underdeveloped regions. The zone could offer, for example:

- Lower personal income tax or tax rebates for those who live and work in the northern zone;
- No payroll tax;
- No fringe benefits tax; and
- No stamp duty.⁷⁰

However, the White Paper specifically rejected the idea of an SEZ.⁷¹

B China's Experience with SEZs and the Development of Northern Australia

A very detailed analysis was undertaken by Jeffrey Fitzpatrick and Zhang Jian on China's experience with SEZs and their potential to have a limited use in developing the north of Australia.⁷² This section of the paper will provide a brief examination of their investigation into China's use of SEZs from the perspective of their strengths and weaknesses, and then speculate on how this knowledge can be used to assess the limited use of an SEZ in the north of Australia within the White Paper plan.⁷³ Fitzpatrick and Jian suggest that the successes and weaknesses of China's SEZ experience can be contrasted with the Australian government's plan to develop the north. Their six contrasting points are as follows:

1. *Government commitment to economic growth in the north.* The administration of the Chinese SEZ was devolved to the local government to provide taxation relief and customs clearance.⁷⁴ In the case of Australia, Fitzpatrick and Jian submit that the Office of Northern Australia operating in Darwin has a role to coordinate the implementation of the White Paper on the development of the north, similar to the role of the Guangdong Provincial Committee in China.⁷⁵
2. *Pragmatism and practicality: A gradualist approach to reform.* The Chinese government adopted a pragmatic and gradual approach to the development of the SEZ in terms of attracting foreign direct investment and exports.⁷⁶ Fitzpatrick and Jian contend that the role and plan of the government in developing the north, which is outlined in the White Paper, is similar in many ways to the approach taken by China.⁷⁷

⁷⁰ *Australians for Northern Development and Economic Vision* <<http://www.andev-project.org/about-us/whats-needed>>.

⁷¹ 105.7 ABC Darwin, above n 69.

⁷² Fitzpatrick and Jian, above n 2.

⁷³ *Ibid* 56.

⁷⁴ *Ibid* 50.

⁷⁵ *Ibid* 59

⁷⁶ *Ibid* 51.

⁷⁷ *Ibid* 59.

3. *Inflow of local and foreign investment.* In China the SEZ used monetary and non-monetary incentives to attract foreign investment such as a lower corporate tax rate and a flexible approach to employment and labour relations.⁷⁸ Much of the foreign investment came from the Chinese diaspora from Hong Kong, Macao and Taiwan. The Chinese diaspora developed learning opportunities, technology and product innovation within the SEZ.⁷⁹ Fitzpatrick and Jian discuss the need for taxation incentives to be offered in Australia for a possible SEZ but at the same time highlight the constitutional problem of not discriminating between states.⁸⁰
4. *Population growth, employment and skill development.* The north of Australia has only a small population of 1.3 million and represents 5.6 per cent of Australia's population, whereas the SEZs in China had no problem in finding sufficient workers.⁸¹ Fitzpatrick and Jian discuss the problems faced in Australia in eventually developing an Australian SEZ, such as climatic conditions, lack of skilled labour, limited financial assistance for individual workers through the isolated zone offset, and high living costs.⁸² They examine the various government schemes for attracting workers to seek employment in isolated and remote areas as one way to overcome a potential labour shortage.⁸³
5. *Land reform.* The Chinese SEZ allowed land within the zone to be leased by investors thus providing investor confidence.⁸⁴ In the Australian context, much of the pastoral land in the north is crown land, which is offered as leasehold or subject to native title. The Australian government wants to reduce administrative approvals and diversify the land usage in order to promote development.⁸⁵
6. *Geographic location.* There are similarities with China's SEZ experience and Australia's proposed approach to developing the north. According to Fitzpatrick and Jian, China located many of their SEZs along the coast so that goods could be exported by sea.⁸⁶ The White Paper contends that the future of trade is in the Asian and tropical regions to the north, and any development in the production of goods or services should be focused on a gateway to the north.⁸⁷

Fitzpatrick and Jian then discuss three specific areas of weaknesses within China's SEZ experience and how this may apply to plans to develop the north of Australia. The first is the need for environmental protection, which was a feature of China's SEZ experience.⁸⁸ At stake in Australia are the Great Barrier Reef and other unique natural assets such as flora and fauna that could be overly exploited if the regulatory requirements were relaxed

⁷⁸ Ibid 60.

⁷⁹ Ibid.

⁸⁰ Ibid 61.

⁸¹ Ibid 62.

⁸² Ibid 64.

⁸³ Ibid 66.

⁸⁴ Ibid 67.

⁸⁵ Ibid.

⁸⁶ Ibid 68.

⁸⁷ Ibid.

⁸⁸ Ibid 69.

in order to develop the north.⁸⁹ The second area of concern relates to the provision of social services. The SEZs in China did not adequately provide social services, such as education and health and transport, as quickly as would have been desired but the north of Australia has very limited social services due to its geographic size and remoteness.⁹⁰ However, according to Fitzpatrick and Jian the White Paper contends that social benefits will emanate from greater employment opportunities as a result of the development of the north. The third area of concern is that of an uneven development of the whole of Australia if the north is singled out for additional financial support from the government at the expense of other areas.⁹¹ The Chinese SEZ experience created better living standards in the cities but not in the rural areas of the west of China.⁹²

C Tax Credits for Development

The Australian government is offering a variety of tax offsets for early stage innovation companies and for research and development expenditure. This type of tax concession could be offered to businesses and investors that want to establish themselves in the north. They are already being provided to investors and businesses in order to encourage development in innovation, so they could be extended to target new businesses being established in the north. Businesses could be offered a special capital allowance rate for their establishment costs and additional tax deductions associated with the cost of doing business in remote areas, similar to the remote zone offset for individuals. If the taxation benefit was in the form of a tax offset rather than a tax deduction, then the contention made by Fullarton, above, may overcome the constitutional issue that the north of Australia is being given a preference contrary to s 51(ii) and s 90 of the Constitution.

Other taxation considerations could consist of state and Northern Territory tax concessions on payroll tax and stamp duty. While these tax concessions are less than those that could be offered by the Australian government, they do assist new businesses.

VI CONCLUSION

The Australian government's White Paper on developing the north is a start in the right direction but words must be followed by actions. As discussed above, in order to attract individuals to live and work in the north the remote zone offset needs to be increased to take into account the cost of living in the north and the remoteness of the work environment. The climate is also an important consideration. Employers would benefit if they were not required to pay higher wages and salaries in order to attract staff.

For new businesses to be attracted to the north the Australian, state and Northern Territory governments must make it financially attractive. It is contended in this paper that the existence of free trade agreements between Australia and its northern neighbours is not enough to attract investment to the north. It is also contended in this

⁸⁹ Ibid.

⁹⁰ Ibid 71.

⁹¹ Ibid.

⁹² Ibid.

paper that the taxation concessions related to the promotion of innovation by enterprises by the Australian government will not necessarily result in business development and investment in the north without some additional taxation benefits. In this respect, an SEZ should be given more consideration by the government. As discussed above, the Fitzpatrick and Jian contention that the Chinese experience with SEZs is relevant for Australia with the concept of a limited SEZ in the north is an important consideration for the future.

This paper has examined two significant issues that need to be resolved once and for all before an SEZ can be implemented in the north of Australia: first, the problem with providing taxation or preferential financial benefits to parts of Australia that may be unconstitutional; and second, the problem of infringing Australia's obligations under GATT. If these concerns can be overcome then perhaps an SEZ in some form might be developed for the north.

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