

Department of Environment, Parks, Heritage and the Arts

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| For..... | |



Dr Ken Henry
Chair AFTS Review Panel
C/- AFTS Secretariat
The Treasury
Langton Crescent
PARKES ACT 2600

Dear Dr Henry

The Tasmanian Department of Environment, Parks, Heritage and the Arts (the Department) welcomes the opportunity to make a submission to Australia's Future Tax System Review.

The Department is responsible for the sustainable management, protection and promotion of Tasmania's natural and cultural assets, including the State's national parks, arts, culture, pristine environment and its unique Aboriginal and historic heritage. It also plays a significant role in driving Tasmania's economy through high quality visitor experiences.

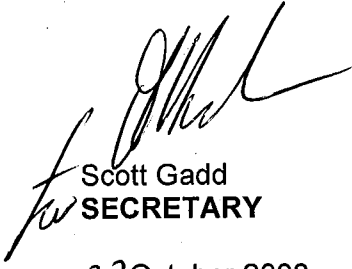
As the custodian of much of the natural and cultural heritage which sets Tasmania apart from the rest of the world, the Department plays a critical role in ensuring the State's heritage is protected, valued, understood and celebrated by the community. The Department endeavours to provide areas for recreation, reflection, conservation and artistic outlets, to protect the environment and to help foster Tasmania's sense of place.

The Department's portfolio responsibilities are integral to both the immediate and long-term wellbeing of the broader community.

Tasmanians benefit from the support and encouragement the Department gives to creativity and innovation, through environment, heritage and arts projects and programs aimed at connecting, educating and engaging communities around the State. Through the best possible use of the State's natural and cultural assets, the Department aims to enhance Tasmania's economic, environmental and social well being, both now and in the future.

The Department wishes to see the positive outcomes of participation in arts and cultural activities and the broader sectoral outcomes noted above (natural, cultural, environmental) continue to be achieved through tax deductibility status and other incentives as appropriate, under any new tax structure. Further comments from the Department specific to the historic heritage and arts sectors are attached.

I trust this information is of assistance to you and look forward to the Panel's consultation paper on the outcome of the initial stages of this Review.

A handwritten signature in black ink, appearing to read 'Scott Gadd', is written over the typed name and title.

Scott Gadd
SECRETARY

27 October 2008

Response to: **Australia's Future Tax System Review Panel**

Historic Heritage

The Department, through Heritage Tasmania, provides for the protection, sustainable management and promotion of Tasmania's historic heritage, by developing increased knowledge and understanding of the importance of heritage and working collaboratively with heritage owners, developers and the wider community. It provides free expert advice on heritage conservation and conservation grants, and supports community education and development activities which promote good heritage outcomes. It also supports the statutory role of the Tasmanian Heritage Council.

In reviewing the current tax system and tax expenditure instruments, it is important that opportunities for tax incentives or tax relief options for the owners, managers and operators of historic heritage places are explored. Such places entail important social, economic and environmental values. The cost of sound conservation can come at a premium in many cases, and reflects a trans-generational cost that can exceed the capacity of one generation. There is an urgent and pressing need to maintain access to tax deductible gift programs for conservation works in particular and explore ways by which other forms of fiscal incentives can be provided.

Arts

The Department, through Arts Tasmania, provides support to local artists and art organisations. It aims to broaden the engagement of Tasmanians in the arts, highlight the State's diverse arts and cultural sector and deepen Tasmanian cultural experiences. It also provides funding to major Tasmanian cultural institutions in order to assist their planning and realisation of projects, as well as to attract and encourage new work.

In response to the Terms of Reference for the review, the following issues, specific to the arts sector, have been identified.

1. Artists being Recognised as Professionals by the Australian Taxation Office

Currently, if you are not carrying on business as an artist, then you cannot offset losses from your art practice against other taxable income (such as teaching income, or income from other jobs or activities). If you are carrying on business as an artist, then you may still be caught by the "non-commercial losses" rules in the *Income Tax Assessment Act 1997* (Tax Act), with the same result.

The question of whether an artist is carrying on a business has been extremely difficult to answer, with the ATO and arts bodies grappling with this question for many years.

The Ruling

In January 2005, the ATO issued public ruling TR 2005/1, entitled 'Income Tax: carrying on business as a professional artist'. The ruling looks at how business as an artist contrasts to other types of business, and how to draw the line between an arts business and a hobby.

The ATO was concerned that an artist continually returning losses couldn't demonstrate the profit motive necessary to show that they were carrying on business as an artist. However, it is difficult for an artist to demonstrate this. Art depends upon unique ideas and originality, and the reality is that many artists return losses from their art activities.

The Ruling notes that the law applying to artists is no different to the law applying to any other business, but discusses the legal tests of a business with particular reference to the circumstances of artists, and applies to artists practising across all art sectors. Importantly, it recognises that arts businesses typically have different characteristics to those found in other businesses. It also accepts that a large part of being in business as a professional artist may involve activities directed towards reputation building and audience/market creation.

The Pedley Case

The Administrative Appeals Tribunal (Tribunal) decided a test case (*Pedley v Commissioner of Taxation*) in February of this year, finding that an installation artist was carrying on a business, despite returning net losses over a number of years.

The taxpayer had been an artist for over twenty years and had some minor sales of art, but had failed to return a profit from art activities in tax returns. The taxpayer said that she intended to carry on business as a professional, practising artist. However, the test under tax law was not what she thought, but what a reasonable person would objectively think - and in that regard the ATO said that it was impossible to predict when and if commercial success (and profits) would be achieved.

A previous case decided by the Tribunal after the Ruling was issued in 2005 (*VBF v Commissioner of Taxation*) found that an artist was carrying on a business once he had established his works in a format which could be commercially exploited.

It is also clear (from other cases and from the Ruling) that a taxpayer can be primarily motivated by excellence, rather than money, and still be carrying on a business. Further, a business can be carried on in conjunction with other income producing activities such as employment.

In the Pedley case, the ATO focussed upon a lack of sales, and noted that most of the artist's income came from grants. They argued that the artist would not be able to continue as an artist without grants funding, which raises the question of how then could that constitute a business?

The Tribunal found that installation art was an artistic area in which it was difficult, although not impossible, to achieve commercial success. The evidence demonstrated the relevant "profit making intention" notwithstanding that no profits had eventuated to date, or could be forecasted with any precision or certainty. Accordingly, the case was decided in the artist's favour, finding that the artist did carry on business as a professional artist in the relevant year.

The non-commercial losses rules

Even if an artist is carrying on a business, there is a risk that losses from that business may be caught under the non-commercial losses rules in Division 35 of the Tax Act. If they apply, the losses cannot be used to offset other income. They can only be offset against income from the art business which is earned in future years.

The rules do not generally apply if the income from other (i.e. non-arts) sources is less than \$40,000 in a particular year.

Artists should however be exempted from these rules due to the increased certainty over the "business" tests applying to artists.

2. Tax Smoothing to Match Income

Artists inevitably have income streams that vary considerably from year to year and as such can be subject to varying taxation issues. Consideration of the introduction of a taxation smoothing rule would be of considerable benefit to the arts industry.

3. Lower Tax Rates for Artists (the Ireland Model)

It is also suggested that consideration be given to a Tax Exemption for Artists similar to the Irish model outlined below to further enhance the "Creative Economy" and "Innovation" concepts being developed and promoted by Arts Tasmania and the Tasmanian Government.

Irish Resident Artists' Tax Exemption

If you have produced a painting or sculpture or written a book, play or musical composition then you may be entitled to receive any income from your work tax free. Providing the work is original and creative or has cultural or artistic merit then it should qualify. It is important to note that approval has to be granted by the Irish Revenue Commissioners and only applies from the beginning of the tax year in which you apply. An Irish income tax return still has to be made in the normal manner and you have to be a tax resident in Ireland.

An application was recently received for an Irish based artist who moved to Ireland from the UK. The client is now entitled to receive income from his work tax-free. Artists thinking of moving to Ireland may apply for an advance opinion in respect of their work and on approval by the Revenue Commissioners have to become a tax resident in Ireland.