



REPORT OF THE

STANDING COMMITTEE ON
CONSTITUTIONAL AFFAIRS

IN RELATION TO

***THE FINANCIAL RELATIONS AGREEMENT
(CONSEQUENTIAL PROVISIONS) BILL 1999 AND
THE STATE ENTITIES (PAYMENTS) BILL 1999***

Presented by the Hon Murray Nixon JP MLC (Chairman)

Report 44

STANDING COMMITTEE ON CONSTITUTIONAL AFFAIRS

Date first appointed:

21 December 1989

Terms of Reference:

1. The functions of the committee are to inquire into and report on:
 - (a) the constitutional law, customs and usages of Western Australia;
 - (b) the constitutional or legal relationships between Western Australia and the Commonwealth, the States and Territories,

and any related matter or issue;
 - (c) a bill to which SO 230 (c) applies but subject to SO 230 (d);
 - (d) any petition.

2. A petition stands referred after presentation. The committee may refer a petition to another standing committee where the subject matter of the petition is within the terms of reference of that standing committee. A standing committee to which a petition is referred shall report to the House as it thinks fit.

Members as at the date of this report:

Hon Murray Nixon JP MLC (Chairman)

Hon Ray Halligan MLC

Hon Tom Helm MLC (resigned from the Committee November 9 1999)

Hon Kenneth Travers MLC¹ (appointed to the Committee on November 10 1999)

Hon Helen Hodgson MLC (participating member for this inquiry)

Staff as at the date of this report:

Ms Felicity Beattie, Advisory/Research Officer

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¹ See Appendix 1.

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**Report of the Standing Committee on
Constitutional Affairs**

in relation to

***The Financial Relations Agreement (Consequential Provisions) Bill 1999 and the State
Entities (Payments) Bill 1999***

1 EXECUTIVE SUMMARY

1.1 The purpose of the *Financial Relations Agreement (Consequential Provisions) Bill 1999* (the Financial Relations Bill) is to put in place a number of measures to reform Commonwealth-State financial relations required by the commencement of the Goods and Services Tax (GST) from July 1 2000 as agreed by the Commonwealth and all States and Territories in June 1999. The full agreement, known as the *Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations* (the IGA), is attached as Schedule 1 of the Financial Relations Bill.

1.2 In addition to attaching the IGA as a schedule, the Financial Relations Bill gives effect to a number of matters contained in the IGA, namely:

- ceasing to apply financial institutions duty from July 1 2001;
- ceasing State diesel subsidies as a result of the new Commonwealth scheme;
- ensuring payroll tax is not levied on top of GST;
- ceasing to apply the stamp duty on shares quoted on a recognised stock exchange from July 1 2001;
- adjusting stamp duties to be inclusive of GST; and
- abolishing the tobacco sellers' licensing scheme.

1.3 The purpose of the *State Entities (Payments) Bill 1999* (the State Entities Bill) is to provide for GST equivalent payments to be made by State and local government entities to the Australian Taxation Office. It also gives the State Treasurer the power, if required, to issue written directions to State and local government entities to make GST equivalent payments.

- 1.4 Under the IGA, Commonwealth, State and local governments and their agencies will voluntarily comply with Commonwealth GST legislation as if they were subject to the GST legislation. This avoids the Constitutional problem created by section 114 of the Constitution which prevents the Commonwealth taxing the property of the States.
- 1.5 The State Entities Bill provides the legal authority for State and local government entities to voluntarily comply with the provisions of the GST legislation where it would otherwise not apply by authorising State and local government entities to make GST equivalent payments.

2 RECOMMENDATIONS

- 2.1 This report outlines selected clauses and parts of the *Financial Relations Agreement (Consequential Provisions) Bill 1999* and the *State Entities (Payments) Bill 1999* which require explanation.

Recommendation 1: The Committee recommends that all clauses of the *Financial Relations Agreement (Consequential Provisions) Bill 1999* be passed.

Recommendation 2: The Committee recommends that all clauses of the *State Entities (Payments) Bill 1999* be passed.

**Report of the Standing Committee on
Constitutional Affairs**

in relation to

***The Financial Relations Agreement (Consequential Provisions) Bill 1999 and the State
Entities (Payments) Bill 1999***

3 REFERENCE AND PROCEDURE

- 3.1 The *Financial Relations Agreement (Consequential Provisions) Bill 1999* (the Financial Relations Bill) and the *State Entities (Payments) Bill 1999* (the State Entities Bill) were referred to the Standing Committee on Constitutional Affairs (the Committee) by the Legislative Council under Standing Order 230(d).

4 THE NEW TAX SYSTEM

- 4.1 The Federal Government has passed legislation to implement a goods and services tax at a 10% rate from July 1 2000. The GST will replace the Commonwealth's existing wholesale sales tax and a number of State taxes, namely Financial Institutions Duty and stamp duty on the sale of shares quoted on a recognised stock exchange. Debits tax will cease to apply by July 1 2005, subject to review by the Ministerial Council comprising Commonwealth, State and Territory Treasurers. The exclusion of basic food from the final GST package means fewer State taxes can be abolished in the short term than originally proposed.
- 4.2 Other key changes include a review by the Ministerial Council by 2005 of the need to retain a range of stamp duties levied on businesses (including stamp duties on non-residential conveyances; leases, mortgages, debentures, bonds and other loan securities; credit arrangements, instalment purchase arrangements and rental arrangements; and on cheques, bills of exchange, promissory notes; and unquoted marketable securities) and an adjustment of gambling taxes by States and Territories to take account of the impact of the GST on gambling operators.
- 4.3 The Commonwealth Government has guaranteed that the State and Territory budgets will be no worse off as a result of the new tax system and will top up the GST in the initial years to meet this commitment. The Commonwealth Government will provide transitional assistance as follows:

- in 2000-2001 the Commonwealth Government will provide interest free loans and grants to the States and Territories; and
 - in subsequent transitional years the Commonwealth will provide grants to States and Territories.
- 4.4 The GST will replace Commonwealth financial assistance grants, the franchise fee replacement revenues, the abolished State taxes and a reduction in gambling taxes. The GST will be distributed between the States on the basis of fiscal equalisation, as is the case with financial assistance grants currently.
- 4.5 The Financial Relations Bill and the State Entities Bill, together with the *New Tax System Price Exploitation Code (Western Australia) Bill 1999* and the *New Tax System Price Exploitation Code (Taxing) Bill 1999* (for a discussion of these bills see Report Number 45 of the Standing Committee on Constitutional Affairs) encompass most of the GST-related measures to be implemented by Western Australia. Some measures will be dealt with separately, including:
- price monitoring legislation;
 - legislation for a first home owners' assistance scheme to help offset the impact of the GST on house prices. The scheme will entitle eligible people to a lump sum payment of \$7000 from July 1 2000; and
 - regulations for changed liquor and gambling arrangements.

5 BENEFITS OF THE NEW TAX SYSTEM TO WESTERN AUSTRALIA

- 5.1 According to figures provided to the Committee by WA Treasury Department, Western Australia stands to benefit significantly from the GST.
- 5.2 Business costs will fall due to the abolition of sales tax and some State taxes, and the effective reduction in fuel costs. Fuel costs are significant in Western Australia due to the large distances over which goods must be transported.
- 5.3 The GST will be of particular benefit to exporters, as exports will be GST-free. Western Australia is a heavily export-oriented State (contributing 25% of the nation's exports) and the GST should therefore give the State's economy a significant boost.

5.4 In the short term, the arrangements are likely to be largely revenue neutral for State finances. However the GST is expected to grow more rapidly than the Commonwealth grants and State taxes that it will replace, giving Western Australia more revenue in the long term. Current estimates indicate that Western Australia can expect to start to accrue benefits in a net sense after the first three to four years of the introduction of the new tax system.

5.5 Based on current estimates provided by the WA Treasury Department, Western Australia would expect to be between \$700 million and \$1.5 billion better off over the first ten years of the GST, depending on the extent to which the State abolishes business stamp duties in the future. If the Ministerial Council decides to abolish those stamp duties, the benefit to the State would be less and the point at which Western Australia would start to accrue financial benefits would be deferred for much longer.

6 CONTENTS AND PURPOSE OF THE *FINANCIAL RELATIONS AGREEMENT (CONSEQUENTIAL PROVISIONS) BILL 1999*

6.1 The purpose of the *Financial Relations Agreement (Consequential Provisions) Bill 1999* (the Financial Relations Bill) is to put in place a number of measures to reform Commonwealth-State financial relations required by the commencement of the Goods and Services Tax (GST) from 1 July 2000 as agreed by the Commonwealth and all States and Territories in June 1999. The full agreement, known as the *Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations* (the IGA), is attached as Schedule 1 of the Financial Relations Bill.

6.2 The Financial Relations Bill also gives effect to a number of matters contained in the IGA, namely:

- ceasing to apply financial institutions duty from July 1 2001;
- ceasing State diesel subsidies as a result of the new Commonwealth scheme;
- ensuring payroll tax is not levied on top of GST;
- ceasing to apply the stamp duty on shares quoted on a recognised stock exchange from July 1 2001;
- adjusting stamp duties to be inclusive of GST; and
- abolishing the tobacco sellers' licensing scheme.

6.3 The Financial Relations Bill contains 39 clauses in seven parts. It also contains one schedule:

Part 1 - Preliminary

Part 2 - Financial Institutions Duty Act 1983

Part 3 - Fuel Suppliers Licensing Act 1997

Part 4 - Pay-roll Tax Assessment Act 1971

Part 5 - Stamp Act 1921

Part 6 - Tobacco Sellers Licensing Act 1975

Part 7 - Related amendments

Schedule 1 - Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations

6.4 Parts 2 - 6 inclusive of the Financial Relations Bill and Schedule 1 are outlined below. The Committee has provided comment on those parts.

6.5 As part of its review, the Committee placed an advertisement in *The West Australian* newspaper inviting submissions on the Financial Relations Bill. The Committee did not receive any submissions as a result of the advertisement.

6.6 As a further part of the review, the Committee invited comment from a number of parties who it considered may wish to make a submission. The witnesses who appeared before the Committee were:

- Mr David Smith, Director, Intergovernmental Relations, WA Treasury Department;
- Ms Anne Nolan, Assistant Under Treasurer, WA Treasury Department;
- Mr Mark Altus, Director, Revenue Policy, WA Treasury Department;
- Mr Michael Barnes, Acting Assistant Director, Revenue Policy, WA Treasury Department;
- Ms Nicki Suchenia, Acting Assistant Commissioner, Policy and Legislation, State Revenue Department;
- Mr Bill Mitchell, Fair Trading Policy Advisor; and
- Mr Nick Roberts, Policy Officer, Ministry of Fair Trading.

7 SELECTED PARTS OF THE *FINANCIAL RELATIONS AGREEMENT (CONSEQUENTIAL PROVISIONS) BILL 1999*

7.1 Part 2 - *Financial Institutions Duty Act 1983*

7.1.1 Part 2 of the Financial Relations Bill deals with proposed amendments to the *Financial Institutions Duty Act 1983*. Financial institutions duty (FID) is levied by the State Government on all receipts by financial institutions and on liabilities and investments of short term money market dealers.

7.1.2 This Part provides for FID to cease to apply from July 1 2001 by amending the *Financial Institutions Duty Act 1983* to ensure that no liability will arise in respect of receipts or dealings after midnight on June 30 2001. In addition, amendments are proposed to ensure that no returns will be required to be lodged in respect of receipts or dealings arising in any month after June 2001.

7.1.3 FID could not be abolished at the same time GST starts (July 2000) as the Commonwealth was not prepared to provide the extra funding that would be needed to ensure State budgets were no worse off.

7.1.4 The WA Treasury Department has estimated that Western Australian taxpayers will save approximately \$130 million in 2001-2002 as a consequence of the removal of FID.

7.2 Part 3 - *Fuel Suppliers Licensing Act 1997*

7.2.1 Part 3 of the Financial Relations Bill seeks to amend the *Fuel Suppliers Licensing Act 1997* to provide for the cessation of State diesel fuel subsidies for both off-road and on-road users with effect from July 1 2000.

7.2.2 The State subsidies are largely replaced by the Commonwealth's new expanded diesel fuel rebate scheme, together with excise reductions and GST input credits available for business purchases of fuel.

Off-road Diesel Subsidies

7.2.3 Off-road diesel subsidies currently amount to approximately \$147 million per year.

7.2.4 The Commonwealth will effectively take over most of the off-road subsidies by expanding its current industry-specific off-road diesel fuel rebate scheme to rail and

marine diesel, and increasing the amount of the rebate to 100% of the excise for all eligible uses.

- 7.2.5 Accordingly, it is proposed that Western Australia's off-road subsidies will cease in respect of diesel fuel supplied from July 1 2000.
- 7.2.6 Commercial farming and fishing will not be affected by this measure. They will continue to pay no effective tax on diesel fuel, as they will qualify for a full rebate of the diesel excise from the Commonwealth, and also being able to claim an input credit for the GST on diesel.
- 7.2.7 The mining sector will be better off as they will pay virtually no effective tax on diesel by qualifying for a full rebate of the diesel excise from the Commonwealth. The current 93% rebate under the Commonwealth's rebate scheme will increase to 100%.
- 7.2.8 Some users of diesel fuel who currently receive the State off-road subsidy will be worse off under the proposed arrangements because the expanded Commonwealth rebate scheme will still be less than comprehensive. In particular, diesel fuel used in power generation other than as part of an eligible mining operation, construction, manufacturing, and recreational activities will not get the Commonwealth rebate. However for business users of diesel fuel this will be largely offset by the reduction in diesel excise to make room for the GST and the fact that they will be able to claim back an input credit of approximately 7 cents per litre for the GST component.
- 7.2.9 Recreational users of diesel fuel (for example boating and off-road four wheel driving) will not be able to claim an input credit for the GST component and will therefore face higher fuel costs.

On-road Diesel Subsidies

- 7.2.10 On-road diesel subsidies currently amount to approximately \$8 million per year.
- 7.2.11 The Financial Relations Bill proposes the abolition of these subsidies, which apply at a rate of 0.66 cents per litre.
- 7.2.12 For business users of on-road diesel (mainly transport firms) the loss of the 0.66 cents per litre State subsidy will be offset by the much larger benefit from the general reduction in fuel excise and GST input credits. They may also receive an additional grant from the Commonwealth which will reduce the effective excise rate from the

current rate of around 43 cents per litre to 20 cents per litre for transport vehicles over 4.5 tonnes in rural areas and all other vehicles over 20 tonnes.

7.3 **Part 4 - *Pay-roll Tax Assessment Act 1971***

7.3.1 Part 4 of the Financial Relations Bill seeks to amend the *Pay-roll Tax Assessment Act 1971* to clarify the pay-roll tax treatment of certain payments considered "wages" for the purposes of that Act, which may also be subject to GST. The amendments will ensure that pay-roll tax is not applied on top of GST, where the form of remuneration attracts GST. Examples include payments by employment agents to workers supplied to a third party and payments under prescribed classes of contract, such as in the shipbuilding industry.

7.3.2 To ensure consistency in all cases with the general rule that activities done as an employee or other PAYE earner are not subject to GST, this Bill proposes that pay-roll tax is not to be charged on the increase in such payments directly attributable to the GST. This will ensure the same pay-roll tax treatment of differing types of wages and maintains the status quo.

7.4 **Part 5 - *Stamp Act 1921***

7.4.1 This part seeks to amend the *Stamp Act 1921* to:

- clarify the interaction of the existing stamp duty bases with the GST; and
- give effect to the requirement under the IGA that stamp duty ceases to apply from July 1 2001 to transfers of quoted marketable securities.

7.4.2 Unlike pay-roll tax, the various heads of stamp duty generally apply to values that directly or indirectly include wholesale sales tax. For example, sales tax is directly included in the market value of new motor vehicles for stamp duty purposes. In other cases, sales tax is an embedded cost that increases the price of property such as a home, which is subject to stamp duty when sold.

7.4.3 As the GST is to replace the current wholesale sales tax regime, it is appropriate that stamp duty be based on the GST inclusive price, value or consideration.

- 7.4.4 Under this approach, some revenue bases are still likely to go down because the 10% GST is replacing a much higher wholesale sales tax. This is likely to occur in the case of motor vehicle stamp duty, rental business duty and car and household contents insurance policies.
- 7.4.5 There will be increases in other stamp duty bases, however, particularly on property conveyances, insurance premiums paid by businesses and on leases and mortgages. These increases in stamp duty bases are likely to more than offset the decreases.
- 7.4.6 Part 5 of the Financial Relations Bill also seeks to amend the *Stamp Act 1921* by abolishing the stamp duty liability arising on the transfer of shares which are quoted on a recognised stock exchange. In accordance with the IGA, the abolition is intended to occur in respect of transfers which occur on or after July 1 2001.
- 7.4.7 The WA Treasury Department estimates that stamp duty on quoted marketable securities currently raises approximately \$18.5 million per annum in Western Australia. As in the case of FID, this revenue will be replaced by revenue to the State from the GST.
- 7.4.8 The specific amendments included as part of this measure seek to ensure:
- the removal of the charging provision for securities quoted on a registered stock exchange;
 - the removal of the broker return arrangements which allow brokers to pay duty by a return in respect of their on-market trades;
 - the removal of the CHES (Clearing House Electronic Sub-register System) provisions which allow participants to pay duty by a return for off-market trades of quoted marketable securities;
 - the removal of the United Kingdom Stock Exchange provisions which allow approved persons to pay duty by return in respect of any changes in beneficial ownership of Western Australian company shares that are quoted on the UK Exchange; and
 - the removal of the concessional rate of duty for transfers of short-dated shares.

7.4.9 Even though the liability to duty for these share trades is to be removed from July 1 2001, audit activity will continue after that date in respect of liabilities that arose prior to July 1 2001.

7.5 Part 6 - Tobacco Sellers Licensing Act 1975

7.5.1 The sole current function of the *Tobacco Sellers Licensing Act 1975* is to license tobacco sellers to provide information for monitoring the tobacco franchise fee replacement revenues. These replacement revenues will be abolished when the GST begins.

7.5.2 Part 6 of the Financial Relations Bill seeks to repeal the *Tobacco Sellers Licensing Act 1975* with effect from July 1 2000. The *Tobacco Sellers Licensing Act 1975* will therefore no longer serve any function after the introduction of the GST.

7.5.3 Abolition of the licensing arrangements from July 1 2000 is expected to result in approximately \$14 000 being foregone each year.

7.6 Schedule 1 - Intergovernmental Agreement on the Reform of Commonwealth-State Financial Relations

7.6.1 The IGA, which was signed by the Premier of Western Australia on June 29 1999, is attached as a schedule to the Financial Relations Bill. The Financial Relations Bill also records the intention of the State to comply with the IGA. This measure has no legal impact; rather the intention is to maximise the political authority of the IGA.

7.6.2 The IGA makes clear the conditions under which the State has agreed to abolish State taxes and also describes processes governing the reformed Commonwealth-State relationship which are not specified in the legislation, such as the new Ministerial Council.

7.6.3 The IGA sets out those aspects of the Commonwealth tax reform package which directly impacts on the States. Major provisions include:

- a commitment by all parties to fully implement the GST in the public sector;
- the States to introduce price monitoring legislation to facilitate the monitoring by the Commonwealth of price exploitation in areas outside the Commonwealth's Constitutional jurisdiction;

- a Commonwealth commitment not to cut specific purpose payments to the States as part of the reforms;
- the requirement that changes to the GST rate and base will require the unanimous agreement of the Commonwealth and the States; and
- the establishment of a Ministerial Council of Commonwealth and State Treasurers to oversee the operation of the GST and the IGA.

Recommendation 1: The Committee recommends that all clauses of the *Financial Relations Agreement (Consequential Provisions) Bill 1999* be passed.

8 CONTENTS AND PURPOSE OF THE *State Entities (Payments) Bill 1999*

- 8.1 The purpose of the *State Entities (Payments) Bill 1999* (the State Entities Bill) is to provide for GST equivalent payments to be made by State and local government entities to the Australian Taxation Office. It also gives the State Treasurer the power, if required, to issue written directions to State and local government entities to make GST equivalent payments.
- 8.2 Under the IGA, Commonwealth, State and local governments and their agencies will voluntarily comply with Commonwealth GST legislation as if they were subject to the GST legislation. This avoids the Constitutional problem created by section 114 of the Constitution which prevents the Commonwealth taxing the property of the States.
- 8.3 The State Entities Bill provides the legal authority for State and local government entities to voluntarily comply with the provisions of the GST legislation where it would otherwise not apply by authorising State and local government entities to make GST equivalent payments.
- 8.4 In the event that a State entity (which includes government departments, local governments, statutory corporations and authorities to the extent that they are exempt from GST because of section 114 of the Constitution) tries to avoid the operation of the legislation, the State Entities Bill authorises the Treasurer to issue directions concerning the payment of notional GST. This deals with the possibility that a State entity might feel that it was not in its interests to pay voluntary GST (for example, a commercial

entity might feel that paying voluntary GST was not consistent with its profit-maximising objective, if it had sufficient confidence that its activities were protected by section 114 of the Constitution).

8.5 The State Entities Bill contains four clauses. Clauses 3 and 4 are explained below. As part of its review, the Committee placed an advertisement in *The West Australian* newspaper inviting submissions on the State Entities Bill. The Committee did not receive any submissions as a result of the advertisement.

8.6 As a further part of the review, the Committee invited comment from a number of parties who it considered may wish to make a submission. The witnesses who appeared before the Committee were:

- Mr David Smith, Director, Intergovernmental Relations, WA Treasury Department;
- Ms Anne Nolan, Assistant Under Treasurer, WA Treasury Department;
- Mr Mark Altus, Director, Revenue Policy, WA Treasury Department;
- Mr Michael Barnes, Acting Assistant Director, Revenue Policy, WA Treasury Department;
- Ms Nicki Suchenia, Acting Assistant Commissioner, Policy and Legislation, State Revenue Department;
- Mr Bill Mitchell, Fair Trading Policy Advisor; and
- Mr Nick Roberts, Policy Officer, Ministry of Fair Trading.

8.7 Clause 3 of the State Entities Bill provides each State entity (which includes government departments, local governments, statutory corporations and authorities to the extent that they are exempt from GST because of section 14 of the Constitution) with the authority to voluntarily pay notional GST, and to do things that would be necessary or expedient to do if it were liable to GST. These things would include complying with GST administrative processes including registration and lodgement of returns as if the entity were subject to the GST. This measure will ensure equal tax treatment for public and private sectors.

- 8.8 Clause 4 provides the Treasurer with authority to issue directions to a State entity to make GST equivalent payments and to do anything else that it is authorized by section 3 to do.

Recommendation 2: The Committee recommends that all clauses of the *State Entities (Payments) Bill 1999* be passed.

Hon Murray Nixon JP, MLC
Chairman

Date:

APPENDIX 1

APPENDIX 1

LETTER FROM HON KENNETH TRAVERS MLC TO HON MURRAY NIXON JP MLC,
CHAIRMAN OF THE COMMITTEE DATED NOVEMBER 16 1999.



