Chapter 3

Views on specific schedules

3.1 The chapter considers the views raised by stakeholders on each of the schedules of the bill. The majority of concerns were raised in relation to the multinational anti-avoidance law and Country-by-Country reporting.

Schedule 1: Significant global entities

3.2 A number of issues were raised by stakeholders in relation to the definition of a significant global entity.

Threshold for determining a significant global entity

3.3 Some stakeholders submitted that the proposed threshold of $1 billion was too high and could be set at a lower level.[1] For example, the Tax Justice Network Australia proposed that the threshold should be lowered to $250 million, consistent with the ATO definition of a large business.[2]

3.4 In addition, Greenpeace Australia Pacific questioned whether limiting the definition of a significant global entity to $1 billion may limit the ability of the ATO to investigate multinational companies with revenues below this level.[3]

3.5 Guidance provided by the G20/OECD indicates that there should be exemptions from general filing requirements for multinational groups with annual consolidated revenue of less than €750 million or a near equivalent in domestic currency (which has been set at $1 billion for Australia). The G20/OECD considers that this revenue threshold will exclude approximately 85 to 90 per cent of multinational groups from filing requirements but will nevertheless capture those multinational groups controlling approximately 90 per cent of corporate revenues. According to the OECD:

> The prescribed exemption threshold therefore represents an appropriate balance of reporting burden and benefit to tax administrators.[4]

Exchange rate fluctuations

3.6 The Tax Institute noted that consolidated income for accounting purposes includes 100 per cent of the financial attributes (including income) of any majority-owned subsidiary. As a result, the consolidated income of a group may be inflated by the inclusion of income that is attributable to non-group owners of minority stakes. While this is consistent with accounting practice, the Tax Institute is

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1 See CPSU, *Submission 4*; Greenpeace Australia Pacific, *Submission 2*;

2 *Submission 10*, p. 1.

3 *Submission 2*, p. [3].

4 OECD/G20 Base Erosion and Profit Shifting Project, *Action 13: Guidance on the Implementation of Transfer Pricing Documentation and Country-by-Country Reporting*, 2015.

concerned that this treatment will capture more groups than would be the case if only economic interests were used as the basis for determining group income.[5]

3.7 It is unclear how many additional multinational groups would be captured by either differences in thresholds arising from exchange rates or the inclusion of only economic interests in determining group income.

Total annual income

3.8 KPMG was concerned that defining a significant global entity by reference to total annual income in section 960–565 of the ITAA 1997 would introduce uncertainty as this latter term does not appear in the Australian Financial Reporting Standards and, as such, has no defined meaning itself.[6] However, section 960–570 of the ITAA 1997 refers to accounting principles and auditing principles in the preparation of 'global financial statements' from which annual global income (and, thus total annual income) is determined.

3.9 KPMG recommended that a replacement term for 'total annual income' should be adopted, such as 'consolidated revenue', which can be referenced to financial and accounting standards. Further, it was noted that additional guidance is needed for multinationals headquartered in other jurisdictions which prepare consolidated accounts using foreign accounting standards.[7]

3.10 To reduce the compliance burden on affected businesses, GSK submitted that it would be important for the ATO to publish relevant average exchange rates regularly to enable taxpayers to comply with the proposed law.[8]

Committee view

3.11 The committee is satisfied that the annual income threshold of $1 billion is an appropriate near equivalent amount in domestic currency for the purposes of defining a significant global entity. The government considers that this is an appropriate threshold as the former Treasurer, in his second reading speech, indicated:

> With over 1000 multinational entities operating in Australia with revenues greater than $1 billion globally, this means these rules will have a far-reaching effect and ensure that multinationals do not inappropriately slip through our tax net.[9]

3.12 The committee also notes that while the total population may be 1000 companies, for many companies the legislation will have no effect.[10]

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5 *Submission 12*, p. 4.

6 *Submission 3*, p. 3.

7 *Submission 3*, p. 3.

8 *Submission 11*, p. [2].

9 The Hon. Joe Hockey, *House of Representatives Hansard*, 16 September 2015, p. 10324.

10 Mr Chris Jordan, Australian Taxation Office, *Proof Committee Hansard*, Senate Economics Legislation Committee Supplementary Estimates 2015-16, p. 39.

3.13 Subject to implementation in other jurisdictions, the consolidated income for accounting purposes should continue to include 100 per cent financial attribution as is consistent with accounting practice.

3.14 The committee considers the ATO could provide further guidance in relation to how companies should calculate global annual income, including publishing relevant average exchange rates.

Schedule 2: Multinational anti-avoidance law

3.15 The multinational anti-avoidance law (MAAL) provision of the bill attracted the most comments from stakeholders. Many of the concerns raised in submissions reflected changes as a result of the exposure draft consultation process.

Scope of the multinational anti-avoidance law

3.16 Stakeholders raised a number issues in relation to the scope of the MAAL, particularly in relation to how it would interact with existing tax avoidance measures and the effect of not having a 'low or no tax jurisdiction condition'.

3.17 The Australian Financial Markets Association submitted that the legislation needs to be clearer:

> …where the foreign supplier has permanent establishment in Australia through which activities in relation to the supply are undertaken, then the proposed measures in the Bill do not apply and any determination as to the appropriateness of the income taxed in Australia is determined through existing transfer pricing rules.[11]

3.18 In response, the Commissioner of Taxation explained that:

> Part IVA [the anti-avoidance provision] is often referred to as a provision of last resort. You would seek to apply other provisions first before you would ever go to Part IVA. The MAAL, multinational anti-avoidance legislation, is an amendment to Part IVA. So generally we would not necessarily have that as the first provision that we would bring out…It is a safety net provision.[12]

3.19 The Corporate Tax Association was concerned that Australian headquartered multinationals may be inadvertently captured by the MAAL and proposed that a 'carve out' for these groups could be introduced to ensure that the MAAL does not apply.[13] However, it is unlikely that Australian headquartered multinationals would be captured by the MAAL unless they were engaging in egregious tax avoidance and would most likely be captured by other tax avoidance provisions, such as controlled foreign company rules and/or transfer pricing provisions, before the application of the MAAL would be contemplated.

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11 *Submission 6*, p. 3.

12 Mr Chris Jordan, Australian Taxation Office, *Proof Committee Hansard*, Senate Economics Legislation Committee Supplementary Estimates 2015-16, p. 40.

13 *Submission 13*, p. 2

3.20 Stakeholders were also critical that the 'low or no tax jurisdiction' condition was removed from the exposure draft of the bill. EY advised that this condition was originally inserted to address the issue of 'stateless income' and meet the intended aim of the MAAL to address the avoidance of permanent establishment. By removing the condition, however, they contended that there is the potential to introduce significant uncertainty or override double tax agreements in situations where there is little or no risk of 'stateless income'. EY also noted that submissions to the exposure draft did not advocate for its removal but recommended clarification in a definitional sense.[14]

3.21 The Australian Financial Markets Association contended that:

> …the removal of the need for the existence of an entity, without substantial activity, located in a 'low or no tax jurisdiction,' as was required in the Exposure Draft, potentially expands the ambit of the proposed measures significantly.[15]

3.22 In relation to the removal of the 'low or no tax jurisdiction condition', the Treasury indicated that:

> Through the consultation process, it became apparent that the expression 'no or low tax' caused a lot of concern—that is, people were saying, 'What if it's just a straightforward business being done in Singapore and Singapore has a tax rate of 18 per cent, would that be low tax?' Certainly compared to 30 per cent it is low but it did not really get at the issue of putting it into basically a zero-tax country. So that was dropped.[16]

3.23 Some stakeholders have noted that the removal of the condition broadened the number of companies affected from 30 to closer to 100.[17] While these companies may incur compliance costs of reviewing their arrangements to make sure they comply with the law, the Treasury considers that this change strengthens the proposed measure.[18]

Principal purpose test

3.24 A number of stakeholders expressed concerns about the introduction of a 'principal purpose' test for the MAAL which will operate alongside the existing 'sole or dominant purpose' threshold for Australia's general anti-avoidance rules.

3.25 KPMG put forward two arguments against introducing a 'principal purpose' test. First, introducing a new threshold will increase complexity and uncertainty, and interpretations of the new concept may take many years to conclusively determine.

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14 *Submission 5*, p. 3

15 *Submission 6*, p. 3.

16 Mr Rob Heferen, Department of the Treasury, *Proof Committee Hansard*, Senate Economics Legislation Committee Supplementary Estimates 2015-16, p. 39.

17 See, for example, KPMG, *Submission 3*; and, The Tax Institute, *Submission 12*.

18 Mr Rob Heferen, Department of the Treasury, *Proof Committee Hansard*, Senate Economics Legislation Committee Supplementary Estimates 2015-16, p. 39.

Second, the introduction of a new test is unnecessary to achieve the MAAL's stated aim, particularly so when foreign tax benefits will be considered.[19]

3.26 On the first point, the Australian Financial Markets Association noted that the 'precise meaning of the term lacks clarity, and particularly judicial clarity'.[20]

3.27 KPMG also put forward two arguments for adopting the new threshold. First, this threshold is currently used in some treaties and is a recommended test for Action 6 of the BEPS Action Plan (Treaty Abuse). Second, it is understood that the ATO believes that this lower threshold will make it easier for them to apply the MAAL.[21]

3.28 The CPSU indicated that its members were supportive of the introduction of a principal purpose test but cautioned that proving it may be problematic where the necessary information is kept offshore.[22]

3.29 In terms of the bill as drafted, EY submitted that section 177DA(1)(b) should have the word 'principal' inserted such that the provision reads '…or for more than one principal purpose that includes a **principal** purpose of…' (insertion in bold). This insertion would provide clarity and unambiguously achieve the result alluded to in paragraphs 3.57 and 3.61 of the Explanatory Memorandum which indicates an intention to apply the MAAL when there is a principal purpose of enabling a taxpayer to obtain a tax benefit or to obtain a tax benefit and to reduce a foreign tax liability.[23]

Interactions with double tax agreements

3.30 A number of stakeholders were particularly concerned about how the MAAL would interact with double tax agreements and treaties. For example, EY contended that the MAAL will undermine confidence in the integrity of the Australia's double tax agreements and create uncertainty for foreign investment in Australia.

3.31 The Law Council of Australia submitted that:

> …broadening of the scope of the MAAL in the CMTA [Combating Multinational Tax Avoidance] Bill and the early start for the MAAL of 1 January 2016 means that the potential for double taxation becomes even more of an issue that needs to be resolved before the measure is introduced.[24]

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19 *Submission 3*, pp. 4–5.

20 *Submission 6, p. 3.*

21 *Submission 3*, p. 5.

22 *Submission 4*, p. [2].

23 *Submission 5*, pp. 4–5.

24 *Submission 14*, p. 3.

3.32 The Tax Institute also raised the potential for double taxation where the ultimate recipient of the profits generated from sales to Australian sales is resident in another jurisdiction.[25]

3.33 Despite these concerns, no submissions to the inquiry provided any tangible examples of multinationals that would be subject to double taxation as a result of the introduction of the MAAL.

Other issues

3.34 Shell Australia was concerned that the bill did not resolve how the deemed profit of permanent establishment would be calculated where the MAAL applies. They submitted that urgent guidance was required to provide sufficient certainty for affected multinationals with imminent reporting obligations in relation to the tax risks generated by the legislation.[26]

3.35 Stakeholders also identified a number of terms and phrases in Schedule 2 that they considered required further clarification. EY contended that:

> …it is vitally important that the provisions, from the start, are drafted with as much clarity as possible and that key terms and phrases are clearly defined.[27]

3.36 The terms that stakeholders identified as ambiguous were:

- 'directly in connection';
- 'commercially dependent';
- 'reasonable commercial grounds';
- 'supply';
- 'Australian customer';
- 'attributable'; and,
- 'activities undertaken in Australia'.

Committee view

3.37 While the committee appreciates the concerns of stakeholders, it is satisfied that the provisions of the MAAL will operate in harmony with existing tax avoidance measures and will not place undue compliance burdens on the significant global entities affected. It is also satisfied that concerns about the operation of the MAAL with tax agreements and treaties will be resolved with the development of a multilateral instrument on tax treaty measures to tackle BEPS (Action 15).

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25 *Submission 12*, p. 4

26 *Submission 15*, p. 3.

27 *Submission 5*, p. 6

3.38 The committee agrees with the former Treasurer that:

> By removing the 'no-tax or low-tax' condition and relying solely on a 'principal purpose' test, we are sending a clear message that, if you deliberately and artificially avoid paying tax in Australia, this is not acceptable.[28]

3.39 In addition to providing greater guidance about the operation and implementation of the MAAL, the committee believes that the government should give consideration to more clearly defining key terms in the schedule.

Schedule 3: Scheme penalties for significant global entities

3.40 Some stakeholders were supportive of increased penalties for tax avoidance. For example, GSK Australia indicated that, in principle, it:

> …welcomes and supports the implementation of a stricter penalty regime for those taxpayers found to have contravened Australia's anti-avoidance provisions. However, increasing penalties makes it even more important that these rules are clear in their scope and application…[29]

3.41 However, the Law Council of Australia was concerned that increased penalties will have a wider application than just the MAAL. The Council noted that increased penalties will apply in relation to any successful application of an adjustment provision that results in the imposition of administrative penalties under Subdivision 284-C of Schedule 1 of the *Tax Administration Act 1953* on a significant global entity that does not have a reasonably arguable position. The Council submitted that the 100 per cent penalty in Schedule 3 of this bill should be limited to circumstances in which the MAAL applies and where the entity does not have a reasonably arguable position.[30]

Committee view

3.42 Multinational tax avoidance, particularly by large multinationals, is a very serious issue that has the potential to undermine the integrity of the tax system. As such, the committee considers that this measure to increase the penalties is appropriate for any significant global entity that does not have a reasonably arguable position.

Schedule 4: Country-by-Country reporting

3.43 Chartered Accountants Australia and New Zealand supported the proposed approach to allow administrative flexibility in the implementation of CbC reporting obligations, including the ability to adapt to changes as the new CbC reporting framework across jurisdictions evolves.[31]

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28 The Hon. Joe Hockey MP, Second Reading Speech, *House of Representatives Hansard*, 16 September 2015, p. 10324.

29 *Submission 11*, p. [2].

30 *Submission 14*, p. 5.

31 *Submission 16*, p. [3].

3.44 That said, a number of submitters indicated that strong, clear and practical guidance from the ATO is urgently required before the CbC reporting regime commences on 1 January 2016.[32]

Transitional arrangements

3.45 Some stakeholders were concerned that the Australian timeline for CbC reporting implementation may be in advance of implementation in other countries. This has the potential to create an additional administrative burden for Australian entities.[33]

3.46 Deloitte raised concerns about the transitional arrangements for the implementation of CbC reporting in circumstances where the information is not yet required to be gathered and collated by the parent entity. In its opinion, such circumstances may impose onerous obligations for an Australian subsidiary to comply with filing requirements.[34]

Exemptions

3.47 Stakeholders argued for a variety of exemptions to CbC reporting requirements.

3.48 The Tax Institute highlighted that fluctuations in exchange rates may trigger reporting requirements in Australia for some companies with annual revenue levels near the threshold that are not required to report in their home jurisdiction. In such circumstances, the Australian subsidiary may not have sufficient information to meet the reporting obligations (particularly in relation to a 'master file'). The Tax Institute called for further clarity around exemptions, either specifically in the bill or through guidance provided by the Commissioner at the time of enactment.[35]

3.49 Some stakeholders argued for an exemption to CbC reporting requirements for large domestic groups with small cross-border activities and large multinationals with very small Australian operations through a *de minimis* rule. KPMG recommended consideration of a threshold set at 0.2 per cent of total annual income for both an inbound and an outbound *de minimis* rule.[36]

3.50 The Tax Institute submitted that:

> Whilst there is scope for the Commissioner to administratively not seek information, a *de minimis* exemption would minimise compliance costs for both the ATO and the relevant taxpayers, and increase certainty in the law…[37]

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32 See, for example, Chartered Accountants Australia and New Zealand, *Submission ?*; The Tax Institute, *Submission 11*; and, Deloitte, *Submission 8*;

33 See, for example, Shell Australia, *Submission 15*; and, Deloitte, *Submission 3*.

34 *Submission 8*, p. 2.

35 *Submission 12*, p. 5.

36 *Submission 3*, p. 3.

37 *Submission 12*, p. 5.

3.51 Other stakeholders proposed that existing transfer pricing rules be better aligned with CbC reporting requirements to reduce the compliance burden. GSK Australia proposed exempting companies that have a valid Advanced Pricing Agreement (APA) from, at the very least, the provision of a local file.[38] The Corporate Tax Association proposed that current transfer pricing requirements should be considered local files for the purposes of the statements required for CbC reporting.[39]

Country-by-Country reports should be publicly released

3.52 A number of stakeholders sought to make the information contained in CbC reports publicly available as this would increase transparency and facilitate greater scrutiny of tax affairs.[40]

3.53 The Tax Justice Network Australia strongly argued for the public release of CbC reports as:

> Making the country-by-country reports public would ensure that more sets of eyes, across different stakeholder groups, could help digest the mass of data filed by companies and flag any indicators of risk to appropriate tax authorities…
>
> It is also important that the data from country-by-country reports should be made available for analysis and research purposes…Tax returns of individuals and legal entities are already made available for research purposes by tax authorities in a number of countries subject to protections.[41]

3.54 Other stakeholders did not share the view that CbC reports should be made public. For example, Chartered Accountants Australia and New Zealand submitted that:

> …a measured and considered approach to any public disclosures relating to CbC reporting is warranted. Although we appreciate and accept the need for increased transparency, it is crucial that multinational groups can be confident that sensitive business information will not be disclosed publicly.[42]

Committee view

3.55 The committee is comfortable that the proposed CbC reporting requirements are consistent with those outlined in the G20/OECD BEPS Action Plan. Indeed, the committee considers that these provisions underscore the important lead role that Australia can play in implementing the G20/OECD work.

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38 *Submission 11*, p. [2].

39 *Submission 13*, p. 5

40 See, for example, Greenpeace Australia Pacific, *Submission 2*; and, Tax Justice Network Australia, *Submission 10*.

41 *Submission 10*, pp. 2–4.

42 *Submission 16*, p. [4].

3.56 That said, the committee recognises the issues raised by stakeholders and believes that the ATO should work with affected businesses to provide clarity and guidance through the implementation period and as CbC reporting is adopted by other countries. Such guidance should address concerns around transitional arrangements and exemptions. While some multinationals may be required to file in Australia that are not required to file overseas due to fluctuations in exchange rates, the committee notes that the Commissioner can provide an exemption from reporting requirements and expects that guidance will be provided as part of the implementation process.

3.57 Consistent with the principle that tax affairs should remain confidential, the committee does not believe that CbC reports should be made publicly available.

Recommendation 2

3.58 The committee recommends that the Senate should pass the bill.

Senator Sean Edwards
Chair