Coalition Members' Dissenting Report

Recommendation: That the Bill not be passed.

Liberal Members of the House Standing Committee on Economics were not afforded the opportunity to have a public hearing into this legislation. This was a Committee decision that Coalition committee members disagreed with.

15 submissions were received by the inquiry into this legislation, with many critical of the content of this Bill. Most notably absent from these was that of Treasury.

However, we note that today (12 March 2013), an undated electronic submission had been uploaded from Treasury and has subsequently been published on the Committee's website, apparently in response to enquiries from the Committee.

Coalition members of the Committee view this to be highly unsatisfactory.

Coalition Members of the Committee find it difficult to support the passage of this Bill without having been afforded the opportunity to question the assumptions underlying the Government's policy intent and to address many of the issues raised from submissions to the Committee. These issues include but are not limited to:

- Questions around the financial impact of this Bill and specifically how it applies to Schedule 1, Part IVA of the *Income Tax Assessment Act 1936*. The Explanatory Memorandum to the Bill states that schedule 1 is expected "to prevent the loss of over a $1 billion a year" but little detail has been provided as to how this amount has been quantified. Also, it would have been prudent to confirm whether there was any financial impact from the changes put forward in Schedule 2 of the Bill relating to the modernisation of the transfer pricing rules , despite the EM stating that the impact would be nil.

Schedule 1 Part IVA:

- There are legitimate concerns that the drafting of the schedule may have been an over-reaction and would have greatly benefited from a public hearing.
- In responding to a number of court cases the Commissioner of Taxation has lost when applying Part IVA in recent times, there is a real risk that the Government, via these amendments, has over-reacted and given the Commissioner too much power to raise tax and penalties in the context of alleged income tax avoidance. This is a position held by several submissions including from The Tax Institute, the Corporate Tax Association (CTA), and the Law Council of Australia (LCA) – that the failures of the current GAAR or Part IVA may have been more to do with the ATO's poor case selection or management, or extending it to situations where the rule was not intended to apply.
- It is important to be certain that an over- reach has not occurred and that these proposed amendments do not have give the ATO Part IVA unintended powers that could cause unintended consequences such as excessive compliance costs and uncertainty which would be damaging to investor confidence.
- The amendments as introduced risk tipping the balance the other way. They are worthy of further consultation and testing, in order to avoid circumstances where either:
  - ⇒ Part IVA should not apply and it does as a result of the amendments; or
  - ⇒ when it does apply, that the ATO reconstruction (of a reasonable alternative postulate) may not be fair and realistic, leading to excessive additional tax and penalties.
- If the ATO's reconstructed alternative is not what a taxpayer focused after tax return would ever have undertaken or even contemplated – as it lacks common sense or commercial reality/judgment – then the tax difference which arises is arguably excessive and unfair.
- The amendments apply to schemes entered into, or commenced to be carried out, on or after 16 November 2012, the day on which draft legislation was released for public comment. Given that the legislative amendments as introduced are significantly different to those proposed by the Minister at the time, it is reasonable to argue that this Bill will have a retrospective effect from 16 November 2012, as taxpayers could not have known the proposed legislative landscape at the time.

Modernisation of Transfer Pricing:

Australia's transfer pricing legislation has rarely been amended, and largely stood the test of time.

Given the Government's moves to block hearings by the House Standing Committee on Economics into this Bill, we are concerned that the design and drafting of the schedule may have been rushed and requires further testing (ie consultation and scrutiny) before it is passed to ensure that it is both robust and workable, and will stand the test of time. This is a position held by many submissions including from the Corporate Tax Association (CTA), PricewaterhouseCoopers (PwC), KPMG and The Tax Institute of Australia (TIA).

For example, on page 7 of its submission to the House Standing Committee on Economics's inquiry into the Bill, the TIA said that:

> "*… we are concerned that the Bill as currently drafted will not yield many of the lauded simplicity and certainty benefits and will increase the compliance burden especially and disproportionately on small to medium enterprises*."

The schedule could benefit from further consultation and scrutiny in the following key areas:

- The de minimis or threshold at which entities need not apply these complex and compliance-costly rules, nor suffer penalties where tax errors exceed the threshold, appears to be too low relative to the revenue at risk – as submissions argue, the tax-error de minimis/threshold could be raised significantly without much of an increase in revenue risk, but with a likely large saving in complexity and compliance costs, especially at the smaller end of business.
- The documentation requirements for penalty leniency appear onerous in terms of timeframes and extent, especially for SMEs – with a greater de minimis/threshold, these concerns could be significantly and acceptably reduced.
- Retaining the time limit of 7 years (from notice of initial assessment) that the Commissioner of Taxation has to make a transfer pricing adjustment appears excessive – the Inspector General of Taxation recently recommended 4 years (see further details below), which would also align with the standard amendment period.
- The OECD guidelines/provisions have been reworded a little, rather than simply referred to, in the new legislation – as submissions argue, this rewording or use of new language could give rise to unnecessary risks, confusion and possible inconsistencies at law.

- The scope of the ATO's power to reconstruct (or annihilate) unlikely, uncommercial, transactions to arrive at the right level of tax may be excessive – it may be broader, and more commonly used, than appropriate and intended, and not used "only in exceptional circumstances" (as the OCED commentary contemplates).
- Financial impact – it is difficult to fathom how the impact of this schedule is estimated at zero extra tax dollars per year whereas the impact of Schedule 1 is expected to prevent the loss of over $1 billion per year – discussed further in Schedule 1.

Mr Steven Ciobo MP
Deputy Chair

Ms Kelly O'Dwyer MP

Mr Scott Buchholz MP