

**Questions on Notice for Roche Products Pty Ltd
("Roche Pharma Australia")**

Tax Inquiry – 1 July 2015

Senator Xenophon: Can you tell us what is charged for drugs in other countries where your respective companies operate? In other words, is the same amount being charged here as it is in other countries? Can you provide us with that comparator?

Senator MILNE: Yes: what is being paid for the same drug across those jurisdictions, and also the profit formula that is being applied — the rate of profitability return — as we asked previously.

Roche adheres to the internationally accepted principles of transfer pricing, and aims to ensure that the value of a good or service is taxed in the countries where the "value adding" activities have occurred. In this regard, Roche applies the *OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations* for cross-border transactions of goods and services and adheres to the main BEPS (Base Erosion and Profit Shifting) principle that profits should be taxed where they are generated.

The profit margins and transfer prices for Roche affiliates around the world are determined according to the "arm's length" principle, taking into account the risks, investment and functions performed of the local operation; and local benchmarks, including the profit margins of companies performing similar activities (e.g. medicines distributors) in the same market. Differences in either of these factors, as well as any specific local requirements especially local market regulations imposed by the respective healthcare authorities and local legislation, must be taken into account when comparing transfer prices and margins around the world.

Under the terms of our Advance Pricing Agreement (APA), Roche's Pharma Australia's transfer pricing methodology has been thoroughly reviewed by the Australian Tax Office (ATO) and accepted as reasonable and fair and we adhere to a defined target profit.

Roche has conducted a comparison of the affiliate Roche Australia with similar Roche affiliates in highly-developed markets on the basis of revenues, cost of goods sold (COGS) and gross profit in local currency. This allows consideration of the average transfer prices of drugs across countries, taking into account differences in exchange rates and variations between product margins. Markets compared were: Germany, Spain, the United Kingdom, Italy and South Korea.

In 2014, Roche Pharma Australia's gross profit margin (revenue less COGS (transfer prices), as a percentage of revenue) was 28.5%. By comparison Roche affiliates in the other highly-developed countries' profit margins ranged from 16.6% to 26.5%. As Roche Pharma Australia's gross profit margin is in line with, or higher than, other distributor Roche affiliates it shows that Roche Pharma Australia's transfer prices, as agreed with the ATO through our APA are in line with, or even lower than, other distributor Roche affiliates in highly-developed markets.

As per the terms of our APA, Roche Australia's profitability has been assessed with respect to our local operations and risks, and assessed as fair and appropriate by the ATO.

Senator Xenophon: It was a decision made by the Administrative Appeals Tribunal. Did you end up paying less or more tax as a result of that court case?

Roche was involved in a case before the Administrative Appeals Tribunal (AAT) regarding transfer pricing that was resolved in 2008. The dispute was about the complex matter of balancing the relevant factors in a determination of arm's length pricing. There was no question of avoidance or inappropriate practices. The AAT found a range of possible outcomes that could reflect "fair" pricing.

In general, the AAT confirmed Roche's appropriate behaviour in this matter. In some instances, the AAT found that Roche had a higher taxable income than originally reported but in most cases this was also lower than the amount on which the Australian Tax Office (ATO) had sought to impose tax. There was a reduction in the overall transfer pricing adjustment for Roche for the period under review.

Few cases have provided specific guidance on the determination of arm's length pricing for the operation of the transfer pricing provisions (whether under the former or the new provisions). This case provided important guidance to the ATO, Roche and other taxpayers. The most important factor is that the legacy of the case has been the clarification of key issues about arm's length pricing and agreements with the ATO going forward. Specifically, as a result of the case, Roche was able to enter into an APA with the ATO. This gives the ATO and Roche certainty and ensures that Roche is assessed as paying the appropriate amount of tax in Australia.