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Mr Tim Bryant
The Secretary
Senate Economics Legislation Committee
PO Box 6100
Parliament House
CANBERRA ACT 2600

Via email to: economics.sen@aph.gov.au

Dear Mr Bryant,

We refer to your correspondence dated 21 June 2011 inviting Moore Stephens to make a written submission to the Senate Economics Legislation Committee in relation to draft Subdivision 815-A of the Income Tax Assessment Act 1997. We are grateful for the opportunity to provide comment on the draft legislation and comment briefly below on a number of the key concerns that we have in relation to Subdivision 815-A.

1. **Proposed retrospectivity to 1 July, 2004**

We are most concerned at the retrospective nature of Subdivision 815-A and believe that there is absolutely no acceptable basis whatsoever for the proposed law to apply from 1 July, 2004. Our reasons for this are well canvassed in our firm's submission to Treasury dated 29 November, 2011; however, several further observations are warranted, they include:

We are exceptionally concerned at the likely adverse impact on the reputational damage to the Australian Taxation Office (ATO) (and Australia, as an investment destination) that can be expected to follow in the event that the legislation is back-dated as planned.

The principle of good government is that the 'rule of law' operates in a transparent, established and known manner. Whilst Treasury and Government must be responsible for retrospective nature of the proposed legislation, there is commentary that the ATO has endorsed this approach and appears to have agitated for it. The ATO is at the forefront of **stating** the importance of openness, transparency, a commitment to a strong working relationship with taxpayers etc. If this is to be believed, the ATO must 'walk the talk'. The proposed amendment, some say, is a response to the ATO's poorly run transfer pricing disputes and an attempt to 'cover-up' this with retrospective legislation. We suggest that this is unacceptable.

It is noteworthy too that the Explanatory Memorandum accompanying the draft legislation states that Subdivision 815-A will have "...no revenue impact as it is a revenue protective measure." As tax professionals, we know this statement to be incorrect. Indeed, if it were correct, why on earth does the legislation need to be retrospective in nature? If, as we believe, the statement is proven false in the future, the adverse impact upon trust that Corporate Australia has in Treasury and the ATO is readily apparent; clearly, this position is to be avoided.

In addition, the suggestion that there is no revenue impact does not reconcile with the written explanation of the Bill to the Parliament wherein the comment is made: "There is a reasonable expectation that there will be additions to the revenue..." arising from the legislation.

It is also instructive to note that in discussions before the Senate Economics Legislation Committee, Hansard records of 30 May, 2012 note that Senator Cormann commented, in response to a comment from a Treasury official:

> "Let me get this right: these new laws, which seek to stop shifting profits offshore, will not apply to trade and investment through tax havens, which will effectively receive ***preferential tax treatment*** in Australia."[My emphasis]

Division 13 applies to Treaty and non-Treaty countries alike whereas Division 815 presently applies only to Treaty countries.[1] In the absence of further amending legislation (which I expect is imminent) this is not only curious and complex but arguably contrary to Australia's Treaties. Our Treaties include a non-discrimination article which provides inter alia that:

> "Nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith, which is more burdensome than the taxation and connected requirements to which nationals of that other State in the same circumstances...are or maybe subjected."[2]

This begs the question whether the retrospective nature of the legislation has any legal effect whatsoever. If it's the case, as Treasury has stated, that Subdivision 815-A will apply prospectively to taxpayers from non-Treaty countries, the logical finding would appear to be, if and when challenged in the Courts, that the new provisions may only apply prospectively to taxpayers from Treaty countries. Clearly grounds are potentially being laid down in the draft legislation for taxpayer disputes to clarify this element of the law.

If one assumes that the retrospective nature of the law has its desired effect, a critical issue all Treaty based taxpayers with international related party transactions will need to consider is what do they need to do, if anything, to attend to their "potential" taxation obligations of the past? This will involve a review of the pricing of their international related party transactions **and** profitability and a consideration of two versions of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (OECD Guidelines), along with other legislated/prescribed material. In addition, do those taxpayers that have been the subject of an ATO transfer pricing record review or audit need to do anything or will the ATO accept that they have been reviewed and their pricing and operating performance of the past accepted? Whilst the Explanatory Memorandum deals with this in part in stating that settled cases

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[1] Refer Hansard Senate Economics Legislation Committee of 30 May, 2012 (Page 97) where in response to a question as to the differing tax treatment of Division 815 as between Treaty and non-Treaty countries Treasury responded, rather "cutely": "....parliament clearly intended that the treaty rules would operate to supplement the other rules in domestic law. So in clarifying that the new law operated as intended, that the treaty rules have been incorporated into the domestic law, *is only relevant to treaty countries.*"

[2] Refer for example to Article 24 of the New Zealand Treaty and Article 26 of the Japan Treaty

"...would generally be prevented by the terms of the settlement deed...." from being reopened, this is far from 'conclusive' insofar as the inclusion of the word "generally" in the sentence makes it almost meaningless. It is all very well for our Commissioner of Taxation, Mr Michael D'Ascenzo, when questioned about the retrospective nature of the legislation before the Senate Economics Legislation Committee to say:

> *"When we talk about the retrospective application of these laws, we do not see it as if all of a sudden the ATO will be using new laws to go back. It was really a method of maintaining the status quo."*[3]

Regrettably, once again, this comment leaves much to be desired and, if correct, why is the Government not simply amending the law on a prospective basis?

2. ATO Determinations under Subdivision 815-30(3)

In making a "determination" under Subdivision 815-A the ATO is called upon to identify the particular assessable income, deductions or capital gain or loss to which the determination relates **"...unless it is not possible or practicable for the Commissioner so to do."**[4] We submit that this failure to require the Commissioner to identify the underlying income, deductions, capital gain or loss is an abject failure of the legislation as without understanding the technical basis for the amendment, how would it be possible for a taxpayer to seek relief from double taxation under the relevant Treaty?

3. Double and Multiple Taxation

The proposed legislation, as referred to above, creates a not-insignificant risk for the potential imposition of double taxation as alluded to above. The failure of the legislation to "require" the ATO to identify the counterparty and specific transactions in relation to each and every 'determination' made by the Commissioner is a grave error in legislative design.

We are aware of horrendous situations arising whereby taxpayers have been taxed on the same income in multiple countries; the failure of our Treaties to 'require' Treaty partners to come to agreement so as to avoid multiple jurisdictional taxation will only be enhanced by the proposed legislation.

One possible solution, set down in our submission to Treasury dated 29 November, 2011,is to revise all Australia's tax Treaties and include therein an appropriate 'arbitration' article along the lines as laid down in Article 25 of the OECD Model Tax Convention on Income and Capital. A real disappointment, for us, is Australia's poor track record in negotiating inclusion of an appropriate arbitration clause in recently negotiated Treaties.

4. The interaction between our thin capitalisation and transfer pricing rules

In relation to the impact of the proposed debt, debt deduction and thin capitalisation provisions within Subdivision 815, there is a very real and substantive change to the status quo. Historically there has been "...no legislative provision specifically addressing the relationship between transfer pricing and thin capitalisation rules."[5] **To suggest that the retrospective nature of this element of the legislation is in any way justified is false.** This element of the legislation should only be implemented on a prospective basis for reasons outlined above.

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[3] Hansard Senate Economics Legislation Committee 30 May, 2012 page 90
[4] Section 815-30(3)
[5] Explanatory Memorandum Page 17

5. Further Amendments to our Transfer Pricing Legislation

Taxpayers were alerted to expect amendments to Australia's transfer pricing legislation in addition to those outlined in Subdivision 815-A. We are at loss to understand why it is that over 8 months has passed since these **other amendments** were foreshadowed and yet to date there has been no communication as to what shape the proposed laws may take. Indeed, arguably, all the legislation dealing with reform of our transfer pricing rules should be brought down in one fell swoop if Government has any real concern for the administrative burden and costs to taxpayers of dealing with such substantive legislative change.

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Regrettably, time does not allow us to comment further on the draft legislation and we ask that this submission be read in conjunction with our submission to Treasury dated 29 November, 2011. In this regard, we particularly draw the Committee's attention to our comments on: the **Model Tax Convention- the Arbitration Option; Requirement to Retain Contemporaneous Documentation and Advance Pricing Arrangements.**

In closing, we note that when you wrote requesting a written submission from us you state that... **"Submissions are 'confidential' until the Committee releases them."** We find this statement curious and difficult to accept. We are constantly communicating with business and clients....taxpayers vitally interested and concerned at the legislative developments in question. In short, taxpayers have a vital interest in this matter and a 'right' to understand the implications of the proposed legislation and, as may be appropriate, to lobby their Senators in relation to the proposed changes. Once again, the 'rule of law' comes to mind. We submit that confidentiality should only be preserved for a reasonable time period in the interest of open discussion and debate. We submit that this time period is the equal of the time allowed to us to write this submission. We would be pleased to discuss this with you should you have any concerns; in the absence of hearing from you on this matter, our stated intentions herein are clear.

Yours sincerely

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