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Senate Economics References Committee  
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Parliament House  
Canberra ACT 2600

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By email: [economics.sen@aph.gov.au](mailto:economics.sen@aph.gov.au)

Dear Dr Dermody

**Re: Inquiry into Corporate Tax Avoidance and Minimisation**

I refer to your letter dated 27 October 2014 inviting Fortescue Metals Group Ltd (**Fortescue**) to make a submission in relation to the Senate Economics References Committee's inquiry into corporate tax avoidance and minimisation.

Fortescue welcomes the efforts of the G20 and the cooperation amongst governments around the world to improve global taxation liability transparency. In relation to Australia, Fortescue is aware of the need for tax reform and as it has been in the past, is a willing participant in this important process.

Fortescue supports the Australian government's efforts to create a fair and efficient tax system in Australia, and we look forward to engaging with the government regarding the potential reforms to Australia's tax regime.

Fortescue acknowledges and is committed to its role in contributing to the Australian community, and sees the opportunity to contribute its fair share of tax to the Australian government as a key part of this contribution.

**Background of Fortescue**

Fortescue is listed on the ASX (FMG) with a market capitalisation (as at the date of this letter) of approx. \$6.35 billion. Fortescue employs over 5,000 people, and has a very diverse shareholder base of over 66,000 shareholders, comprised of approximately 85% resident and 15% non-resident shareholders. Fortescue is a proud Australian iron ore producer that has grown from first production in 2008 to today being one of the four largest seaborne suppliers of iron ore globally, with a target annual production rate of 155 million tonnes per annum from its three operating iron ore mines. From its foundation in 2003, Fortescue has grown into a substantial company that by 31 December 2014 has paid more than \$4.5 billion in corporate income tax and royalty payments to Federal and State Governments.



Additionally, Fortescue will by the end of this year carry a balance sheet provision in relation to environmental care of more than \$1 billion, and will have granted in excess of \$1.7 billion in contracts to Aboriginal businesses and joint ventures.

### Fortescue's relationship with the Australian Taxation Office

Fortescue takes its tax obligations extremely seriously and is committed to working openly and collaboratively with the Australian Taxation Office (ATO) in relation to its tax affairs.

Fortescue has for several years now, engaged with the ATO as part of a Pre-lodgement Compliance Review (PCR) process. The purpose of the PCR process is to enable the ATO to gain an understanding of the transactions and commercial operations of Fortescue prior to lodgement of its income tax return. Additionally, the PCR process seeks to ensure engagement between Fortescue and the ATO through the early identification, assessment and evaluation of potential areas of concern. This approach of total disclosure is evidence of Fortescue's cooperative and transparent relationship with the ATO.

As part of the PCR process, the ATO shares with Fortescue their views on the key areas of tax, and also provides a risk rating on these areas. Fortescue is currently in the process of engaging with the ATO in relation to the PCR for the year ended 30 June 2014.

In respect of prior years, Fortescue has obtained clearances from the ATO confirming that Fortescue has a low risk rating in relation to its tax treatment of all identified key tax issues – an outcome Fortescue is extremely proud of.

In a recent letter dated 20 January 2014 from the Commissioner of Taxation (Commissioner) to Fortescue, the Commissioner highlighted the valuable contribution of Fortescue's tax team as part of the PCR and other review processes, and felt it necessary to commend the team on their willingness to participate in the tax review process and engage cooperatively with the ATO across all taxes to ensure a good working relationship.

In addition, and other than its participation in the PCR process, there are no "open" audits, reviews or issues currently being considered by the ATO.

### Fortescue's Effective Tax Rate

The table below summarises Fortescue's effective company tax rate for the income years ended 30 June 2012 to 30 June 2014.

Item	30 June 2014 *US\$m	30 June 2013 *US\$m	30 June 2012 *US\$m
Profit before income tax	3,913	2,466	2,263
Tax payable at the Australian tax rate (30%)	1,174	740	679
Research and development	9	(20)	(9)
Foreign exchange	(11)	9	1
Tax impact of overseas jurisdiction	(9)	-	-
Other	10	(9)	33
Income tax expense	1,173	720	704
Effective tax rate	29.98%	29.20%	31.11%

\*Fortescue has a US\$ functional currency for income tax purposes.



Due to the relative straightforward nature of Fortescue's business, the fact that Fortescue's operations are almost entirely in Australia, and Fortescue's attitude towards tax risk, Fortescue consistently has an effective tax rate of approximately 30%.

For completeness, we note the minor permanent tax adjustments (which are routine in nature) to Fortescue's accounting profit relate to:

- the Research & Development Tax Incentive;
- the foreign exchange implications associated with dealing with foreign customers;
- the tax implications of the operation of foreign subsidiaries; and
- other items such as share-based payments (which relate to Fortescue's employee incentive plans) and minor adjustments.

Fortescue's robust in-house tax team is committed to complying with all relevant Australian and global tax laws and are supplemented with external support from tax advisors where required. In addition, Fortescue has implemented a Tax Risk Management Policy (TRMP) which ensures all tax matters are addressed in a coherent and considered manner, with appropriate personnel (including the Board) involved where appropriate.

The above clearly illustrates the nature of Fortescue's proud attitude to pay their fair share of tax.

### **Corporate Social Responsibility**

Fortescue aspires to be a good corporate citizen and believes in empowering communities, providing economic opportunity and behaving with respect and care for people and the environment. Fortescue is committed to clearly articulating its ethical business principles and practices and implementing sound systems of corporate governance.

In this regard, and consistent with Fortescue's values, Fortescue incorporates corporate social responsibility into all of its decision-making processes and transparently reports on its performance to its stakeholders. This commitment to ethical business principles and transparency is aligned to Fortescue's attitude towards its tax obligations.

As outlined by Fortescue Chairman Andrew Forrest in Fortescue's 2014 Annual Report, Fortescue makes a significant contribution to the Australian economy and broader community through the billions of dollars it pays to State and Federal Governments in taxes and royalties.

*"It is these contributions that allow Fortescue's success to be shared across the cities and towns that make up this great nation of 23 million people. Fortescue plays significant roles in supporting local communities, who have taken our friendship to their hearts and welcomes us onto their land. More than just a mining company, we are a totally involved member of the communities in which we operate. In 11 short years, we have built a major business that is changing lives at home and abroad." – Andrew Forrest, Fortescue Chairman*

As outlined above, at 31 December 2014 Fortescue has paid more than \$4.5 billion in corporate income tax and royalty payments to Federal and State Governments. In the year ended 30 June 2014 alone, Fortescue paid approximately \$790 million in income tax with an additional \$717 million in royalties to the Western Australian State Government's Royalties for Regions program which reinvests 25 per cent of those royalties into projects that help build regional communities, including healthcare and education. As a direct consequence, as at 30



June 2014, Fortescue had \$539 million in available franking credits representing tax paid by Fortescue which has not yet been returned to shareholders via franked dividends.

It is important to note that Fortescue has also invested over \$20 billion in capital expenditure which represents its commitment to contributing to the broader community and its stakeholders. This is a significant contribution and one which Fortescue is proud of.

In addition to the payment of income (and other) taxes and royalties, Fortescue invests significantly in the community as part of its corporate social responsibilities. Some of our most valued contributions to the community include:

- Aboriginal engagement and employment, including Fortescue's Vocational Training and Employment Centres;
- Aboriginal business development;
- Providing support for, and partnering with, not-for-profit organisations and community groups; and
- Environment initiatives with a focus on environmental management systems, water management and land rehabilitation.

Fortescue is proud of its ongoing contribution to the Australian community and the way in which it interacts with Government, other corporates and the community at large.

### Global presence and structuring

Fortescue's operations are predominantly based in Australia and as a result, its revenue is primarily derived from Australian sources – this is evident through Fortescue's consistent effective tax rate of 30%. Relevantly, Fortescue does not engage in aggressive strategies to minimise its tax exposure in Australia (or overseas) and does not use tax havens to reduce its Australian or global tax liabilities.

As disclosed in Fortescue's Annual Report for the year ended 30 June 2014, Fortescue has eight foreign subsidiaries which operate commercial businesses in their respective jurisdictions (with the exclusion of the dormant entities). The table below outlines the details of the companies in each of the relevant jurisdictions. It is important to note, the total amount of capital invested in these foreign subsidiaries is less than 1% of Fortescue's share capital and is therefore immaterial in nature.

Jurisdiction	Number of subsidiaries	Fortescue ownership	Description
New Zealand	1	100%	Dormant
United States of America (USA)	1	100%	Financing entity for Fortescue's US borrowings as required by US bond holders
Singapore	3	100%	Shipping and sales related activities
Hong Kong	1	88%	Holding company in respect of Fortescue's Australian Iron Bridge magnetite iron ore project (currently under development)
Mozambique	1	100%	Dormant
Guernsey	1	100%	Global insurance company "captive insurer"

All of the abovementioned entities were set up and continue to operate purely for commercial purposes, some of which are outlined in further detail below.



## *US*

As requested by Fortescue's US bondholders, and as is common for US bond/note types of financing arrangements, Fortescue established its US subsidiary to issue US bonds/notes.

## *Singapore*

Given its proximity to Fortescue's Asian customers, Fortescue undertakes limited shipping related activities in Singapore, and has contracted with 3<sup>rd</sup> parties for the construction of ships to be used for transportation of iron ore. Any such income derived by Fortescue's Singaporean operations is attributed back to Fortescue Australia (under the Controlled Foreign Company (CFC) provisions) and taxed at the Australian corporate tax rate of 30%.

## *Hong Kong*

Fortescue's holding company for its Australian Iron Bridge magnetite project was incorporated in Hong Kong. This is purely a holding company.

## *Guernsey*

Fortescue's captive insurer is located in Guernsey as this is a very common jurisdiction for captive insurers due to the lower cost of insurance.

Non-resident captive insurers are generally deemed to have a taxable income equal to 10% of gross premiums received or receivable in respect of its Australian business, and therefore the captive insurer pays 3% Australian tax on its gross premiums. Further, all income derived by the captive insurer is subsequently attributed back to Fortescue Australia (under the CFC provisions) and taxed at the Australian corporate tax rate of 30% (less the 3% Australian tax on gross premiums).

We note that the ATO have confirmed as part of the PCR process that Fortescue has a low risk rating in relation to CFCs and attributable income.

## **Tax Reform**

It has been highlighted in the media that there is a clear need for tax reform globally. This is particularly relevant in Australia given the increasing Budget deficit over the forward estimates.

In Fortescue's opinion, it would be harsh, unfair and distortionary to impose upon one sector or industry (i.e. the resources sector) a disproportionate tax cost. The recent fall in the iron ore price supports the proposition that the iron ore market is volatile and the risk / reward dynamic is balanced.

As an Australian company competing with multinational organisations within the resources sector, Fortescue's ability to compete is in part dictated by the competitiveness of the Australian tax regime. The current focus on Base Erosion and Profit Shifting (BEPS) is a clear example that companies who seek to adopt aggressive tax avoidance and minimisation practices can lead to such companies having a competitive advantage over say Australian domestic companies. As a result, it is important for industry to contribute, and Fortescue supports (and is a willing participant), in an informed and substantial tax reform debate.

## **Conclusion**

Fortescue is proud of its transparent, low risk tax profile and it sees its obligation to paying its fair share of tax as an important part of its contribution to the Australian community. Fortescue will continue to engage cooperatively with the ATO across all taxes to ensure its excellent working relationship is maintained and enhanced.

In closing, Fortescue supports the Australian government's efforts to create a fair and efficient tax system in Australia and globally, and we very much welcome any opportunity to engage with the government regarding considered meaningful reforms to Australia's tax regime.

*Yours sincerely*

**Neville Power**  
Chief Executive Officer