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16 July 2015

Committee Secretary
Senate Economics References Committee
PO Box 6100
Parliament House
Canberra ACT 2600

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

Dear Secretary,

RE: Inquiry into Corporate Tax Avoidance

Thank you again for providing Pfizer Australia with the opportunity to participate in the Senate Economics References Committee's ("the Committee") *Inquiry into Corporate Tax Avoidance.*

I write in reference to your correspondence dated 2 July 2015, which seeks additional information from Pfizer Australia following our appearance at the public hearing on 1 July 2015.

As requested, please find attached for your consideration:

(1) Pfizer Australia's proposed corrections to the Hansard transcript of evidence (which address typographical and transcription errors exclusively)

(2) Pfizer Australia's responses to questions taken on notice during the public hearing

(3) Clarification of evidence provided by Pfizer Australia at the public hearing

(4) Pfizer Australia Holdings' Annual Financial Reports for the years 2005-2014.

We trust this information assists the Committee with its inquiry.

Yours sincerely,

David Gallagher
Chairman & Managing Director

Gennie Small
~~Finance~~ Director Australia & New Zealand

ATTACHMENT 2

Responses to Questions on Notice

Question #1

Hansard Excerpt:

> **(Page 8)**
>
> **Senator EDWARDS:** How about you provide us with an indication of how your companies are held—who the shareholders are and where you believe the tax is paid? You do not have that in your submission. But otherwise you are going to try and educate four senators as to how you are structured. We can look at that afterwards; we still have the other witnesses here.
>
> **Mr Gallagher:** We will do that and take it on notice.

Answer:

One Australian incorporated company in the Pfizer group is wholly-owned by Pfizer PFE Australia Holdings B.V. (a Netherlands company). The rest of Pfizer's Australian group are owned by the same shareholders as listed below who hold the same shareholding rights in the proportions listed below:

- Pfizer Global Holdings B.V. – Netherlands based (45% ownership)
- Pfizer Australia Holdings B.V. – Netherlands based (45% ownership)*
- Pfizer Shareholdings Intermediate SARL – Luxembourg based (10% ownership)

The only income any of these shareholders receive from Pfizer's Australian group is in the form of dividends, which are distributed from profits that have already been subject to taxation in Australia at the corporate tax rate of 30% (i.e., they have been "fully franked"). Therefore, there is no additional Australian tax payable on the distributed dividends.

** NB: this is a different entity to Pfizer Australia Holdings Pty Ltd, which is one of the Australian-incorporated companies.*

Question #2

Hansard Excerpt:

> **(Page 11)**
>
> **Senator MILNE:** Now I want to come back to any ASIC exemptions you might have in terms of your financial reporting. One of the frustrations is that people cannot get hold of your full annual financial reports for the past 10 years. Can you tell me, in each case, whether you have an ASIC exemption so that you only have to provide consolidated financial reports? If that is the case, would you now provide on notice to the committee the past 10 years of annual financial reports so we can actually have a look at this? I would like to know in the three cases whether you have any ASIC exemption because the structure of ownership does not force you to make the same level of disclosure in Australia that other corporations do.
>
> **Mr George:** We have an asset (sic) [ASIC] class order that allows us to prepare consolidated accounts for the local entity, so we only prepare one set of accounts for Pfizer Australia Holdings, and that includes its operating subsidiaries.
>
> **Senator MILNE:** My point is that, in order for people to have a really good look at this, we would like to have more information than that. Are you prepared to take that on notice, please?

Answer:

The audited financial reports of Pfizer's Australian group are publicly available (and have been at all relevant times) and we hereby attach (Attachment 4) the audited annual financial reports for Pfizer Australia Holdings Pty Ltd ("PAHPL") for each of the 10 years from 2005-2014, which are the reports referred to in the transcripts.

Note that these audited financial reports are prepared on a consolidated basis under the ASIC Class Order.

Question #3

Hansard Excerpt:

> **(Page 15)**
>
> **Senator XENOPHON:** Could you take on notice how much Pfizer pays for drugs in other countries, compared to what Pfizer pays for drugs in this country.
>
> **Mr Gallagher:** I will take it on notice.

Answer:

The information sought by the Inquiry in this question is highly competitively sensitive information. It is difficult for Pfizer to provide such information which, consistent with its obligations under competition laws, it does not disclose to the public or competitors.

Further, we note that at the hearing on 1 July, Mr. Konza, Deputy Commissioner from the ATO confirmed that one would not compare "what the companies pay for the same product in other jurisdictions compared to what they are transferring it into this country for…..because they are not independent transactions either. Also, a distributor-marketer in America has completely different market conditions to a distributor-marketer in Australia, so getting a price on an American distributor-marketer is very little help in pricing the transaction here" (refer page 55 of the Senate Transcript)

Pfizer Australia's transfer pricing policies, procedures and outcomes are in compliance with the OECD arm's length principles, as well as Australian transfer pricing regulations.

Every year, Pfizer Australia engages a major accounting firm (Deloitte) to review its transfer pricing. Specifically, Deloitte's review assesses whether Pfizer Australia would derive the same operating margins by sourcing products from external third parties as it does by sourcing products from Pfizer Inc. affiliates. Deloitte has concluded that Pfizer Australia does derive appropriate arm's length operating margins. Pfizer Australia's average operating margin for the five years up to and including 2014 was 5.46% and this sits well above the median of the operating margins of other uncontrolled (i.e. non-global parent) companies with similar operations and undertaking similar risks. Pfizer Australia therefore believes the pricing of the products purchased from Pfizer affiliates is consistent with pricing conducted with third parties on arm's length terms.

Question #4

Hansard Excerpt:

> **(Page 23)**
>
> **Senator XENOPHON:** No, it was not written down. The product development rights were written down by $161 million, but investments in the subsidiaries were written down by $591 million.
>
> **CHAIR:** They are your figures, from your documents. You can take them on notice, Mr George. They are your own figures

Answer:

The write down of Investments in Subsidiaries and write down of Developed Products Rights were unrelated transactions that were in different companies and occurred almost four years apart and are explained as follows:

2011 – Investments in Subsidiaries

In 2011, various Australian subsidiaries of PAHPL paid dividends (distributed from after tax profits) of $593 million to PAHPL. The resultant decline in the value of these subsidiaries, due to their reduced cash balances, meant that PAHPL was required by Australian accounting standards to write down its investment in its subsidiaries by $591 million.

The 2011 accounts were audited and signed off by KPMG, verifying that PAHPL's accounting treatment followed Australian accounting standards.

Further, and importantly, PAHPL received no Australian tax benefit from either the payment of the dividend or the write down of its investment in its subsidiaries. These transactions were disregarded for tax purposes as they were between members of the same tax consolidated group.

2014 – Developed Products Rights

In 2014, the carrying value of Developed Product Rights held by Pfizer Australia Pty Ltd (a subsidiary of PAHPL) was decreased by $160 million. The book value of the Developed Product Rights at that time was higher than their market value and this meant the Developed Product Rights were impaired and were required under Australian accounting standards to be written down to their current market value.

The 2014 PAHPL consolidated accounts were audited and signed off by our independent auditors, KPMG, which verified that the accounting treatment of the Developed Product Rights followed Australian accounting standards. Furthermore, the market value was supported by an independent valuation of the Developed Product Rights which was performed by Deloitte.

The impairment amount of $160 million was non-deductible for taxation purposes and Pfizer Australia Pty Ltd received no Australian tax benefit from the write-down.

Question #5

Hansard Excerpt:

(Pages 23-24)

Senator XENOPHON: Again, I just want to be fair and put this to you. Mr West says that this:

… was a share-capital-stripping scheme designed to denude the Australian taxpayer.

In particular, Mr Knapp, the academic, said:

These rights probably never had any value … In my opinion, they are a vulgar artifice. They were needed to create share capital that could be returned from future cashflows without attracting tax consequences. The rights were given life to create share capital and the intangible asset likewise dies when the share capital is returned.

Mr Gallagher: We got the independent valuation.

Senator XENOPHON: It is a pretty strong assertion, and it was published. Presumably you have not taken legal proceedings against Fairfax for that. It is a very strong allegation. What do you say about that?

Mr George: If I could just answer in regard to the tax effect of that transaction, neither the creation of the developed product rights nor the impairment over those years has created any tax benefit. Although we expense them for accounts, they are not deductible for tax purposes, so we do not have a tax benefit from either the annual impairment or the $160 million write-down we took in our 2014 accounts.

Senator XENOPHON: I invite you, should you think it necessary, to elaborate on that, because they are quite damning allegations. Can you address the allegations on notice. You have addressed them in part, but I invite you to address them further if you think it is necessary to do so.

Answer:

Much of the recent media about Pfizer's financial and tax affairs, including the referenced article, contain inaccurate information and are therefore misleading. Pfizer has chosen not to respond to such articles as it's our policy not to respond to media commentary on the company's financial filings.

PAHPL (or any member of the Pfizer Australia group) did not engage in any share capital creation scheme. There was no "scheme" (as referenced in the article) and, therefore, the Part IV A provisions of the Income tax Assessment Act 1936 would not apply. Not only were the two transactions referred to in the article nearly four years apart, most importantly, no Australian tax benefit was obtained by any entity in the Pfizer Australia group.

The acquisition of the Wyeth group by Pfizer Inc. was a global transaction between two unrelated public companies. As a result of the acquisition, the Wyeth Australia group was integrated into the Pfizer Australia group shortly after the global acquisition was completed. This is a fundamental fact that the article not only fails to note, but represents a critical omission in its analysis. The purchase price paid by Pfizer Australia Pty Ltd for the Wyeth Australia group in 2011 was above the book value of its assets and the difference included intangible assets such as Developed Product Rights and goodwill. The Developed Product Rights of $427 million were independently valued by Deloitte and were reported in our 2014 financial reports that were audited and signed off by KPMG applying Australian accounting standards. The Developed Product Rights had considerable value when first recognised in the accounts following the acquisition of Wyeth and there is no basis for the assertion that they never had any value.

In 2014, Pfizer Australia Pty Ltd, in accordance with Australian accounting standards, determined that the book value of the Developed Product Rights at that time was higher than their market value, which was supported by an independent valuation conducted by Deloitte. Accordingly, Australian accounting standards required Pfizer Australia Pty Ltd to write down the carrying value of Developed Product Rights by $160 million. The decline in the market value of the Developed Product Rights arose principally as a result of PBS price reductions and generic/tender pricing impacts that were forecast to reduce future sales and, therefore, profits. These factors clearly could not be anticipated when the Developed Product Rights were initially valued and booked approximately four years earlier.

This 2014 write down (or any annual amortisation thereof) did not give rise to any tax deductions in Australia and had no favourable Australian tax impact for Pfizer Australia Pty Ltd.

ATTACHMENT 3

Clarification of Evidence Provided at the Public Hearing

Introduction

Pfizer Australia would like to clarify three items of evidence provided by Mr Gallagher during the public hearing on 1 July 2015. These clarifications are included below, with reference to the relevant Hansard excerpt.

Clarification #1

Hansard Excerpt:

> **(Page 5)**
>
> **CHAIR:** Let's not pussyfoot around this. Let's get to the nub of it. According to your figures, you have a company which has sales of $1.2 billion, you get something in the vicinity of $700 million of taxpayers' funds and yet your final tax bill was only $21 million. You are saying your taxable profit you have out of that is about $80 million?
>
> **Mr Gallagher:** After exceptional items, our taxable profit was $51 million or $52 million in 2014, of which we then paid $21 million tax, yes.

Clarification from Mr Gallagher:

I have subsequently double-checked the figure I quoted in response to Senator Dastyari's question. The correct response should have been: "Our underlying accounting profit was $51.7 million in 2014, of which we then paid $21 million tax, yes."

Clarification #2

Hansard Excerpt:

> **(Page 10)**
>
> **Senator MILNE**: And do you pay any incentives for people who dispense your drugs or sell your drugs?
>
> **Mr Gallagher:** No, we do not pay incentives to anybody to sell or dispense our drugs.
>
> **Senator MILNE:** Do you pay them any rewards? Do you give them anything?
>
> **Mr Gallagher:** No, again, under the local code of practice, which we are a signatory to, there are no gifts allowed in Australia, so we provide no gifts. I think, as one of my colleagues mentioned, we do, on occasion, support healthcare professionals to go to international conferences in order that they are exposed to the most recent data for the benefit of patients.

Clarification from Mr Gallagher:

When addressing Senator Milne's question "And do you pay incentives for people who dispense or sell your drugs", I interpreted the question as asking whether Pfizer pays incentives to pharmacists, being the people who dispense and sell Pfizer drugs. I answered: "No we do not pay incentives to anybody to sell or dispense our drugs". This is correct. The Medicines Australia Code does not allow members to pay incentives to pharmacists and Pfizer never does so. If the Senator was asking whether the remuneration of our sales representatives has an incentive component, then the answer to that question is yes.

Clarification #3

Hansard Excerpt:

> **(Page 20)**
>
> **Senator MILNE**: Has your personal remuneration been going up as the company's performance here in Australia has been going down?
>
> **Mr Gallagher:** Embarrassing though it is to admit, I have not had a pay increase in the last three years.

Clarification from Mr Gallagher:

When addressing Senator Milne’s question “Has your personal remuneration being going up as the company’s performance here in Australia has been going down?” from memory I said that “Embarrassing though it is to admit, I have not had a pay increase in the last three years”. I subsequently checked and the correct answer is that I have not had a pay increase in the last two years.