

27 April 2015

Dr Kathleen Dermody
Committee Secretary
Senate Standing Committees on Economics
PO Box 6100
Parliament House
Canberra ACT 2600

Dear Ms Dermody

Senate: Economics References Committee

Please find below the response of Apple Pty Limited (Apple Australia) to the questions taken on notice (in bold below) by Mr Tony King, Managing Director, Apple Australia, during the sitting of the Economics References Committee on 8 April 2015.

In responding to these questions of the Committee, we have referred to various sources including the financial statements lodged with ASIC by Apple Australia, disclosures made to the ATO as part of Apple Australia's income tax return and also the terms of the most recent Advance Pricing Agreement (APA) with the ATO. While Apple Australia's most recent APA renewal negotiations with the ATO were suspended last year, as Mr King noted in evidence, Apple Australia has continued to apply the same methodology as adopted in the previous APA.

In response to questions from Senator Xenophon (refer to pages 53-54 of the proof Hansard transcript) about **how much of Apple Australia's revenue went overseas**, Mr King confirmed in his evidence that the revenue from all sales was booked in Australia. Given its role as a distributor, in order to make any sales of Apple products, Apple Australia has to purchase those products it is going to distribute, and it does so from non-Australian affiliate companies. The amount paid to affiliates in relation to these purchases in the 2014 financial year was \$4,967 million. We confirm that as required by Australian law, this price paid for purchases is calculated in line with the arm's length principle.

As Senator Canavan correctly noted, there is no market price to directly benchmark these product prices. In this regard, for many years, Apple Australia has participated in the ATO's well-regarded and transparent APA program, in order to agree with the ATO on the application of arm's length principle to these international related party transactions.

As part of the APA, Apple Australia and the ATO concluded that the most appropriate method to apply the arm's length principle was a profit based method (specifically, a Transactional Net Margin Method or TNMM). This is a method which is generally recognised by the OECD and the ATO.

Under the TNMM, and as indicated by Mr King in his evidence, Apple Australia's cost of purchasing Apple products from affiliates is not computed on a product by product basis. Rather, per the APA methodology, *all international related party dealings are covered through the application of a Transactional Net Margin Method (TNMM) applied at a whole of entity level. ... The profit level indicator considered most appropriate to determine the arm's length consideration to be received by Apple Australia is the ratio of operating margin/sales.* Consistent with Mr King's evidence that revenue from all sales is recorded in the books of Apple Australia, per the APA, sales include *gross receipts derived by Apple Australia from the trade sales of finished goods, software and services.*

The application of the TNMM ensures an arm's length operating margin remuneration to Apple Australia for its distribution business in the Australian market in the context of Apple's overall global value chain.

In line with Australian and OECD guidance, this is determined having regard to the functions performed, the assets owned and the risks assumed by Apple Australia.

As Mr King noted in his evidence, a key component of this arm's length profit based method is an economic analysis which identifies independent companies with comparable functions performed, assets owned, and the risks assumed, to those undertaken by Apple Australia.

The actual cost to Apple Australia of all products purchased from foreign affiliates is computed on an aggregate basis, after taking into account the benchmarked arm's length operating margin, Apple Australia's own operating expenses and other costs, such as those paid to third party suppliers. There are no costs incurred by Apple Australia for the purposes of decreasing Apple Australia's profits or its Australian tax liability.

The description of the APA methodology is also relevant to Senator Canavan's question (refer to page 56 of the proof Hansard transcript) in relation to **how much of the price paid by an Australian customer for a digital download from iTunes is reported by Apple Australia as income to the ATO?**

Again, in response to this question it is noted that the net profit reported is not computed per product or download; rather, the whole of entity transactional net margin methodology ensures an arm's length net margin consideration for Apple Australia having regard to its activities as a whole.

As noted above, Apple Australia has confirmed to the ATO for its most recent income tax return, that for the 2014 financial year, the amount paid to non-Australian affiliates for the purchase of Apple products by Apple Australia was \$4,967 million. Apple Australia considers this amount complies with the arm's length principle.

Further, Apple Australia confirms that it remits GST for all sales made by it, including sales in relation to its iTunes and its online business. The proceeds of sale (net of GST) are fully reported in Apple Australia's assessable income.

Both Senator Milne, (refer to page 49 of proof Hansard transcript) and Senator Canavan, (refer to page 58 of proof Hansard) asked **whether Apple Australia's cost of buying goods from foreign affiliates was higher than the price paid by other countries around the world globally.**

Mr King noted in evidence that to the best of his knowledge the costs for equivalent products were consistent around the world, but agreed to provide more details. In this regard we can confirm that in other countries in Europe and the Asia Pacific region where there are Apple subsidiaries with a similar distribution business model to Apple Australia, the same methodology is adopted to determine the arm's length purchase price of products sold.

As noted before, in applying the arm's length principle, Apple would look to the functions, assets, and risks of the relevant Apple distribution entity in order to identify comparable, unrelated distribution companies operating in each relevant local market. While arm's length profit margins will vary across markets due to local market and economic factors, the approach adopted in similar markets will be comparable and therefore the cost to Apple's distribution subsidiaries of buying finished products from foreign affiliates would be broadly comparable

Also relevant to determining such an arm's length operating margin percentage (operating margin / sales) in any relevant jurisdiction, we confirm that Apple seeks to achieve broadly equivalent worldwide recommended

retail prices for its products at the time of product introduction/transition, (net of GST, VAT or similar taxes and adjusted for foreign exchange.)

Accordingly, the transfer price charged to Apple Australia for Apple products is not allocated differently than other Apple companies operating in a manner comparable to Apple Australia. Further, Apple Australia confirms the evidence Mr King provided to the Inquiry that Apple does not artificially inflate the price which Apple Australia pays to lower its profit, and therefore the corporate tax which Apple Australia pays in Australia

Finally, Senator Canavan requested (refer to page 58 proof Hansard) that Apple Australia **provide its taxable income and revenues for the last 5 years.**

The table below provides the taxable income and revenues for the last 5 years.

	FY10	FY11	FY12	FY13	FY14
Revenue	\$3,586 M	\$4,875 M	\$5,991 M	\$6,103 M	\$6,073 M
Taxable Income	\$166 M	\$125 M	\$293 M	\$240 M	\$247M

We trust these explanations are of assistance to the Committee in considering the evidence heard at the Inquiry.

Very truly yours,

Ann Rollins
Director, Government Affairs