FINANCIAL SERVICES COUNCIL

Treasury Laws Amendment (Making Multinationals Pay Their Fair Share–Integrity and Transparency) Bill 2023

Senate Economics Legislation Committee Inquiry on Government Amendments

December 2023

FSC FINANCIAL SERVICES COUNCIL

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1 About the Financial Services Council

The FSC is a peak body which sets mandatory standards and develops policy for more than 100 member companies in one of Australia's largest industry sectors, financial services.

Our full members represent Australia's retail and wholesale funds management businesses, superannuation funds, investment platforms and financial advice licensees. Our supporting members represent the professional services firms such as ICT, consulting, accounting, legal, recruitment, actuarial and research houses.

The financial services industry is responsible for investing more than $3 trillion on behalf of over 15.6 million Australians. The pool of funds under management is larger than Australia's GDP and the capitalisation of the Australian Securities Exchange, and is one of the largest pool of managed funds in the world.

The FSC's mission is to assist our members achieve the following outcomes for Australians:

- to increase their financial security and wellbeing;
- to protect their livelihoods;
- to provide them with a comfortable retirement;
- to champion integrity, ethics and social responsibility in financial services; and
- to advocate for financial literacy and inclusion.

2 Introduction

The FSC thanks the Senate Economics Legislation Committee for the opportunity to provide a submission on proposed Government amendments to the *Treasury Laws Amendment (Making Multinationals Pay Their Fair Share-Integrity and Transparency) Bill 2023* (**the Bill**) currently before the Senate.

We appreciate the engagement from the Government on amendments to Schedule 2 of the Bill (relating to interest limitation or thin capitalisation rules) to address matters identified during the inquiry held by this Committee earlier this year and subsequent consultation by Treasury. This submission provides additional comment on the Government amendments in light of our previous submissions to these processes.[1]

The FSC considers that the Government has taken into account the issues raised in our contributions and has resolved most of the technical challenges identified. We commend the Government for constructively consulting on these amendments and particularly appreciate the positive engagement with Treasury to ensure the Government's policy outcomes are achieved while minimising unintended consequences for taxpayers.

In finalising the amendments, we encourage the Committee to consider further minor refinements to the Bill. In particular, a level playing field between superannuation funds and other forms of widely held trust would be provided by expanding the exemption from the associate entity test to all widely held funds.

3 Debt deduction creation rules

The FSC previously identified a number of concerns with the proposed debt deduction creation rules in the original Bill. It contained provisions that were broadly drafted and could capture many commercially justifiable transactions, as well as having the potential for significant retrospective effect that could make compliance difficult to achieve.

We recognise that the Government amendments adopted many of the refinements recommended in prior submissions to consultation by this Committee and the Treasury, which will improve the Bill overall if approved by the Senate. These include the initial broad scope of application for the rules, which would have captured a much wider range of transactions than intended.

The proposed Government amendments will ensure the legislation is better targeted at specific nominated types of arrangement that present a greater risk of use in debt creation schemes that lack genuine commercial justification. As well as providing certainty over the types of transaction that are the focus of compliance measures, this change also limits the scope of the rules to exclude many ordinary commercial arrangements that may have otherwise been captured.

In order to further tighten application of the rules, there is benefit to the Government considering including an overarching purpose test in the legislation to allow for discretion to be exercised where legitimate arrangements inadvertently fall within the scope of the rules.

Additionally, concerns were raised about the retrospectivity of the debt deduction creation rules, considering the commencement date of 1 July 2023 and the difficulty of tracing back borrowings for arrangements made prior to the introduction of the Bill on 22 June 2023.

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[1] Available from the FSC website: https://fsc.org.au/resources/submissions

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As the amendments will defer the start date for the rules to apply for income assessments made from 1 July 2024 onwards, an opportunity will be provided for commercially justified arrangements to be restructured in a way that allows compliance to be demonstrated where applicable.

The FSC **supports** the Government amendments specifying targeted application of the debt deduction creation rules and providing for their commencement from 1 July 2024.

We further **recommend** a simple overarching purpose test be introduced to ensure that commercially justifiable transactions are excluded from the rules.

4 Application of rules to trusts and partnerships

The Government amendments address concerns the FSC held concerning the application of the third party debt test to trusts and partnerships, as well as issues with tax EBITDA calculations relating to interest deductions by Attribution Managed Investment Trusts (AMITs) and distributions from subsidiary trusts.

Regarding the third-party debt test, use of the defined term 'Australian entity' as proposed by the amendments ensures that the test is available to trusts and partnerships.

Access to interest deductions for AMITs that borrow is enabled by proposed section 820-52, which will modify the calculation of tax EBITDA to apply for AMITs that incur an interest expense. This amendment makes the EBITDA test apply to AMITs in the same way as other types of trust.

The amendments also provide for excess tax EBITDA amounts to be transferred between unit trusts. This enables more financial arrangements using subsidiary trusts while addressing concerns that a head trust would not be able to use income from subsidiary trusts for when calculating EBITDA for tax purposes.

The FSC **supports** changes to the third party debt test and tax EBITDA provisions relating to trusts and partnerships as proposed by the Government amendments.

5 Associate entity test exemption

While the FSC is supportive of the Bill providing for an exemption from the associate entity test for superannuation funds, we reiterate the view that this exemption should be extended to other widely held investment funds. We encourage the Committee to support this change and provide a level playing field between investment vehicles with similar characteristics.

As the essential features of superannuation and widely held investment funds are very alike, the rationale for exempting superannuation funds can also be applied to entities such as AMITs, Managed Investment Trusts (MITs), and Corporate Collective Investment Vehicles (CCIVs).

As outlined in our previous submission to this Committee, the specific characteristics relevant to the exemption are:

- These funds collectively have significant investments in different assets.
- They are important sources of capital investment for Australian assets, particularly infrastructure assets.
- Under current interest limitation rules, some investment funds may have a relatively large number of associate entities, potentially bringing their investments into scope of the thin capitalisation rules.
- Both superannuation and widely held investment funds are subject to a strong regulatory regime.
- Neither fund generally exercises any meaningful control over associate entities.

The potential for competitive non-neutrality between investments made by a superannuation fund compared with other widely held entities still persists without further amendment.

Current drafting has the potential to distort market outcomes for similar investments, granting additional benefits to superannuation funds over other comparative forms of investment vehicle. This could create a disincentive for these entities to invest in assets requiring significant gearing, such as housing and renewable energy projects.

We again stress that this inequity should be resolved through additional amendments prior to passage of the Bill by Parliament.

The FSC **recommends** the Bill be further amended so that the proposed exemption from the associate entity test for superannuation funds also applies to other investment funds that satisfy the existing 'widely held' test, specifically MITs, AMITs and CCIVs.