

Chapter 2

Evolution of the multinational tax framework

2.1 Over the course of this inquiry, Australia's tax framework has been progressively amended to address concerns about the level of tax being paid by multinational corporations. This chapter explores both Australia's involvement in, and implementation of, the G20 and OECD initiatives to address multinational tax avoidance globally and the unilateral measures designed to strengthen the integrity of Australia's tax system.

International initiatives to address base erosion and profit shifting

2.2 Over the last 5 years, there have been a number of significant international initiatives that have developed proposals and recommendations designed to support a collaborative approach to reduce multinational tax avoidance. The most notable of these is the OECD Base Erosion and Profit Shifting (BEPS) project.

2.3 The BEPS project represents an unparalleled effort by OECD and G20 countries to restore confidence in the international tax system. More than 60 countries worked together to deliver a comprehensive package of action items in just two years which represents the first substantial renovation of the international tax standards in almost a century.¹

2.4 The project sought to reduce opportunities for base erosion and profit shifting by multinational enterprises and ensure that profits are taxed where economic activities take place and value is created. This work was driven by a number of goals:

- to restore the trust of ordinary people in the fairness of their tax system;
- to level the playing field among businesses; and
- to provide governments with more efficient tools to ensure the effectiveness of their sovereign tax policies.²

2.5 On 5 October 2015, the final BEPS reports were released with a commitment by countries involved to the consistent implementation of agreed measures. In some areas, minimum standards were agreed to tackle specific issues where a failure to act by some countries would have created negative spill overs (including adverse impacts on competitiveness) on other countries.³ A summary of the BEPS Action Plan items and the Australian Government's response is listed at Appendix 1.

2.6 Following the release of the final report, the Treasurer commented that:

1 OECD, *Explanatory Statements*, OECD/G20 Base Erosion and Profit Shifting Project, 2015, pp. 4–5.

2 OECD, *Explanatory Statements*, OECD/G20 Base Erosion and Profit Shifting Project, 2015, p. 4.

3 OECD, *Explanatory Statements*, OECD/G20 Base Erosion and Profit Shifting Project, 2015, p. 6.

The intricate and sensitive nature of international taxation demands precise and targeted responses to policy challenges, responses that are developed with our international partners to maximise their effectiveness.⁴

2.7 The OECD emphasised the importance of countries working together to consistently implement and apply the BEPS recommendations:

...BEPS by its nature requires coordinated responses, particularly in the area of domestic law measures; it is therefore expected that they [countries] will implement their commitments, and that they will seek consistency and convergence when deciding upon the implementation of these measures.⁵

2.8 An important ongoing aspect of the BEPS project is a focus on monitoring the implementation and effectiveness of the measures adopted by individual countries as well as the impact on both compliance by taxpayers and proper implementation by tax administrators. Monitoring will consist of reports on what countries have done to implement the BEPS recommendations and also involve some form of peer review. The proposed monitoring process will also have broader benefits through reducing misunderstandings and disputes between governments, and provide better data and analysis to support an ongoing evaluation of the quantitative impact of BEPS, as well as the impact of the countermeasures developed by the project.⁶

2.9 Progress on the implementation of the BEPS recommendations has been ongoing with the *OECD Secretary-General Report to G20 Leaders* noting that:

2017 is the year of implementation: implementation of the Common Reporting Standard with the first automatic exchanges of financial information to take place in September 2017; and, implementation of the measures to address base erosion and profit shifting (BEPS), with the OECD/G20 Inclusive Framework on BEPS implementation now fully operational.

...

Looking ahead, support on implementation across all areas of the G20's tax agenda will continue. In the Inclusive Framework, technical discussions amongst its members continue, in particular on a number of important issues relating to transfer pricing, and with a growing sense of urgency among many governments for the development of policy options to be advanced in relation to taxation of the digital economy, we will publish an interim report in the first half of 2018.⁷

4 The Hon. Scott Morrison MP (Treasurer), *OECD report supports Australian Government action on multinational tax avoidance*, Media Release, 6 October 2015.

5 OECD, *Explanatory Statements*, OECD/G20 Base Erosion and Profit Shifting Project, 2015, p. 9.

6 OECD, *Explanatory Statements*, OECD/G20 Base Erosion and Profit Shifting Project, 2015, pp. 10–11.

7 Mr Angel Gurría (OECD Secretary-General), *OECD Secretary-General Report to G20 Leaders*, July 2017, pp. 5–6.

Reforms to the Australian corporate tax system to address avoidance

2.10 Since the referral of this inquiry in October 2014, the Australian Government has announced a number of significant measures to address multinational tax avoidance in four successive budgets from 2015–16 through to 2018–19. Such a continued emphasis reflects the importance to the government to address, and be seen to address, this issue which has become increasingly important to the wider community.

2.11 While there is debate as to whether some measures represent unilateral action outside the BEPS project, the Australian Government considers that all of its actions to address multinational tax avoidance are consistent with the BEPS project.

2.12 It is worth noting that many of these tax measures apply only to significant global entities, defined as either a 'global parent entity' or a member of a group of entities (consolidated for tax purposes as a single group) with an annual global income of AUD\$1 billion or more.⁸

Multinational Anti-Avoidance Law

2.13 The Multinational Anti-Avoidance Law (MAAL) is a unilateral measure that applied from 1 January 2016 to significant global entities. It is designed to counter complex, contrived and artificial schemes intended to avoid paying Australian tax. Instead of prescribing specific actions, the MAAL makes it possible for the ATO to collect tax where a foreign entity has set up a scheme to obtain a tax benefit—that is, to avoid paying tax on profit it has made in Australia.

2.14 The MAAL targets multinational entities that avoid a taxable presence by booking their revenue offshore despite undertaking significant work in Australia with direct connection to Australian sales.⁹ Penalties associated with tax avoidance schemes were also increased as part of the MAAL enabling legislation (see below).¹⁰

2.15 The MAAL is intended to encourage multinationals to restructure their operations by creating permanent tax establishments in Australia and subsequently be part of the mainstream tax system. As the Commissioner of Taxation explained:

Part IVA [the anti-avoidance provision] is often referred to as the provision of last resort. You would seek to apply other provisions first before you would ever go to Part IVA. The MAAL...is an amendment to Part IVA. So generally we would not necessarily have that as the first provision that we would bring out.

...

8 Schedule 1, *Tax Laws Amendment (Combating Multinational Tax Avoidance) Act 2015*.

9 Explanatory Memorandum, *Tax Laws Amendment (Combating Multinational Tax Avoidance) Bill 2015*, p. 20.

10 Schedule 3, *Tax Laws Amendment (Combating Multinational Tax Avoidance) Act 2015*.

It is a safety net provision.¹¹

2.16 The 2017–18 Budget proposed further strengthening of the MAAL legislation to negate attempts to use foreign trusts and partnerships in corporate structures to circumvent the MAAL. The amendments, which came into effect from 1 January 2016, when the MAAL came into effect, apply to:

- corporate structures that involve the interposition of partnerships that have any foreign resident partners;
- trusts that have any foreign resident trustees; and
- foreign trusts that temporarily have their central management and control in Australia.¹²

Diverted Profits Tax

2.17 The Diverted Profits Tax (DPT) applies from 1 July 2017 to significant global entities and is aimed at those which have arrangements with offshore related parties that lack economic substance in order to divert Australian profits to lower tax countries and avoid paying Australian tax. The DPT would apply to any scheme that is assessed to provide a tax benefit to the multinational. Under a DPT assessment, tax would be payable on the amount of diverted profits at a penalty rate of 40 per cent.¹³ Similarly to the MAAL, the DPT is a provision of last resort under Part IVA of the *Income Tax Assessment Act 1936*.

2.18 The Government considers that the DPT is consistent with the global approach to tax avoidance as it supports the OECD BEPS transfer pricing reforms by encouraging greater cooperation, and provides an additional power for the Commissioner of Taxation to address arrangements that divert profits offshore and lack economic substance. The DPT is also not in conflict with tax treaties as it is not subject to Australia's bilateral treaties because it is an anti-avoidance measure.¹⁴

GST on digital goods and services

2.19 Goods and Services Tax (GST) was announced to apply to cross border supplies of goods and services imported by consumers from 1 July 2017. This measure is intended to restore the integrity of the consumption tax regime so that GST applies to non-exempt products and services, including digital supplies purchased from overseas and from Australia. A registration threshold of A\$75 000 per annum,

11 Mr Chris Jordan, Australian Taxation Office, *Proof Committee Hansard*, Senate Economics Legislation Committee, Supplementary Estimates 2015–16, 21 October 2015, p. 57.

12 Australian Government, *Budget Paper No. 2 2017–18*, p. 39.

13 Explanatory Memorandum, *Treasury Laws Amendment (Combating Multinational Tax Avoidance) Bill 2017 and Diverted Profits Tax Bill 2017*, pp. 8–10, 101.

14 Explanatory Memorandum, *Treasury Laws Amendment (Combating Multinational Tax Avoidance) Bill 2017 and Diverted Profits Tax Bill 2017*, pp. 105–106.

equivalent to the threshold for domestic businesses, has been set for those overseas businesses that supply imported services or digital goods.¹⁵

2.20 The measure reflects Australia's early adoption of guidelines for business-to-consumer supplies of digital products being developed by the OECD as part of the BEPS project (see BEPS Action 1 in Appendix 1).

2.21 The introduction of GST on low value imported goods (valued at less than \$1000) by consumers will come into effect from 1 July 2018.¹⁶

2.22 In addition, the 2018–19 Budget announced the government's intention to ensure that offshore sellers of hotel accommodation in Australia calculate GST turnover in the same way as local sellers from 1 July 2019.¹⁷

Amendments to the transfer pricing regime

2.23 Australian transfer pricing guidelines were updated in 2017 to reflect changes to the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrators that were approved by the OECD Council on 23 May 2016.¹⁸

2.24 The amendments also introduced Country-by-Country (CbC) reporting, which requires significant global entities to provide certain information to tax authorities to assess transfer pricing risks, and, when necessary, assist in commencing and targeting audit enquiries.¹⁹ CbC reporting obligations require entities to provide each of the following statements:

- a master file providing an overview of the multinational enterprise group business, including the nature of its global business operations, its overall transfer pricing policies, and its allocation of income and economic activity;
- a local file focusing on specific transactions between the reporting entity and its associated enterprises in other countries, as well as the amounts involved in those transactions, and the entity's analysis of transfer pricing determinations it has made; and
- a CbC report containing certain information relating to the global allocation of the multinational enterprise's income and taxes paid together with certain indicators of the location of economic activity within the multinational enterprise group.²⁰

15 Schedule 1, *Tax and Superannuation Laws Amendment (2016 Measures No. 1) Act 2016*.

16 *Treasury Laws Amendment (GST Low Value Goods) Act 2017*.

17 *Budget 2018–19: Budget Paper No. 2*, p. 29.

18 Schedule 3, *Treasury Laws Amendment (Combating Multinational Tax Avoidance) Act 2017*.

19 Explanatory Memorandum, *Treasury Laws Amendment (Combating Multinational Tax Avoidance) Bill 2015*, pp. 60.

20 Explanatory Memorandum, *Treasury Laws Amendment (Combating Multinational Tax Avoidance) Bill 2015*, pp. 63.

2.25 CbC reporting statements are required to be filed within 12 months after the end of the period to which they relate.²¹ As CbC reporting requirements were introduced for income years starting on or after 1 January 2016, the first CbC reporting statements were lodged late in 2017. As of 14 March 2018, the ATO had received 42 CbC reports.²²

Stronger penalties

2.26 In addition to the measures outlined above, the Australian Government has introduced stronger penalties to ensure more economic activity is accounted for in Australia, and to encourage multinationals (and all corporate taxpayers in general) to provide relevant information to tax administrators in a timely fashion. Maximum penalties were doubled for significant global entities that enter into tax avoidance or profit shifting schemes and do not have a reasonably arguable position.²³

2.27 Increased administrative penalties are intended to encourage significant global entities to comply with their taxation obligations, including lodging tax documents on time and taking reasonable care when making statements. The increased penalties apply to all lodgements required in the approved form, which includes income tax returns, activity statements, CbC reports and general purpose financial statements. Where a significant global entity fails to lodge on time, the base penalty amount is multiplied by 500, which is 100 times larger than for a 'large entity'.²⁴ This means that the maximum administrative penalty could be up to \$525 000 for failing to lodge tax documents on time.

Relaxed transparency measures for private companies

2.28 In October 2015, the Australian Parliament changed income tax transparency laws to remove the reporting requirements for Australian-owned private companies with total annual income of more than \$100 million. Reporting requirements were retained for public companies and foreign owned companies with total annual income of more than \$100 million.²⁵ Subsequently, in November 2015, the income tax transparency laws were amended again to impose reporting requirements for Australian-owned private companies with total annual income of more than \$200 million.²⁶

21 Schedule 4, *Treasury Laws Amendment (Combating Multinational Tax Avoidance) Act 2015*.

22 Mr Mark Konza, Australian Taxation Office, *Committee Hansard*, 14 March 2018, p. 66.

23 Schedule 3, *Treasury Laws Amendment (Combating Multinational Tax Avoidance) Act 2015*.

24 Explanatory Memorandum, *Treasury Laws Amendment (Combating Multinational Tax Avoidance) Bill 2017 and Diverted Profits Tax Bill 2017*, p. 71.

25 *Tax and Superannuation Laws Amendment (Better Targeting the Income Tax Transparency Laws) Act 2015*.

26 Schedule 1 amendment to *Taxation Administration Act 1953, Treasury Laws Amendment (Combating Multinational Tax Avoidance) Act 2015*.

Voluntary Tax Transparency Code

2.29 The Voluntary Tax Transparency Code (TTC) is a set of principles and minimum standards to guide medium and large businesses on public disclosure of tax information. The TTC was developed by the Board of Taxation and endorsed by the Australian Government in the 2016–17 Budget. It is designed to encourage greater transparency within the corporate sector, particularly by multinationals, and to enhance the community's understanding of the corporate sector's compliance with Australia's tax laws.²⁷

2.30 TTC reporting requirements differ depending on the size of the business. For medium sized businesses with Australian turnover of between \$100 and \$500 million, the TTC report should contain a reconciliation of accounting profit to tax expense and to income tax paid or payable; identification of material temporary and non-temporary differences; and accounting effective company tax rates for Australian and global operations (pursuant to Australian Accounting Standards Board guidelines). In addition to content required for medium businesses, TTC reports for large businesses with Australian turnover of greater than \$500 million should contain an approach to tax strategy and governance; a tax contribution summary of corporate taxes paid; and, information about international third party related dealings.²⁸

2.31 Businesses may elect to satisfy the minimum standards of the TTC by publishing improved disclosures of tax information in their general purpose financial statements, a Taxes Paid Report or another document. There is no prescribed template or format for TTC content.²⁹

2.32 As of 9 May 2018, 56 TTC reports were available for 2015–16, 52 reports were available for 2016–17, and 26 reports were available for 2017–18.³⁰ The ATO reports that, in total, 101 corporates have published at least one report and a further 25 have signalled an intention to adopt the code by registering.³¹

27 Australian Taxation Office, *Voluntary Tax Transparency Code*, <https://www.ato.gov.au/Business/Large-business/In-detail/Tax-transparency/Voluntary-Tax-Transparency-Code/> (accessed 31 October 2017).

28 Australian Taxation Office, *Voluntary Tax Transparency Code*, <https://www.ato.gov.au/Business/Large-business/In-detail/Tax-transparency/Voluntary-Tax-Transparency-Code/> (accessed 31 October 2017).

29 Australian Taxation Office, *Voluntary Tax Transparency Code*, <https://www.ato.gov.au/Business/Large-business/In-detail/Tax-transparency/Voluntary-Tax-Transparency-Code/> (accessed 31 October 2017).

30 *Voluntary Tax Transparency Code*, <http://data.gov.au/dataset/f71709a8-2eeb-4592-ad1f-443f7f520186> (accessed 9 May 2018).

31 Mr Jeremy Hirschhorn, Australian Taxation Office, *Committee Hansard*, 14 March 2018, p. 70.

