CHARTERED ACCOUNTANTS
AUSTRALIA + NEW ZEALAND

16 June 2015

General Manager
Law Design Practice
The Treasury
Langton Crescent
PARKES ACT 2600

Email: taxlawdesign@treasury.gov.au

Dear Sir/Madam,

Tax integrity: Multinational anti-avoidance law

Chartered Accountants Australia and New Zealand welcomes the opportunity to make a submission on the exposure draft of Tax Laws Amendment (Tax Integrity Multinational Anti-avoidance Law) Bill 2015 (**ED**) and the accompanying explanatory material (**EM**).

Chartered Accountants Australia and New Zealand is made up of over 100,000 diverse, talented and financially astute professionals who utilise their skills every day to make a difference for businesses the world over. Our members are known for professional integrity, principled judgment and financial discipline, and a forward-looking approach to business. We focus on the education and lifelong learning of members, and engage in advocacy and thought leadership in areas that impact the economy and domestic and international capital markets.

We are represented on the Board of the International Federation of Accountants, and are connected globally through the 800,000-strong Global Accounting Alliance, and Chartered Accountants Worldwide, which brings together leading Institutes in Australia, England and Wales, Ireland, New Zealand, Scotland and South Africa to support and promote over 320,000 Chartered Accountants in more than 180 countries.

Introductory comments

Chartered Accountants Australia and New Zealand recognises that the Government wishes to introduce an anti-avoidance rule into the Australia tax environment to target certain schemes designed to artificially avoid the attribution of business profits to a permanent establishment in Australia. As such, we do not comment in this submission on the government's policy. Nor do we comment on what overseas countries may perceive to be the ramifications of Australia introducing the Multinational Anti-avoidance Law (**MAAL**).

Chartered Accountants Australia and New Zealand

33 Erskine Street, Sydney NSW 2000,
GPO Box 9985, Sydney NSW 2001, Australia
T +61 2 9290 1344 F +61 2 9262 4841

charteredaccountantsanz.com

Our comments are directed instead towards improving the ED and EM as, in our view, the level of uncertainty of the proposed rules as they currently stand is too high. In the absence of certain clarifications in the ED and EM identified in this submission, we believe the provisions would place a very heavy burden on taxpayers having to navigate the rules and the Australian Taxation Office (ATO) in having to administer them.

Chartered Accountants Australia and New Zealand would be pleased to assist in any planned consultation on further development and clarification of the measures in the ED.

1. Clarification of key concepts required

Chartered Accountants ANZ considers that a number of pivotal aspects of the proposed law need to be clarified in order to enable taxpayer self-assessment and indeed for the ATO to administer the law for 1 January 2016 commencement. Our view is that these aspects ought to be addressed in the final legislation and explanatory material to the extent possible for consideration by the Parliament rather than being the subject of ATO interpretative advice at a later stage.

The major issues that require clarification as a matter of urgency for global groups to understand their Australian tax exposures under the proposed MAAL are set out below.

1.1 Low or no tax - section 177DA(1)(e)

We note that currently there is no definition of “low tax” in the ED. We believe that there are essentially five options for dealing with this.

1. Create a list of “low tax” jurisdictions in the regulations which would be updated by legislative instrument
2. Leave it to the ATO to create a list of jurisdictions that would be considered to be low tax (this could be dealt with through the public rulings system)
3. Create a series of principles that would guide whether a country is low taxed
4. Provide a specific rate (say 10%)
5. Provide a percentage of our company tax rate (say 33%) to determine whether a country is low taxed

We support Option 4 and believe that a specific rate embodied in the legislation is simple, clear and effective. We believe that rate should be 10% or less.

1.2 Commercially dependent entities - section 177DA(1)(a)(iv)

The proposed measures apply where a non-resident makes a supply to a non-associated Australian resident and some or all of the activities in connection with that supply are undertaken by an Australian resident or Australian PE of an entity who is an associate of or is “commercially dependent” on the non-resident.

The term ‘commercially dependent’ is a new concept on which clear guidance is needed.

Based on commentary in the EM at paragraphs 1.56 and 1.57, the intention of the provision appears to be to link ‘commercially dependent” to an Australian resident or Australian permanent establishment (**PE**) that is not a broker, general commission agent or any other agent of an independent status acting in the ordinary course of their business (as referenced in Article 5(6) of OECD Model Convention, Article 5(7) of the UK treaty or

paragraph (e) of the permanent establishment definition in section 6 of the Income Tax Assessment Act 1936).

However, based on the current wording, it is not clear for example, whether an independent agent acting at arm's length that has a high level of sales from a non-resident (say 90% of the business from one non-resident supplier) is intended to be caught. For example, there could be offshore leasing companies with on-shore people undertaking activities of an independent nature in Australia. It is unclear whether the nature of these activities would be caught.

We recommend that clearer guidance be provided on the term 'commercially dependent' for the purposes of section 177DA(1)(a)(iv). Consideration should also be given on whether a safe harbour or comfort zone threshold is acceptable in determining what "commercially dependent" means.

1.3 Connected with low or no tax jurisdiction – interaction of sections 177DA(8)(a) and 177DA(8)(b)

Clarification is required as to the difference between:

- section 177DA(8)(a): income that is subject to no corporate income tax under a law of a foreign country.
- section 177DA(8)(b): income that is not subject to corporate income tax under any Australian or foreign law

More specifically, what is the intended difference between an amount of income that is "subject to no corporate income tax" versus an amount that is "not subject to corporate income tax"?

Section 177DA(8)(b) is stated to be relevant to stateless income / stateless entities (refer EM, paras 1.27, 1.38 and 1.40). Consider the following example, which is intended to address a so-called stateless entity or stateless income case:

- An entity is incorporated in State A, but is not a tax resident in State A, as it is not centrally managed and controlled in State A
- The entity is either
    - tax resident in State B under the test of residency in State B law, or
    - not tax resident in any State.

On one view, section 177DA(8)(a) can be applied to State A. For example, it can be concluded that under the law of State A, the entity is "subject to no corporate income tax" and so the no tax / low tax condition is met under section 177DA(8)(a).

The interaction as between section 177DA(8)(a) and section 177DA(8)(b) should be clarified.

A consequential issue arising in relation to the interaction as between section 177DA(8)(a) and section 177DA(8)(b) is that the substantial economic activity test in section 177DA(10) is stated to only apply to an entity covered by section 177DA(8)(a). It is submitted that the substantial economic activity test in section 177DA(10) should be amended to cover an entity that falls within section 177DA(8)(b).

1.4 Activity not related directly or indirectly to the Australian supply - section 177DA(9)

Consideration should be given to expanding the number of examples in the EM which deal with the question of whether an activity in a MNE is related indirectly to an Australian supply.

One example may be where an MNE has a captive insurance company located in the Cayman Islands (as many do). This should not be considered to be related indirectly to the Australian supply of selling widgets to Australian customers where the insurance related to workers in the supply chain are covered by the captive insurance company. That is, the example should make it clear that such a connection would be too remote.

1.5 Substantial economic activity – section 177DA(10)

Broadly, the non-resident will not be connected with a no or low tax jurisdiction if, in relation to the Australian sales, the entity in the low or no tax jurisdiction undertakes "substantial economic activity" in relation to those sales.

There needs to be clear guidance on the meaning of "substantial economic activity" in the EM. Currently the only example in the EM (Example 1.8) considers a situation where the entity "employs thousands of highly valuable employees who add significant value in relation to their Australian sales". This is considered to be at the extreme end of the scale and so provides little guidance. Our view is that more examples are needed in the EM to clarify where the boundaries lie and relevant factors for determining the meaning of substantial economic activity.

1.6 Activities undertaken in Australia in connection with the supply – section 177DA(1)(a)(iii)

Section 177DA(1)(a)(iii) requires that activities are undertaken in Australia in connection with the supply. In our view, where the services performed, in relation to sales by a non-resident to associated parties by an associate are immaterial or trivial, the profit on that supply of goods and services should not be exposed to Australian taxes.

The ED and EM currently have no materiality rules or de minimis exclusions in relation to support services which might be related but are immaterial or minimal. We recommend that a materiality or de minimis threshold be introduced in this regard. This could also be by way of examples in the EM.

2. Other comments

2.1 Expected reach of the proposed measures

The Treasurer's media release of 11 May 2015 announcing the MAAL stated that the measure "deals with the activities of 30 identified multinational companies". We expect that there will be many more than 30 global groups potentially affected by these rules.

Although clarification of the key concepts set out above will go a long way towards reducing uncertainty, we predict that a considerable number of MNEs will potentially be caught by the measures and will wish to approach the ATO to obtain certainty. This is due in particular to the risk of unanticipated exposure to Australian tax and harsh penalties if the measures were applied by the Commissioner.

2.2 Position of the ATO as administrator of the MAAL – legislative measures

We submit that the law should clearly position the ATO as the administrator of these rules by delegating sufficient authority and administrative scope to it.

This is of particular importance given that the ATO will be required to administer the measures for a 1 January 2016 start date in connection with a scheme, "whether or not the scheme was entered into, or was carried out, before that day".

To assist in the administration of the MAAL, we recommend that the Bill in its final form:

(i) Clearly expresses the precise policy intent of the measure – including an objects clause to the rule;

(ii) Provides a clear legislative discussion about the role of the ATO in approving existing and new arrangements involved in foreign supplies of goods and services;

(iii) Provides that there is not an automatic exposure to the rules from 1 January 2016 in the absence of a determination by the ATO;

(iv) Indicates that global groups can obtain binding guidance from the ATO as to whether their arrangements might be covered by these rules or might not be covered;

(v) Provide a mechanism to relieve taxpayers from penalty exposures where they are in discussions with the ATO about confirming the extent of any exposure under the measure and any required measures to rectify their position.

As well as the legislative issues above, the ATO will still need to be ready to provide additional guidance and resolve global groups' exposures to the law, through for example, the use of private binding rulings, advance pricing agreements or advance compliance agreements. To help the broader tax professional community, some of these private rulings should be turned into public rulings so that we have some transparency as to how the provisions are being applied in practice.

Chartered Accountants Australia and New Zealand would be pleased to assist the ATO in progressing these matters.

2.3 Interaction with the Organisation for Economic Co-operation and Development (OECD) project on Base Erosion and Profit Shifting (BEPS)

The measures in the ED are directed at certain arrangements that have been identified as part of the OECD's comprehensive 15-point BEPS Action Plan to address tax base erosion attributable to cross-border structures and transactions, in particular Action 7 "Prevent the artificial avoidance of PE status" and to a lesser extent Action 6 "Prevent treaty abuse".

The OECD is currently on target to take its final recommendations on Action 7 and the last outstanding issue on Action 6 to the G20 Finance Ministers meeting in October 2015 and the G20 Leaders meeting in November 2015.

In our opinion, it will be crucial for the role of the MAAL to be re-assessed once the OECD's final recommendations are delivered. Australia should then look at the feasibility of adopting the

OECD's global best practice solution to ensure consistency with other jurisdictions and to address possible double taxation through mutual agreement procedures under tax treaties. This may also involve entering into some form of multilateral instrument that is currently being developed by the OECD (Action 15), scheduled for completion late 2016.

Although it will ultimately depend on the directions of the OECD's work and government's response, we envisage that the measures in the ED are then likely to be of diminished relevance. We submit therefore that the Government should introduce the ED measures with a formal commitment to review the law in say three years, when Australia's position on the planned multilateral instrument to amend double tax agreements and the final actions arising from BEPS Actions 6 and 7 are known.

Should you have any queries concerning the matters discussed in our submission, or wish to discuss them in further detail, please contact me via email at: michael.croker@charteredaccountantsanz.com; or telephone (612) 9290 5609

Yours sincerely

Michael Croker
Tax Australia Leader