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Dear Sir or Madam

**SUBJECT: SUBMISSION ON EXPOSURE DRAFT LEGISLATION CONCERNING TAX LAWS AMENDMENT (TAX INTEGRITY MULTINATIONAL ANTI-AVOIDANCE LAW) BILL 2015**

CPA Australia represents the diverse interests of more than 150,000 members in 120 countries, including more than 25,000 members working in senior leadership positions. Our vision is to make CPA Australia the global accountancy designation for strategic business leaders.

Against this background, we provide this submission in relation to the Exposure Draft Legislation 'Tax Laws Amendment (Tax Integrity Multinational Anti-avoidance Law) Bill 2015' and the accompanying Explanatory Materials (EM) which were issued by Treasury on 12 May 2015.

## GENERAL COMMENTS

CPA Australia has broadly supported the proposal that Australia explore the development of its own measures to attack egregious tax arrangements if the current laws were deemed insufficient.

We believed that such an approach was appropriate given that attempts to achieve a multilateral solution to these practices as part of the Organisation for Economic Co-operation and Development (OECD) Base Erosion and Profit Shifting (BEPS) project appeared so protracted that Australia's income tax base could be significantly eroded in the interim, as would public confidence in the taxation system.

While we continue to encourage the Government to remain vigilant in considering appropriate unilateral responses to any deficiencies identified in our current taxation laws, we also note significant progress on multilateral negotiations.

The OECD has now released a revised discussion paper on BEPS Action Item 7 (on 15 May 2015) which seeks to improve the OECD model approach in determining whether a PE exists. We further understand that the OECD anticipate issuing a final discussion paper outlining an agreed multilateral approach to BEPS Action Item 7 in October 2015, and that they will issue a multilateral instrument that will implement the recommendations of BEPS Action Item 7 by 31 December 2016.

Accordingly, if the results of BEPS Action Item 7 are adopted by Australia and other OECD members from 1 January 2017 we may have a potential consensus approach with various treaty partners on how to implement common rules on how to attack avoidance by multinationals through a more contemporary definition of Permanent Establishment (PE).

This approach has the potential added benefit that it will not undermine confidence in Australia's Double Tax Agreements (DTAs) as the proposed Multinational Anti-Avoidance Law (MAAL) changes envisage that tax could be paid by a taxpayer who otherwise complies with the existing definitions of PE under the DTAs and satisfies the current integrity provisions of such treaties.

This more uniform approach would also prevent creating uncertainty regarding foreign investment as it is expected that this multilateral approach will result in a more level playing field amongst OECD members as it is expected that there will be an internationally agreed wider definition of PE.

Hence, we recommend that the proposed MAAL changes to Part IVA of the Income Tax Assessment Act 1936 (the ITAA) be reviewed should Australia choose to legislate the results of BEPS Action Item 7 as the need for the MAAL may be significantly reduced, if not eliminated, given our understanding that the OECD approach is aimed at similar outcomes, but under a simpler approach.

**SPECIFIC COMMENTS**

We also make the following specific comments in respect of the exposure draft legislation on the MAAL:

**1. Transitional Arrangements**

We recognise that there is a tension between the need to send out a clear message to multinational groups that they may need to alter behaviour if they have avoided attributing profits to an Australian PE, and to provide such groups with sufficient time to restructure their local activities so that they do not potentially trigger the proposed MAAL provisions.

We would expect that many such groups would need to seek professional advice as to whether they are subject to the MAAL changes, and if so, what action the business should take and when. For example, they will need to consider issues such as how a restructure should be implemented, obtain internal management agreement for changed arrangements, satisfy any external regulatory approvals, change systems, renegotiate contracts, and realign complex international global supply chain operations.

As the proposed changes are to commence from 1 January 2016 regardless of when a multinational group structured its activities in a particular way, we do not believe that that current deadline of effecting the necessary changes that may be required will, in every case, be feasible.

We also understand that many multinational groups will seek guidance from the ATO as to whether they are subject to the MAAL. Accordingly the ATO also needs appropriate time to issue consistent and considered guidance on the proposed changes which are highly complex and also introduce a range of new concepts.

Hence, we recommend that the start date of the proposed MAAL be deferred until 1 July 2016 as their imminent introduction will help assist behavioural change, but a deferred start date will also give multinational groups more adequate time to review - and reconfigure their operations where necessary - so as to be compliant.

**2. Scope of the MAAL**

In the Treasurer's Media Release dated 11 May 2015 the Treasurer Mr Hockey described the MAAL changes as a targeted measure which '…deals with the activities of 30 identified multinational companies.'

Furthermore, paragraph 1.13 of the EM provides that the MAAL '…will target the most egregious tax structures by multinational companies, while limiting the impact on legitimate international business activities.'

However, we are concerned that the proposed MAAL exposure draft legislation is potentially broader in scope and may therefore apply beyond the currently targeted 30 multinational groups. Indeed, we believe that many multinational groups will seek guidance from the Australian Taxation Office (ATO) including private binding rulings to clarify whether they are subject to the proposed amendments.

Accordingly, we believe that the proposed legislation and/or the EM should be amended to provide further examples of how this targeted anti-avoidance measure is to operate in practice so that multinational groups will have a better understanding on how the proposed changes will practically apply.

As a corollary, further examples should also be provided in the EM in relation to the carve-outs from the regime under proposed sections 177DA(7) and (8) as these exemptions concerning a multinational carrying on activities in a no or low tax jurisdictions require considerable elaboration as to when a supply by a group is not related to an Australian supply and when there is substantial economic activity in the no or low tax jurisdiction.

**3. Penalties**

CPA Australia is supportive of the proposal that the proposed 100 per cent penalty should be limited to transactions arising on or after the commencement date of the MAAL measures (but note we suggest 1 July 2016 as a more appropriate date given the circumstances).

## 4. Improving clarity of proposed section 177DA

We believe that various terms and concepts used under proposed section 177DA require clarification as set out below:

- The provisions of proposed section 177DA(1)(c) refer to a taxpayer obtaining a tax benefit being the foreign entity who is being attributed profits arising from its Australian operations. However, it is not clear that a foreign entity is a taxpayer as defined under section 6(1) of the ITAA (1936) meaning a person deriving income or deriving profits or gains of a capital nature, since such a foreign entity will not have any presence in Australia. Furthermore, it is currently unclear how payment of any Australian tax liability (including penalties) arising on the MAAL can be enforced against the relevant foreign entity. We believe that all these issues need to be addressed prior to any enactment of amending legislation, and that many of these issues may be able to be more readily addressed in any legislative response arising in relation to any multilateral instrument arising from BEPS Action Item 7.

- Proposed section 177DA may apply where an associate or an entity is 'commercially dependent' on the non-resident entity making supplies to Australian residents. However, the term commercially dependent is not defined in the current income tax law and appears to be a new concept. Further guidance on the meaning of this expression should be provided either in proposed section 177DA and/or in the EM as taxpayers need to understand the criteria that will be applied in determining whether an entity is commercially dependent on a foreign entity. For instance, example 1.12 of the EM provides that an entity operating as a legally independent agent or broker will not be regarded as commercially dependent where they act for a foreign business in the ordinary course of the agent's or broker's business. However, where, say, 70 per cent of the agent's business arises from sales made on behalf of the foreign entity it could presumably be contended that the agent is commercially dependent on that foreign entity given the quantum of sales involved. Hence, some additional criteria which sets out what constitutes commercial dependence would be welcome such as whether it is intended to apply to entities that would be independent agents under a DTA and whether particular metrics should apply in determining whether activities are commercially dependent such as arranging a certain percentage of sales on behalf of the foreign entity.

- As currently drafted, section 177DA will apply where a 'principal purpose' of a scheme was for the taxpayer to obtain a tax benefit. However, there is no equivalent concept of principal purpose under the existing law which will lead to considerable uncertainty as it differs from the 'sole or dominant purpose' test that otherwise applies under the existing provisions of Part IVA. In the absence of any compelling argument to the contrary we believe that reference to the principal purpose of a scheme should be replaced with the existing sole or dominant purpose test which has been to some extent judicially clarified.

- One of the perquisites to the application of proposed section 177DA is that it will potentially apply where income is subject to no or low corporate tax under a law of a foreign jurisdiction, an arrangement with a foreign government or authority or is not subject to corporate tax under any Australian law or foreign law.

  Crucially, neither the current law nor the proposed changes elaborate on what will constitute a low corporate tax rate. It is essential that some form of guidance be given as to what constitutes a low rate of corporate tax. In our view there would be some merit in including a prescriptive list of low corporate tax jurisdictions in the income tax regulations which could be periodically updated for changes in tax rate.

  In addition, the application of section 177DA(1)(e) also needs to recognise that foreign tax rules may change and may result in a broadly comparable tax regime becoming a low tax jurisdiction because the foreign jurisdiction introduces some tax concession or exemption. In these circumstances, such a change may inadvertently trigger an Australian exposure under the proposed MAAL rules without the multinational group realising that it has triggered such an exposure, which means that multinational groups, their advisers and the ATO all need to be vigilant about any changes in global corporate tax rates.

  It also prima facie appears that the foreign entity will be potentially subject to tax at a rate of 60 per cent (inclusive of the penalty) without receiving any tax credit for tax paid in the formerly low tax jurisdiction.

  Indeed, it does not appear that any tax credit is provided for any foreign tax paid by the foreign entity in the low tax jurisdiction.

- Proposed section 177DA(9) provides a carve-out from the MAAL where the foreign entity undertakes substantial economic activity in the foreign jurisdiction classified as a no or low corporate tax jurisdiction. The issue of what constitutes 'substantial economic activity' is also a new concept which is not defined elsewhere in the income tax law, and there is insufficient explanation of the concept in the EM. Accordingly, we believe that some indicia as to what will constitute substantial economic activity needs to be provided in either the exposure draft legislation or the accompanying EM.

If you have any questions regarding the above, please contact Mark Morris, Senior Tax Counsel, on (03) 9606 9860 or via email at mark.morris@cpaaustralia.com.au.

Yours faithfully

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