CHARTERED ACCOUNTANTS
AUSTRALIA + NEW ZEALAND

3 July 2015

Mr Tom Reid
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Dear Mr Reid,

Better targeting the income tax transparency laws

Chartered Accountants Australia and New Zealand welcomes the opportunity to comment on the exposure draft *Tax and Superannuation Laws Amendment (Better Targeting the Income tax Transparency Laws) 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

In Chartered Accountants Australia and New Zealand's 2015-16 pre-Budget submission[1] we expressed concerns about the impact of the current domestic tax transparency measures for private companies. Most of those concerns are alluded to under the heading *Assessment of the laws and their impact* on page 4 in the EM.

[1] Refer: http://www.charteredaccountants.com.au/Industry-Topics/Tax/Exposure-drafts-and-submissions/Submissions/Government/090215-PreBudget-submission-lodged.aspx

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We are supportive of narrowing the scope of the current measures. In considering the policy drivers behind the current transparency measures we are interested to see Tax Commissioner Chris Jordan quoted on March 19, 2015[2] about the proposal for excluding private companies from the public reporting with all its issues:

> *"… Asked about the rollback, Mr Jordan, speaking at the Tax Institute conference on Queensland's Gold Coast, said "it's clearly a matter for government".*
>
> *But he said the laws were originally intended to capture overseas-based multinationals that were not paying tax on billions of dollars of sales in Australia, rather than private business owners.*
>
> *"I think if you look at the history of the matter, it was really for multinational companies operating here, disclosing quite low revenue," he said".*

When we consider the outcomes of the ATO public reporting which has been already legislated we see limited actual usefulness of the disclosed information and its potential for misinformation of the public. It is clear from ATO consultations that even widely held public companies are concerned about the potential adverse reputational effect, and the need for the ATO to produce extensive explanatory material to explain to readers of the disclosures that they may be quite misleading because they provide no information about the many legitimate causes of companies having low taxable income (causes such as eligibility for tax concessions for R&D and capital allowances, companies recovering prior year tax losses, and companies experiencing low profit margins in today's business environment). Even public companies are considering significant efforts in many cases to ensure the companies are ready for queries and comments from media and from advocacy groups about perceived low tax payable.

We note that, for the same reasons, some private companies might need to incur significant costs in communicating their tax positions, in situations where the private companies have never had to date a public reporting or investor relations or public relations team. Private groups must not only deal with all of the above issues but also face significant privacy concerns. We highlight that private companies represent very small collections of natural persons, who are as natural persons exempted from disclosures of their own tax affairs on the basis of their human rights to privacy. We find it difficult to distinguish on human rights or privacy grounds between a single individual natural person which has no current public reporting of their affairs and a private company representing a family group of natural persons which does under current law have public reporting.

So we are supportive of narrowing the scope of the current measures on policy grounds.

We do, however, have a number of observations on the current ED and EM noted below.

1. Observations on ED and EM

1.1 Subsection 3C amendments and 3D and 3E reporting

Whilst we acknowledge the privacy concerns are greater with the income tax disclosures in subsection 3C, and there might be few Australian private companies that in fact have information disclosed pursuant to subsections 3D (MRRT) and 3E (PRRT), nevertheless, we

[2] Tax Institute conference, Gold Coast, Queensland March 2015

recommend, for consistency, that entities excluded from the revised subsection 3C disclosures should also be carved out of subsections 3D and 3E disclosures.

1.2 Current focus is only on Australian owned private companies

Following a review of the ED, EM and discussions with Treasury, it is apparent that there are a number of competing tensions in these proposed amendments.

For example, the amendments seek to address privacy concerns for Australian owners of closely held companies. However, many of the arguments advanced for these amendments are, from a policy viewpoint, equally applicable for foreign owners of closely held companies.

If the disclosed information could be used against them in commercial negotiations, or, will give rise to otherwise unnecessary restructuring costs to avoid public disclosures, we query why the amendments are not just extended to all private companies. This is particularly so given some of the unusual practical outcomes under the current ED (discussed below).

1.3 Policy intent and legislative drafting vs practical outcomes

An example of the tensions in the proposed amendments is the practical application of the legislative provisions in subsection 3C(1)(b).

We highlight some issues which in our view should be clarified, ideally in the Bill or alternatively by clear ATO binding public guidance.

In order to achieve the lowest compliance costs for taxpayers (which admittedly is a commendable objective), it is apparent that a taxpayer's disclosures at items 1, 2 and 3 on the company tax return will govern whether or not one or more of the criteria in subsection 3C(1)(b)(i), (ii) or (iii) apply.

Thus, for example, the EM and discussions with Treasury suggest the following:-

- If the company indicates in its tax return it is an Australian resident and a private company (item 3 on the return) then subsection 3C(1)(b)(i) is not satisfied and no ATO public reporting will arise provided no other criteria is satisfied. In this regard the policy, legislative provisions and EM seem to be aligned;
- If the company indicates in its tax return that it has a ultimate holding company and the foreign country code box is filled in (item 1 on the return), then we understand the intention is that subsection 3C(1)(b)(ii) is satisfied and ATO public reporting will occur. However, the company tax return instructions are not clear on this matter given there is some debate as to whether the instructions are intended to:

  a) limit the meaning of a ultimate holding company (for the purposes of completing the tax return) as being the relevant holding company in the ED phrase at 3C(1)(b)(ii), namely, "…member of a wholly-owned group during the income year that has a foreign resident *ultimate holding company*" and

  b) the definition of 'ultimate holding company' for the purposes of the instructions takes its meaning from section 124-780(7) of the ITAA 97.

  If the current tax return instructions are intended to achieve these outcomes then one practical solution would be to revise the 2016 tax return instructions. In the meantime however, some impacted taxpayers (and their tax advisors) that have taken a more

conservative filing position in 2014 and 2015 tax returns may want to engage with the ATO in order to revise their prior disclosures. Thus, there is a practical dimension to the wording of 3C(1)(b)(ii) that should be considered;

- If, in accordance with the short form calculation methodology in the tax return instructions, the company indicates in its tax return that it has a direct foreign shareholding of greater than 50% (item 2 on the return) then the EM indicates subsection 3C(1)(b)(iii) is satisfied and the ATO will publicly report the tax data for that company. In this regard, we would question whether the current wording of the ED is limited to the practical outcomes alluded to in the EM and whether changes to the ED drafting maybe be prudent;
- We also observe that the EM and ED need to be clearer in relation to the impact of foreign interests held ultimately by entities other than a single foreign ultimate holding company, We note that some of the curious practical outcomes of the ED and EM raise questions on what exactly is the tax policy towards foreign owned, closely held groups. Thus, in Example 1.1 of the EM, if the Australian Holding Company is 100% owned by a foreign resident trust, or is owned 99% / 1% by foreign residents, the example is silent on whether, as it appears, Operating Company is entitled to an exemption from the tax transparency laws.

  This lack of clarity may be a consequence of tax compliance cost issues 'trumping' any tax policy logic that foreign multinational closely held entities should fall within the tax transparency regime.

  Nevertheless, we query whether the tax policy becomes 'blurred' in the ED and we refer back to our previous observations in paragraph 1.2 of our submission above.

  Indeed, the proposed Voluntary Corporate Disclosure Code[3] may:-

  a) ultimately make the ATO website disclosures redundant;

  b) become a far more important 'tax transparency' initiative; and

  c) foreign owned closely held companies could more appropriately be dealt with under this code.

2. Other comments

Depending on drafting and Parliamentary timeframes, and whether the policy reflected in the ED is supported by non-Government parties and independents in the Senate, it is possible that the policy intention reflected in the ED may not come to fruition in time for the ATO's planned first release of information for the 2013-14 income year.

If the ED does become law, but after the ATO has already disclosed the 2014 income tax return disclosures, the disclosures will already have gone 'public'. However, we still believe there is merit is considering whether the 2014 private company disclosures should be removed from the ATO website and new tables uploaded, given that the 2014 disclosures are intended to have a very long shelf life.

[3] Refer Treasurer's press release, 12 May 2015. Source: http://jbh.ministers.treasury.gov.au/media-release/043-2015/

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 (02) 9290 5609.

Yours sincerely

Michael Croker
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