

EXPOSURE DRAFT

STRONGER PENALTIES TO COMBAT TAX AVOIDANCE AND PROFIT
SHIFTING

EXPLANATORY MATERIALS

Chapter 1 Stronger penalties to combat tax avoidance and profit shifting

Outline of chapter

1.1 The amendments in the Exposure Draft double the maximum administrative penalties that can be applied by the Commissioner of Taxation to large companies that enter into tax avoidance or profit shifting schemes.

1.2 The increased penalties only apply to companies with global revenue exceeding \$1 billion and will help to deter tax avoidance.

Context of amendments

Operation of the existing law

1.3 The administrative penalties for entering into tax avoidance or profit shifting schemes are in Subdivision 284-C in Schedule 1 to the *Taxation Administration Act 1953*. All legislative references are to Schedule 1 to that Act unless otherwise specified.

1.4 Section 284-145 imposes an administrative penalty if an entity seeks to obtain a scheme benefit under a tax avoidance or transfer pricing scheme. The amount of the scheme benefit is generally the amount by which the entity's tax-related liability would be reduced under the scheme if the relevant anti-avoidance or transfer pricing provision did not apply (section 284-150).

1.5 Penalties are worked out by reference to a base penalty amount for a particular breach. The base penalty amount generally reflects a portion of the underlying scheme benefit sought. To work out the penalty imposed, adjustments may be made to the base penalty amount to take into account aggravating or mitigating factors (sections 284-220 to 284-225 in Subdivision 284-D).

1.6 Division 298 sets out the machinery provisions for the collection of penalties.

Summary of new law

1.7 The amendments in the Exposure Draft double the penalties imposed on large companies that enter into tax avoidance or profit shifting schemes. The amendments will only apply to companies with global revenue exceeding \$1 billion that do not adopt a tax position that is reasonably arguable.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
<p>The maximum penalty applicable is 120 per cent of the amount of tax avoided under the scheme.</p> <p>The increased penalty only applies to companies with global revenue exceeding \$1 billion.</p> <p>Taxpayers that adopt a tax position that is reasonably arguable will not be liable to increased penalties.</p>	<p>Administrative penalties are imposed on taxpayers that enter into tax avoidance or profit shifting schemes. The maximum penalty applicable is 60 per cent of the amount of tax avoided under the scheme.</p>

Detailed explanation of new law

1.8 The amount of the penalty imposed for entering into a tax avoidance or profit shifting scheme is doubled for certain large companies that do not have a reasonably arguable position. [*Exposure Draft, item 1, subsection 284-155(3)*]

The global revenue threshold

1.9 The amendments only apply to companies with global revenue exceeding \$1 billion in an income year that relates to the penalised scheme. [*Exposure Draft, item 1, paragraph 284-155(3)(a)*]

1.10 The global revenue of an entity is determined in accordance with the proposed amendments inserting section 177DA into the *Income Tax Assessment Act 1936*. See paragraphs 1.30 to 1.37 of the Explanatory Materials to the Exposure Draft of the Tax Integrity: Multinational Anti-Avoidance Law.

1.11 The Multinational Anti-Avoidance Law Exposure Draft determines the global revenue of certain non-residents. Nevertheless, an

entity may satisfy the global revenue threshold for the purposes of the present amendments if it is an Australian resident.

Reasonably arguable position

1.12 The amendments do not apply to taxpayers who have a 'reasonably arguable position' on the application of the relevant adjustment provision. [*Exposure Draft, item 1, paragraph 284-155(3)(b)*]

1.13 The purpose of this exclusion is to ensure that penalties are not increased where the breach is the result of uncertainty in the tax laws.

1.14 Subsection 284-15(1) sets out the test to determine whether a particular way of applying the law is reasonably arguable.

1.15 The reasonably arguable position is an objective standard involving an analysis of the law and application of the law to the relevant facts. The position must be a contentious area of law, where the relevant law is unsettled or where, although the principles of the law are settled, there is a serious question about the application of those principles of the circumstances of the particular case. Miscellaneous Taxation Ruling 2008/2 provides further information on the interpretation of this standard.

1.16 Additional documentation requirements, imposed under Subdivision 284-E, must be satisfied before a taxpayer can have a reasonably arguable position in transfer pricing matters.

Summary of penalty amounts

1.17 The following table sets out the new penalties that apply to taxpayers that satisfy the global revenue threshold and enter into tax avoidance or profit-shifting schemes. Penalties are expressed as a percentage of the relevant scheme shortfall amount.

Table 1.1 Scheme penalty amounts for taxpayers that satisfy the global revenue threshold

<i>Culpable behaviour</i>	<i>Base penalty amount</i>	<i>Aggravating factors apply</i>	<i>Disclosure during examination</i>	<i>Disclosure before examination</i>
Tax avoidance schemes*	100	120	80	20
[if position is reasonably arguable]	[25]	[30]	[20]	[5]
Profit-shifting schemes	50	60	40	10
[if position is reasonably arguable]	[10]	[12]	[8]	[2]

* Tax avoidance schemes include profit-shifting schemes where the taxpayer has a sole or dominant purpose of obtaining a transfer pricing benefit from the scheme.

Application and transitional provisions

1.18 This measure applies to scheme benefits obtained, or that would be obtained, on or after 1 July 2015 (regardless when the scheme was entered into or carried out). [Exposure Draft, item 2]