KPMG submission

Exposure Draft

Tax Laws Amendment (Tax Integrity Multinational Anti-avoidance Law) Bill 2015: Country by country reporting

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Executive Summary

Introducing CbyC reporting, Master File and the Local File requirements will place Australia as an early-adopter in the spirit of the Organisation for Economic Co-operation and Development's (OECD) guidelines for transfer pricing documentation. Hopefully this will help Australia set the agenda for the formulation of rules by other countries.

It will be important, wherever possible, to ensure Australia's implementation of these initiatives is consistent with the OECD Implementation Guidance in order to maximise the compliance benefits of standardised global reporting and to keep the additional compliance cost burden to the minimum necessary.

There is a question of balance between what is included in the legislative provisions and Explanatory Memorandum and what is left for the future to be adopted in a legislative instrument. Our recommendations tend towards greater detail in the legislative provisions, but with flexibility for change by legislative instrument where appropriate. The key recommendations are as follows:

Exclusion of obligations on subsidiaries of an Australian tax consolidated or MEC group. Currently, the obligation to provide information will fall on all members of an Australian consolidated or MEC group, thereby requiring such subsidiaries to apply for an exemption. This is unnecessary red tape and can be dealt with by a legislative exclusion.

Exclusion of large domestic groups with small cross border activities and a large MNE with small Australian operations. In both cases the exclusion should be embodied in the legislation. The concept of "small" should be where local income, customer revenue and assets are each less than 0.2% of Global Revenue.

Penalty mitigation on the same footing as currently exists for a reasonably arguable position should be available where there is compliance with the Master File and Local File record keeping requirements.

A local company should not have an obligation to produce CbyC and Master File reports during a transitional period of 4 years where reports are not obtainable from the Ultimate Parent Company.

Income year. The CbyC and Master File should be lodged in respect of the Ultimate Parent Entity's foreign accounting year end, whereas the Local File should be prepared based on the tax year end of the local entity.

The Annual Global Revenue threshold should be tied to annual global revenue of the immediately preceding fiscal year of UPE, consistent with OECD guidance.

Detailed comments

1. General

1.1. KPMG welcomes the opportunity to comment on the following Exposure Draft (ED) and associated Explanatory Memorandum (EM) as published by Treasury on 6 August 2015, namely, *Tax Laws Amendment (Tax Integrity Multinational Anti-avoidance Law) Bill 2015: Country by country reporting* (CbyC ED).

1.2. KPMG is supportive of the global initiatives to introduce CbyC reporting, Master File and the Local File requirements. It will be important, wherever possible, to ensure the local implementation of these initiatives is consistent with the OECD Implementation Guidance in order to maximise the compliance benefits of standardised global reporting and to keep the compliance cost burden on multinational enterprises to the minimum necessary.

2. "All in" approach of s 815-355

2.1 The existing structure of the legislation begins with an 'all in' approach under s 815-355, and then allows for certain taxpayers or groups of taxpayers to be exempted from the reporting regime under s 815-360 (or to have their reporting obligations modified) through administrative action by the ATO. This means *every* person satisfying the requirements in s 815-355(1)(a) and (b) must file a statement unless exempted by the Commissioner.

2.2 We consider further consideration should be given to mitigate the risk of higher administrative costs for the ATO and higher compliance costs for the taxpayers. In particular, we understand that the use of a legislative instrument to exclude 'groups of taxpayers' is not currently being considered.

Exclude obligations on subsidiaries of tax consolidated groups or MEC group

2.3 Pursuant to our discussions with Treasury, we understand that in a tax consolidated group context, each member of the tax consolidated group prima facie has a reporting obligation under s 815-355. Thus, whilst s 815-360 may ultimately operate so that only the head company of the tax consolidated group has a reporting obligation, as a matter of legislative drafting, each member of the tax consolidated group must request an exemption from the ATO. The ATO must allocate resources to process such requests.

We submit that there should be legislative exclusion of obligations on subsidiaries of an Australian tax consolidated or MEC group. The EM should provide greater insights on the intended outcome, including transitional issues surrounding entry and exits from such groups.

Exclude obligations on large domestic groups with small cross border activities and a large MNE with small Australian operations

2.4 We submit that both should be excluded from the reporting requirement. In both cases it would be preferable to embody the exclusion in the legislation, but with the potential for modification through a legislative instrument.

2.5 For the purposes of applying the exclusions, consideration should be given to a concept of "small" where local income, customer revenue and assets are each less than 0.2% of Global Revenue.

Penalty mitigation for compliance with Master File and Local File requirements

2.6 The Master File and the Local File requirements are in reality a modern variant on Australia's existing transfer pricing documentation rules in Subdivision 284-E of Schedule 1 to the *TAA 1953*. The additional record keeping requirements of Master File and Local File undoubtedly leads to higher and potentially unnecessary compliance costs.

2.7 The ED makes no attempt to address whether satisfactory completion of these new reporting obligations should warrant some compliance benefits for taxpayers, such as tax penalty mitigation in the event of a transfer pricing adjustment.

2.8 We recommend that taxpayers are afforded penalty mitigation on the same footing as currently exists for a RAP where there is compliance with the Master and Local File record keeping requirements.

2.9 If the current legislative deadline precludes the above suggestions from being actioned, then we submit the EM commentary should at least flag the possibility that future legislative (and administrative) changes may well be required, pending the outcomes of the ATO's consultation processes.

Legal obligation on local subsidiary of inbound MNE & four year transitional period where report unobtainable from UPE

2.10 A critical issue remains unanswered in the ED and the EM as to what happens to an Australian subsidiary (and its Public Officer) where the non-resident Ultimate Parent Entity (UPE) of the group is not required to produce a CbyC report (or a Master File).

2.11 Australia is an 'early adopter' and the level of global take up of CbyC reporting is currently unclear. The OECD Implementation Guidance on CbyC infers that a 'drop down' approach may be adopted if the UPE does not produce a CbyC report.

2.12 We submit that a flexible approach be required under s 815-360 during a transitional period of four years, where a local company should not have an obligation to provide CbyC and Master File reports where reports are not prepared by the UPE overseas.

2.13 It would be beneficial for the EM to explain the transitional approach in detail and note what might be some of the matters that would be subject to further ATO consultation.

Intended outcome of 'income year'

2.14 The CbyC ED proposes that the CbyC report, the Master File and the Local File are required to be lodged 'in relation to an income year'. However, it is unclear which of the potential outcomes below are intended:

- The CbyC report and the Master File are to be based on the foreign accounting year end of the UPE (NB the OECD Implementation Guidance seems to infer this to be the case at least with respect to the CbyC report), whereas the Local File is to be prepared based on the tax year end of the relevant reporting entity in Australia;
- Only the CbyC report is to be based of the foreign accounting year end, whereas the Master File and the Local File are to be based on the tax year end of the relevant reporting entity in Australia;
- All three reports are to be based on the tax year end of the relevant reporting entity in Australia; or
- All three reports are to be based the UPE's foreign accounting year end.

2.15 We note KPMG have MNE clients where the tax year ends of their subsidiaries do, and do not, equate to the accounting year end of the UPE and thus in the latter case, the matter is of some importance.

2.16 We submit that the CbyC ED should clarify the intended outcome and that this matter not be left to the ATO to administer under s 815-360. We recommend the ED clarifies the 'year end' issue as follows:

- Both the CbyC report and the Master File are lodged in respect of the UPE's foreign accounting year end. This means in respect of each year the UPE only has to produce one CbyC report and one Master File and the same two documents will ultimately be provided to the revenue authorities of the countries in which it operates; and
- A Local File is required to be prepared for each relevant taxpaying entity in the local jurisdiction based on the tax year end of the relevant entity.

2.17 We also submit that changes to s 815-355(2) are required given that, as currently worded, lodgement is required 'before the end of the next income year'. This may not tie up with the ultimate conclusions reached above on the 'year end' issue.

3. 'Annual Global Revenue' definition and its potential impacts

3.1 Section 815-355 provides that an 'annual global revenue' (AGR) of $1 billion or more triggers the requirement to provide the CbyC report, subject to any exemptions. Section 995-1(1) defines AGR by reference to the proposed s 177DA(5) to (7) of the *Income Tax Assessment Act 1936* (ITAA 1936).

3.2 This definition is currently subject to separate consultation as part of the Multinational Anti-avoidance Law Exposure Draft (MAAL ED). The Explanatory Memorandum of the MAAL ED suggests that AGR is determined with reference to, inter alia, audited account financial reports, or based on accounting principles.

3.3 Following discussions with Treasury, we understand that changes to the 'AGR' definition are already under active consideration, particularly in how it might be applied in the CbyC ED.

3.4 We have assumed it continues to be important to identify a global group (CbyC group) that are consolidated for accounting purposes and there will still be linkages to revenue as determined by reference to consolidated financial reports, or based on a Commissioner's estimate as this is broadly consistent with the OECD Implementation Guidance.

AGR threshold to be determined by reference to preceding fiscal year of UPE

3.5 The current drafting (as per the MAAL ED) determines annual global revenue by reference to the 'income year' to which reporting relates. We submit the AGR definition should be amended to tie to OECD's Guidance, which asserts the AGR threshold is to be tied to annual global revenue of the immediately preceding fiscal year of UPE (refer paragraph 9 of the OECD Implementation Guidance: "*there would be an exemption from the general filing requirement for MNE groups with annual consolidated group revenue in the immediately preceding fiscal year…*").

CbyC group equates to Master File group

3.6 We also submit that the ED should make it clear that the Master File reporting requirements will be in respect of this CbyC group as determined for CbyC reporting. This is currently not clear in the CbyC ED.

AGR definition for certain large groups and other issues

3.7 We note that certain types of 'large groups' (e.g. sovereign wealth funds, State owned entities, pension funds, educational institutions etc) may have their own reporting rules that may or may not coincide with the consolidation/accounting standards applicable to private sector entities. We recommend that the final AGR definition accommodate nuances with their existing financial reporting rules.

3.8 Another issue for some 'large groups' is where they are not required to produce audited consolidated accounts (or possibly not any accounts at all) in their home jurisdiction. In such cases, questions will be asked as to how a CbyC group is to be determined (if at all) and how the Commissioner's revenue estimate will be determined.

3.9 A good understanding of accounting/consolidation standards and their interactions with the CbyC ED will be important in addressing the basic question of which entities are considered to be part of a CbyC tax group for CbyC reporting (and presumably for the purpose of the Master File). We submit that the EM guidance at present is scant and ultimately the ATO may need to call on the assistance of accounting specialists to help explain some of the CbyC ED reporting impacts.

4. Other issues

Territorial nexus of 'you'

4.1 The current drafting of the CbyC ED places a reporting obligation on 'you', if a global revenue threshold is satisfied. Nothing else in the CbyC ED elaborates on the territorial nexus required for an entity to fall within the CbyC ED. The EM at various paragraphs attempts to clarify the CbyC ED's scope, noting an Australian resident or a foreign resident entity with a permanent establishment (PE) in Australia is covered (refer paragraphs 1.11, 1.12, 1.19, 1.23 and 1.24 of the EM). The EM therefore suggests that a foreign resident entity without a PE in Australia will not be required to report.

4.2 We submit that the ED (and the EM) should provide further clarity with respect to the territorial nexus, such as:

- Including a specific reference to PEs;
- Whether PE status is determined pursuant to domestic rules, pursuant to tax treaties (where relevant) or is to be cross referenced to the MAAL ED definition; and
- In what circumstances (if any) is a foreign investor in an Australian trust considered to have a PE in Australia, either because of the trust's underlying activities or the location of the trustee?

Legislative adoption of OECD reporting templates or explain variance

4.3 We submit that if the intention is for the Commissioner's 'approved form' to replicate the OECD CbyC reporting template, the ED should state this. If any possible Australian variations to this global template have already been identified and will be the subject of separate ATO consultation processes, the EM should highlight this to the reader. The EM can greatly assist CbyC implementation projects by giving as much guidance as possible on the extent to which Australia will be following the OECD Implementation Guidance.

Revise 'all or nothing' approach in s 815-360 exemption

4.4 Under the current s 815-360, the Commissioner has the power to provide an exemption to taxpayers or groups of taxpayers. The exemption appears to be an all or nothing approach. We submit that the s 815-360 should to be modified such that the Commissioner may still require an' approved form' to be lodged but may vary the content of the disclosures. By way of examples, this proposed wording might more readily cater for flexibility in the approved form disclosures in the transitional phase of the regime, or, for circumstances where a local subsidiary can provide some, but not all, of the information required in a CbyC report or a Master File.

4.5 Two typos in s 815 -360(1) and s 815-360(4) should, we submit, be rectified. The references to 'this section' under those provisions should, we believe, refer to 's 815-355'.