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Income Tax: cross –border profit allocation – review of transfer pricing rules (“the consultation paper”)

The Corporate Tax Association (CTA) welcomes the opportunity to make a submission on the Treasury consultation paper on the incorporation of the latest OECD transfer pricing guidelines contained in the 2015 OECD Report into Australia’s transfer pricing architecture.

In what follows we address the four consultation questions posed in the consultation paper.

1 Would there be any significant unintended consequences for Australia in adopting the 2015 OECD report?

We do not see any significant unintended consequences for Australia in adopting the 2015 OECD report as long as the 2015 OECD report has prospective operation and provides sufficient time for taxpayers and the ATO to consider the implications in the context of other changes on the BEPS agenda that are currently in the process of being implemented.

2 Are there any significant challenges with commencing the new guidance for income years starting on or after 1 July 2016?

In our view the implementation of the 2015 report should be deferred until the income year commencing on or after 1 January 2017 to enable taxpayers the necessary time to put in place processes to review the specific impact of the 2015 OECD report as well as implement other BEPS and transparency initiatives currently in train.

Challenges exist in having the 2015 OECD guidance operative for income years that commence on or after 1 July 2016, ostensibly due to the extremely short time frame for groups to determine if current arrangements may be impacted.

We note that the consultation paper indicates that the effective introduction of 2010 OECD guidelines was introduced in a relatively short time frame after Royal

Assent and that this is a reasonable rationale for the early introduction of the 2015 OECD report. Although the introduction of Subdivision 815-B appears on its face to have had a relatively quick transition date, it should be borne in mind that the transitional rules in Subdivision 815-A effectively referenced back to existing OECD guidelines, including the 2010 OECD report which were known to exist for at least 2 years prior to their incorporation into our law. As mentioned in the Explanatory Material accompanying the introduction of Subdivision 815-A “the long standing administrative practice has been to apply Australia’s transfer pricing rules in accordance with the relevant OECD guidance”. (Refer to the comparison table of key features of new law and current law at page 17 of the EM at http://www.austlii.edu.au/au/legis/cth/bill_em/tlatpb12012518/memo_0.html). In our view the introduction of the 2015 OECD report is a very different set of circumstances than applying back in 2012 and 2013 when the 2010 OECD guidance were part of long standing administrative practice. It was widely known to taxpayers and the ATO that the 2010 OECD guidelines were effectively operative well before they were formally adopted as part of our rules as from 29 June 2013.

Additionally we note that there is a significant level of activity in the BEPS/tax transparency space that is still in the process of being implemented and adding to the existing compliance burden in the current environment needs to be seriously considered, in particular:

- Some large corporate groups are in the process of implementing Country by Country reporting with effect for years commencing on or after 1 January 2016, which includes the requirement to develop Country by Country reports and master files. Many have commenced or are in the process of commencing the collation of the required system changes to meet these requirements and resources are stretched.
- Moreover, documentary support and technical specifications for Country by Country local files in particular still needs to be settled. At present high level design guidance material is yet to be finalised by the ATO and we believe the interaction of the requirements of the 2015 OECD report should be analysed by the ATO and taxpayers in order to influence the final design requirements.
- Specific work needs to be undertaken to understand the interaction of the proposed simplified model for low value adding intra-group services in the 2015 OECD report with what is currently published by the ATO in relation to documentation safe harbours for intra-group services. In essence the 2015 OECD report indicates a simplified approach to documentation for low value adding intra-group services at effectively a 5% mark-up over costs, regardless of company size or other financial attributes whereas current ATO documentation simplification measures appears to severely restrict the operation of one of the key recommendations in the 2015 OECD report by effectively having a 5% mark-up only apply to a limited range of management and administration services.

See: https://www.ato.gov.au/Business/International-tax-for-business/In-detail/Transfer-pricing/Simplifying-transfer-pricing-record-keeping/?page=6#Intra_group_services

- Corporates are also currently awaiting the outcome of the Board of Tax recommendations and implementation of the voluntary tax transparency code which is mooted to apply from 1 July 2016 for most large taxpayers.

3 Are there any reasons why regulation (as opposed to legislative amendment) is not the appropriate method to incorporate the 2015 OECD report

No

4 What new ATO guidance will the ATO need to prepare and what existing guidance will need to be updated if the changes in the 2015 OECD report are adopted?

Currently the ATO are working on guidance in relation to marketing hubs which to some degree may be impacted or influenced by the 2015 OECD report dealing with intangibles. We would encourage this work and work in relation to the interaction of the low value intra group services and current transfer pricing documentation requirements (mentioned above) be given the highest priority.

To some degree all existing ATO guidance on the implementation of Division 815 is currently being reviewed by ATO officers as part of the work previously undertaken by the ATO Division 815 Technical Working Group and we would encourage and anticipate that work (and consultation thereon) will factor in the impact of the 2015 OECD report.

Other issues

We note that the consultation paper does not at this stage propose any change to Australia's transfer pricing rules in relation to permanent establishments (contained in subdivision 815-C of the ITAA 1997).

The 2010 OECD report on the Attribution of Profits to Permanent Establishments (2010 PE Report) follows a two-tier approach in considering the arm's length principle in the Head office-Branch relationship, called the "Authorized OECD Approach" ("AOA"). In our view the incorporation of the 2010 PE Report into Subdivision 815-C would greatly reduce the uncertainty for financial services businesses in particular and align Australia's rules with best international practice.

In addition, many of the revisions and further guidance in the 2015 OECD report aligns with the approach in the 2010 PE Report. Specifically the 2015

OECD report and 2010 PE report focus on ensuring that transfer pricing analysis is based on an accurate delineation of what the associated enterprises actually contribute.

We therefore ask that Treasury consider including the 2010 PE report as a guidance document in subdivision 815-C as it would reduce uncertainty and provide a more consistent approach to transfer pricing treatment of PEs and subsidiaries.

Should you have any questions in relation to the above, please contact me on (03) 9600 4411.

Regards

A handwritten signature in black ink, appearing to read "Paul Suppree". The signature is fluid and cursive, with the first name "Paul" and last name "Suppree" clearly distinguishable.

Paul Suppree
Assistant Director