Views on the implementation of Diverted Profit Tax

Conceptually it is a step in right direction however I visualise followings issues around the implementation of this tax.

a) This tax is being proposed on transaction(s) which results 80% reduction in the tax liability. It is not clear whether the comparison will be made on individual type of transaction or the combined effect of all transactions with a related entity. For example, if an entity has Australian turnover of $500 million and wants to divert $150 million from Australian profit. It may divert this amount in following way with capturing the provisions of DPT on few transactions only.

Type 1	Australian tax	Foreign jurisdiction tax	Difference	% mismatch
Interest	$10 million	$6 million	$4 million	60%
Management fee	$40 million	$33	$7 million	82.5%
Royalty	$100 million	$81	$19 million	81%

In accordance with the proposed legislation it seems that only first transaction of interest will be caught by DPT provisions and DPT would be just $1.6 million (40% of $4 million) whereas total saving in these three transactions to the company would be $30 million.

b) It is not clear from this paper how this tax will operate if a foreign jurisdiction starts applying a higher income tax however start offering a tax credits for income from foreign jurisdictions.

c) The ATO would be hard pressed to collect information to prove that transactions were designed to secure the tax deduction for insufficient economic substance test.

d) There would be some transactions where in spite of an effective tax mismatch the taxpayer might able to prove a reasonable economic substance. Example a head company may lend to its subsidiary company with borrowing cost + reasonable percentage loading. Reasonable percentage of loading is very subjective and will have different parameters depending on the circumstances.

Hope this submission would be of your interest and will help in drafting the final legislation.

Regards

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