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International Tax and Treaties Division  
The Treasury  
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Our ref ED Submission 12 April 2012

Contact Anthony Seve (02 9335 8728)

13 April 2012

Dear Lisa

### **Submission on Exposure Draft of proposed retrospective transfer pricing amendments**

We appreciate the opportunity to comment on the Exposure Draft of *Tax Laws Amendment (2012 Measures No.3) Bill 2012: Cross-border transfer pricing* proposing amendments to Australia's domestic transfer pricing rules (the ED) and accompanying draft Explanatory Memorandum (the EM) which were released on 16 March 2012.

KPMG has played a significant role in drafting submissions both for the Institute of Chartered Accountants in Australia and The Tax Institute and supports the issues raised in these submissions. Our intention in providing this submission is to highlight our key areas of concern.

#### **Key areas of concern**

Our key areas of concern with the ED and accompanying EM are the following:

##### ***Retrospective application***

- The proposal to make subdivision 815-A retrospective to years of income commencing on or after 1 July 2004 in circumstances which could materially disadvantage taxpayers.
- We believe the effect of the proposed amendments goes beyond a simple clarification of the law, but provides the Commissioner of Taxation (Commissioner) with additional taxing powers.

##### ***Reconstruction power***

- In general terms, the provision of a retrospective reconstruction power being provided to the Commissioner under subdivision 815-A. More specifically:
  - Any reconstruction powers should apply to the most exceptional of circumstances such that these powers would have limited potential application. This position is advanced by the OECD Transfer Pricing Guidelines. As such, given the limited potential

application, this power should be excluded in full from subdivision 815-A to avoid confusion for taxpayers and the Australian Taxation Office (“ATO”);

- To the extent that reconstruction powers are not excluded in totality, we are of the view that subdivision 815-A should not be modified by way of partial amendments in relation to this matter, as there is a real risk that such amendments could inadvertently alter the law in favour of the ATO, rather than clarifying the existing law (in line with the stated objectives of the Treasury);
- In contrast, the Commissioner’s ability to amend assessments on a prospective basis in reliance on a new reconstruction power should be strictly and expressly limited in the “phase two” prospective ED.

### ***Characterisation of adjustments***

- The absence of the Commissioner being required to provide taxpayers with details of how any adjustments to taxable income, tax losses, or net capital have been established once a determination under section 815-30(1) has been made. This lack of transparency is not consistent with principles of good tax policy development or good tax administration.
- In particular, we submit that this position, if not amended, may cause significant issues in relation to:
  - Characterising adjustments so as to efficiently address double tax issues under a Mutual Agreement Procedure;
  - Characterising adjustments that might otherwise not be assessable under other parts of the Income Tax Legislation; and
  - Characterising adjustments for other purposes including Australian customs duty.

### ***Carried forward losses***

- The absence of a mechanism by which taxpayers can use any carry-forward losses that are available to them under section 36-17 ITAA 1997 to offset against an additional amount of taxable income that has been determined under subsection 815-30(1)(a) for a particular year of income.

### ***Thin capitalisation***

- That proposed subsections 815-22(4) and (5), which seek to give legislative effect to the ATO’s position in TR 2010/7 with respect to the interaction between the thin capitalisation rules in Division 820 and the transfer pricing rules, do not necessarily achieve the desired policy intent as articulated in TR 2010/7.
- In particular, the requirements to analyse the commercial outcome of the financing transaction as part of an initial step in the thin capitalisation analysis is not in line with the position outlined in TR 2010/7 which requires such analysis in more limited circumstances only.

***Penalties***

- The failure of the ED to make it clear that administrative penalties under Division 284 are limited. That is, penalties cannot be imposed on taxpayers following the issuing of an Amended Assessment in reliance upon Subdivision 815-A of an amount greater than the amount that might reasonably have been expected to have been imposed by way of an Amended Assessment made in reliance upon Division 13.

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We would appreciate discussing these and any other issues relevant to the ED and the EM with you and your team throughout the ongoing consultation process. In this regard please feel free to call us at any time.

Yours faithfully



Anthony Seve  
Partner



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Director