Minerals Council of Australia

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Submission to issues paper: 'Implications of the Modern Global Economy for the Taxation of Multinational Enterprises'

The Minerals Council of Australia (MCA) welcomes the opportunity to comment on Treasury's issues paper on risks to Australia's corporate tax base posed by profit shifting and the current international tax rules.

The MCA is the peak industry organisation representing Australia's exploration, mining and minerals processing industry, nationally and internationally. MCA member companies produce more than 85 per cent of the nation's annual minerals output and account for more than 50 per cent of Australia's exports. MCA member companies pay over $20 billion in tax to the Federal and State governments.

The current debate and focus by the OECD on international tax reform is appropriate given changes in the global economy and fast paced technological changes that have occurred since the current framework was put in place.

Much of the recent debate has been driven by recent high profile examples of complex arrangements by certain US based multinationals.

Australia has a strong regime to protect the integrity of the tax system. Jurisdictions in which concerns about certain structures have been raised (e.g. the 'Double Irish Dutch Sandwich') do not have the same integrity and business tax rules in place as Australia to deal with tax transfers and deferrals offshore.

It is the MCA's view that evidence of base erosion and profit shifting in Australia presented in the issues paper is not persuasive.

Throughout the debate and consideration of the need for changes to Australia's tax regime, it is important that Australia's tax system is competitive. There will always be differences in tax regimes between jurisdictions, and there will also be competition between countries to attract investment. The challenge for Australia is in ensuring continuous improvement to ensure Australia has a competitive tax system that does not impede foreign investment or offshore expansion of Australian companies balanced with appropriate integrity measures.

It is with this in mind that consideration of any changes to Australia's tax regime should be made.

Australia's international tax rules

Australia's rules tax rules must strike a balance between **effectively** countering tax deferral and unnecessarily inhibiting Australian business from competing globally.

In guiding Government' consideration of changes to address any integrity concerns, it is vital that Governments have particular regard to the principles of good taxation – efficiency, equity and certainty. Underpinning these principles in the context of international taxation is the basic principle of ensuring there are not instances of double taxation.

Australia has been at the forefront of efforts to target international tax avoidance and evasion practices – particularly in recent years through a number of Taxation Information Exchange Agreements (TIEA) entered into with new jurisdictions. Australia demonstrated leadership by only providing the concessional withholding tax rate on payments from Australian Managed Investment Trusts to non-residents in countries that have entered into TIEAs with Australia. This comes on top of Australia's disciplined approach to tax treaties.

Australia has a strict anti-tax deferral regime and existing measures, most of which are stronger than comparable jurisdictions, which operate to restrict excessive debt deductions in Australia. These include Australia's comprehensive transfer pricing, thin capitalisation, general anti-avoidance and controlled foreign company anti-deferral rules.

This regime has recently been tightened further - ahead of the OECD action plan - through reforms to Part IVA and the transfer pricing provisions. Additional proposals were announced in the recent Budget to further restrict Australia's thin capitalisation regime, tighten the type of financial instruments eligible for the non-portfolio dividend exemption and repeal the provision providing a tax deduction for interest costs incurred in gaining non portfolio dividend income. These changes and announcements relate to four of the five 'key pressure areas' identified in the issues paper for early action.

It is important that these, and any further changes, are grounded in real evidence of the need for changes. Australia must balance the need for investment with risk to revenue.

Regarding more comprehensive structural reform of the international tax rules, updating tax treaties, and measures such as limiting concessional withholding rates to countries with which Australia has entered an TIEA will do more to address the issue of tax havens than imposing more compliance costs, complexity and unnecessary tightening of Australia's existing rules.

Evidence of BEPS in Australia

The arguments put in the issues paper as evidence of base erosion due to profit shifting practices in Australia do not make for a particularly strong case.

The paper notes that evidence of transfers offshore may be found in the lower than expected company tax take since the Global Financial Crisis (GFC). Taking the issues paper's point that 2011-12 tax collections remain below that expected pre GFC while gross business profits have recovered to the level expected before the crisis, this can be attributed to the well-publicised reasons currently being debated around revenue forecasts. Treasury has noted in recent days that structural changes that have taken place in the economy since the GFC have affected nominal GDP growth and revenue. A consequential impact on the corporate tax take is not necessarily evidence of profit shifting.

The paper compares the ratio of company tax paid to net operating surplus to calculate the effective company tax rate. This comparison can give a misleading picture of the tax burden, particularly for industries that are capital intensive and have higher levels of deductions and depreciation. In the case of mining companies, profits have declined since the GFC due to commodity prices and the large pipeline of investment - which is expected to peak this year. This has resulted in corresponding deductions for capital expenditure against income. The fact that the aggregate effective rate of company tax may be 3 per cent lower than the statutory rate is likely to be at

least partly attributable to deductions during an unprecedented period of resources investment. Treasury has acknowledged this most recently in a speech by Secretary Martin Parkinson.

Chart 4 in the issues paper shows that company tax to net operating surplus has been below the statutory rate of company tax for most of the last 20 years apart from three brief periods that correlate to times of particularly high corporate profits. This is because the tax base includes deductions for depreciation and any number of policy decisions on the tax base – it is no indication of base erosion be it due to profit shifting or some other reason.

A more accurate measure of the tax burden is tax paid compared to taxable income. In the case of mining companies, the latest available data in the ATO 'Taxation Statistics', shows that in 2010-11 the mining industry paid an effective tax rate of 28 per cent. This accounts for deductions for depreciation and capital investment demonstrating the high level of tax paid in Australia. It should be noted that this does not include the large amount of royalties paid by the mining industry to the States. The data also shows that the mining industry paid $14 billion in tax - the second biggest contributor to corporate tax in Australia (23% of total) in 2010-11.

The use of ABS data on intellectual property charges also does not provide evidence of profit shifting in Australia. As the paper itself acknowledges, the amount of intellectual charges paid is small and has been relatively constant as a share of GDP over the last ten years. The fact that intellectual property charges paid to non-residents might have trended down very slightly since the GFC, while royalty withholding tax paid was steady, does not suggest much, if anything.

The MCA does not support the issues paper's conclusion that these are indicators of base erosion and profit shifting in Australia.

As already noted, Australia has a strict anti-tax deferral regime. The Government has address perceived flaws in Australia's transfer pricing laws through the introduction of Division 815-A.

Data collection on Australia's corporate tax system

The Government's proposal to increase transparency by publishing income and tax paid by large corporate entities has not been backed up by any evidence that suggests it would encourage taxation compliance.

The MCA has made a submission on the proposal to publish income and tax paid by business as part of the Government's efforts to 'improve transparency' in Australia's business tax system, noting that if not done carefully, the release of taxpayer information can provide misleading information from which incorrect conclusions could be drawn by the public and policy makers.

Further, a number of companies already publicly disclose taxation information and tax data is publicly available through the ATO's 'Taxation Statistics' publication. Companies also disclose extensive taxation information, including information regarding international related party dealings, as part of the annual income tax return lodgement program.

Requiring that companies provide further information to enable an assessment of the extent of base erosion and profit shifting in Australia would increase compliance costs, significantly for large multinationals in particular. A fair and reasonable balance needs to be achieved between the additional compliance burden imposed and the benefit achieved.

Conclusion

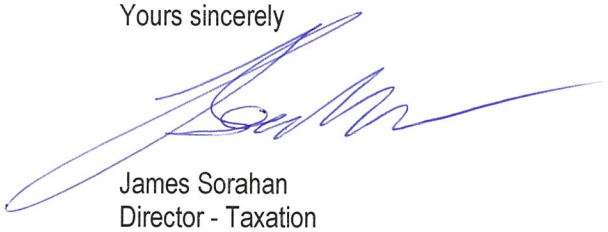
Australia's existing regime is strong and there is little evidence of any significant profit shifting problem in Australia.

Despite this, Australia is right to remain vigilant and encourage a comprehensive co-ordinated approach by jurisdictions to target tax avoidance and evasion through profit shifting and ensure Australia's tax laws are adequate to deal with profit shifting.

Any tax policy response to perceived BEPS risks should be both measured and targeted. In this regard, a tax policy response to BEPS should be distinguished from a compliance enforcement response or a transparency response that is designed to enforce and promote compliance with existing tax laws.

The MCA appreciates the opportunity to provide these comments to the Treasury. Should you require any further explanation of the issues raised in this submission, please contact me (James.Sorahan@minerals.org.au or 02 6233 0651).

Yours sincerely



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