RULE OF LAW
INSTITUTE OF AUSTRALIA

Level 4, 131 Macquarie Street
Sydney, New South Wales
Australia 2000
Telephone: (02) 9251 8000
Fax: (02) 9251 5788
www.ruleoflaw.org.au

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General Manager
Tax System Division
The Treasury
Langton Crescent
PARKES ACT 2600

Dear Sirs

IMPROVING THE TRANSPARENCY OF AUSTRALIA'S BUSINESS TAX SYSTEM - SUBMISSION

The Rule of Law Institute of Australia (RoLIA) was founded in 2009. It is an independent not-for-profit body formed to uphold the rule of law in Australia. RoLIA aims to promote discussion on, to raise awareness of, and encourage active adherence to, the principles which underpin the rule of law.

RoLIA welcomes the opportunity to provide a submission on the discussion paper *Improving the Transparency of Australia's Business Tax System* issued by the Treasury in April 2013, set out in the enclosed Submission.

Thank you for considering this Submission to the discussion paper and the fundamental rule of law issues which arise.

We would value the opportunity to discuss the issues further with you.

Kind regards,

Kate Burns
Chief Executive Officer

IMPROVING THE TRANSPARENCY OF AUSTRALIA'S BUSINESS TAX SYSTEM – DISCUSSION PAPER

RULE OF LAW INSTITUTE OF AUSTRALIA

SUBMISSION

The *Improving the Transparency of Australia's Business Tax System* discussion paper released by Treasury in April 2013 (discussion paper) sets out three broad proposals to improve the transparency of Australia's business tax system. This submission focuses on the first proposal set out in the discussion paper - disclosing the identity and tax payable information of certain large and multinational businesses.

Summary

The Rule of Law Institute of Australia considers the proposed disclosure laws set out in the discussion paper breach fundamental rule of law principles – the proposed disclosure laws in the name of "transparency" are intended to "name and shame" a certain group of taxpayers and are discriminatory.

Only a small group of taxpayers will be subject to disclosure, all other taxpayers will be subject to non-disclosure.

This small group will be discriminated against notwithstanding having duly observed the tax laws.

It is easy to pick on multinationals and large companies but the same objections would exist if, in the name of "transparency", the proposed information to be disclosed related only to people of Greek heritage, or another race living in Australia, and no one else.

It is submitted that the proposed disclosure laws will not result in the stated objective, but instead will serve to put the targeted entities to undue, uninformed scrutiny and resulting cost, without genuinely improving the transparency of Australia's business tax system nor engendering genuine debate about those taxes for large corporate taxpayers.

The Institute certainly favours multinationals and large companies paying their fair share of Australian tax but the proposed disclosed laws are not the answer. What is required is amendments to the tax laws to ensure this occurs.

Fundamental Principals of The Rule of Law in Australia

It is a well established principle of good government in Australia that Australia's laws, including tax laws, should be subject to and accord with the principles of the rule of law. A fundamental aspect of the rule of law is the principle that laws should not target certain classes of persons unfairly or

unjustly. Rather, the tax laws of the country should apply equally to all taxpayers and not be oppressive, unjust, or discriminatory.

The Objective of the Discussion Paper

The stated objective of the proposed disclosure laws set out in the discussion paper is to "enable the public to better understand the corporate tax system and engage in tax debates, as well as to discourage aggressive tax minimisation practices by large corporate entities."

There has been much debate and review of the Australian tax system in recent times – including the Ralph Review of Business Taxation (1999) in the Review of Australia's Future Tax System (2010), the Australian Tax Forum (2011), and the various reviews conducted by the Board of Taxation. Those reviews have each generated significant public discussion of Australia's business tax system in a discursive, inclusive way.

In speeches at the Australian Tax Forum in 2011, the then-Assistant Treasurer Mr Bill Shorten described Australia's tax system as "better than most of our contemporary societies." He went on to say "we are having, I believe, a sophisticated, sensible, informed and gentle conversation about the future of our tax system which is a testament to the truth that we understand that Australia is doing pretty well by global comparisons."

Open and constructive discussion and debate about Australia's business tax system is desirable and welcomed, and discouraging aggressive tax minimisation practices is important. However, RoLIA strongly objects to the proposed disclosure laws as they have been propounded in the discussion paper, as they are fundamentally inconsistent with the rule of law and the principles of equality and generality, and it is considered will not result in that sensible, informed conversation about the Australian tax system, or necessarily discourage aggressive tax minimisaiton. In particular, the proposed disclosure laws:

- discriminate between taxpayers;
- result in disclosures that are likely to mislead and not inform the general public;
- will not achieve the stated policy objectives of generating tax policy debate, but rather will create a power imbalance between the general public and the disclosing entities by a "naming and shaming" in the media without giving the disclosing entities a proper recourse to justify and explain the tax disclosures; and
- impose unnecessary compliance burden without any demonstrable or real benefit to the government or community.

Each of these issues are discussed below.

1. Discrimination between different classes of taxpayers

"Corporate tax entities" whose gross income (gross *accounting* income – discussed further at 2 below) is $100 million or more would be captured by and subject to the proposed disclosure laws.

The result is a gross inequity which discriminates against and segregates only certain "large" taxpayers from other taxpayers, and subjects them to a higher level of public scrutiny and disclosure compared to other taxpayers, purely based on the quantum of its revenue in a particular year.

The proposed disclosure laws will apply only to 'corporate tax entities', and not to trusts (which are not 'public trading trusts' or 'corporate unit trusts') or partnerships (which are not 'corporate limited partnerships'). The increased public disclosure and resulting scrutiny will thus apply only to such corporate tax entities – in most cases companies – which have total income in a year exceeding the stated threshold. This approach clearly discriminates against those companies, as against other forms of business entity as against entities with a lower gross revenue subjecting them to a different level of scrutiny, public disclosure, and resulting burden (discussed at 4 below) that other taxpayers are not subjected to.

The measure of total accounting revenue for a period has no regard to the true economic position of a company. For instance, if Company A has $101 million in gross income but has $99 million in expenses, it would be subject to the tax disclosure rules. However, Company B may have $99 million in gross income but only $50 million in expenses and have a greater market share than Company A, but it would not be subject to the proposed disclosure laws. Company B may have a stronger financial position and performance, and larger market share than Company A, Company B may engage in "aggressive tax minimisation practices" while Company A does not, and discussion of Company B's overall tax position may be more illuminating than that of Company A, yet it is Company A's tax return information that would be disclosed.

Those businesses operated through trusts or partnerships, or a lower gross revenue, will be at a competitive advantage to companies – not facing the same disclosure burden and resulting public scrutiny and cost.

The proposed disclosure rules also discriminate against privately owned corporations. The proposed disclosure laws are generally discussed in respect of multinational, widely held public companies, or subsidiaries of such companies. There are however a number of corporate tax entities in Australia whose gross accounting income will or may exceed the $100 million threshold – which are private companies whose shareholders are individuals, families or small family groups. For those private companies, disclosing the income and tax information of the corporation is tantamount to publishing the financial and tax position of the individual shareholders, or family group shareholders, particularly where they are high profile individuals or companies, and closely connected with the operations of the company.

Such individual shareholders would be at high risk of excessive public scrutiny and effective disclosure of their personal income and tax information, which is well beyond the stated intention of the proposed law.

The proposed disclosure laws fundamentally breach the principles of the rule of law - they will by their very design discriminate between entities and taxpayers in a way that can result in effectively disclosing certain tax information of individual shareholders of successful corporations, and discriminating between taxpayers entities of different types and different income levels.

2. Disclosures will mislead and not inform

The proposed disclosure laws would require the Commissioner of Taxation to publish the name and Australian Business Number of the targeted taxpayers, their reported "total income", their "taxable income" and their Australian income tax payable.

Reported "total income" is said to be the gross accounting income already disclosed in the entity's income tax return. An entity's gross accounting income is merely one component of the total financial performance of an entity, it is a recording of gross receipts and other income items and including complicated and abstract notional accounting items, and does not take into account, amongst other things:

- 'notional' accounting income recognition unrelated to actual cash receipts;
- general business and corresponding accounting expenses;
- whether there are any accounting losses;
- whether the income is a consolidated figure for accounting purposes and therefore incorporates various related entities (not just the head company);
- whether any extraordinary, one-off transactions have occurred during the financial year which is not usual revenue of the disclosing entity; and
- the significant and fundamental differences between a gross accounting revenue measure and actual Australian taxable income.

Disclosure of gross revenues alone is not an indicator of the financial performance of an entity, or of its 'tax profile'. The general public would not likely be familiar with specific accounting concepts, and in particular the fact that the gross accounting revenue of a company bears little or no direct relationship to its Australian taxable income, reduced by expenses and related deductions, and specific taxation allowances and rules. Accordingly publication of that amount will serve to mislead readers as to size, operation and performance of the disclosing entity, and especially as to the relationship between that gross revenue amount and actual tax payable under the law.

By only disclosing one aspect of the financial performance of an entity, readers of that information will be readily misled, making their own assumptions (which will almost invariably be incorrect), which does not foster sensible and unimpassioned discussion of Australia's business tax system.

Misleading as to the "tax profile" of disclosing entities

As noted in the discussion paper, the reported gross accounting income of an entity will usually bear little or no direct relationship to that entity's taxable income and tax payable. Gross income for accounting purposes will usually include amounts which are not actually taxable, in accordance with the Income Tax Assessment Acts, such as:

- specific notional deductions (which do not match a physical expense) like depreciation, building allowance, research and development allowance, investment allowance, and so on;
- prior year losses;
- amounts subject to capital gains tax roll-overs;
- items of exempt income, and non-assessable non-exempt income, such as dividends received from previously taxed attributed income of a foreign subsidiary; and
- income which is taxable but on which tax has been paid in another country, for which a credit is allowed in Australia.

Taxable income of a taxpayer entity is calculated according to the specific and prescriptive provisions of the Tax Acts. The amount of tax payable is the taxable income determined in accordance with those provisions, multiplied by the tax rate, less any taxes withheld and tax offsets. All these are specific tax terms which are determined under the voluminous and highly detailed tax legislation and bodies of case law. They are complex tax concepts which the general public may find difficult to understand without a complete and open description. The proposed disclosure laws will not elucidate any of those concepts, but are apt to cause only more confusion by attempting to relate Australian tax payable to a company's gross accounting income.

Without having a proper understanding of the tax concepts which determine taxable income and tax payable, the general public cannot appreciate nor properly assess the tax profile of the disclosing entity, particularly when they are given only a gross accounting revenue comparison.

Merely disclosing the taxable income and tax payable by a company in a vacuum, absent any other supporting information, does not properly or accurately present the tax profile of a disclosing entity. Instead, it can seriously risk misleading the general public particular where these figures would be disclosed alongside the reportable gross income amount.

It is therefore impossible to gauge the true tax profile of the disclosing entity in order to stimulate any sensible discussion on Australian tax practices and policies. It is considered that this would lead to the general public speculating, in absence of any real information, and thus generating harsh public scrutiny of the disclosing entities rather than genuine tax debates – a resulting 'name and

shame' in the press, with public outcry, where Australian tax payable does not accord with the public's expectations from the gross total income amount.

3. The proposed disclosure law will not stimulate genuine public debate about tax system design

The proposed disclosure laws targeted will lead to a power imbalance between the general public and the disclosing entities – that is, the general public is given very limited tax information about the disclosing entity, and no explanation of the complex and robust business tax system which results in the actual taxable income and Australian tax payable. There is no provision under the proposal of the information necessary to properly critique and assess tax system design and principles which give rise to the ultimate taxable income and tax payable. The proposed disclosure laws will publish the very limited information, in the form of 'bare' numbers, and do not provide a proper channel through which the disclosing entities can respond or explain the position under the law.

Moreover, it is difficult to conceive how disclosing limited tax information of large entities can generate any useful tax policy debate – the discussion paper certainly does not provide any explanation of this objective. Without reviewing the supporting material on how accounting and tax differences are reconciled and how an entity's taxable income is determined in accordance with the detailed and prescriptive provisions in the Tax Acts, it is impossible to understand any industry trends or practices, how particular taxpayers are applying the tax laws, or how Australia's business tax system is functioning. Disclosing only the accounting revenue, taxable income and tax payable of large entities is grossly insufficient to assess Australia's current tax policies and stimulate any sensible debate.

Simply advertising tax payable figures alongside gross accounting revenues makes no sense as there is no numerical or principal comparison between the two. No genuine tax policy debate can be generated from the disclosure of such amounts, without detailed and comprehensive publication and explanation of the myriad business tax rules which result in the taxable income and tax payable amounts under Australia's world class tax system.

Such bare publication of numbers is not the "sophisticated, sensible, informed, gentle conversation" about tax system design that Mr Shorten described at the Australian Tax Forum. In that speech Mr Shorten also noted that "One thing I think we can do better, and it has been canvassed repeatedly at the various sessions over the last 12 hours or so, is the tax system needs to be better at listening. We need to be more transparent and consistent and improving the governance of the Australian Tax System will substantially assist this process."

Public disclosure, a public "telling", of individual taxpayer's tax payments, is not "listening", it is not transparent, and it is not consistent.

Further, the discussion paper does not explain how the publication of these amounts will discourage aggressive tax minimisation, when those figures are apt to be completely misleading for an entity which has not engaged in any "aggressive tax minimisation practices", let alone one which has. For an entity which has, it may be able to further obfuscate the position in its own publications.

4. Additional compliance burden

Whilst the discussion paper states that the proposed disclosure laws ensure that no additional compliance costs are placed on taxpayers, this will in practice be far from the truth.

Given the public disclosure of the abstract elements an entity's accounting income and taxable income/tax payable, and the resulting high of public scrutiny without any form of explanation or channel for the provision of information to the public to explain those amounts, or the business tax system generally, disclosing entities will be effectively compelled to prepare and publish documents to explain the context of the limited tax information disclosed. This would create onerous work for the disclosing entity's tax division, financial department, and executives to prepare that information, and investor relations/public relations departments in having to respond to public commentary/criticism of the figures disclosed.

The Boards of disclosing entities will have additional disclosure documents to review and consider before publication.

Whilst many corporate tax entities which will be subject to these new rules will also lodge financial reports with the Australian Securities and Investments Commission, those reports are fundamentally different to what will be published by the Commissioner of Taxation without any surrounding explanation. The proposed new tax disclosures will require a different and unique level of additional explanation.

The Rule of Law Institute of Australia estimates that for a large multi-national corporate with business activities in multiple jurisdictions, explanatory reports will likely require up to, or over, twenty pages of detailed and very tax specific tax information and explanation (as seen by similar reports voluntarily produced by a very small number of very large companies). It is considered that the general public is unlikely to actually read so much detailed information, and will revert back to headline – getting 'discrepancies' of gross income to net Australian tax payable, with reputational damage for those disclosing entities highly probable.

The result of the additional burden on those targeted 'large' corporate entities will be to cause the publication of that abstract and incomplete information, with a corresponding burden on the disclosing company to produce an accurate and detailed explanation of the corporate tax system, which despite great care and cost is unfortunately still likely to be ignored or misinterpreted by the general public. It is difficult to see how the proposed disclosure law will genuinely enhance real debate about the design and operation of the business tax system, or reduce any perceived

aggressive tax minimisation, without simply embarrassing the targeted companies with a public 'name and shame' exercise in the press – which is fundamentally abhorrent to the rule of law in Australia.

Conclusion

The proposed disclosure laws are contrary to established and fundamental principles of the rule of law.

It is further difficult to see how the proposed disclosure law will improve transparency of the Australian tax system. The information sought to be published will be too limited, and it would have the effect of creating unnecessary and excessive public scrutiny of only a targeted selection of corporate tax entities, putting them to significant burden and scrutiny, for no revenue raising or discernible tax policy reason.

The proposed disclosed laws are oppressive, unjust and inequitable, and the Rule of Law Institute of Australia considers they should not be progressed.

Yours faithfully

Kate Burns
Chief Executive Officer