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Pillar Two Unit
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Dear Pillar Two Unit

SUBMISSION TO CONSULTATION ON INTERNATIONAL TAXATION - GLOBAL AND DOMESTIC MINIMUM TAX – EXPOSURE DRAFT PRIMARY LEGISLATION

We thank you for the opportunity to provide a submission on the above exposure draft legislation ("**Draft Primary Legislation**") and reiterate our support for the Government's intention to ensure entities pay their fair share of tax.

AIA Australia is a life, health and wellbeing insurer, which is part of the AIA Group (collectively, "AIA"). AIA is headquartered and listed in Hong Kong and operates in 18 markets throughout Asia-Pacific. For more than a century, AIA has provided health and financial protection to millions of people across Asia-Pacific.

As a multinational insurance group with significant operations in Australia, AIA is keenly interested in assisting Treasury to find a balance between the imposition of a minimum effective tax rate of 15% and upholding the advantages of Australia's tax system. The recommendations included in our submission aim at ensuring the implementation of any tax changes is conducted in a manner that continues to provide the certainty and simplicity needed by multinationals enterprises ("**MNEs**") in respect of their affairs and offers competitive conditions for the carrying on of activities in Australia. With respect to the introduction of a global and domestic minimum tax in Australia, we recognise that tax reforms, including the implementation plan, play a crucial role in shaping the economy to meet the Government's objectives.

Although the exposure draft legislation provides that the Australian provisions are to be interpreted in a manner which is consistent with specified OECD documents (including the Global Anti-Base Erosion ("**GloBE**") Model Rules, commentary, agreed administrative guidance and safe harbour rules), these are global rules that are not tailored to the Australian tax system and do not address issues faced by the insurance industry. Our concerns and recommendations on other issues to be considered in an Australian context, and with respect to the insurance industry, are set out below. With that in mind, our feedback will help inform the Australian Taxation Office's ("**ATO**") administrative approach and public advice and guidance on these measures.

1. Deferral of implementation to 2025

The proposed changes are based on the 15% global minimum tax for large multinationals and the 15% domestic minimum tax applying to years commencing on or after 1 January 2024. We share the same concerns as other stakeholders in terms of the time and resources required to comply with these rules, especially with regard to the data points involved to comply (which require system changes and manual interventions).

Allowing more time to prepare for new tax rules is essential for ensuring compliance, reducing risk of errors and promoting an "efficient, fair and sustainable tax system". It also minimises disruption to our core business which is about paying claims for our customers. Given we are now in 2024 and these measures are not yet enacted in law, we recommend deferring the implementation of these new tax rules by at least one year, to:

- Ensure a more successful implementation that minimises the risk of unintended non-compliance, which would in turn impact the revenue collected from the implementation of these rules for the Government
- Foster more trust in the tax system and how it serves the public interest, by allowing taxpayers more time to better understand the new tax rules, comply with the required obligations without unintended disruption to business.

We note deferred implementation has been adopted by with other jurisdictions such as New Zealand, Hong Kong, Malaysia, Singapore and Thailand.

2. Qualified Refundable Tax Credit ("QRTC") based on an insurer's regulatory or economic capital and other QRTCs

In recent years, tax practitioners and policymakers globally, including in Australia, have been focused on the introduction of QRTCs since their treatment under the Model Rules was announced.

The importance of providing tax incentives like QRTCs cannot be overstated: in July, after months of lobbying from the United States, the OECD accepted that similar tax credits introduced under the US Inflation Reduction Act could qualify for the same treatment as QRTCs. These credits are expected to help generate US$3 trillion in investments in the United States over the next 10 years.

More recently, Singapore proposed in its 2024 budget the introduction of a refundable investment credit intended to qualify as a QRTC. The Singapore government anticipates this will significantly enhance Singapore's attractiveness for investments and encourage companies to make sizeable investments that bring substantive economic activities to Singapore.

In the context of Australia having benefitted from "open international markets built on a trusted, rules-based, global trading systems"[1] and the Government's interest in continuing to open the Australian economy to support continued economic growth, we recommend the development of tax incentives in Australia that would qualify as QRTCs. We also recommend a review of existing tax incentives (e.g., an R&D tax offset regime, which serves to encourage innovation and stimulate economic growth by encouraging investment in R&D activities that involve a degree of uncertainty or risk) to determine if they could effectively be replaced with QRTCs.

As a life, health and wellbeing insurer that is committed to helping more people live Healthier, Longer, Better lives, AIA is focused on ensuring people have access to financial protection in the event of death, illness or injury, and is driving a shift in healthcare from treatment to prevention. More broadly, AIA is part of an industry that plays a key role in enhancing Australia's economic resilience and social cohesion by providing financial security to families and individuals in need, thereby reducing reliance on Government assistance.

In this context, we ask that the Government should consider supporting the insurance industry by offering a QRTC based on an Australian insurer's regulatory or economic capital. Work will be needed to determine an appropriate percentage, but the number may not need to be significant to be meaningful for insurers.

From a fiscal standpoint, the provision of incentives like QRTCs can be funded from revenue generated from the introduction of global and domestic minimum tax in Australia. Due to the time required to develop and consult on such tax policy proposals, and considering the announcements made in other jurisdictions, we recommend that the Government begins work on QRTCs now, in parallel with its work on introducing the global and domestic minimum tax in Australia.

3. Consideration of voting rights under the definition of "portfolio shareholding"

[1] See Note 3 - *Intergenerational Report 2023: Australia's future to 2063*. Intergenerational Report 2023 (treasury.gov.au)

Article 10.1.1 of the Model Rules indicates that an "ownership interest" in an entity is an equity interest that must entitle its holder to rights in a share of the *profits, capital or reserves* of that entity. In accordance with this requirement, the rights to exercise votes in an entity alone cannot be regarded as an ownership interest in that entity under Article 10.1.1. Furthermore, Article 10.1.1 defines "portfolio shareholding" as *ownership interests* in an entity that are held by one or more constituent entities of an MNE group and that carry rights to less than 10% of the *profits, capital, reserves, or voting rights* of that entity at the date of distribution or disposition.

As rights to exercise votes in an entity alone do not constitute ownership interests, it appears that an MNE group would be unable to take into account those voting rights in determining the existence of a portfolio shareholding, even in cases where the group held all of the rights to profits, capital, reserves, and votes in aggregate. In our view, the non-consideration of these voting rights in this context is not justified and could have important consequences. For example, an MNE group holding the entirety of the rights to profits, capital, reserves, and votes in an entity may still fail the 10% test and hold a portfolio shareholding in the entity and not be able to avail itself of excluded dividends or equity gains – potentially leading to double taxation. The issue is also particularly important in an Australia investment fund context where the segregation of economic rights and voting rights between different share classes is common in practice.

We note that the United Kingdom's Finance (No. 2) Act 2023 (the "Act") resolves this issue by adding the concept of "qualifying interest" under the definitions of "excluded dividends" and "excluded equity gain or loss" in Sections 141 and 142 of the Act, respectively. For the purpose of these provisions, "qualifying interest" in an entity means a direct ownership interest in the entity or an entitlement to exercise voting rights in relation to the entity. The approach adopted by the United Kingdom therefore ensures that all voting rights held by an MNE group in an entity will be taken into account when determining the amounts of excluded dividends and excluded equity gain or loss of an MNE group for a financial year.

We recommend Australia adopts similar drafting as the UK under its global and domestic minimum tax regime.

4. Aggregation of ownership interests

The OECD commentary on the definition of "portfolio shareholding" implies that the 10% test is applied separately to each class of ownership interest that carries different rights, rather than the MNE group's entire aggregate holding of ownership interests in the entity. This approach could lead to an entity with different share classes being wholly-owned by an MNE group but still through a portfolio shareholding – leading to potential double taxation where dividends or equity gains are not excluded as a result. The issue is also relevant in an Australian investment fund context.

Therefore, we recommend the global and domestic minimum tax regimes make explicit that the 10% test must be applied based on the rights from all ownership interests (or 'qualifying interests' as discussed above) held by constituent entities of the same MNE group in aggregate, irrespective of different rights attaching to different interests. This is consistent with UK's drafting of the Act and we recommend Australia adopts similar drafting.

5. Recharge of 'top-up" tax

When top-up tax is collected outside of the jurisdiction of the entities to whose low-taxed profits it relates, for example under an income inclusion rule or the undertaxed profits rule ("**UTPR**"), for commercial and regulatory reasons, it is likely that a recharge for this tax expense will need to be made by the entity charged with the top-up tax to the entity whose low-taxed profits resulted in the top-up tax. Relevantly, life insurance is a highly regulated industry due to the significant role it plays in the financial wellbeing of individuals, families and the broader economy; this includes regulatory requirements relating to the maintenance of appropriate funds for the purpose of policyholder/consumer protection, which can limit an insurer's ability to bear what effectively are group liabilities. It is not clear how recharges of top-up tax between entities in an MNE group will be treated for accounting purposes or domestic tax purposes in all cases. Further, without specific provision being made for their treatment, they may impact the effective tax rate of a jurisdiction for GloBE purposes, which is circular and undesirable, and there might be differences in accounting or domestic tax treatment of the recharge between the payor and recipient.

Similar recharges could also arise under the domestic minimum tax regime where the domestic minimum top-up tax liability is paid on behalf of the liable entity by another group entity.

The Draft Primary Legislation does not address how such recharges would be treated under the global and domestic minimum tax regimes. Given that these payments would seek to ensure that the entity who created the liability bears the economic burden associated with the liability without altering the application of the global and domestic minimum tax regimes, we recommend that any reimbursement received (under these regimes) should not be treated as a receipt, and the payment made should not be treated as an expense and for Australian income tax purposes.

6. Single top-up tax filing

The adoption of separate tax returns for the global and domestic minimum tax regimes, and a separate filing obligation for the GloBE Information Return ("**GIR**") under "BEPS Pillar Two" is not, in our view, an optimal design choice for the tax reporting regime for these measures and will likely carry additional costs for MNE groups subject to these rules.

Specifically, the introduction of separate filing obligations means that each return will require its own completion, review and approval processes, with the result that more time and resources will likely have to be allocated in practice to the new tax reporting requirements. In our view, it would be more efficient to combine the GIR, and global and domestic minimum tax filing obligations into a single top-up tax return, especially since the filing due date is proposed to be the same across all three documents (i.e., 15 months after the end of a financial year, or 18 months in the case of the transition year).

By comparison, we note that Hong Kong has proposed the introduction of a single top-up tax return covering both Hong Kong's global and domestic minimum tax regimes. For the GIR, the Hong Kong Inland Revenue Department would rely on the information reported in the top-up tax return of a Hong Kong headquartered group and would extract the GIR information from the top-up tax return itself and exchange this information with other relevant jurisdictions which have a qualifying competent authority agreement in place with Hong Kong.

The approach proposed by Hong Kong is, in our view, better adapted to the realities of MNE groups and will have a positive impact on their compliance burden with respect to BEPS Pillar Two.

We strongly recommend that Australia modifies its tax reporting regime for BEPS Pillar Two and introduces a single top-up tax return for these measures.

In summary

We would welcome the opportunity to provide assistance to Treasury in relation to the development of the Draft Primary Legislation in any way that it considers may be helpful. We would also like to express our interest in participating in ATO consultation on the implementation of a global and domestic minimum tax.

Should you wish to discuss any of the issues raised, please contact in the first instance Sarah Phillips, GM Communications and Corporate Affairs, sarah.phillips@aia.com or 0498 494 791.

Yours sincerely

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