

## Tax highlights

15 September 2014

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### Key developments this week

**Large business bulletin – September 2014 – focus on risk:** The ATO's [Large business bulletin](#) for September 2014 provides detail about the ATO's risk approach for the superannuation, banking and finance, insurance, and energy and resources industries. In 2014–15, the main risks the ATO will focus on are:

#### **Banking and finance:**

- Taxation of permanent establishments and attribution issues, including:
  - taxation of global derivate trading businesses
  - the allocation of capital and debt
  - intra-entity interest charges under Part IIIB of *Income Tax Assessment Act 1936* (ITAA 1936)
  - the allocation of expenses in relation to capital management and liquidity requirements, for example, Treasury charges and lines of credit
- Thin capitalisation issues, including the application of the provisions to outward investing authorised deposit-taking institution (ADI) entities that have a conglomerate business with one consolidated tax group
- Transfer pricing, including related-party arrangements associated with outsourcing IT and other services on an inbound and outbound basis. This includes items such as guarantee fees and other credit management arrangements between related entities
- The offshore banking unit (OBU) regime, including issues associated with the allocation of income and expenses, structuring, funding and eligible activities
- Issues related to taxation of financial arrangements (TOFA) and consolidation.

#### **Energy and resources:**

- Transfer pricing, including:
  - intra-group financing and derivatives
  - marketing/procurement and service hubs
  - freight and logistic charges
  - cross-border restructuring activities
  - exit charges for transfer of business activities
  - inbound and outbound technical services
  - commodity pricing, for example, liquid natural gas (LNG) and petroleum pricing
- Financing, including large capital investment cycles with increased levels of debt, derivatives and swaps
- Permanent establishments, including the use of and payment for plant and equipment
- Mergers, acquisitions and divestments

- Losses, including the failure to meet the continuity of ownership test, same business test or recoupment tests
- Research and development tax incentive, including looking at the nature, purpose and timing of the activities conducted
- Exploration expenditure under income tax and petroleum resource rent tax (PRRT)
- Thin capitalisation issues including the proposed new safe harbour threshold, arm's length debt rules and assets revaluations
- PRRT deductible expenditure and starting base
- Other risks, including disposal of mining rights and project pools.

***Life insurance:***

- TOFA, consolidation and Division 320 of the *Income Tax Assessment Act 1997* (ITAA 1997) interaction
- Segregation mechanism under Division 320, including transfer values and annual valuations
- Consolidation treatment of intangible assets and treatment of deferred tax assets
- Foreign investment, foreign exchange (forex) gains/losses and foreign income tax offset (FITO) calculations
- Profit shifting and thin capitalisation safe harbour
- Permanent establishments and attribution – intra-entity derivative transactions or risk transfers

***General insurance:***

- Valuation and documentation of insurance liabilities under Division 321 of the ITAA 1997 for tax purposes
- International taxation of insurance business, including branches, subsidiaries and re-insurance
- Interaction with consolidation and TOFA legislation

***Health insurance:***

- Establishing the income tax treatment of underwriting profits or losses arising from health insurance business, given the scope of the term 'general insurance company' for the purposes of Division 321 of the ITAA 1997
- Transition from non-taxable to taxable status – including Division 57 of Schedule 2D to the ITAA 1936, consolidation issues and demutualisation
- Income tax treatment of overhead expenses attributable to both non-taxable health insurance business and other taxable business within a single economic group

***Managed investment trusts/public unit trusts:***

- Capital account and fund payment withholding rules
- General application of Division 6 of the ITAA 1936
- Treatment of trust distribution amounts in excess of the net income

***Superannuation industry:***

- New, unusual or significant transactions, such as large infrastructure investment and mergers
- Exempt current pension income claims
- Correct tax treatment of expenses, including those arising from changes to the super industry environment, such as SuperStream and merger costs
- Over-claiming of imputation credits

- Tax treatment of offshore investments, including limited partnerships
- The application of the FITO limit to hedging transactions
- Capital gains reporting and capital loss utilisation
- Tax treatment of repurchase and securities lending arrangements
- Tax deferrals from the pay as you go (PAYG) instalment system.

The *Large Business Bulletin* also discusses the future of the ATO risk-differentiation framework.

**Federation White Paper – Release of First Issues Paper:** On 12 September 2014 the first [issues paper](#) to inform the White Paper on the Reform of the Federation was released.

The process of reform will be as follows:

- Five issues papers will be published in the second half of 2014. These will include the paper above on informing the White Paper (1), roles and responsibilities in respect of health (2), education (3), housing and homelessness (4) and issues with federal financial relations (5).
- A Green Paper setting out options for reform will be published in the first half of 2015
- The White Paper will be released towards the end of 2015.

The White Paper aims to clarify roles and responsibilities to ensure that, as far as possible, the States and Territories are sovereign in their own sphere. The objective will be to:

- Reduce and end, as far as possible, the waste, duplication and second guessing between different levels of government;
- Achieve a more efficient and effective federation, and in so doing, improve national productivity;
- Make interacting with government simpler for citizens;
- Ensure our federal system:
  - a. Is better understood and valued by Australians (and the case for reform supported);
  - b. Has clearer allocation of roles and responsibilities;
  - c. Enhances governments' autonomy, flexibility and political accountability; and
  - d. Supports Australia's economic growth and international competitiveness.

This paper will consider the following matters:

- Values and goals that should underpin the Federation so it becomes more efficient and drives national productivity
- Principles and criteria to be applied when allocating roles and responsibilities between different levels of government
- Practical application of principles in the allocation of roles and responsibilities
- How to address the issue of State governments raising insufficient revenues from their own sources to finance their spending responsibilities
- The most appropriate approach for ensuring that horizontal fiscal equalisation does not result in individual jurisdictions being disadvantaged
- Effectiveness and governance of the current Intergovernmental Agreement on Federal Financial Relations
- Improvements to the Council of Australian Governments (COAG)
- Performance reporting, transparency and data arrangements

The Federation White Paper will be closely aligned with the White Paper on the Reform of Australia's

Tax System. The White Paper will also draw on any relevant findings and recommendations of the Commission of Audit and other White Papers and review processes currently underway.

**MRRT repeal – proclamation date:** As reported last week, the legislation to repeal the Minerals Resource Rent Tax (MRRT) and to repeal or rephase measures that were intended to be funded by expected MRRT revenue such as the company loss carry-back rules, capital allowance concessions for small business and increases in the superannuation guarantee charge percentage ( [Minerals Resource Rent Tax Repeal and Other Measures Act 2014](#) ), received Royal Assent on 5 September 2014. The legislation provided that the schedules for the repeal of the MRRT and certain other measures in the Bill would commence on the earlier of a date fixed by proclamation or twelve months after the date of Royal Assent. On 9 September 2014, the Government [announced](#) that it will be recommending to the Governor-General that he affix by proclamation, 30 September 2014 as the relevant commencement date. As a result, the following measures will have the following dates of effect for most taxpayers:

- Abolition of the mining tax from 1 October 2014 (with taxpayers final MRRT year (even if it is a part year) ending on 30 September 2014)
- Abolition of the company loss carry-back from 1 July 2013
- Reduction of the instant asset write-off from 1 January 2014
- Abolition of accelerated depreciation for motor vehicles from 1 January 2014, and
- Abolition of geothermal energy concessions from 1 July 2014.

In response, the ATO has also issued a [media release](#) setting out its administrative approach. The ATO will waive all penalties and interest in cases where taxpayers have chosen not to prepare their returns on the basis of the Government's announcement of relevant measures if they seek to have their income tax assessments amended within a reasonable time.

For further information about the implications for the MRRT, please refer to our article in [Tax highlights 8 September 2014](#) titled "MRRT – Residual compliance obligations"

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## **Business tax**

**Revised ATO access policy – corporate board documents:** The ATO has released a revised version of Practice Statement [PS LA 2004/14](#) (Access to 'corporate board documents on tax compliance risk'). Under the revised PS LA 2004/14, advice prepared for a corporate board on tax compliance risk should, in all but exceptional circumstances, remain within the confidence of a board of company directors. The ATO has extended this concession to cover minutes of board discussions on tax risk and tax risk registers. However, this concession applies only to companies that can demonstrate that they have tax risk management and governance frameworks in place.

**ATO has released minutes from NTLG meeting:** On 11 September 2014 the ATO released the [minutes](#) from the National Tax Liaison Group meeting held on 19 June 2014. Agenda items for this meeting were broadly focused around:

- Issues of significance in the tax law interpretation, policy and law design space
- Reinventing the ATO with plans to shape customer experience and interactions
- Strategic ATO initiatives such as revision of the risk differentiation framework for high wealth individuals and ATO's current consultation arrangements
- ATO input into tax policy and law design processes and approach to test case litigation,

compliance matters, tax transparency measures and current operation of NTLG.  
The next NTLG meeting will be held on 18 September 2014.

**ATO 2013 Annual Report – public hearing transcript:** The [transcript](#) of the public hearing held on 27 August 2014 by the House of Representatives Standing Committee on Tax and Revenue's inquiry into the ATO's 2013 Annual Report, has been released. Topics covered at the hearing included progress on the Reinventing the ATO program, an update on the overseas voluntary disclosure initiative, consultation processes and the cash economy. As well, the Commissioner indicated that the consultation process run by Treasury on section 25-90 of the *Income Tax Assessment Act 1997* has been completed and advice has been provided to the Government, although a decision is yet to be made.

**BCA releases tax reform discussion paper:** On 11 September 2014, the Business Council of Australia (BCA) released a discussion paper: [The Future of Tax: Australia's Current Tax System](#) which is the first in a series of papers that the BCA will release in the lead-up to the Commonwealth Government's tax white paper reform process.

The discussion paper broadly outlines:

- Why tax reform matters for Australia's future prosperity
- The characteristics of the current tax system
- Some future directions for reform
- Some fundamental matters for the upcoming tax white paper process.

**Financial System Inquiry deliverables:** At the ANZ Economic Leadership Luncheon on 5 September 2014, the Treasurer [announced](#) that the final report on the Financial System Inquiry which is expected to be delivered to the Government in November 2014, will be released publicly "relatively immediately" and put to consultation again to report back by March to April 2015.

**FATCA – links to key information:** The ATO has [updated](#) its website with links to key information on the US Internal Revenue Service (IRS), US Department of Treasury, Australian Treasury and ATO websites concerning the US *Foreign Account Tax Compliance Act* (FATCA). FATCA was enacted by the United States Congress to improve compliance with US tax laws and imposes certain due diligence and reporting obligations on foreign (non-US) financial institutions, including Australian institutions. These institutions will be required to report to the US IRS information on US citizens with financial accounts.

**Effective life review – coal seam gas extraction industry:** The ATO is [seeking](#) industry participation in a review of assets used in the coal seam gas extraction industry in order to make new effective life determinations for tax depreciation purposes.

**ATO Rulings Program updated – FBT and PRRT:** The ATO has updated its Public Rulings Program [as at 5 September 2014](#). There has been little change from the last update of the Rulings Program regarding draft and final rulings to issue within the next two months apart from the following:

- Draft tax determination – Fringe benefits tax (FBT): When are the duties of an employee of a government body exclusively performed in, or in connection with, a public or non-profit hospital for the purposes of section 57A(2) of the *Fringe Benefits Tax Assessment Act 1986*? Planned issue date 29 October 2014
- Final tax ruling – Petroleum resource rent tax (PRRT): What does 'involved in or in connection with exploration for petroleum' mean? Planned issue date had been 26 August 2014, but the

updated Rulings Program indicates that its release will now be on a date to be advised.

**Personal services income – draft tax determination (TD) scheduled for release on 17**

**September 2014:** Draft TD 2014/D15 will consider whether a payment received by a personal services entity from a service acquirer in relation to a period is personal services income within the meaning of section 84-5 of the ITAA 1997 notwithstanding during that period the service provider is not providing services to the service acquirer until further called upon.

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**[International tax](#)**

**BEPS – OECD webcast – presentation of first deliverables:** The OECD has [announced](#) that it will launch the first seven deliverables under the OECD's Action Plan to address base erosion and profit shifting (BEPS), together with an official Explanatory Statement, during a news conference which will be [streamed live](#) on 16 September 2014.

These papers are instruments and reports relating to:

- The Tax Challenges of the Digital Economy
- Hybrid Mismatch Arrangements
- Harmful Tax Practices
- Tax Treaty Abuse
- The Feasibility of Developing a Multilateral Instrument on BEPS
- Transfer Pricing & Intangibles
- Transfer Pricing Documentation and Country-by-Country Reporting

This will be followed by a [technical briefing via webcast](#). During the webcast, senior members from the OECD's Centre for Tax Policy and Administration will discuss the details of the first set of deliverables, the involvement of developing countries, the input from stakeholders, as well as the planned next steps. This first set of BEPS deliverables will be presented to the G20 Finance Ministers in Cairns on 20-21 September 2014.

**Dbriefs Bytes:** Deloitte Dbriefs Bytes is a short weekly video summary of the significant international tax developments impacting the Asia Pacific region – click to view the latest [Dbriefs Bytes](#).

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