



Tax highlights

17 March 2014

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Key developments this week

Draft Tax Determination released on interpretation of the UK tax treaty in respect of dividend withholding rates:

- [TD 2014/D9](#): A United Kingdom resident company (UK Co), which beneficially owns a dividend paid by an Australian resident company (Aus Co), 'holds directly' at least 10 per cent of the voting power in Aus Co for the purposes of Article 10.2(a) of the Australia-UK Double Tax Agreement in the following circumstances:
 - A nominee shareholder owns shares carrying at least 10 per cent of the voting power in Aus Co for the benefit of UK Co
 - The nominee undertakes to UK Co to exercise all rights of voting and other privileges attaching to the shares in such manner as UK Co shall direct or approve.

Comment: TD 2014/D9 represents a welcome U-turn as compared to the ATO position in [ATO ID 2013/17 \(withdrawn\)](#). The ATO has, on a number of previous occasions, adopted a black letter law approach to interpreting the term "hold directly" under various treaties. The issue arises in the context of the availability of treaty benefits (reduced dividend withholding tax rates). The ATO has now adopted a purpose-based approach to treaty interpretation, concluding that the interposition of the nominee should not prevent the availability of treaty benefits. This treaty interpretation approach is to be welcomed. Whilst on its face, TD 2014/D9 is quite narrow – limited to nominee arrangements and the application of the UK treaty – it is submitted that the principles have wider application. For example, the term "hold directly" is used in many other treaties, and presumably, the same answer should result under those treaties. In addition, the reasoning that was contained in [ATO ID 2013/17 \(withdrawn\)](#), and which has now been abandoned in TD 2014/D9, is relied upon by the ATO in other cases, such as [ATO ID 2011/14](#) (dealing with a New Zealand company which is a member of a NZ limited partnership (NZLP) where NZLP owns shares in an Australian company). It is difficult to reconcile the black letter law approach in [ATO ID 2011/14](#) with the purpose-based approach in TD 2014/D9. It would be prudent to review arrangements where treaty benefits have been denied in various situations involving "intermediate arrangements" such as nominees, trusts, or fiscally transparent entities (such as limited partnerships or limited liability companies).

Policy design for Exploration Development Incentive – discussion paper released: On 14 March 2014, the Assistant Treasurer released a [discussion paper](#) on the Exploration Development Incentive which is proposed to apply to exploration undertaken from 1 July 2014. Under the proposal, companies with exploration expenditure and tax losses in the same income year would be able to provide exploration credits to their shareholders thereby providing the shareholders with an entitlement to a refundable tax offset. The discussion paper outlines possible implementation arrangements for the Exploration Development Incentive and canvasses several issues, including the following:

- **Targeting junior minerals explorers:** The purpose of the scheme is to provide an incentive for investment in junior mineral exploration companies, that is, companies that engage in exploration for new mineral discoveries that meet the 'no taxable income' test. The 'no taxable income' test is proposed so that exploration credits can only be distributed by a company that has a tax loss for the year in which the relevant expenditure is incurred. In addition to this test, the scheme could exclude companies that derive assessable income from mining activities in the income year in which exploration expenditure is incurred. Alternatively, any assessable income from mining activities could reduce the exploration expenditure eligible for the scheme. Eligibility to participate in the scheme is proposed to be confined to Australian resident companies that are widely held
- **Investors to receive exploration credits:** It is proposed that companies will be able to distribute exploration credits to their members that have equity interests when exploration credits are distributed
- **Definition of 'eligible expenditure' and 'greenfields':** The definition of 'eligible exploration expenditure' is proposed to be based on the current definitions of exploration and prospecting in the tax legislation. The definition of 'greenfields' is proposed to include exploration expenditures incurred on activities that are deployed for the purpose of determining the existence, location, extent or quality of a new mineral resource in Australia
- **Options for capping the scheme:** It is proposed that the scheme will be capped at \$100 million over the forward estimates period, specifically \$25 million for exploration expenditure incurred in 2014-15, \$35 million for exploration expenditure incurred in 2015-16 and \$40 million for exploration expenditure incurred in 2016-17. This aspect of the scheme will require special rules and it is proposed that a modulation process be used to ensure that the cap is not breached
- **Exploration credit system:** As mentioned above, it is proposed that the incentive would allow companies with exploration expenditure and tax losses in the same income year to provide exploration credits to their shareholders, giving their shareholders an entitlement to a refundable tax offset. Exploration credits would flow through trusts and partnerships. However, it is proposed that the Exploration Development Incentive would be voluntary and a company that incurs exploration expenditure could elect to carry forward its losses instead.

Submissions on the discussion paper are due by 4 April 2014.

Comment: The proposed Exploration Development Incentive is intended to provide a mechanism to allow Australian junior minerals exploration companies to pass the benefit of their tax losses back to their Australian resident shareholders. The incentive is expected to assist Australian junior minerals exploration companies in raising equity capital to fund minerals exploration projects and is therefore a positive development for the sector.

OECD – BEPS developments: In a flurry of activity, the OECD has released papers on transfer pricing and tax treaty abuse and is expected to release two further papers in the next week as part of the base erosion profit shifting (BEPS) project. Please see our [International tax](#) section below for further details.

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Weekly tax news

Business tax

Parliament resumes sittings this week: Parliament will sit for the next two weeks (17 March to 27 March 2014). These will be the last sitting weeks of the 2014 Autumn sittings. The [2014 Winter sittings](#) of Parliament will commence on Federal Budget day, 13 May 2014.

Debate scheduled to resume in the House of Representatives: According to the [draft legislation program](#), debate is scheduled to resume in the House of Representatives this week on the following tax-related Bill:

- [Export Market Development Grants Amendment Bill 2014](#).

Debate scheduled to resume in the Senate: According to the [draft legislation program](#), debate is scheduled to resume in the Senate this week on the following tax-related Bills:

- [Clean Energy Legislation \(Carbon Tax Repeal\) Bill 2013](#) and related bills
- [Clean Energy \(Income Tax Rates and Other Amendments\) Bill 2013](#)
- [Minerals Resource Rent Tax Repeal and Other Measures Bill 2013](#).

Taxation Ruling (TR) released:

- [TR 2014/1](#): This TR considers when commercial software developers derive income for the purpose of section 6-5 of the *Income Tax Assessment Act 1997* (ITAA 1997) from:
 - Licence agreements for proprietary software
 - 'Hosted' or 'cloud' arrangements for use of proprietary software.

Draft Taxation Determination (TD) released:

- [TD 2014/D8](#): The exemption in section 820-39 of the ITAA 1997 can apply to the special purpose entity (SPE) that seeks finance for the project which is established as part of the securitised licence structure used in some social infrastructure public private partnerships provided the SPE satisfies the conditions in subsection 820-39(3) of the ITAA 1997.

Practice statement on private advice, guidance and objections updated: The ATO has updated [PS LA 2008/5](#), which provides direction to ATO personnel making decisions about private advice, guidance or objections about:

- Requesting further information from taxpayers
- What to do if requested information is not provided
- The use of third party information or assumptions.

According to the ATO, the practice statement has been substantially revised to:

- Expand concepts to oral rulings, administratively binding advice, objections and written guidance
- Apply a principles based approach to content.

Productivity Commission – draft report – inquiry into public infrastructure: On 13 March 2014, the Productivity Commission [released](#) a draft report on funding and financing, and the scope for reducing costs, for major public infrastructure projects. The draft report outlines a proposed process for improving infrastructure investment across all levels of government. Issues discussed in the draft report include:

- Funding arrangements, including which revenue sources should be used for government funding
- Options for improvements to financing mechanisms for infrastructure, including options to address specific concerns related to the role of superannuation funds in greenfields projects.

According to the Commission Chairman, Mr Peter Harris, governments can attract higher levels of private infrastructure investment and improve their capacity to fund infrastructure “through the judicious use of pricing mechanisms and by collectively establishing stronger transparent processes for project identification, selection, design and implementation”. The Commission is seeking comments on the draft report by 4 April 2014 and will hold public hearings in early April. The final report will be prepared after submissions have been received and is expected to be forwarded to the Government in late May 2014.

Appeals update – *Taras Nominees*: The taxpayer has lodged a notice of appeal to the Full Federal Court against the decision of the Federal Court in [Taras Nominees Pty Ltd as Trustee for the Burnley Street Trust v Commissioner of Taxation of the Commonwealth of Australia \[2014\] FCA 1](#) . In that case, the Federal Court dismissed the taxpayer’s appeal from the Commissioner’s objection decision and found that CGT event E1 (Creating a trust over a CGT asset by declaration or settlement) applied on the transfer of land from the taxpayer to a land trustee set up to facilitate a joint venture development of its land. For more information, refer to [Tax highlights 3 February 2014](#).

TD scheduled for release on 19 March 2014:

- TD 2014/2: Value of goods taken from stock for private use for the 2013-14 income year.

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[Non-profit organisations](#)

Restating and centralising the special conditions for tax concession entities – exposure draft (ED) legislation released: On 12 March 2014, Treasury released [ED legislation and explanatory material](#) concerning the proposal to restate and centralise the special conditions for tax concessions entities. This follows the Government’s [announcement](#) on 14 December 2013 that it intends to proceed with this measure. The proposed measure:

- Re-states the ‘in Australia’ special conditions for income tax exempt entities, ensuring that they generally must be operated principally in Australia and for the broad benefit of the Australian community

- Centralises and simplifies in one place the other special conditions entities must meet to be income tax exempt, such as complying with all the substantive requirements in their governing rules, and
- Codifies the 'in Australia' special conditions for deductible gift recipients ensuring that they must generally operate solely in Australia, and pursue their purposes solely in Australia.

This exposure draft makes modifications to legislation proposed in Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012 which was introduced into Parliament on 23 August 2012, and lapsed at the dissolution of Parliament on 5 August 2013, to address concerns raised by the not-for-profit sector. Submissions on the ED legislation are due by 7 April 2014.

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Indirect taxes

Luxury Car Tax Determination (LCTD) released:

- **LCTD 2014/1:** Provides that the luxury car tax (LCT) value for a car acquired under a hire purchase agreement does not include the consideration provided for the supply of credit under the agreement.

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International tax

OECD BEPS Webcast: On 2 April 2014 (Central European Time), the OECD will be [broadcasting](#) a webcast giving an update on the BEPS Project. This will include an update on:

- Transfer Pricing Documentation and Template for Country-by-Country Reporting
- Tax Treaty Abuse
- The Tax Challenges of the Digital Economy
- Hybrid Mismatch Arrangements
- Consultation with developing countries.

OECD discussion drafts expected: According to the [revised timetable](#) for planned stakeholder input in relation to the BEPS/G20 project, the following discussion drafts are expected to be released soon:

- Hybrid mismatch arrangements: 19 March 2014
- Tax challenges of the digital economy: 24 March 2014.

OECD paper on transfer pricing: The OECD has [released](#) a [paper](#) for comment concerning four possible approaches to address the concerns expressed by developing countries over the availability and quality of financial data on transactions between unrelated parties that can be used for comparisons, as well as the availability and quality of information regarding the financial results of operations of comparable independent enterprises. The four approaches include:

- Expanding access to data sources for comparables, including steps to improve the range of data contained in commercial databases, expanding developing country access to such databases, and improving access to comparables data in developing countries with a significant number of sizeable independent companies
- More effective use of data sources for comparables, including guidance or assistance in the effective use of commercial databases, the selection of foreign comparables, whether and how to make adjustments to foreign comparables to enhance their reliability, and alternative approaches to finding comparables

- Approaches to identify arm's length prices or results without reliance on direct comparables, including guidance or assistance in making use of proxies for arm's length outcomes, the profit split method, value chain analysis, and safe harbours, an evaluation of the impact, effectiveness and compatibility with the arm's length principle of approaches such as the so called "sixth method", which is increasingly prevalent particularly in developing countries, and a review of possible anti-avoidance approaches
- Advance pricing agreements and mutual agreement proceedings, including a review of developing country experiences with the pros and cons of advance pricing agreements and negotiations to resolve transfer pricing disputes, as well as guidance or assistance with respect to mutual agreement proceedings.

The paper will be discussed in two parallel sessions on the last day of the Global Forum on Transfer Pricing meeting of 26–28 March 2014. Comments on the paper are due by 11 April 2014.

OECD Action 6 on Treaty Abuse – discussion draft: The OECD has [released](#) a discussion draft on Action 6 (Prevent Treaty Abuse) of the OECD's [Action Plan on Base Erosion and Profit Shifting](#). The discussion draft includes the preliminary results of the work carried out in the three different areas identified in Action 6:

- Development of model treaty provisions and recommendations regarding the design of domestic rules to prevent the granting of treaty benefits in inappropriate circumstances
- Clarification that tax treaties are not intended to be used to generate double non-taxation
- Identification of the tax policy considerations that, in general, countries should consider before deciding to enter into a tax treaty with another country.

Comments are due on 9 April 2014. The comments will then be examined by a Focus Group in the following week.

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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