Deloitte.

14 June 2018
Australia 2018/10

Tax Insights

Senate Inquiry into corporate tax avoidance final report

Snapshot

The long running Senate Inquiry into corporate tax avoidance, which commenced in 2014, recently issued its third and final report.

The Inquiry has provided a platform for significant debate about corporate tax in Australia, and has seen appearances by the ATO (on a number of occasions), multinationals from a range of sectors (digital, pharmaceutical, mining, oil & gas, sharing economy), advisers, academics and social action groups.

The Inquiry has run in parallel to transformative change in the Australian tax system, driven by the global BEPS process, recent court decisions and significant changes in Australian law, with measures such as the Multinational Anti-Avoidance Law, the Diverted Profits Tax and increased transparency requirements.

The final report included 13 recommendations across three areas:

- Two recommendations relating to base erosion and profit shifting;
- Seven relating to transparency, and
- Four relating to petroleum resource rent tax (PRRT).

It is not clear at this stage exactly what action will flow from the recommendations.

It is already on the public record that the Government will make further announcements on a number of tax matters in the short term: likely changes to the PRRT regime and a discussion paper on digital tax. It may be that the expected Government actions on PRRT align with some of the recommendations of the Inquiry.

The recommendations of the Inquiry are set out below together with our comments:

Recommendation	**Deloitte comments:**
1. The committee recommends that the thin capitalisation rules be amended so that the worldwide gearing ratio is the only method by which interest related deductions should be calculated for the purpose of tax treatment in Australia.	This recommendation is consistent with existing ALP and The Greens tax policy positions. Coalition Senators opined strongly against this recommendation in dissenting comments to the report, noting that removing the existing arm's length test would result in investment and jobs being put at risk. It is also noted that the Government is already strengthening the thin capitalisation rules with the introduction of financial statement asset values for thin capitalisation purposes as announced in the 2018-19 Federal Budget. The ATO currently also have a heavy focus on thin capitalisation compliance particularly around the inappropriate calculation of debt values for safe harbour calculation purposes, the use of the arm's length debt test and the use of insolvency remote vehicles to avoid thin capitalisation rules. The ATO have advised that extensive guidance products are under development to support tax certainty in this area and to underpin the ATO's compliance activities.

Recommendation	Deloitte comments:
2. The committee recommends that the government undertake an independent review into the detriment to Australian tax revenue that arises from the current transfer pricing regime, and explore options to modify transfer pricing rules, or other tax laws, to ensure multinational enterprises make the appropriate contribution to Australian tax revenue	In 2012 the Government passed new transfer pricing laws which explicitly embraced the OECD guidance on transfer pricing. The ramifications of these laws, together with recent court decisions, continue to shape the transfer pricing environment. All political parties during the inquiry have struggled to understand the scope of pricing choices that transfer pricing rules provide. This recommendation reflects this distrust of the flexibility of options available to taxpayers to price transactions. Coalition Senators have "noted" Recommendation 2 and acknowledged the importance of maintaining the integrity of the corporate tax base. This may mean that a future review of the current transfer pricing regime is a possibility. However, although the current law was introduced in 2012-13, it should be remembered that the law has been modified regularly since then to include: • The Country by Country reporting requirements, • Reference to the 2017 update to the OECD Transfer Pricing Guidelines (the accepted global consensus position); • Reference to the final OECD reports on BEPS Actions 8-10 (Aligning Transfer Pricing Outcomes with Value Creation). Australia's current transfer pricing law is therefore already up to date with global best practice so it is not clear yet what sort of further modifications could be adopted.
3. The committee recommends that all companies with a total income equal to or exceeding $100 million for an income year be required to release tax information of the level specified in the Tax Laws Amendment (Combating Multinational Tax Avoidance) Act 2015.	Currently the ATO produces a *Report of entity tax information* annually on • Australian public and foreign owned corporate tax entities with total income of $100 million or more • Australian-owned resident private companies with total income of $200 million or more • Entities that have petroleum resource rent tax (PRRT) payable. This recommendation proposes that the threshold for reporting on Australian-owned resident private companies is dropped from $200M to $100M. This reflects previously announced ALP policy and mirrors the ALP Private Members Bill currently in the Senate, introduced in August last year. The Greens position is noted in dissenting comments to the report, calling for a lower reporting threshold for all private and public groups of $50 million. The Coalition Senators in their dissenting comments to the report did not make specific reference to Recommendation 3 and instead noted: "*Coalition Senators agree that transparency is important to ensure that companies pay the right amount of tax, however a balance must be struck between taxpayer confidentiality and the need for any information made public to be well understood and relevant.*" From these comments we understand that there is no immediate desire from Coalition Senators to change the status quo, however a change in Government would almost certainly result in a lower reporting threshold for private companies.

Recommendation	Deloitte comments:
4. The committee recommends that: • **companies, trusts and other corporate structures be required to disclose information regarding their beneficial ownership;** • **a publicly accessible, central register be maintained by a suitable government agency; and** • **this information be included in the review as set out in Recommendation 6, with the intent to find ways to provide this information free of charge or at a reduced cost.**	This recommendation is consistent with existing ALP policy for a publicly accessible central registry of the beneficial ownership of companies, trusts and other corporate structures to be established, together with previous public statements by The Greens. In early 2017, on behalf of the Government, Treasury undertook consultation on the details, scope and implementation of a beneficial ownership register for companies. There have been no further public developments since this time. The focus of the Government consultation appears to be on this information being available to key regulators for enforcement purposes; rather than for the public at large. The Government has not publicly announced any intention to include the beneficial ownership of trusts in any proposed register. This may be due to the difficulty in undertaking this task in light of the wide use of discretionary trusts in Australia, often with broadly defined classes of beneficiaries.
5. The committee recommends that the government require all companies, trusts and other financial entities with income above a certain amount to lodge general purpose financial statements with the Australian Securities and Investments Commission.	In the report, the Committee discussed that consideration should be given to aligning the threshold of requiring mandatory general purpose financial statements with other transparency thresholds, such as the $100 million threshold for the ATO's *Report of entity tax information*. Currently the Government has already legislated for corporate tax entities, that are significant global entities (income threshold $1 billion) with an Australian presence, provide the ATO with general purpose financial statement (GPFS). In dissenting comments to the report, Coalition Senators noted that the AASB is currently consulting on how to introduce the IASB's revised *Conceptual Framework for Financial Reporting* into Australia and improve the consistency, comparability and transparency of financial reports prepared in accordance with the Australian Accounting Standards. The AASB's consultation paper addresses the special purpose financial statement problem caused by Australia's unique accounting requirements that allow entities to self-assess as 'non-reporting entities'. The Coalition Senators, therefore, have suggested that any action in respect of this recommendation be deferred to take into account any matters arising out of the AASB's consultation.

Recommendation	Deloitte comments:
6. The committee recommends that the government undertake an independent, public review of the Australian Securities and Investments Commission's statutory fees and charges to explore options for reducing or eliminating fees to access company information, including financial statements	This recommendation should be read in conjunction with Recommendation 5 above, which would result in an expanded collection of information by ASIC. In turn, under this recommendation, ASIC would make information which it routinely collects available to the public without charge. Making this information available without charge would potentially result in a funding shortfall for ASIC. However, the Government has recently been looking at ASIC funding and already has a Bill in Parliament which will allow ASIC charge corporates a cost reflective fee for the services it provides for a specific entity. This is consistent with a general move across several regulators to recover the costs of administering the regulatory regimes from the underlying entities being regulated. Many journalists, academic and/or social justice groups have long complained about the cost of obtaining bulk financial statements through ASIC. This measure largely reflects their advocacy efforts.
7. The committee recommends that excerpts of Country-by-Country reports be made publicly available free of charge. Information to be released from Country-by-Country reports would include, at a minimum, high level data on how much revenue is collected and tax is paid in jurisdictions the firm operates in, and the number of employees	This recommendation is consistent with current ALP policy for extracts of Country-by-Country reports to be made public. The Government in dissenting comments to the report noted that the OECD's Base Erosion Profit Shifting (BEPS) recommendation on Country-by-Country reports explicitly states that jurisdictions should enforce legal protections of the confidentiality of the reported information and that Australia is bound by an international multilateral agreement. The ATO have also expressed operational concerns about releasing excepts of Country-by-Country report publicly on the basis that this valuable flow of information would stop if Australia was to breach its multilateral agreement obligations for confidentiality.
8. The committee recommends that the existing voluntary tax transparency code be converted, as soon as practicable, to a mandatory code for all large and medium corporations operating in Australia, including subsidiaries of multinational corporations	The *Tax Transparency Code* is currently voluntary, with the take-up of the code being encouraged by the Board of Taxation, the Business Council of Australia and Corporate Tax Association. On its launch in 2016, it was announced that the level of participation was to be reviewed in three-years time (that is 2019). With a review on the uptake pending, together with the varying levels of participation, this recommendation could foster the political impetus to make the code mandatory, despite the increased administrative burden on business. The Government has already started moving in this direction, with the 2018-19 Budget announcement in connection with procurement, which proposed that Government suppliers with contracts over $4 million be required to comply with the code where their turnover is in excess of $100 million per annum.

Recommendation	Deloitte comments:
9. The committee recommends that the Australian Taxation Office include a dedicated section on the number and value of significant tax settlements of $50 million or greater in its annual report	This recommendation is consistent with current ALP policy. In dissenting comment to the report, The Greens have gone further and specified that an ATO settlement register should publicly name the companies with settlements, list the amount that the ATO originally as the company's tax liability and the amount of the final settlement. The Government has previously supported the ATO's wishes to only disclose aggregated information in its Annual Return, on the basis that the complexity of disputes and settlements cannot be properly reflected in a table.
10. The committee recommends that the government finalise and release its response to the Callaghan report into the Review of the Petroleum Resource Rent Tax.	The Callaghan report into the review of the PRRT was released by the Treasurer in April 2017. At the time the Treasurer requested additional work be undertaken in considering reforms to the framework, and consequently additional consultation was undertaken by Treasury during August 2017. A further report sent to Government at the end of September 2017. The Government has yet to release its response to the report, which was largely expected around the time of the 2018-19 Federal Budget.
11. The committee recommends that the government overhaul uplift rates for future Petroleum Resource Rent Tax eligible projects, so as to make them less generous	The Callaghan review noted that a key feature of the PRRT is that tax losses are carried forward with an uplift to be offset against future positive cash flow from the project. The uplift rate at which losses (deductions) are carried forward has a significant impact on when/if a project will pay PRRT. The review noted some possible changes to the uplift rates, including changing the arrangement for the uplift rates to be more commensurate with the risk of losing PRRT deductions, taking into account transferability and that this risk will vary over the life of a project. Given that the Government has yet to release its response to the report, it is uncertain whether the Government is in favour of altering the uplift rate.
12. The committee recommends that the ordering of deductions be rationalised for future Petroleum Resource Rent Tax eligible projects so that those with the highest compounding rates are used first for tax deduction purposes	The Callaghan review noted that reforms could be considered to ensure that classes of expenditure with the highest uplifts are deducted first, having regard to how deductions can compound in large long-life projects.

Recommendation	Deloitte comments:
13. The committee recommends that the gas transfer pricing method for Petroleum Resource Rent Tax eligible projects be reformed to make it simpler and more transparent so as to ensure that it delivers a fair return to the community	This recommendation reflects comments in the Callaghan Report that the government should consider examining the gas transfer pricing arrangements to identify possible changes that would achieve greater simplicity and transparency, ease of compliance, and fair treatment of the economic rent from each stage of an integrated petroleum operation.

Deloitte view:

Whilst this is a cross party report, it is noted that the majority of the Committee consisted of non-government members, in particular, representatives from the opposition ALP and The Greens. The recommendations of the Committee are very consistent with the publicly announced tax policy platforms of both the ALP and The Greens.

Despite the previous wide ranging media focus of testimony before this Inquiry, the report itself has received a fairly quiet reception in the media to date. Absent this political pressure, it is therefore difficult to estimate to what extent the measures recommended will be taken up by the Government.

However, with a Federal election expected in Australia in the next year, the recommendations could be seen as a roadmap for potential tax changes in the event of a change of Government and accordingly should be examined in that light.

The Coalition Senators dissenting comments to the report were highly critical of the inquiry, which was protracted and at times appeared to focus more on politics, industrial relations, the pharmaceutical benefits scheme and matters unrelated to tax.

But some important learnings did occur:

1. The media attention given to the Inquiry put pressure on both the ATO and the Government to be more transparent and pro-active in addressing multinational tax avoidance (and will continue to do so)
2. Tax is big news. There is an ever widening spectrum of stakeholders taking an interest in what has historically been seen to be a niche technical subject.
3. Tax Policy and the fairness debate could potentially influence the result of the next election.

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