



Australia's new penalty laws for CbC reporting and an update on its implementation approach

Global Transfer Pricing Alert 2017-014

Australia's approach to country-by-country (CbC) reporting is characterized by the severity of its penalties for noncompliance, its divergence from the OECD Action 13 standard regarding the local file, and the fact that it places the obligation for compliance squarely with the local Australian taxpayer.

On 4 April 2017, the Australian government passed legislation to significantly increase late lodgement penalties for Australian taxpayers that are members of an accounting consolidated group with annual global income in the preceding period of AUD 1 billion or more (referred to as significant global entities, or SGEs), to potentially AUD 525,000 for each statement.

This change is crucial, given that Australia's implementation of CbC reporting places primary responsibility for lodging the CbC report and the master file with the local taxpayer. Further, the Australian local file deviates significantly from the OECD standard, requires a significant amount of transactional information, and must be lodged in a particular XML format specified by the Australian Taxation Office (ATO).

Introduction

As part of the local implementation of the OECD's *Transfer Pricing Documentation and Country-by-Country Reporting, Action 13 – 2015 Final Report*, the ATO has issued guidance on CbC reporting requirements effective for income years commencing on or after 1 January 2016. SGEs will be required

to provide the ATO with a CbC report, a master file, and a local file within 12 months of the end of the applicable financial year in the specific format required by the ATO.

Existing Australian transfer pricing laws and associated transfer pricing documentation laws, which first came into effect for income years commencing 1 July 2013, still apply. Australia's transfer pricing documentation laws and CbC reporting laws are mutually exclusive, and neither fully aligns with OECD guidance. The Australian local file for CbC reporting purposes is not consistent with the OECD-designed local file outlined in Annex II to Chapter V of the *Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations*. Further, the Australian local file is not equivalent to Australian transfer pricing documentation requirements for penalty reduction purposes. The ATO's adoption of the term "local file" has caused confusion, given that this term may be interchangeable with transfer pricing documentation in other countries.

Key Australian Country-by-Country and Transfer Pricing Requirements

Overview

A high-level summary of the five transfer pricing-related documents and statements for upcoming income years is provided in the following table.

	Transfer pricing report	International Dealings Schedule	CbC Report	Master File
Regime	Existing laws	Tax return	CbC reporting	CbC reporting
Application	All taxpayers	Taxpayers with international related-party dealings (including loan balances) of AUD 2 million or more	SGEs	SGEs
Mandatory	No, but required for penalty protection	Yes	Yes	Yes
Exemption available	No	No	Yes	Yes
Per OECD guidance	No	No	Yes	Yes
Filing requirement	No	Yes	Potentially	Yes

Deadline (post-year-end)	6.5 months	6.5 months	12 months	12 months	12 months
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Additional details of these statements are outlined below.

Existing transfer pricing compliance requirements

Transfer pricing documentation. There are very specific requirements that must be met in order for the transfer pricing documentation rules in Subdivision 284-E of the Taxation Administration Act 1953 to be satisfied. A taxpayer can be eligible for a reasonably arguable position (and therefore potential penalty reduction in the event of a transfer pricing adjustment) only if it has transfer pricing documentation prepared prior to lodgement of its income tax return. The ATO has indicated to Australian taxpayers that, on their own, preparation of an Australian local file (as described below), or preparation of an OECD-designed local file (that is, in accordance with BEPS Action 13 recommendations) will not meet the requirements of the transfer pricing documentation rules, given that the documentation is required to explain, among other things, the particular way in which Subdivision 815-B of the Income Tax Assessment Act 1997 (the transfer pricing laws) applies (or does not apply) to a taxpayer's international related-party dealings.

Section A of the international dealings schedule (IDS). All taxpayers with total international related-party dealings over AUD 2 million (including loan balances) are required to complete an IDS, which is a schedule to the corporate income tax return. The IDS provides a summary of the nature of a company's international related-party dealings, the jurisdictions of major counterparties, the level of transfer pricing documentation available for each dealing, and the main pricing method used for each dealing. The ATO uses the IDS as a risk assessment tool to identify taxpayers with either perceived high-risk or material international related-party dealings.

Country-by-Country reporting requirements

CbC report. SGEs have the primary obligation to obtain the CbC report and file it with the ATO, unless it is filed in a country that is signatory to the Multilateral Competent Authority Agreement on Automatic Exchange of CbC Reports. Exemptions may be granted in limited circumstances.

Master file. An SGE must obtain a copy of the master file in English from its parent entity and file it with the ATO. The required contents of the master file are consistent with those outlined in Annex I to Chapter V of the OECD transfer pricing guidelines.

Australian local file. SGEs must prepare and lodge an Australian local file with the ATO. The Australian local file is an electronic file that must be lodged as an XML file in a specific format outlined by the ATO. The contents and the format of the Australian local file are not like those of a traditional transfer pricing report (for example, neither a functional analysis nor an economic analysis is required) and do not align with that outlined by the OECD in Annex II to Chapter V of the transfer pricing guidelines. The Australian local file should

instead be seen as a far more detailed version of the IDS in that it will act as a more powerful risk assessment tool for the ATO to better identify risk review or audit candidates. The Australian local file consists of the following:

- Short form local file – a document that includes information relating to the three bullet points outlined under the “local entity” heading of Annex II to Chapter V of the transfer pricing guidelines. While all taxpayers will need to prepare a short form local file, those that do not exceed certain materiality thresholds and meet other criteria will not have to prepare or provide the ATO with any of the other information below.
- Part A of the local file – SGEs are required to provide transactional information on all international related-party dealings, including counterparties, type of dealing, amount, method used to price the dealing, level of documentation maintained to support the arm’s length nature of the dealing, and the foreign exchange gain or loss incurred in relation to each dealing. The format of Part A of the local file is best described as being analogous to a highly granular, transaction-based version of the CbC report, with 26 disclosures required for every dealing. Given that Part A of the local file is in substance a more detailed version of the IDS, the ATO has indicated it will provide SGEs with an exemption from having to lodge the IDS should they voluntarily file Part A of the local file at the same time as they lodge their tax return.
- Part B of the local file – as an extension to Part A of the local file, SGEs are required to provide a further 18 disclosures for all “material” international related-party dealings in relation to the nature of agreements relating to those dealings.
- Other attachments – the SGE must attach copies of several files as part of its local file lodgement, including the master file, all intercompany agreements for “material” international related-party dealings, copies of foreign advance pricing agreements (APAs) that relate to Australian dealings and financial statements (noting that SGEs may need to prepare these as general purpose financial statements for income years commencing on or after 1 July 2016).

Exemptions and replacement reporting periods

An SGE can apply to the ATO for an exemption from filing one or more of the CbC documents. For example, it can request an exemption from filing the CbC report for the first year of reporting on the grounds that the parent company jurisdiction is implementing CbC reporting requirements at a later date than Australia. If an SGE has a different income year-end than its parent, it will need to make a written application to the ATO requesting the use of a 12-month period aligned with the

income year of an SGE's parent entity (replacement reporting period) for the CbC report and master file.

New late lodgement penalties

Lodging required documents with the ATO is now particularly important, given that a new penalty regime was recently introduced for SGEs with effect from 1 July 2017. SGEs will be subject to a penalty of at least AUD 105,000 in relation to the late lodgement of any document, rising to a maximum of AUD 525,000 in instances when these become overdue by more than 16 weeks.

Each of the CbC reporting statements (master file, local file, and CbC report) constitutes a separate statement subject to this penalty regime, which also extends to an SGE's failure to lodge any other tax document (for instance, an income tax return) with the ATO on time or in the approved form. Lodging numerous tax documents late therefore could result in material (and nondeductible) penalty amounts being payable.

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