



Australia releases draft law implementing country-by-country reporting and increasing penalties for tax avoidance and transfer pricing

Executive summary

On 6 August 2015, the Australian Treasury released exposure draft law (draft law) for Australia to implement reporting requirements for large multinational businesses in line with recommendations by the Organisation for Economic Co-operation and Development (OECD) and G20. Submissions are due on 2 September 2015.

The draft law also increases penalties for tax avoidance and transfer pricing where the taxpayer does not have a reasonably arguable position. Both measures were announced in the 2015 Budget.

Australian large businesses, and Australian subsidiaries of large multinationals, need to analyze the broader reporting requirements and develop and implement required changes to documentation, policies, and systems in advance of the 1 January 2016 start date.

The draft law will give effect to the OECD/G20's "standardized 3-tier" approach to transfer pricing documentation under Action 13 of the G20 and OECD's Action Plan on Base Erosion and Profit Shifting (BEPS Action Plan). The three tiers of documentation are a Country-by-Country (CbC) report, a master file and a local file.

From 1 January 2016, the draft law requires entities that are part of a group with annual global revenue for the income year that exceeds A\$1 billion to provide the Australian Taxation Office (ATO) with a statement in a form to be determined by the ATO. As part of the reporting it is expected that each entity will need to provide

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an OECD local file, and each group must provide its OECD master file. The CbC report may not need to be lodged by the Australian subsidiary of a global group where the group's parent entity is in a jurisdiction with which Australia has an information sharing agreement in place. The ATO has been given considerable flexibility in the implementation of this reporting.

Detailed discussion

OECD transfer pricing documentation standards

The OECD's 2014 report on Action 13 of the BEPS Action Plan outlined a standardized 3-tiered approach for transfer pricing documentation, being a:

- ▶ CbC report
- ▶ Master file
- ▶ Local file

The Explanatory Material to the draft law confirms that Australia also will adopt a 3-tiered approach for its CbC reporting requirements.

Reporting obligations

Entities whose annual global revenue exceeds an A\$1 billion threshold are required to provide a statement to the ATO in relation to an income year, before the end of the next income year. For entities whose income year commences 1 January 2016, the reports would be due by 31 December 2017.

This threshold is calculated by reference to the definition of "annual global revenue" set out in the proposed multinational anti-avoidance law (MAAL), s177DA, dealing with arrangements to avoid

a taxable presence in Australia, which was released in draft form on 12 May 2015.

Australian taxpayers with relatively small Australian operations, that nonetheless satisfy the global A\$1 billion threshold, must comply with the proposed additional reporting requirements. This is consistent with Treasury's intention of detecting groups generating significant profits in Australia which do not currently recognize significant local activities and profits. However it will place a significant additional compliance burden on many small and medium sized taxpayers that are part of a multinational group.

The ATO has considerable discretion and will have the power to exclude certain entities from having to report in one or more income years by written notice, with administrative guidance to be issued for entities seeking exclusion from the CbC reporting obligations.

CbC report, master file and local file

The three reports require entities to provide detailed information relating to the global allocation of a multinational group's income and taxes paid, as well as information about the location and main business of each constituent entity within the group.

Every group identified under the draft law will be required to lodge the master file in Australia for at least one entity, which includes an overview of the multinational group's business operations, transfer pricing practices, organizational structure,

its intangibles and intercompany financial activities, its financial and tax positions, and a description of the group's businesses.

Each local subsidiary will also be required to lodge a local file, which focuses on specific relevant related party transactions, the amounts involved in those transactions, and the entity's analysis of the transfer pricing determinations they have made.

The CbC report also will be required under the Australian reporting, but is likely not to be required where it will be filed in the jurisdiction of the multinational group's worldwide parent entity and it will be automatically exchanged with Australia under information sharing agreements. It is possible that the ATO might develop some transitional arrangements here as the global reporting processes unfold.

The deliberate non-inclusion of the specific reporting requirements in the draft law is designed to enable the administration of the CbC reporting to align with the final arrangements of Action 13 of the BEPS Action Plan, as well as providing the administrative flexibility to specify the precise form. It also reflects the ATO's efforts in working through the CbC reporting requirements and seeking to manage the interactions with the International Dealings Schedule and other data.

We understand the ATO will develop and release exposure draft guidance on the contents of the CbC reports. EY has advocated for this guidance to be provided before the 2015

year end to enable multinationals to have clarity on the information requirements prior to the 1 January 2016 commencement date.

Penalties for non-compliance

Penalties may be imposed on entities that fail to provide a statement for the purposes of the transfer pricing laws (Subdivision 815-E) on time, or in the approved form, to the ATO. The penalty for non-compliance is 5 penalty units per 28 day period, up to 5 periods. The ATO has the discretion to remit an administrative penalty to the taxpayer.

The taxpayer will retain a reasonably arguable position in relation to a transfer pricing matter (despite late lodgment of its CbC reports) provided it otherwise meets the relevant transfer pricing documentation requirements.

Overlap with existing transfer pricing documentation

Although there is a degree of overlap between the documentation requirements under Subdivision 284-E to have a Reasonably Arguable Position (RAP) and the local file to be lodged under the draft law, it is clear they are intended to be separate requirements.

The local file can require more data than the RAP documentation in terms of the transactional detail required.

The RAP documentation can go beyond the local file in terms of explaining the way the Australian law applies in terms of the reconstruction provisions, interaction with thin capitalization, and how the transfer pricing benefit is determined, among others.

Doubling of penalties for tax avoidance and transfer pricing schemes

Amendments in a separate exposure draft bill double the administrative penalties for large companies due to avoidance or profit shifting schemes. These increased scheme penalties apply to companies with annual global revenue exceeding A\$1 billion that do not adopt a tax position that is reasonably arguable.

The maximum uplift to the scheme shortfall amount in the base penalty calculation is now 120%. Increased penalties apply to any scheme benefit an entity gets on or after 1 July 2015, regardless of when the scheme was entered into.

This significantly increases the relative importance of having transfer pricing documentation that can provide a RAP under Subdivision 284-E.

Next steps

Larger businesses should:

- ▶ Conduct a CbC readiness review and pilot to identify and head off risks, including a review of existing data capturing systems' capabilities.
- ▶ Analyze the CbC reporting requirements and to plan to implement required changes to documentation, policies, and systems in advance of the 1 January 2016 start date.
- ▶ Plan to incorporate the CbC report, master file and/or local file into existing Transfer Pricing documentation.

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