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The White Paper Task Force
The Treasury
Langton Crescent
PARKES ACT 2600

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Dear Sirs

Re:Think Discussion Paper

Rio Tinto welcomes the opportunity to provide comment on the “Re:think” discussion paper, and looks forward to ongoing participation in this important debate to address the key strategic issues for Australia’s tax and transfer system in what is a dynamic global environment.

Rio Tinto is one of the largest taxpayers in Australia. In 2014 we paid US$7.1bn in taxes and royalties globally of which A$6.2bn was paid in Australia. In addition a further A$1.2bn was collected on behalf of employees in Australia. Since first publishing our Taxes Paid Report in 2010 Rio Tinto has contributed more than A$32bn in taxes and royalties in Australia. Rio Tinto is extremely proud of the contribution it makes to the Australian economy.

Rio Tinto has long supported reform that enhances the efficiency and competitiveness of the Australian economy and improves the equity of the outcomes that it delivers. Reform must also address the significant challenges currently facing our economy, and the need for a stable and reliable revenue base to meet Government expenditures. Importantly these should not be seen as conflicting outcomes as increasing economic growth through competitiveness and increased productivity will ultimately translate into increased tax revenues.

The need to be competitive is not confined to the resources sector. There is a need for productivity driven reforms to encourage the hard work and innovation needed to drive economic growth and to lock in prosperity across the nation. This is not the time for short term measures but requires an enduring policy framework to ensure Australia’s future prosperity.

Meaningful tax reform will require bold vision and bipartisan support at all levels of government. The full benefits of substantive tax reform will evolve over the medium to longer term which presents obvious challenges in terms of political policy settings and election cycles. Success will require genuine consultation across the community - first to acknowledge the need for tax reform, but ultimately to endorse those reforms.

It is widely acknowledged that Australia's revenue base is overly reliant on inefficient taxes such as personal and corporate income taxes, which impede international competitiveness and economic growth, while underutilising progressive taxes.

The tax system must be competitive to encourage investment and growth

Australia's political and fiscal stability has historically played to our advantage. However, as Africa and other non-OECD competitors enhance their political and social stability, this advantage is being eroded placing further pressure on Australia to focus in other areas to enhance its international competitiveness.

In the 2015 IMD World Competitiveness Yearbook Australia's overall competitiveness ranking has declined further to 18th out of the 61 countries assessed. This continues a concerning trend from a ranking of 9 in 2011. The report identifies tax reform as a significant challenge facing Australia to become more efficient and internationally competitive.

It is acknowledged that both Government and business have a vested interest in driving economic growth. This point was made by the Prime Minister Tony Abbott in the lead up to the G20 Summit in Brisbane in 2014 where he stated: "Unapologetically, we've put our focus on and our faith in the private sector. Because making life easier for business to invest to employ, to produce and to trade is what drives national growth and prosperity and helps to lift people out of poverty." In this regard it is vital for governments to provide a regulatory and policy framework which encourages investment which in turn will drive economic growth.

While there are many factors which impact on competitiveness and influence the decision to invest, the corporate income tax rate is a significant driver of returns on investment. Australia's company tax rate is simply too high when compared not only to the OECD average but importantly to our regional competitors. Australia's tax rate needs to be internationally competitive to attract the necessary foreign investment required to fund the large upfront capital required for resource projects and infrastructure more generally. In an increasingly globalised world economy, capital is mobile and becoming increasingly scarce and will move to where the returns are greatest.

Lower corporate taxes will increase returns and the relative attractiveness of investment in Australia resulting in increases in foreign investment with flow on increases in productivity, growth and ultimately higher real wages. Some of our regional competitors have been extremely successful in attracting and building entire industries off the back of internationally competitive tax systems. Australia is currently unable to compete in this area. While Australia may not be able to match the low company tax rates implemented by some countries in our region it is imperative that we move towards the OECD average if we are to compete for foreign investment dollars. A phased reduction may be the means by which this can be achieved - as has been seen in some other countries. A clear policy signal is necessary to demonstrate that Australia is open for business and has a desire to compete for globally mobile capital.

Whilst investment in capital intensive industries like the resources sector has declined somewhat, continued investment in these industries will continue to be important to the Australian economy. Australia needs to ensure that its Capital Allowances regime is internationally competitive in order to attract foreign capital for investment into these industries to leverage additional productivity and growth. A more competitive capital allowances regime would improve Australia's attractiveness as a destination for capital investment. A review of the tax treatment of intangibles is also long overdue to address the fact that current rules have not kept pace with the evolution and innovation of modern business. Intangible assets are of increasing significance and arguably will underpin the future economy. It is difficult to see why assets of this nature should not be afforded comparable tax treatment to tangible assets. Australia is currently at a competitive disadvantage to the many countries which have implemented a comprehensive tax amortisation regime for intangible assets.

Notwithstanding the above, a reduction in the corporate tax rate is considered a priority over capital allowance reforms as the corporate tax rate will encourage broader investment across all sectors of the economy. A strong and vibrant economy generates flow on benefits for all sectors of the economy.

Australia has strong integrity rules governing the treatment of debt deductions. The Thin Capitalisation rules were further strengthened recently and are arguably the most stringent in the developed world. The tax treatment of financing costs related to new investments is a key component of the after tax return on that investment and is therefore also significant to investment attractiveness as is the headline corporate tax rate. Any further tightening of the thin capitalisation rules will inherently increase the effective tax rate on new investments and must be carefully considered in terms of Australia's ability to attract increasingly mobile and scarce investment capital. Preservation of the ability to deduct interest on arm's length debt is of significant importance in this context.

Changes to the Thin Capitalisation rules such as those recently proposed by the Labor party have the potential to further erode Australia's competitiveness and impact on investment in Australia by limiting legitimate tax deductions for interest expenses. The proposed changes are not targeted to tax avoidance arrangements and would impact all business debt funding arrangements, regardless of whether those arrangements are arm's length arrangements or commercially justifiable.

The tax system must be stable and rational in order to underpin investor confidence

Stability in tax policy settings is integral to investor confidence. In the specific area of natural resource taxation policy, we believe that it is essential for tax policy and design to take into account the cyclical nature of the industry and to respect agreements under which investment capital has already been committed. For an industry that makes multi-decade investments, with significant up-front capital expenditure, the risk of fiscal instability will influence the global flow of capital and a country's ability to attract and retain investment. Above all, tax law should never be retrospective.

Australia's tax system is based on the sound principle that tax on business inputs should be minimised. Fuel tax credits (FTC) and GST are examples of this principle. Diesel fuel constitutes a significant cost to resource companies where it is primarily used on privately built roads, power generation and other activities in remote locations. Treasury has publically rejected the view that FTC's are a subsidy to resource companies as advocated by some lobby groups. The means by which FTC's are refunded is simply an outcome of the arrangements in place to efficiently administer the scheme from a revenue collection perspective.

The FTC scheme contributes to achieving international competitiveness and enhancing economic growth and puts Australia on an equal footing with competitor countries which similarly recognise that taxation on business inputs is not economically rational. As noted in the Discussion Paper 60% of all FTC's are received by industries outside of mining. The principle of minimising tax on business inputs and the benefits of the FTC applies equally to these other significant sectors of the economy including agriculture, transport, construction, forestry and fishing.

Encouraging Innovation

Rio Tinto views itself as unique among mining companies in that we place a premium on innovation and technology. Rio Tinto is a leader in innovation and the adoption of technology, and believes that this is a key to competitive advantage. The outcome from innovation is productivity and we are currently delivering real productivity gains from our innovation initiatives. Examples where Rio Tinto has created significant value through innovation include our Mine of the Future™ activities, our operations and process excellence centres and data analytics.

If the Australian mining sector and broader Australian industries are to gain a competitive advantage over our global rivals it is essential to continue to embrace the challenges of innovation and productivity. The government has a role to play in providing a framework of policy settings which encourage investment in innovation. At a time when we are seeking to improve international competitiveness and productivity Australia's tax policy settings related to innovation have retreated, reducing our competitiveness and undoubtedly leading to reduced investment in R&D.

R&D investment capital is increasingly mobile. The Government needs to do more to encourage and attract investment in technology and innovation and to ensure that the outcomes from innovation remain in Australia.

Complexity

In the Discussion Paper it is estimated that the cost to taxpayers of complying with the current tax system is in the vicinity of $40bn annually. This enormous cost is a drag on the economy, diverting resources that could otherwise be employed on productive activities. The drivers of complexity are diverse including tax policing settings, compliance and administration.

As noted above, if Australia wants to attract capital and promote new industries the corporate tax rate must not be overlooked, and nor should Australia's tax complexity.

The burden of compliance can act as a handbrake on entrepreneurial spirit, not just for big companies but also for small businesses seeking to grow. When only ten of the 125 taxes in Australia generate 90 per cent of the revenue it begs the question as to what the other 115 taxes and levies are doing to competitiveness. Such taxes sap entrepreneurialism at a time when it is needed most.

While there will necessarily always be a level of complexity in our tax laws in part due to the underlying complexity of the matters they seek to legislate there is considerable scope to improve the compliance burden.

Rio Tinto supports simplification to address unnecessary complexity and compliance in relation to capital allowances, the fringe benefits tax regime and the implementation of meaningful safe harbours which provide a balance between revenue collection, taxpayer certainty and compliance costs.

In particular, urgent advances are necessary in order to provide certainty to taxpayers in relation to transfer pricing. Transfer pricing is a complex area which lends itself to overwhelming levels of compliance and uncertainty and more needs to be done to address this.

Further alignment between tax and accounting should be cautiously considered in further detail. Full alignment is unlikely to be achievable or beneficial but there may be some areas where greater alignment can achieve greater simplicity.

It is noted that the ATO has recently invested in its Reinvention Program aimed at assisting taxpayers in obtaining certainty and in complying with their obligations. This requires a high level of transparency and trust which can only evolve over time with the commitment of both parties.

Rio Tinto has entered into an Advanced Compliance Arrangement (ACA) whereby our tax compliance is subject to annual review by the ATO. Under the ACA Rio Tinto has agreed to be transparent and discloses all major transactions to the ATO under this process. We regularly engage with the ATO to seek guidance and to assist the ATO in understanding our business. While these processes do not address the underlying complexity of the tax system they assist in providing certainty and minimising the compliance burden for both the ATO and taxpayers and therefore Rio Tinto is supportive of maintaining and advancing these sorts of programs.

State Based Taxation

To achieve the optimal outcome on tax reform it is critical that the States are engaged in the process. The State and Federal Governments must work together to eliminate the most inefficient and insignificant taxes. As noted above and in the Discussion Paper revenue is collected from over 100 different taxes, but the majority of revenue is collected from just a few.

The additional complexity and inefficiencies created by State based taxation are obvious. To the extent that a business operates across different States and Territories it must comply with the different taxing statutes of each jurisdiction and engage with the various revenue authorities. There is obvious scope here for the elimination or harmonisation of state taxes and for centralised collection agencies.

Stamp duty on the transfer of business assets is a significant barrier to investment and reorganisations targeted at achieving synergies and productivity. At a time when investment should be encouraged to stimulate economic growth stamp duty operates to distort business decisions and acts as a deterrent to commercial transactions. In certain situations income tax relief is available to facilitate the implementation of transactions in a tax efficient manner only to find that stamp duty may apply to make the transaction uneconomic. Consideration should be given to removing such barriers to investment.

Integrity

Rio Tinto supports the BEPS initiatives, but to be effective these must be implemented on a multilateral basis. Unilateral action will lead to increased compliance costs and potential double taxation and make doing business harder when more investment is need to stimulate economic growth.

Care must be taken not to inadvertently damage the investment environment when implementing BEPS recommendations. We are also concerned about the potential for double taxation resulting from these initiatives, and about the additional compliance costs that will result from actions being taken by governments and tax authorities in response.

Australia already has some of the strongest integrity measures globally to protect its revenue base such as the Transfer Pricing, Controlled Foreign Company (CFC) and the General Anti Avoidance regimes. As Australia considers its response to the BEPs action items it must ensure that it acknowledges its existing world class integrity measures and avoid actions which will undermine Australia's competitiveness. Importantly, Australia must guard against any actions which could result in double taxation as this will significantly undermine certainty, confidence and, ultimately, future investment.

Transparency the key to building Trust

As noted above, the need for substantive tax reform is well understood. However, such reform cannot succeed without broad community support. That support can only be built on a foundation of trust. History shows us that meaningful reform is difficult and, unless public trust can be built around the need for change, achieving true reform will not be possible.

In 2010 Rio Tinto made the decision that transparency was the only way forward for an informed debate on tax policy and reform. Since that date we have published our Taxes Paid Report annually disclosing taxes and royalties paid globally and setting out Rio Tinto's overall philosophy regarding tax strategy and governance.

Rio Tinto is also a strong supporter of the Extractive Industries Transparency Initiative (EITI). The EITI sets a global standard for transparency on tax and royalty payments to governments which is currently being implemented by 48 countries.

Rio Tinto strongly encourages measures which deliver voluntary transparency and are concerned with the proliferation of new initiatives which will incur significant additional cost for little or no benefit.

Transparency is the key to an informed debate on tax reform. Transparency creates a conversation informed by facts. The more the various issues are understood the better Australians can judge them on their merits. Reform cannot succeed without broad community support and that support can only be built on a foundation of trust. Without transparency there can be no trust.

Rio Tinto strongly encourages the Government to continue with its intention to facilitate a meaningful debate around broad tax reform in Australia and to continue to transparently facilitate a genuine public debate. We look further to engaging further on this important process.

Yours sincerely

Phil Edmands
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