
TREASURY LAWS AMENDMENT (2018 MEASURES NO. #) BILL 2018

EXPOSURE DRAFT EXPLANATORY MATERIALS

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Glossary

The following abbreviations and acronyms are used throughout this explanatory memorandum.

<i>Abbreviation</i>	<i>Definition</i>
BEPS Action Plan	The G20 and Organisation for Economic Co-operation and Development's Action Plan on Base Erosion and Profit Shifting
Bill	Treasury Laws Amendment (2018 Measures No. #) Bill 2018
ITAA 1936	<i>Income Tax Assessment Act 1936</i>
ITAA 1997	<i>Income Tax Assessment Act 1997</i>
OECD	Organisation for Economic Co-operation and Development

Chapter 1

Amending the definition of significant global entity

Outline of chapter

1.1 Schedule # to this Bill amends the definition of significant global entity in the ITAA 1997 so that it:

- applies to groups of entities headed by an entity other than a listed company in the same way as it applies to groups headed by a listed company; and
- is not affected by the exceptions to requirements applying to consolidated or materiality rules in the applicable accounting rules.

1.2 The amendments also modify the rules for entities that must undertake country-by-country reporting under Subdivision 815-E so that these rules apply to country by country reporting entities rather than significant global entities more generally, to ensure these rules are aligned with Australia's international commitments.

1.3 All legislative references in this Chapter refer to the ITAA 1997 unless the contrary is indicated.

Context of amendments

Significant global entity

1.4 The concept of significant global entity was included in the income tax law by the *Tax Laws Amendment (Combating Multinational Tax Avoidance) Act 2015*.

1.5 Broadly, under the definition in section 960-555, an entity will be a 'significant global entity' if either:

- it is a global parent entity with annual global income of \$1 billion or more; or
- it is a member of a group of entities that are consolidated for accounting purposes and the global parent entity of that group has annual global income of \$1 billion or more.

1.6 The Commissioner may also make a determination that results in an entity being a significant global entity for a period if:

- the entity is a global parent entity that has not prepared global financial statements for a period; and
- the Commissioner reasonably believes that if global financial statements had been prepared, the entity's annual global income for the period would have been \$1 billion or more.

1.7 A 'global parent entity' is broadly an entity that is not controlled by another entity according to accounting principles, or if these principles do not apply, commercially accepted principles relating to accounting (see section 960-560).

1.8 Section 960-565 provides that an entity's 'annual global income' for a period is either:

- if it is a member of a group of entities consolidated for accounting purposes—the total annual income of that global parent entity of that group as shown in its latest global financial statements for that period; or
- otherwise—the total annual income of that entity shown in its latest global financial statements for that period.

1.9 If an entity is a significant global entity, it is subject to Australia's country by country reporting rules, the multinational anti-avoidance law and the diverted profit tax. Significant global entities also face increased administrative penalties under the taxation law and may face additional reporting requirements.

Country by country reporting and significant global entities

1.10 Australia's country by country reporting rules implement in domestic law the recommendations in Action 13 of the G20 and OECD's Action Plan on Base Erosion and Profit Shifting – the BEPS Action Plan. Action 13 developed new standards for transfer pricing documentation and country by country reporting.

1.11 Currently Australia's definition of significant global entity means that the country by country reporting rules in Subdivision 815-E may not give the same outcome as would arise under the model legislation in Action 13 of the BEPS Action Plan.

1.12 Specifically, the Australian concept of significant global entity only treats an entity as being part of a group of entities if the head entity of the global group must prepare consolidated accounts covering that entity under the applicable accounting principles. In contrast, the OECD standard also requires reporting by the entities that would have to prepare consolidated accounts had one of the entities in the relevant structure been a listed company.

1.13 The OECD standard also requires reporting to cover entities that are not included in consolidated accounts due to materiality, which is not reflected in the existing Australian law.

Summary of new law

1.14 Schedule # amends the ITAA 1997 to create the concept of a notional listed company group – a group of entities that would be required to consolidate for accounting purposes as a single group if a member of the group was a listed company – and extend the definition of:

- significant global entity so that an entity will be a significant global entity if it is part of a notional listed company group that includes another entity that is a significant global entity; and
- annual global income so that a global parent entity’s annual global income is the total annual income of all members of any notional listed company group of which it is a member, as shown in global financial statements prepared on a consolidated basis for the group.

1.15 The amendments also provide that if an entity does not have adequate global financial statements for a period, its annual global income for that period is the amount a reasonable person would conclude would be its annual global income were such global financial statements prepared.

1.16 Finally, Schedule # also amends the reporting rules in Subdivision 815-E so that these rules now apply to entities that are country by country reporting entities rather than all significant global entities.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
An entity that is not a global parent entity is a significant global entity for a period if: <ul style="list-style-type: none">• it is either a member of:<ul style="list-style-type: none">– a group of entities that are consolidated as a single group for accounting purposes; or– a notional listed company group; and	An entity that is not a global parent entity is a significant global entity for a period if: <ul style="list-style-type: none">• it is a member of a group of entities that are consolidated for accounting purposes; and• another member of the group is a significant global entity.

<ul style="list-style-type: none"> • another member of the group is a global parent entity that is significant global entity. <p>A notional listed company group is a group of entities would be required to be consolidated as a single group for accounting purposes if a member of that group was a listed company.</p>	
<p>If a global parent entity is a member of:</p> <ul style="list-style-type: none"> • a group of entities consolidated for accounting purposes as a single group; or • a notional listed company group, <p>then the entity’s annual global income is the total annual income of all members of the group as reported in the most recent global financial statements.</p> <p>If an entity does not have global financial statements, their annual global income is the amount that a reasonable person in the position of the entity would consider to be their annual global income were global financial statements to be prepared.</p>	<p>If a global parent entity is a member of a group of entities consolidated for accounting purposes as a single group, the entity’s annual global income is the total annual income of all members of the group as reported in the most recent global financial statements.</p>
<p>An entity must report under Subdivision 815-E if, among other things, it is a country by country reporting entity.</p> <p>An entity will be a country by country reporting entity if the entity would be a significant global entity if:</p> <ul style="list-style-type: none"> • it was a global parent entity (even though it may be controlled by another entity); and • exceptions from consolidation (but not materiality) were taken into account in working out if an entity were part of a notional list company group. 	<p>An entity must report under Subdivision 815-E if, among other things, it is a significant global entity.</p>

Detailed explanation of new law

1.17 Schedule #:

- extends the circumstances in which an entity will be a significant global entity; and
- amends the reporting requirements in Subdivision 815-E to apply to subset of significant global entities referred to as country by country reporting entities.

1.18 The amendments to the definition of significant global entity ensures that the definition applies consistently to all types of entities, rather than potentially excluding members of large multinational groups headed by private companies, trusts or investment entities.

1.19 At the same time, the amendments to the country by country reporting rules in Subdivision 815-E ensure these rules are aligned with international practice and the OECD model.

Extending the definition of significant global entity

Significant global entities and annual global income

1.20 The amendments to the definition of significant global entity extends the circumstances in which an entity is a significant global entity to include entities as an significant global entity for a period if:

- for that period they are a member of a notional listed company group; and
- a member of that group is a global parent entity that either:
 - has annual global income of \$1 billion or more; or
 - is the subject of a determination by the Commissioner under subsection 960-555(3).

[Schedule #, item 7, paragraph 960-555(2)(a)]

1.21 If a global parent entity is a member of a notional listed company group its annual global income is the total annual income of all of the members of the group, determined on a consolidated basis, as shown in the latest global financial statements of the entity for the relevant period prepared on that basis. *[Schedule #, item 9, subsections 960-565(2) and (3)]*

1.22 When working out annual global income for this purpose, an entity will only have global financial statements if those statements have been prepared as if all members of the group were consolidated for accounting purposes as a single group. *[Schedule #, item 9, subsections 960-565(2) and (3)]*

1.23 Effectively these entities are treated in the same way as entities that are members of a group of entities that are consolidated for accounting purposes as one entity.

Global financial statements and annual global income

1.24 Schedule # also makes amendments to the interaction between global financial statements and global annual income.

1.25 Under the prior law, if an entity did not have global financial statements, it could not have an annual global income and would not be a significant global entity unless it was the subject of the determination by the Commissioner under subsection 960-555(3).

1.26 As a result of the amendments made by Schedule #, the annual global income of an entity that:

- does not have global financial statements; or
- is a member of a notional listed company group that does not have global financial statements prepared on the basis that the group was a group of entities consolidated for accounting purposes as a single group,

is the amount a reasonable person in the position of the entity would believe its annual global income would be were such global financial statements prepared for the period. [*Schedule #, item 9, subsections 960-565(4) and (5)*]

1.27 This is an objective test based on what would reasonably be determined by a fully informed person. The subjective belief of the actual entity is not relevant.

1.28 As consolidated accounts that meet the requirements to be global financial statements are less to be prepared for a notional listed company group, this amendment ensures that it is clear whether such members of such groups are significant global entities. It avoids any need for such an entity to prepare such accounts or seek a determination by the Commissioner to provide clarity about its status as a significant global entity.

1.29 These amendments do not affect the power of the Commissioner to make a determination under subsection 960-555(3) in relation to an entity if appropriate global financial statements have not been prepared for the entity for the period.

Notional listed company groups

1.30 A notional listed company group is a group of entities would be required to be consolidated as a single group for accounting purposes under the applicable accounting principles or commercially accepted principles relating to accounting, if a member of that group was a listed

company (broadly, has its shares listed for quote on any public exchange – see section 26BC of the ITAA 1936). *[Schedule #, item 10, subsections 960-575(1) and (2)]*

1.31 An entity can be a member of a notional listed company group even if it is actually consolidated with other entities for accounting purposes as a single group. *[Schedule #, item 10, subsection 960-575(5)]*

1.32 When working out if an entity is a member of a notional listed company group, any exceptions in the relevant principles that may permit an entity not to consolidate with other entities are disregarded. This means, for example, that an investment entity that controls other entities but is not able to consolidate with those entities would still be part of a notional listed company group with those entities. *[Schedule #, item 10, paragraph 960-575(4)(a)]*

1.33 Similarly, any rules that permit an entity not to consolidate with another entity or entities as this would be immaterial are also disregarded. *[Schedule #, item 10, paragraph 960-575(4)(b)]*

1.34 These rules ensure that the definition of significant global entity applies consistently to all types of entities. It removes potential gaps in the application of the rules based on the type of entity and the particular requirements applying for accounting purposes.

Country by country reporting

Country by country reporting entities

1.35 Schedule # also amends the country by country reporting regime in Subdivision 815-E. Previously, one of the conditions for an entity to need to report under that regime was that the entity was a significant global entity.

1.36 As a result of the changes to the definition of significant global entity, its scope differs from the scope of the entities required to undertake country by country reporting under Action 13 of the BEPS Action Plan.

1.37 To better align with international standards, the amendments change the scope of Subdivision 815-E so that it requires reporting by country by country reporting entities rather than all significant global entities. *[Schedule #, items 2 and 3, section 815-350 and paragraph 815-355(1)(a)]*

1.38 An entity is a country by country reporting entity if it would be a significant global entity if:

- the entity was a global parent entity (whether or not it is controlled by another entity); and

- exceptions to consolidation (but not rules about materiality) were taken into account in working out the membership of notional listed company groups.

[Schedule #, item 6, section 815-370]

1.39 Effectively, most significant global entities will still be country by country reporting entities. In many cases, the assumptions will not affect whether an entity is a significant global entity (for example, an entity in a group of entities that are consolidated for accounting purposes headed by a significant global entity will be a country by country reporting entity). In these cases an entity will be a country by country reporting entity if it is a significant global entity.

1.40 The assumption that the rules around notional groups take into account exceptions from consolidation means that an entity that is only a significant global entity because these exceptions are disregarded will not be a country by country reporting entity.

1.41 This also means that an entity controlled by such an entity is not automatically a country by country reporting entity.

1.42 However, this is subject to the consequences of assumption that all entities are global parent entities. As all entities are treated as being global parent entities when determining if they are a country by country reporting entity, an entity can be a country by country reporting entity even if it is controlled by an entity that is not a country by country reporting entity.

1.43 For example, a company owned by an investment entity is a significant global entity because it is a member of a notional listed company group headed by the investment entity. For the purposes of the country by country reporting rules, it would not be part of notional listed company group with the investment entity as an exception to consolidation applied. However, if its own annual global income exceeds \$1 billion, it would be a country by country reporting entity as it would be a significant global entity were it a global parent entity itself.

1.44 Similarly, an investment entity may own an entity that controls a group of other entities. For the purposes of the country by country reporting regime, the group of entities may not be part of a notional listed company group as an exception to consolidation applies. However, the group excluding the investment entity may still form a notional listed company group or may be actually consolidated for accounting purposes as a single group. If this is the case, all members of that group will be country by country reporting entities if any member of the group would be a significant global entity disregarding the investment entity.

1.45 This is consistent with international practice and OECD model legislation.

Country by country reporting obligations

1.46 The amendments also make changes to information that is required in the statements that must be provided by country by country reporting entities to be consistent with the changes to the scope of the affected entities.

1.47 Specifically, the statements provided by country by country reporting entities now need to include information on the other members of notional listed company groups of which the entity is a member for the purposes of the country by country reporting provisions. This means that exceptions to requirements to consolidate (but not rules relating to materiality) are taken into account in working out the membership of the group. *[Schedule #, item 4, paragraph 815-355(3)(a)(ii)]*

1.48 As a result, consistent with the treatment of members of groups of entities that are consolidated for accounting purposes, such entities must provide statements dealing with the global operations and activities and the allocation between countries of the tax paid by the group members of any notional listed company group of which they are a member.

1.49 This ensures that the statements that must be provided are consistent with international practice and OECD model legislation.

Consequential amendments

1.50 Schedule # also makes consequential amendments to renumber provisions, add headings and insert definitions in the dictionary in subsection 995-1(1). *[Schedule #, items 1, 8 and 11 to 13, the heading to Subdivision 815-E, section 960-565 and the definitions of ‘country by country reporting entity’, ‘member’ and ‘notional listed company group’ in subsection 995-1(1)]*

Application and transitional provisions

1.51 The amendments made by Schedule # to this Bill apply in income years starting on or after 1 July 2018. *[Schedule #, item 14]*