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TREASURY LAWS AMENDMENT (MEASURES FOR CONSULTATION)  
BILL 2019

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EXPOSURE DRAFT EXPLANATORY MATERIALS



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***Table of contents***

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Glossary..... 1

Chapter 1      Significant global entity ..... 3



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# ***Glossary***

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

<b><i>Abbreviation</i></b>	<b><i>Definition</i></b>
Commissioner	Commissioner of Taxation
ITAA 1997	<i>Income Tax Assessment Act 1997</i>
TAA 1953	<i>Taxation Administration Act 1953</i>



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# Chapter 1

## Significant global entity

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### Outline of chapter

1.1 Schedule # to this Bill expands 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
- applies despite exceptions to when a group of entities must prepare consolidated accounts, including materiality rules, in the applicable accounting rules.

1.2 The amendments also modify the rules that identify which entities must undertake country by country reporting under the tax law 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. All references to dollars are to Australian dollars.

### 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 is 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 where;
  - the group is consolidated for accounting purposes as a single group; 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 under subsection 960-555(3) 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 a 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

model legislation also requires reporting by entities that would have had to prepare consolidated accounts had the parent entity in the relevant structure been a listed company.

1.13 The OECD model legislation also requires reporting to cover entities that are not included in consolidated accounts due to materiality rules. This OECD requirement is not reflected in the existing Australian law.

## **Summary of new law**

1.14 Schedule # to this Bill expands the scope of the concept of a significant global entity in the ITAA 1997 so that it also 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. Under the amendments the criteria for determining if an entity is a significant global entity applies despite exceptions to the rules setting out when a group of entities must consolidate for accounting purposes, including materiality rules, in the applicable accounting rules.

1.15 The scope of significant global entity is expanded by introducing 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 under the applicable accounting rules if:

- any member of the group was a listed company; and
- exceptions to requirements about when a group of entities would be required to consolidate, including materiality rules, were disregarded.

1.16 The amendments also 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.

1.17 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 that would have been its annual global income if such global financial statements had been prepared.

1.18 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 (also referred to as CBC reporting entities) rather than all significant global entities to ensure these rules are aligned with Australia’s international commitments.

1.19 An entity is a country by country reporting entity if, broadly, they would be a significant global entity if the notional listed company group rules took into account exceptions to consolidation other than the materiality rule and did not include individuals.

### Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
<b>Significant global entities</b>	
<p>An entity is a significant global entity for a period if:</p> <ul style="list-style-type: none"> <li>• it is either a member of:                             <ul style="list-style-type: none"> <li>– a group of entities that are consolidated as a single group for accounting purposes; or</li> <li>– a notional listed company group; and</li> </ul> </li> <li>• another member of the group is a global parent entity that is a significant global entity.</li> </ul> <p>A global parent entity is also a significant global entity if its annual global income is \$1 billion or more or if it is subject to a determination by the Commissioner under subsection 960-555(3).</p> <p>A notional listed company group is a group of entities that would be required to be consolidated as a single group for accounting purposes if a member of that group was a listed company and exceptions to requirements to consolidate were disregarded.</p>	<p>An entity is a significant global entity for a period if:</p> <ul style="list-style-type: none"> <li>• it is a member of a group of entities that are consolidated for accounting purposes; and</li> <li>• another member of the group is a global parent entity that is a significant global entity.</li> </ul> <p>A global parent entity is also a significant global entity if its annual global income is \$1 billion or more or if it is subject to a determination by the Commissioner under subsection 960-555(3).</p>

<i>New law</i>	<i>Current law</i>
<b>Annual global income of global parent entities</b>	
<p>If a global parent entity is a member of:</p> <ul style="list-style-type: none"> <li>• a group of entities consolidated for accounting purposes as a single group; or</li> <li>• a notional listed company group;</li> </ul> <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 appropriate global financial statements, their annual global income is the amount that would be their annual global income had appropriate global financial statements been 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 their most recent global financial statements.</p>
<b>Country by country reporting</b>	
<p>An entity must undertake country by country reporting under Subdivision 815-E if, among other things, it is a country by country reporting entity.</p> <p>An entity is a country by country reporting entity if, broadly, it would be a significant global entity if the notional listed company group rules did not disregard exceptions to consolidation other than the materiality rule and did not include individuals.</p>	<p>An entity must undertake country by country reporting under Subdivision 815-E if, among other things, it is a significant global entity.</p>

## Detailed explanation of new law

1.20 Schedule #:

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

1.21 The amendments to the definition of significant global entity ensure 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.

1.22 The amendments to the country by country reporting rules in Subdivision 815-E ensures Australian law is aligned with international practice and the OECD model legislation.

## Extending the definition of significant global entity

### *Significant global entities and annual global income*

1.23 The amendments to the definition of **significant global entity** extend the circumstances in which an entity is a significant global entity to include where an entity is a member of a notional listed company group that includes a global parent entity that either:

- has annual global income equal to or in excess of \$1 billion; or
- is the subject of a determination by the Commissioner under subsection 960-555(3).

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

1.24 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 that show the total annual income of all of the members of the group on a consolidated basis – if such statements exist. If no such statements exist, then the annual global income of the entity is determined using the rules explained in paragraphs 1.28 to 1.33. *[Schedule #, item 10, subsection 960-565(1)(aa)]*

1.25 When working out annual global income for this purpose, the annual global income of an entity is only based on the total annual income reported in its global financial statements if those statements had set out the total annual income of the members of the group on the basis that all members of the group were consolidated for accounting purposes as a single group. *[Schedule #, item 10, subsection 960-565(1)(aa)]*

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

1.27 If an entity is a member of both types of group, it is the annual income of the notional listed company group (which will be the larger group) that is used in determining the income of the entity. *[Schedule #, item 10, subsection 960-565(1)(a)]*

***Global financial statements and annual global income***

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

1.29 Prior to these amendments, if an entity did not have global financial statements, it could not have annual global income and would not have been a significant global entity unless it was the subject of a determination by the Commissioner under subsection 960-555(3).

1.30 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 or a group of entities consolidated for accounting purposes as a single group and 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 that would be the annual global income were such global financial statements prepared for the period. [*Schedule #, items 8, 10 to 12, subsection 960-565(1), paragraph 960-565(1)(aa) and subsections 960-565(2) and (3)*]

1.31 This is an objective test based on what would be expected to be the amount of such income if adequate statements were prepared.

1.32 This amendment ensures that the absence of global financial statements covering the whole of a group does not prevent the total annual income of the members of the group from being taken into account in determining if members are significant global entities. This is particularly important for notional listed company groups, as there is no requirement for the preparation of consolidated accounts for the entirety of such groups. It also avoids any need for such groups to prepare consolidated accounts or seek a determination by the Commissioner to provide clarity about its status as a significant global entity.

1.33 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 global financial statements have not been prepared for the entity for the period.

***Notional listed company groups***

1.34 A **notional listed company group** is a group of entities that 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 an entity was a listed company (broadly, had its shares been listed for quotation on any public

exchange – see section 26BC of the ITAA 1936). *[Schedule #, item 13, subsection 960-575(1)]*

1.35 Each entity in the notional listed company group is a member of that notional listed company group. *[Schedule #, item 13, subsection 960-575(2)]*

1.36 Whether entities would be required to be consolidated for accounting purposes as a single group, is to be determined based on relevant accounting principles or commercially accepted principles relating to accounting (if accounting principles do not apply in relation to those entities). *[Schedule #, item 13, subsection 960-575(3)]*

1.37 However, 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 required to consolidate with those entities would still be part of a notional listed company group with those entities. *[Schedule #, item 13, paragraph 960-575(4)(a)]*

1.38 Similarly, any rules that permit an entity not to consolidate with another entity or entities as the effect of consolidating would be immaterial because of the size of the entities or for other reasons are also disregarded. *[Schedule #, item 13, paragraph 960-575(4)(b)]*

1.39 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 for certain types of entities and the particular requirements applying for accounting purposes.

### **Example 1.1: notional listed company group**

Entity A, is an investment entity and global parent entity that controls Entity B which in turn controls Entity C and Entity D.

As Entity A is an investment entity, it is not required to consolidate with Entities B, C and D for accounting purposes. Entity B is also not required to consolidate with Entity D as Entity D is so small that its activities are not material to Entity B's overall accounts.

However, under the relevant accounting standards Entity A would be required to consolidate if not for the exception for investment entities and the materiality rule. As a result, Entities A, B, C and D are a notional listed company group.

## **Country by country reporting**

### ***Country by country reporting entities***

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

1.41 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.

1.42 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)]*

1.43 An entity is a **country by country reporting entity** (also referred to as a CBC reporting entity) for a period if either of the following apply:

- it is a country by country parent for the period; or
- it is a member of a country by country reporting group and another member of that group is a country by country reporting parent.

*[Schedule #, item 5, subsection 815-370(1)]*

1.44 A entity is a **country by country reporting parent** for a period if:

- it is not an individual;
- is either not a member of a country by country reporting group or is not controlled by any other entity in the same country by country reporting group; and
- either:
  - if it is a member of a country by country reporting group—the annual global income of the group is \$1 billion or more; or
  - otherwise—the annual global income of the entity alone is \$1 billion or more.

*[Schedule #, item 5, subsection 815-375]*

1.45 Effectively, a country by country reporting parent (also referred to as a CBC reporting parent) is an entity that would be a global parent entity and a significant global entity were all entities outside of any country by country reporting group of which it is a part were disregarded. In this context, it does not matter if that entity is controlled by another entity outside the group. The country by country parent concept allows an alternative controlling entity to be identified in circumstances where an entity is controlled by another entity that does not form part of the country by country reporting group. This is illustrated in example #.2 below.

1.46 A **country by country reporting group** (also referred to as a CBC reporting group) is a group of entities that would be a notional listed company group if the definition of notional listed company group took

into account exceptions to consolidation (other than an exception for immateriality) in the relevant accounting principles or commercially accepted accounting principles (if accounting principles do not apply to the entity) and also excluded individuals. It also includes a group of entities consolidated for accounting purposes as a single group. *[Schedule #, item 5, subsection 815-380]*

1.47 Most significant global entity groups that are a notional listed company group will also be country by country reporting entities. However, some exceptions apply. Although an individual can be a significant global entity, an individual cannot be a member of a country by country reporting group. Similarly, investment entities can form part of a group of significant global entities but, subject to the relevant accounting principles, may not be included in a country by country reporting group. *[Schedule #, item 5, subsection 815-380]*

1.48 For example, a non-investment entity 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. It would not be part of a country by country reporting group headed by the investment entity as an exception to consolidation applies in the relevant accounting principles. However, the entity that is owned by the investment entity may form part of a country by country reporting group with other entities with which it would be required to consolidate for accounting purposes if the company was a listed company. In these circumstances the entity that is owned by the investment entity may be a country by country reporting parent (see paragraph 1.44 and example 1.2).

1.49 Each entity in a country by country reporting group is a **member** of that country by country reporting group. The term member clarifies the status of entities within country by country reporting groups. *[Schedule #, item 5, subsection 815-380(2)]*

### **Example 1.2: identifying the country by country parent entity and country by country reporting entity**

Assuming the same facts as in example 1.1 above, Entity A does not form part of a country by country reporting group with Entity B, Entity C and Entity D. This is because the exception to the requirement to consolidate for investment entities is taken into account when working out the entities that form part of a country by country reporting group.

As Entity A is not a member of any country by country reporting group, it may be a country by country reporting parent. It will be a country by country reporting parent and a country by country reporting entity if its own total annual global income is \$1 billion or more.

Entity B controls Entity C and Entity D and, under applicable accounting standards would be required to be consolidated for accounting purposes as a single group were Entity B a listed company,

disregarding the materiality rule. As a result Entities B, C and D are a country by country reporting group.

Entity B is not controlled by any other entity in the group so it too may be a country by country reporting parent. It will be a country by country parent and a country by country reporting entity if, broadly, the annual global income of the group (the total annual income of Entities B, C and D worked out on a consolidated basis) is \$1 billion or more. If Entity B is a country by country reporting parent, Entities C and D will also be country by country reporting entities.

### ***Country by country reporting obligations***

1.50 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.

1.51 Specifically, the statements provided by country by country reporting entities now need to include information on the other members of any country by country reporting group of which the entity is a member for the purposes of the country by country reporting provisions. *[Schedule #, item 4, subparagraph 815-355(3)(a)(ii)]*

1.52 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 country by country reporting group of which they are a member.

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

### **General purpose financial statements**

1.54 Schedule # also amends the requirement for certain corporate tax entities to provide the Commissioner with a general purpose financial statement for a financial year.

1.55 Previously, this obligation applied to entities that were, among other things, significant global entities. Following the amendments, the obligation instead applies to entities that are, among other things, country by country reporting entities. *[Schedule #, items 17 and 18, the heading to section 3CA and paragraph 3CA(1)(a) of the TAA 1953]*

1.56 This ensures that the obligation to provide general purpose financial statements remains aligned with the relevant accounting standards and avoids unnecessary compliance burdens for investment entities.

## Consequential amendments

1.57 Schedule # makes consequential amendments to renumber provisions, add headings and insert definitions in the dictionary in subsection 995-1(1) of the ITAA 1997. It also makes consequential amendments to existing provisions and terms related to significant global entities to ensure that these provisions function as intended given the changes made by these amendments. *[Schedule #, items 1, 6, 8, 9, and 14 to 16, the heading to Subdivision 815-E, sections 960-50(7A) and 960-565 and the definitions of ‘CBC reporting entity’, ‘CBC reporting parent’, ‘CBC reporting group’, ‘country by country reporting entity’, ‘country by country reporting group’, ‘country by country parent entity’, ‘member’ and ‘notional listed company group’ in subsection 995-1(1) of the ITAA 1997]*

## Application and transitional provisions

1.58 The amendments made by Schedule # to this Bill commence from the first day of the first quarterly period that occurs after the day the Bill receives Royal Assent. *[Clause 2]*

1.59 The amendments apply to income years or periods starting on or after 1 July 2018. *[Schedule #, item 19]*

1.60 When determining if an entity has country by country reporting obligations for a period, it is necessary to determine if the entity was a country by country reporting entity for the previous period. For the avoidance of doubt, the amendments specify that if the amendments apply to a period, they also apply for the purpose of determining if an entity was a country by country entity for a previous period when this is relevant to the country by country reporting obligations of the entity in a period after 1 July 2018, even if the previous period began before 1 July 2018.

1.61 The measure generally applies retrospectively from 1 July 2018 as announced in the Budget on 8 May 2018. The retrospective application of the measure is consistent with the Government’s intention to broaden the scope of the significant global entity definition to ensure that Australia’s multinational tax integrity rules apply as intended. Retrospectivity is necessary to ensure that a significant period does not exist between the announcement of the measure and the application of the improved integrity rules. *[Schedule #, subitems 19(2) and (3)]*

1.62 However, to ensure that penalty obligations imposed under the law do not apply retrospectively, the amendments include a transitional provision to ensure the penalties that arise from the measure do not apply until 1 July 2020 for entities that were not previously significant global entities. *[Schedule #, subitems 19(2) and (3)]*

1.63 If an entity is a significant global entity due to the amendments made by this Schedule for the period on or after 1 July 2018 and before

1 July 2020 the entity is not treated as a significant global entity for the transitional period for the purpose of penalty provisions in Divisions 284 and 286 in Schedule 1 to the TAA 1953.