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The Principal Adviser
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The Treasury
Langton Crescent
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Email: transferpricing@treasury.gov.au

Business Council of Australia

Dear Sir/Madam

REVIEW OF TRANSFER PRICING RULES – RETROSPECTIVE APPLICATION

The Business Council of Australia is pleased to have the opportunity to make a submission on the Consultation Paper 'Income tax: cross border profit allocation – Review of transfer pricing rules'.

While the consultation paper addresses a number of technical tax issues, the paper and the Assistant Treasurer's associated media release of 1 November 2011 raise substantive matters around potential retrospective application of tax changes (e.g., that 'the clarifications will apply to income years commencing on or after 1 July 2004 in treaty cases').

The BCA has strong views on retrospective tax law changes. Such changes are inconsistent with long-standing principles of sound tax design and do little to enhance Australia's reputation as a destination for foreign investment.

In highlighting this issue we draw to your attention the Senate procedural orders *(C40 Taxation Bills – retrospectivity, 8 November 1988 J.1104)* which include a presumption against the passage of retrospective tax law.

This view has also been reinforced in the review of the Tax Design Panel from 2008 which noted in its Better Tax Law Design and Implementation report:

- "3.17 considers that tax measures announced by the Government should generally operate prospectively (ie. take effect only after they are enacted). This would enable taxpayers to structure their affairs according to the enacted law and respect the role of Parliament to make laws."

- '3.19, "[w]hile it may occasionally be appropriate to announce measures that apply before the legislation is enacted, these should be kept to a minimum. Where amendments apply before the legislation is enacted, the announcement should clearly state why retrospective application is necessary."

We would further note that the issues of retrospectivity contained in this latest paper follow other recent government announcements involving retrospective tax changes to the income tax laws affecting consolidated groups, and the amendments to the *Petroleum Resource Rent Tax Assessment Act 1997* which were included in the *Tax Laws Amendment (2011 Measures No. 8) Bill 2011*.

The BCA is concerned at what has clearly become an increasing tendency on the government's behalf to pursue retrospective tax law changes. These concerns cannot be understated because the consequences add uncertainty and increased risk to the investment climate in Australia.

Feedback received by the BCA through the course of 2011 from foreign institutional investors on their attitudes to Australia highlight the importance of certainty and policy credibility including in relation to tax policy. Investors are making it known that recent policy changes have made it harder to invest with certainty in Australia.

This background is highly relevant to the Transfer Pricing Consultation Paper given the explicit recognition in the paper's introduction that *'an important consideration in designing these rules is that they should not unreasonably inhibit Australia's attractiveness as a destination for new investment and business activity.'*

As well as endorsing the concerns over retrospectivity outlined in the submission prepared by the Corporate Tax Association (CTA), the BCA supports the thrust of the CTA's views on other aspects of the Discussion Paper.

- The BCA acknowledges that there may be merit in making changes to Australia's transfer pricing rules to align them more closely with agreed international practices such as the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations as revised in July 2010 (the OECD Guidelines). However any changes must have a prospective application.

- We would also support the CTA's comments that 'if the OECD guidelines are to be incorporated into the domestic law we see no good reasons for the Commissioner to have any residual discretion. The Guidelines provide that the most appropriate arms length method should be employed to price the relevant transaction, and it gives the administrations the power (albeit in limited circumstances) to re-characterise the transaction actually entered into. No additional discretion should be required to make any necessary transfer pricing adjustments and the Commissioner having such a discretion would be inconsistent with a full self-assessment system'.

- The BCA supports the CTA's comments on applying time limits for making transfer pricing adjustments so that they are aligned with the general law (i.e., four years versus the current open ended system). Applying an annual statutory threshold of $10 million in related party cross-border dealings before taxpayers become liable to transfer pricing adjustment (or examinations) also has the potential to reduce compliance costs, especially for small and medium sized enterprises.

In concluding this submission we note the intention for the Board of Taxation to be engaged in the review of the transfer pricing rules. I have therefore taken the liberty of copying this letter to the Chairman of the Board of Taxation, Mr Chris Jordan.

I would urge that the issues raised in this submission be given careful consideration in the interests of ensuring Australia's attractiveness as a destination for new investment and business activity are maintained.

Please feel free to contact me or Peter Crone, Director Policy and Chief Economist (03 8664 2604) if you would like to discuss any aspects of this submission further.

Yours sincerely

Jennifer Westacott
Chief Executive

cc: Mr Chris Jordan, Chairman, Board of Taxation