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OF AUSTRALIA

Business Law Section

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Via email: taxlawdesign@treasury.gov.au

3 July 2015

Dear Sirs

Better Targeting the Income Tax Transparency Laws

The Taxation Committee of the Business Law Section of the Law Council of Australia (**the Committee**) welcomes the opportunity to participate in the Government's consultation in respect of the Exposure Draft Tax and Superannuation Laws Amendment (Better Targeting the Income Tax Transparency Laws) Bill 2015 (Draft Bill).

This submission responds to the policy of the provisions referred to in the Draft Bill and the specific amendments it proposes to the Taxation Administration Act 1953. Those provisions were inserted into that Act in 2013 following the release of the Improving the Transparency of Australian Business Tax System discussion paper issued in April 2013 (**Discussion Paper**) by the then Assistant Treasurer. The Committee provided a detailed submission to the Treasury in response to the Discussion Paper (**Previous Submission**). This submission builds on the Previous Submission, specifically in response to the amendments proposed by the Draft Bill.

Outline of Submission

The Committee welcomes the amendments contained in the Draft Bill, as they will alleviate distinctly discriminatory provisions which inappropriately overturn fundamental rights of taxpayer privacy for private Australian companies and their shareholders.

The proposed amendments go a significant way to addressing specific issues with the income and tax publication provisions commented on in detail in the Committee's Previous Submission. The Committee's support for the Draft Bill is discussed in more detail in Part 1 of these Submissions.

The Committee also submits that the Draft Bill should be introduced as a Bill and passed with only minor amendment to clarify aspects of drafting in the proposed new section 3C(1) of the Act. This is discussed in Part 2 below.

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Finally, in Part 3, the Committee notes the lack of public benefit arguments that have been raised since the introduction of the new disclosure laws in 2013 and maintains that despite the efforts of the Draft Bill, the disclosure laws continue to manifestly discriminate, produce unjust results and will not likely achieve the intended policy objectives.

Part 1 – Support for the Draft Bill

The explanatory memorandum (EM) to the Draft Bill outlines four main reasons why the changes to the current tax disclosure laws are necessary for private companies:

1. The disclosures can reveal commercial information of a private company and undermine its ability to engage in proper commercial negotiations;
2. The disclosures may compel private companies to restructure their corporate groups in order to fall below the disclosure threshold;
3. The disclosures would lead to additional costs and compliance burden to private companies in having to justify the tax information to the public; and
4. The disclosures can negatively impact on the personal privacy and security of the shareholders of private companies.

The Committee strongly agrees with the very legitimate concerns raised by the Government in the EM, and adds the following reasons.

a) Taxpayer's fundamental right to privacy

As noted in the Previous Submission, the fundamental right to privacy of taxation affairs for those companies affected by section 3C should not be displaced without first having undertaken a rigorous analysis of the public benefit, based on empirical evidence. No such rigorous analysis has been performed, and no such empirical evidence obtained or discussed. The effect of section 3C is to unfairly and inequitably target only those companies which exceed the arbitrary income threshold, and not other taxpayers (such as trusts, partnerships or otherwise) and not those companies which fall below the arbitrary threshold. Without amendment, section 3C discriminates against company entities which fall within it.

The fundamental issues with a reversal of Australia's long-held principles of taxpayer privacy are amplified for private Australian companies, where simple ASIC searches will usually reveal the individuals or families associated with those companies. This is contrasted with public and foreign multinational corporations with potentially many thousands of shareholders and/or no public disclosure of who those persons are.

For Australian private companies the disclosure of their private taxation affairs is likely to lead to many of the key issues and concerns identified in the Exposure Draft Explanatory Memorandum accompanying the Draft Bill. The Committee considers the issues with such disclosure identified in the Exposure Draft Explanatory Memorandum are cogent and genuine concerns.

b) Misinformation and confusion

The current disclosure laws would also result in substantial misinformation in the public regarding the taxation affairs of the individuals and families behind those companies,

where the income of a company is presumed to be the income of those individuals. This is particularly the case where, for example, ultimate taxation of particular types of income are yet to be borne by those persons, such as exempt and 'non-assessable non-exempt' items of income which will effectively be taxed as an unfranked dividend when ultimately distributed to those individuals; or tax has been paid by other entities or in other jurisdictions but which is credited for the Australian private company, but disclosure suggest the company does not bear tax. Private Australian companies will be put to inappropriate expense to attempt to explain the inherently complex corporate taxation system, or to attempt to reduce the impact of competitors, suppliers and customers seeing that highly commercially sensitive information. To avoid this outcome, many companies will likely restructure affairs to avoid the public disclosure where feasible.

This is a fundamental reversal of the long enshrined principle of taxpayer secrecy in Australia, reversing a longstanding tenet of Australia's taxation laws but only for companies which exceed the arbitrary income threshold, and exacerbated in respect of private companies with identifiable shareholders and owners. The Committee welcomes the removal of this outcome for private Australian companies and their owners.

c) Purpose of the tax disclosure laws

The explanatory memorandum to the Bill which first introduced section 3C in 2013 stated the rationale for publication of the specified confidential income and taxation information of companies meeting the \$100 million 'income' threshold as being "to discourage large corporate tax entities from engaging in aggressive tax avoidance practices" and "to provide more information to inform public debate about tax policy, particularly in relation to the corporate tax system". As observed publicly by the Commissioner of Taxation Mr Chris Jordan, the introduction of section 3C into the Taxation Administration Act "was really for multinational companies operating here, disclosing quite low revenue" and was not intended to capture private Australian companies (AFR 20 March 2015, page 6).

The disclosure laws were introduced in 2013 against a backdrop of discussion about base erosion and profit shifting by multinationals and efforts to discourage aggressive tax practices by large multinationals to ensure they "pay their fair share of tax" in Australia. The consequence of the very broad blanket of the tax disclosure laws as enacted was that they capture private Australian companies that have total accounting income exceeding an arbitrary threshold.

d) No evidence of widespread aggressive tax avoidance

As the Committee set out in its Previous Submission, there has been no evidence provided of widespread aggressive tax avoidance practices by companies in Australia which exceed the \$100 million threshold test, and there is certainly no evidence that publication of isolated aspects of the income and taxation affairs of such companies would properly inform public debate about tax policy.

e) Arbitrary \$100 million total income threshold

There is a misalignment between the Australian Tax Office's (**ATO**) categorisation of large multinationals or similar (being companies with total income of \$250 million and above) and large corporations under the current tax disclosure laws (being companies with total income of \$100 million or greater). This mismatch inevitably captures private Australian

companies that would otherwise traditionally be considered “small and medium enterprises” under the ATO’s classification. Based on a policy of publication of the affairs of “large” companies, many companies affected by the current law were not intended to be caught by the disclosure laws, on the ATO classifications.

The \$100 million total income threshold is an arbitrary gateway which will cause private Australian companies with gross income exceeding this amount to suffer the potentially very damaging consequences of having their sensitive taxation information disclosed publicly.

f) The disclosure laws are inequitable and lead to unjust results

Finally, as noted by the Committee in the Previous Submission, the current tax disclosure laws are inequitable as they breach the fundamental right to privacy and confidentiality of tax information in respect of some taxpayers only – those specifically targeted by section 3C of the Act. Further, the Committee submits there is no public benefit of disclosing such income and taxation information as it would not stimulate genuine public debate on tax policy. This is addressed further in Part 3. Instead, it would add costs both to the Government and the affected taxpayers of disclosing that information, as well as waste time and resources of companies in having to justify their tax position to the public, or restructure their corporate affairs in order to avoid the disclosure laws altogether.

For these reasons, the amendments to the Draft Bill are strongly supported by the Committee in protecting private Australian companies from these discriminatory and unjust disclosure laws, and is a significant improvement to the provisions of the Act enacted in 2013.

Part 2 – Clarification to the Draft Bill

The proposed new section 3C(1) will limit the disclosures to exclude Australian resident companies which do not have a foreign ultimate holding company, or foreign shareholdings exceeding 50%. For this purpose Australian resident companies, private companies, and ultimate holding companies are defined by reference to the Income Tax Assessment Acts. However “foreign shareholding in the entity” (proposed section 3C(1)(b)(iii)) is not a defined term. It is not clear from that phrase whether direct as well as indirect shareholdings are taken into account.

The Exposure Draft Explanatory Memorandum states that the Commissioner of Taxation will determine this from company tax return disclosures, which are based on company tax return instructions.

The Committee submits this would be more appropriate to define in the Taxation Administration Act for this purpose rather than rely solely on the Commissioner’s tax return instructions, which are potentially liable to change and are not determined by the Parliament. The principles of the rule of law require the law to be known, readily ascertainable, and available to taxpayers.

Part 3 – Further commentary on the current disclosure laws

Despite the amendments in the Draft Bill, the Committee’s view is that the disclosure laws continue to be discriminatory and unjust. Public disclosure of selected aspects of the

income and taxation of those companies – the gross accounting income, net taxable income and Australian tax payable, would not likely “discourage large corporate tax entities from engaging in aggressive tax audit practices”, nor “provide more information to inform public debate about tax policy” as was the stated policy of section 3C. The information which would be published does not provide any demonstrative information to explain tax policy or engage a debate about it, nor is there any indication that such information would discourage large companies from engaging in aggressive tax avoidance. Rather, the expected effect of those laws would be a “naming and shaming” in the press without any explanation as to the fundamental differences between gross income for accounting purposes, and net taxable income.

Since the Discussion Paper was released in April 2013, both the Treasury and the ATO, as well as numerous industry bodies, have acknowledged the lack of ability in such a disclosure law generating meaningful public tax debate. The Treasury and the ATO themselves have noted that comparison of accounting and net taxable income is fundamentally different and potentially dangerous. At a Senate Estimates Hearing on 22 October 2014, ATO Second Commissioner Mr Neil Olesen said that comparing accounting profit to taxable income was “meaningless to the extent that taxable income and accounting profits are two fundamentally different concepts, so you cannot draw a conclusion”. He also stated that such comparison creates incorrect perceptions of effective tax rates, which is “an unfair impression to leave, and a damaging one from a tax administrator’s view”.

Executive Director Revenue Group of the Treasury Mr Rob Heferen stated at that Hearing that comparing accounting profit and taxable income is like “comparing an apple with an orange and it not being about fruit”. He also stated that discussion focused solely on the comparison between gross accounting income and net taxable income “is fundamentally a misunderstanding of what taxable income in Australia ought to be about”.

ATO Second Commissioner Mr Andrew Mills went further to give examples of key and fundamental differences between accounting and tax, and of tax credits, and tax policies which without detailed technical explanation would be entirely misleading.

The compliance costs and reputational risks for such companies endeavouring to explain Australia’s highly complex corporate tax system in the press has no justification. To apply those laws, and that level of public scrutiny, to only one type of taxpayer entity – companies, and not trusts, partnerships, individuals, or otherwise – and only to those which exceed a certain threshold, creates a disproportionate and discriminatory rule which would be applied only against those companies who fall into the narrow class.

Conclusion

Excluding Australian private companies from the public disclosure as proposed by the Draft Bill is welcomed by the Committee, and commended as an important and fundamental requirement in the pursuit of equity for Australian taxpayers. The amendments proposed by the Draft Bill are crucially important amendments to address concerns raised by the Committee in the Previous Submission for Australian private companies, and are considered a vital improvement to restore fairness, equity and basic principles of the rule of law for those taxpayers and their owners.

Should the Treasury or the Government wish to discuss these views with the Committee, discussions can be initiated by contacting the Committee Chair, Adrian Varrasso on 03-8608 2483 or via email: adrian.varrasso@minterellison.com

Yours faithfully,

A handwritten signature in black ink, appearing to read 'John Keeves', with a long horizontal flourish extending to the right.

John Keeves, Chairman
Business Law Section