

EXPOSURE DRAFT

COUNTRY-BY-COUNTRY REPORTING AND NEW TRANSFER PRICING
DOCUMENTATION STANDARDS

EXPLANATORY MATERIALS

Glossary

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

<i>Abbreviation</i>	<i>Definition</i>
ATO	Australian Taxation Office
BEPS Action Plan	The G20 and Organisation for Economic Co-operation and Development's <i>Action Plan on Base Erosion and Profit Shifting</i>
CbC	Country-by-Country
Commissioner	Commissioner of Taxation
ITAA 1997	<i>Income Tax Assessment Act 1997</i>
OECD	Organisation for Economic Co-operation and Development
Transfer Pricing Guidelines	<i>OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations</i>
PE	permanent establishment
TAA 1953	<i>Taxation Administration Act 1953</i>

Chapter 1

Country-by-Country Reporting

Outline of chapter

1.1 Schedule # to this Bill implements Action 13 of the G20 and Organisation for Economic Co-operation and Development's *Action Plan on Base Erosion and Profit Shifting* (the BEPS Action Plan) into Australian law. Action 13 has developed new standards for transfer pricing documentation and Country-by-Country (CbC) reporting. These amendments require entities with annual global revenue of \$1 billion or more to provide a statement to the Commissioner of Taxation (Commissioner) with relevant and reliable information to assist the Commissioner to carry out transfer pricing risk assessments.

Context of amendments

Background

1.2 Australia's transfer pricing rules seek to ensure that the appropriate return for the contribution made by the Australian operations of a multinational is taxable in Australia for the benefit of the community. In 2013, Subdivisions 815-B, 815-C and 815-D of the *Income Tax Assessment Act 1997* (ITAA 1997) were introduced to align Australian domestic law with the international transfer pricing standards set out in the *OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations* (the Transfer Pricing Guidelines).

1.3 These Subdivisions provide a legislative framework, based on the arm's length principle, which ensures that an entity's tax position is consistent with that of an independent entity dealing wholly independently with others.

1.4 Section 284-255 of Schedule 1 to the *Taxation Administration Act 1953* (TAA 1953) sets out the records that an entity may prepare and maintain in order to demonstrate that they have correctly applied Subdivisions 815-B or 815-C of the ITAA 1997. This transfer pricing documentation should:

- be prepared before an entity lodges its tax return;

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- be in English, or readily convertible to English; and
 - explain how Subdivisions 815-B or 815-C of the ITAA 1997 apply to the transfer pricing matter.

1.5 If an entity does not meet these documentation standards and the Commissioner makes a transfer pricing adjustment, the administrative penalties in Division 284 of Schedule 1 to the TAA 1953 would apply as though a transfer pricing treatment was not reasonably arguable. The entity may then be liable for a higher base penalty amount than if it had a reasonably arguable position.

1.6 The BEPS Action Plan, adopted by OECD and G20 countries in 2013, is a fifteen-point plan designed to ensure that profits are taxed where activities that generate profits are performed. Action 13 of the BEPS Action Plan recognises that enhancing transparency for tax administrations, by providing them with adequate information to conduct transfer pricing risk assessments, is an essential part of tackling profit shifting.

1.7 The OECD's 2014 report on Action 13, *Guidance on Transfer Pricing Documentation and Country-by-Country Reporting*, contains a new Chapter V of the Transfer Pricing Guidelines that sets out revised standards for transfer pricing documentation. It recommends that jurisdictions require multinationals to provide information through three reports: a CbC report, a master file and a local file.

1.8 These amendments implement Action 13.

1.9 Unlike Australia's existing transfer pricing documentation standards, the CbC report, master file and local file together will provide a clear overview of key financial and operational metrics relevant to a global group, as well as their Australian operations. This information will provide the Australian Taxation Office (ATO) and other tax authorities with useful information to assess transfer pricing risks and, when necessary, to commence and target audit enquiries.

1.10 As outlined in the OECD's February 2015 report, *Guidance on the Implementation of Transfer Pricing Documentation and Country-by-Country Reporting*, it is envisaged that, in most cases, CbC reports will be filed in the jurisdiction of the multinational group's ultimate parent entity and automatically exchanged with tax authorities in other jurisdictions in which the group operates. The OECD has developed three model competent authority agreements that could be used to facilitate the exchange of CbC reports. Australia will make CbC reports filed in Australia available for exchange under such arrangements, and will also receive CbC reports from other jurisdictions.

Summary of new law

1.11 Schedule # inserts new Subdivision 815-E into Division 815 of the ITAA 1997 requiring Australian residents or foreign residents with an Australian permanent establishment (PE) that have annual global revenue of \$1 billion or more to provide a statement to the Commissioner. This statement could include the Country-by-Country report, master file and local file. This documentation will provide the Commissioner with relevant and reliable information to carry out a transfer pricing risk assessment.

1.12 These amendments apply to both Australian headquartered multinational enterprises and Australian subsidiaries of multinational enterprises headquartered outside of Australia with annual global revenue above the \$1 billion threshold.

1.13 Failure to provide this information will not prevent an entity from having a reasonably arguable position if documentation is still maintained in accordance with existing requirements.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
Entities with annual global revenue of \$1 billion or more must provide a statement to the Commissioner. A statement may be required to include one or more of a CbC report, master file and local file. Entities with annual global revenue under \$1 billion do not need to provide such a statement.	In order to have a reasonably arguable position in relation to a transfer pricing position, an entity must maintain specific transfer pricing documentation.

Detailed explanation of new law

The OECD's transfer pricing documentation standards

1.14 Action 13 of the G20/OECD's BEPS Action Plan outlines a standardised, three-tiered approach to transfer pricing documentation. The documents required under the OECD's standards are the CbC report, master file and local file.

1.15 The CbC report requires reporting of high-level information relating to the global allocation of a multinational group's income and taxes

paid, as well as information about the location and main business of each constituent entity within the group.

1.16 The master file provides an overview of the multinational group's business operations that will enable tax authorities to place the group's transfer pricing practices in their global economic, financial, legal and tax contexts. It requires information about the group's organisational structure, its intangibles and intercompany financial activities, its financial and tax positions, and a description of the group's businesses.

1.17 The local file focuses on specific transactions between the reporting entity and their associated enterprises in other countries. It requires identification of relevant related party transactions, the amounts involved in those transactions, and the entity's analysis of the transfer pricing determinations that they have made.

The reporting obligation

1.18 Entities with '*annual global revenue*' of \$1 billion or more are required to provide a statement to the Commissioner before the end of the next income year. These amendments apply to Australian headquartered multinational enterprises and Australian subsidiaries of multinational enterprises headquartered outside of Australia with annual global revenue above the \$1 billion threshold. [*Schedule #, item #, subsections 815-355(1) and (2) of the ITAA 1997*]

1.19 An entity's annual global revenue is calculated under subsections 177DA (5) to (7) of the *Income Tax Assessment Act 1936* contained in the Multinational Anti-Avoidance Law Exposure Draft, which was released for public consultation [on the Treasury website](#) on 12 May 2015. For the purposes of Subdivision 815-E, an entity may meet the global revenue threshold if it is an Australian resident — such as a holding or subsidiary company — or a foreign resident entity with a PE in Australia. Foreign resident entities without a PE in Australia will not be required to report.

1.20 The Commissioner may exclude specific entities from having to report in one or more income years through a written notification. Such notification is not a legislative instrument within the meaning of section 5 of the *Legislative Instruments Act 2003* because it is not legislative in character. Specified classes of entities may also be excluded from reporting obligations by legislative instrument. This provides a level of administrative flexibility that can reduce compliance costs. The ATO will provide advice about how an entity can seek to be excluded from these reporting obligations. [*Schedule #, item #, section 815-360 of the ITAA 1997*]

1.21 The Commissioner may provide exclusions where he or she determines that this would be appropriate — for example, entities with no cross-border related party transactions or insignificant cross-border related party transactions may be exempted.

1.22 The OECD envisages that CbC reports will be filed in the jurisdiction of the multinational group's worldwide parent entity and automatically exchanged with tax authorities in other jurisdictions in which the group operates. As such, an Australian subsidiary of a multinational may not be required to provide a statement with information required by the CbC report in Australia if:

- the local entity's worldwide parent entity is resident in another jurisdiction;
- it provides CbC reports to a tax authority in that jurisdiction;
- there are arrangements in place for the automatic exchange of CbC reports between that authority and the ATO; and
- the ATO is, in practice, able to obtain CbC reports from that authority.

1.23 Every Australian resident entity or foreign resident with an Australian PE with annual global revenue of \$1 billion or more will generally be required to provide the master file as part of its statement to the Commissioner. However, if multiple entities from the same group are resident in Australia, the Commissioner could specify that only one of those entities must provide the master file in its statement.

1.24 Each Australian resident entity or foreign resident with an Australian PE with annual global revenue of \$1 billion or more will generally be required to provide the local file in its statement, as this documentation is entity-specific.

1.25 Entities must provide the statement to the Commissioner in the 'approved form'. The approved form may require information to be provided that is relevant to the Commissioner making a decision under Division 815 of the ITAA 1997 as to whether an entity has received a transfer pricing benefit. The approved form may also require information relevant to performing a function or exercising a power related to making such a decision, or that enables the Commissioner to make such a decision — for example, by carrying out a transfer pricing risk assessment.

[Schedule #, item #, subsections 815-355(1) and (3) of the ITAA 1997]

1.26 The concept of approved forms is used in taxation laws to provide administrative flexibility to specify the precise form of information required

and the manner of providing it. This will allow the Commissioner to flexibly implement the standards in Annexes I, II and III to Chapter V of the Transfer Pricing Guidelines and any updates to those standards that are agreed in future.

1.27 The flexibility of the approved form also allows the Commissioner to specify the information that is required in an entity's statement. The approved form that is relevant to a particular entity may only require the master file and local file, or only the local file, rather than all three documents. One consequence of this approach is that different entities, depending on their circumstances, may need to provide different forms of information to the Commissioner.

1.28 For example, a local entity may only be required to provide the master file and local file in its statement to the Commissioner, in circumstances where its worldwide parent entity has made a CbC report available to a tax authority in a jurisdiction with which Australia has an information-sharing arrangement in place. Similarly, a local entity may be required to provide the local file and not the master file if another member of its multinational group that is resident in Australia has provided the master file to the Commissioner in its statement.

Example 1.1

Ortberger Ltd is a worldwide parent entity with wholly owned subsidiaries across 17 jurisdictions and annual global revenue of \$2.5 billion. Ortberger is a resident of a country with an agreement in place to automatically exchange information with Australia.

Four of Ortberger's wholly owned subsidiaries are resident in Australia and have been included in Ortberger's audited consolidated financial statements for the 2016–17 income year.

Ortberger, as the worldwide parent entity, files a CbC report with its local tax authority. As the Commissioner receives Ortberger's CbC report under the agreement, the Commissioner may specify that the four entities resident in Australia do not need to include the CbC report in their statement.

If one of the entities resident in Australia includes the master file in its statement to the Commissioner, then the Commissioner may specify that the other three entities do not have to provide the master file in their statements.

All four local entities must provide the Commissioner with a statement containing the local file.

1.29 There is a degree of overlap between the documentation standards in Subdivision 284-E of Schedule 1 to the TAA 1953 and the local file as

described in Annex II to Chapter V of the Transfer Pricing Guidelines. Both require entities to analyse and document similar matters in relation to their transfer pricing positions. For example, both require consideration and documentation of:

- the circumstances, including the functions performed, assets used and risks borne by the relevant entities;
- the most appropriate transfer pricing method and the reasons for choosing that method; and
- the existence of any comparable circumstances, the degree of comparability and whether any adjustments are necessary to eliminate the effect of material differences between those circumstances.

1.30 In respect of the local file, it is envisaged that much of the content can be drawn from documentation that meets the requirements in Subdivision 284-E. For example, when an entity has conducted and documented a comparability analysis for a transfer pricing treatment in accordance with Subdivision 284-E, that analysis may be used to meet the relevant local file content requirements without modification.

1.31 However, the content required for the local file can go beyond the requirements in Subdivision 284-E in several respects. For example, the local file will require the amount of intra-group payments and receipts for each category of controlled transactions involving the reporting entity—such as payments and receipts for products, services, royalties and interest—broken down by tax jurisdiction of the foreign payer or recipient. This information will be required in the local file in addition to the documentation prepared in accordance with Subdivision 284-E.

Penalties for non-compliance

1.32 Australia's taxation laws contain a range of penalties for entities that do not comply with their reporting obligations. Division 284 of Schedule 1 to the TAA 1953 sets out the penalties that apply to entities that make false or misleading statements about tax-related matters. Division 286 of Schedule 1 to the TAA 1953 sets out the penalties that apply to entities that fail to lodge statements on tax-related matters on time.

1.33 An entity that fails to provide a Subdivision 815-E statement on time, or in the approved form, may be liable under subsection 286-80(2) of Schedule 1 to the TAA 1953 to a base administrative penalty of five penalty units for each period of up to 28 days from when the document was due to a maximum of five periods.

1.34 The Commissioner has the discretion to remit an administrative penalty in whole or in part under section 298-20 of Schedule 1 to the TAA 1953.

1.35 Failure to comply with requirements under Subdivision 815-E may also result in the application of penalties under Part III Division II of Schedule 1 to the TAA 1953. That Division outlines criminal offences relating to failure to comply with taxation requirements.

1.36 Regardless of whether an entity fails to provide a statement on time, or in the approved form, it would still be eligible to have a reasonably arguable position in relation to a transfer pricing matter if they meet the documentation requirements in section 284-255 of Schedule 1 to the TAA 1953.

Consequential amendments

1.37 This Schedule makes a consequential amendment to include a definition of ‘annual global revenue’ in subsection 995-1(1) of the ITAA 1997. *[Schedule #, item #]*

Application and transitional provisions

1.38 These amendments apply in relation to income years commencing on or after 1 January 2016. *[Schedule #, item #]*