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TREASURY MINISTERIAL BRIEF

PDR No. MS 15-002596 10 August 2015

Treasurer cc: Assistant Treasurer

OPPOSITION POLICY: TIGHTENING THIN CAPITALISATION RULES - FURTHER INFORMATION

Timing: At your convenience.

KEY POINTS

- Following recent policy developments in the OECD and the release of a Board of Taxation Report Section 47C
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  - The proposal was the key part of the Opposition's $1.9 billion multinational tax avoidance package announced in March this year.
  - Under the proposal, deductibility of the debt used to fund the Australian operations of a multinational company would be limited to the gearing level of the global group. In effect this would remove the ability of a multinational to rely on the two alternative tests currently available (the statutory safe harbour and the arm's length debt test).

Section 47C

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  - the recently released Board of Taxation report highlights the importance of the arm's length debt test to industries in the infrastructure, property and services sector Section 47C
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- Further information on these issues can be found at Additional Information.

Section 22

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ADDITIONAL INFORMATION

Background

- On 2 March 2015, the Opposition announced a multinational tax avoidance package which was estimated by the Parliamentary Budget Office (PBO) to raise $1.9 billion over the forward estimates.
  - The proposed changes to Australia's thin capitalisation regime were the most significant part of this package, raising an estimated $1.65 billion over three years.
  - Other aspects of this package included adopting anti-hybrid rules, bringing forward the third-party reporting and data matching measure and increasing compliance funding to the ATO.
  - The Opposition further announced that the PBO had estimated the revenue from the package to be $7.2 billion over ten years.

Section 47C

- On 17 March the Shadow Treasurer wrote to you, calling on the Government to support the package.

Section 47C

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Section 47C

Section 47C

Section 47C

Release of the Board of Taxation report into the Arm's Length Debt Test

- The presence of the arm's length debt test (ALDT) under Australia's thin capitalisation rules allows taxpayers to claim deductions for interest deductions which, although they may not pass the other two tests, are nonetheless considered 'commercial or independent'.

- Under the Opposition's proposal, the ALDT would be removed.

- In 2013 the previous Government asked the Board of Taxation to review the ALDT. The Board's report was released on 4 June 2015.

- The Board's report highlighted broad support (including from the ATO) to retain the ALDT. The Board noted that "most stakeholders noted that the ALDT is an important feature of the thin capitalisation rules and were of a strong view that there is no policy justification for limiting access to the test".
  - Submissions to the Board expressed concern that without the ALDT "many major projects that are highly leveraged particularly in the early stages would be at risk". This included capital intensive sectors, especially infrastructure.

- The Board also noted the importance of the ALDT for investment in infrastructure and large scale LNG projects, and promoting predictable and stable tax outcomes.

Section 47C

Section 47C

ATTACHMENT A

Section 33(b)