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Director
International Tax Branch
Corporate and International Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600
MNETaxTransparency@treasury.gov.au

Re: Comment Letter on the Exposure Draft for Taxation Laws Amendment (Measures for Future Bills) Bill 2023: Multinational Tax Transparency - Tax Changes

The National Foreign Trade Council (the "NFTC") is pleased to provide written comments on the Australian Government's Exposure Draft for Taxation Laws Amendment (Measures for Future Bills) Bill 2023: Multinational Tax Transparency - Tax Changes published in April 2023 (the "Exposure Draft").

The NFTC, organized in 1914, is an association of U.S. business enterprises engaged in all aspects of international trade and investment. Our membership covers the full spectrum of industrial, commercial, financial, and service activities. Our members value the work of the OECD and the Inclusive Framework in establishing and maintaining international tax norms that provide certainty to enterprises conducting cross-border operations. We understand Australia's stated goal of providing a transparency measure for multinational entities to prepare for public release of certain tax information "to improve information flows to help investors and the public compare entity tax disclosures, to better assess whether an entity's economic presence in a jurisdiction aligns with the amount of tax they pay in that jurisdiction." The NFTC welcomes the opportunity to provide written comments on the Exposure Draft.

General Comments

NFTC has previously expressed its concerns with publicly available CbCR data. In reviewing the Exposure Draft, we urge Australia to reconsider the overly broad approach and instead pursue a more balanced approach which takes into account the risks of public disclosure, including the disclosure of commercially sensitive information and the creation of investor and public confusion around corporate taxation. The United States and U.S.-headed MNEs agreed to share data as part of the development of international standards at the OECD with the explicit understanding that such data would be kept confidential and be used by tax authorities only for risk analysis. Thus, mandating public disclosure of CbCR would breach the OECD agreement reflected in the outcome of BEPS Action 13. Moreover, mandating public disclosure of this

information would disadvantage MNEs with substantial operations in Australia and would discourage future investment in Australia.

Securities and accounting authorities, while recognizing the continuing desire for increased transparency, are appropriately proceeding cautiously in developing additional requirements and balancing the interests of all stakeholders. With these proposed rules, Australia has decided to disregard this cautious and balanced approach in favor of sweeping and over-broad requirements which represent risk to the competitiveness of MNEs on a global basis, national security risk to Australia and its allies, and present a significant incentive to avoid investment in Australia for any MNEs not already operating there.

Ultimately, NFTC fears that selective reading and sensational reporting of corporate tax filings, such as CbCR data, would inevitably confuse and misinform the public as they would likely fail to inform the reader of the intricacies of international taxation. In fact, the risk of misinterpretation arising from public disclosure of income tax information is one of the reasons why OECD BEPS Action 13 specifically preserved the confidentiality of CbC reports. The OECD agreement allows for tax authorities to receive CbCR data from MNEs on the condition that such information is used for risk analysis purposes only. We continue to believe that this strikes the right balance, that the tax information published by MNEs in their public stock exchange filings and statutory accounts is the best source of public information, and that it provides an appropriate level of public detail regarding an MNE's tax affairs. In fact, the effectiveness of the proposal in achieving its intended outcomes, such as reducing tax avoidance and increasing transparency is unclear, particularly as the ATO already has both detailed CbC reporting information for local entities and the power to act on that information. Further, we question whether the Exposure Draft achieves the appropriate balance between providing a comprehensive tax picture (arguably already provided by entities to the ATO) and minimizing the compliance burden on MNEs.

Notwithstanding our comments above cautioning against further public disclosure, if Australia chooses to pursue public CbCR as suggested by the Exposure Draft, we recommend a more limited and proportional approach to disclosure that closely aligns with international standards, including the European Union (EU) Directive's approach. The Exposure Draft proposes to require public disclosure of country-by-country data for every jurisdiction in which the reporting group operates. The requirement to publicly report this information would be unique globally. It is not required by similar public CbCR in the U.K. or under the EU Directive, for example. The objectives of the draft legislation would be better met by requiring information for Australia and for all other jurisdictions in the aggregate. If there is a concern regarding the inappropriate use of jurisdictions that do not exchange information with Australia or otherwise do not meet international standards for tax transparency, fair taxation, and anti-BEPS measures, the draft legislation could take the approach of the EU Directive: require the reporting of jurisdiction-level information for each uncooperative jurisdiction, with the reporting of information for all other jurisdictions in the aggregate.

Specific Comments

The Exposure Draft goes further than any other country or standard enacted or proposed today. The information being requested is not currently collected or compiled by MNEs and would take time and system changes to implement. The fact that it is required for 2023 makes it essentially impossible and adds an extraordinary burden for MNEs to comply.

Scope

The proposed scope of information requested in the Exposure Draft is extremely broad, and well beyond what is included in OECD Confidential CbCR. The scope of CbCR was agreed at the OECD as 'appropriate' to enable tax authorities to make a confidential risk assessment of an MNE's tax affairs. While we understand the need for this data to conduct risk assessments, there seems to be no objective policy goal for publishing that information.

Similarly, the information requested goes far beyond that required under the public CbCR EU Directive. The lack of consistency with the EU proposal increases the potential for confusion amongst stakeholders and the compliance burden for taxpayers. The EU Directive requires separate disclosure of each EU member state together with those jurisdictions deemed to be non-cooperative tax jurisdictions. Additionally, small local operations of MNEs (i.e., operations where there is minimal impact on the overall tax picture) are excluded to reduce unnecessary compliance costs. Data for the rest of the is then reported in the aggregate. In line with the EU Directive, the information to be disclosed should be limited to Australian operations with the rest of the world in aggregate.

The Exposure Draft notes that information must be published "if regulations...prescribe [disclosure of that] information." NFTC strongly urges that any information required to comply with the Australia CbCR regime should be clearly identified and apply equally to all MNEs prior to adoption. In the absence of doing so, it will be virtually impossible for MNEs to fully comply as they will be unable to prepare and implement the required reporting in a quality and timely manner.

Furthermore, there is no clear materiality threshold in relation to any of the data required to be published. Not only is the lack of a materiality threshold troubling from a compliance burden perspective, but it is not helpful from a stakeholder perspective in interpreting and understanding the published data. Accordingly, if data on a jurisdictional basis is required, we would propose limiting disclosure to the largest jurisdictions covering in aggregate eighty percent of revenue and employees.

While recognizing that it is in the best interest of all parties to achieve transparency, it is also critically important to acknowledge the importance of the Arm's Length Standard, which is recognized and generally applied on a global basis. NFTC strongly believes that requiring an MNE to publicly provide data which a local affiliated company would not have access to under the Arm's Length Standard, is contradictory to the principles and spirit of the Arm's Length Standard. This will disrupt the validity of the Arm's Length Standard itself as a measure, which governments and MNEs need in order to appropriately evaluate transfer pricing. We do not believe it is necessary to report transactions between Australia and other countries that have adopted the Arm's Length Standard, since these countries will have assessed the correctness of the Arm's Length Standard in regard to these transactions. As such, we strongly encourage Australia to re-evaluate the adoption of a public CbCR measure, especially one which is even more far reaching than that which was published by the OECD.

Section 6 - Listed Information

The Exposure Draft enumerates items to be listed in the proposed CbCR. Many of these items are not readily available, difficult to obtain, or would create further confusion.

Section 6(e) of the Exposure Draft has identified that expenses arising from transactions with related parties that are not tax residents of the jurisdiction should be included. Much of this information is accounted for in transfer pricing calculations. The collection and disclosure of this information would be overly burdensome as companies do not tend to maintain this data at a jurisdictional level. Moreover, the Exposure Draft specifying Australian CbCR differs from OECD CbCR as the OECD does not require the elimination of revenue from related parties that are in the same jurisdiction. The Exposure Draft requires this elimination. In addition, it would impose challenges to the Enterprise Resource Planning (“ERP”) systems used by MNEs, as there might be a need to change the ERP configuration. We strongly encourage Australia to align with the OECD in all aspects of the information required to be published in the CbCR.

Section 6(g) requires publication of a list of tangible and intangible assets by jurisdiction, including book value. On its face, this would require each asset (e.g., building, vehicle, laptop, etc.) and each item of intellectual property (“IP”) (e.g., patent, trademark, etc.) to be itemized separately. The scope of this reporting requirement is far from feasible. At a minimum we recommend a clarification that assets can be grouped together using categories typically found in financial statements. The explanatory comments should clarify that the assets do not need to be listed separately, which would be extremely burdensome to MNEs. Without clear and concise guidance, use of inconsistent definitions for each tangible and intangible asset will occur and will create confusion. Providing lists of intangible assets by entity would be impracticable to obtain and generally useless to stakeholders with benign intent. Fixed asset systems are typically maintained at an entity level rather than being easily accessible to central resources and may exist in dozens or more different ERP systems, making retrieval and submission extremely difficult and time-consuming, with unclear benefits to anyone.

For comparison, the OECD CbCR does not require a list of tangible assets; GRI207 (which is voluntary) appears to only require a valuation as a whole; and the EU Directive does not appear to require details of tangible assets. For intangible assets, no other CbCR requires a list of intangible assets. Further, the Exposure Draft has identified the inclusion of the book value of tangible and intangible assets at the end of the income year. We believe the public disclosure of this information will lead to behaviors that will have a direct impact on the ability of MNEs to operate competitively. As such, we strongly encourage Australia to remove this information from the Australia CbCR requirements.

Exposure Draft section 6(l) provides that MNEs should explain the difference between the income tax accrued and the amount of income tax due if the income tax rate applicable in the jurisdiction were applied to the profit or loss before income tax. In addition to driving complexity and cost in preparation of the CbCR, this information requires and introduces significant manual work. First, it requires MNEs to reconcile tax attributes across legal entities within a jurisdiction. Next, it requires MNEs to bridge different tax systems, accounting measures, currency differences, etc. to explain any such differences. We fail to comprehend the additional value obtained by requiring reconciliations between a jurisdiction’s statutory and actual tax rates when the jurisdictional effective rate will be at least the globally agreed 15% under the Pillar Two framework. Requiring MNEs to build the bridge on a global basis is a significant and very labor-intensive exercise. None of this information is gathered globally at the level of detail required to meet this information disclosure and no such straightforward systems fix can solve this. It can only be executed by manual work. The burden this would place on MNEs cannot be understated. NFTC recommends that the rate reconciliation requirement should be limited to Australian activities only.

Section 6(k) requires publication of the effective tax rate (“ETR”). While the Exposure Draft relies on calculations as per Article 5.1 of the *Tax Challenges Arising from the Digitalisation of the Economy — Global Anti-Base Erosion Model Rules (Pillar Two): Inclusive Framework on BEPS* (2021), additional clarity is needed on applying those rules to Australia. This would likely require the introduction of new processes and systems modifications to report this type of information centrally on a global basis, it makes it impossible for MNEs to implement such a measure in the timeline defined by Australia. In addition, no Pillar Two ETRs are required for 2023 and the first Pillar Two return (for 2024) is not due until June 2025 - six months after the 2023 CbCR report would be due in Australia. If the ETR to be published is computed under Pillar Two principles, it should be noted that the proposed commencement date requires publication earlier than the GLOBE return is required to be prepared and filed. In addition, it is not clear how the safe harbors under the GLOBE rules will interact. Section 7 (d) of the exposure draft refers to the “pre-Pillar 2” top up tax ETR. This Pillar 2 GLOBE ETR would be misleading if published as the ETR would at a later stage be topped up to 15%, (e.g., Ireland may initially show as a 12.5% ETR for Australia Public CbCR but would be increased to 15% as part of the Pillar 2 Globe Tax return). The way the legislation is written will give a misleading representation of the ETR once the Pillar 2 rules are implemented. We strongly encourage Australia to align with the international standards developed at the OECD (with the participation of Australia) in all aspects of the information required to be published in the CbCR.

Lack of Safeguards for Commercially Sensitive Data

NFTC is very concerned about the lack of safeguards to protect against disclosure of commercially sensitive data regarding business operations. While there is reference to allowing exemptions, there is no clarity on what might qualify for an exemption, and it appears to be at the discretion of the Commissioner. Such disclosures could harm the competitive position of businesses, eventually resulting in market distortions, particularly when compared to competitors not subject to disclosure (e.g., competitors with no operations in Australia).

As a result of the requirement to publish jurisdiction by jurisdiction information, this distortion could occur in any market in the world (not just Australia) in which one business is required to publish as a result of Australian legislation and a competitor is not. By not providing an exemption from publication of commercially sensitive data and requiring disclosure of data for all jurisdictions (not just Australia), these requirements create a direct and significant disincentive for growing businesses to commence operations in Australia. This concern is particularly acute due to the lack of a materiality threshold for the publication of jurisdiction-by-jurisdiction data. Accordingly, information regarding a jurisdiction could reflect start-up operations, or business costs with a single customer, or a single contract, any of which could be commercially sensitive.

There is no safeguard exempting publication of data that is otherwise publicly available (e.g., through a public stock exchange filing). It is also concerning that the proposal seems to create a “work-around” to the confidentiality requirements agreed to by Australia and other governments who ratified the MLI negotiated as part of the OECD BEPS project. Requiring companies to participate in the elimination of the confidentiality protections afforded by that instrument is a violation of those agreements.

The EU Directive permits reporting groups to withhold reporting of commercially sensitive information. Consistent with the EU Directive, the draft legislation should be modified to permit reporting groups to withhold reporting of commercially sensitive information. At a minimum, we

recommend that Australia adopt a safe harbor allowing MNEs to defer publication of confidential and commercially sensitive data for five years, in line with the public CbCR EU Directive.

Exemptions

The Exposure Draft makes provision for the Commissioner to exempt certain entities from reporting certain data under subparagraph (13) but does not provide a standard for considering such exemptions. NFTC suggests that Australia specifically enumerate which class of entities the Exposure Draft will apply to, and which will be exempt. These exemptions must be clear and transparent, with Australia's purpose for exemption publicly articulated to ensure fairness and equity. Transparency should be a standard adopted not only with regards to MNEs, but to the governmental authorities that are requesting such transparency.

Industries

We further suggest that there are certain industries, such as the defense industry and segments of other MNEs, where such exemptions should apply given national security and intelligence concerns. Specifically, large defense contractors regularly participate in classified programs and projects with the U.S. Department of Defense and other government agencies around the world, including Canada, the UK, and Australia. The activities of large defense contractors and segments of other businesses under these programs and projects generate a significant inventory of classified equipment, including end products and components, prototypes, and intellectual property in the form of patents, technological data, manufacturing processes, product specifications and blueprints. Requirements to disclose and list associated intellectual property pose a threat to national security and each respective nation's defense secrets. The disclosure of classified equipment sales and associated service activities, through revenue reporting metrics, tangible asset, and employee metrics, provide information that, in the wrong hands, could also pose a threat to each country's national security and defense secrets. Moreover, such disclosures may involve export-controlled information that would require authorization to be obtained from a regulatory agency prior to release. Authorization to release export-controlled information is tightly managed and restricted for specific destinations, end-users and purposes. As advanced technology is vital to each nation's military capabilities, efforts to require disclosure of such information poses a threat to these capabilities and input from the U.S. Department of Defense and other impacted government agencies should be solicited and approved by such agencies. Failure to provide such an accommodation would effectively sanction the release of significant information with high intelligence value to geopolitical competitor states and harm Australia's relations with allies.

Entity Type

The Exposure Draft applies to every entity that is: (1) a constitutional corporation, or (2) a partnership (or a trust) in which each of the partners (or trustees) is a constitutional corporation. This definition excludes partnerships in which the partners are natural persons, presumably because the income of such partnerships typically is taxed at the level of the natural person owners. Reporting income and tax information for such entities serves no policy purpose as taxes are paid by the natural person owners, not the entity. Some jurisdictions, such as the United States, have rules that permit corporations that meet certain criteria (for example, where all owners are U.S. natural persons or trusts of such persons) to be treated as fiscally transparent. The draft legislation should be modified to exclude from its scope a constitutional corporation or other entity that is treated as fiscally transparent for tax purposes in its country of

organization unless each of the owners is a constitutional corporation that is not treated as fiscally transparent for tax purposes in its country of organization.

Compliance with other CbCR Regimes

The proposed rules reference GRI 207 as a source of authority. However, we are unaware of any jurisdiction where GRI 207 is a mandatory standard. Despite the fact that GRI 207 is not universally accepted, we suggest that to the extent an MNE group is already reporting under GRI 207, including GRI 207-4, the MNE group would be exempt from these additional reporting requirements. We would suggest the exemption also apply to MNE groups already subject to EU Public CbC reporting (as implemented in the various EU member states) so long as they report Australia-specific information. For the purposes of an EU exemption, we suggest that the MNE group (and any Australian component entity or PE) would be deemed to have complied with the reporting requirements if the MNE group includes the information required under the EU Directive for the Australian component entity(ies) or PE. By aligning and exempting entities already providing this data, it will significantly reduce the compliance burden as well as provide for consistency in reporting.

Compliance Burden

It is wrong to assume that the increased compliance costs imposed by an Australia-specific regime would simply replace costs that might otherwise be incurred through the introduction of OECD BEPS or EU Public CbC reporting requirements, or that they should simply be absorbed by MNEs. By creating a bespoke regime and imposing obligations on different timetables, the proposed CbCR rules would unnecessarily duplicate or increase compliance costs due to these other international initiatives. In particular, the proposed CbCR rules would result in: more information required to be collected than under current Australian CbC reporting requirements (under BEPS Action 13); the imposition of new definitions on points such as the effective tax rate, which depend on processes not yet completed in the OECD Pillar Two process; and a reconciliation with audited financial statements of the parent entity, which are prepared for different purposes. Making that determination and providing explanations is likely to impose additional compliance costs.

The proposals are extremely broad and will impose a disproportionate administrative burden on taxpayers. Such disclosure increases the compliance burden at a time when large MNEs are already facing the complex implementation of Pillar Two and work is on-going with respect to Pillar One. The information requested goes far beyond that included in OECD Confidential CbC under BEPS Action 13. As a result, many in-scope businesses will not have this data readily available. Much of the information required is not something that many companies ordinarily prepare or retain today. For example, as noted above, the requirement to prepare a tax rate reconciliation on a jurisdictional basis (section 6 (i)) will require jurisdictional consolidations and tax rate reconciliations to be prepared. For a large group, collecting this data and preparing these reconciliations for every jurisdiction in which they operate will impose significant and disproportionate administrative and resource challenges.

We note that there does not appear to be a materiality threshold in relation to any of the data required to be published. As such, for large MNEs operating globally, the level of information required is extremely burdensome and, in some cases, it may not be practical to comply. Indeed, it is not at all clear what purpose is served by requiring publication of such data for jurisdictions in which the MNE has no material operations or income.

Implementation Timeline

As discussed throughout this comment letter, an overwhelming majority of the required information is not available today. As a result, companies need time to define requirements, amend systems and test outputs before being able to furnish this data. The new reporting obligations are proposed to apply for the 2023-24 and later income years, which could mean the first reporting year is fiscal year 2023. However, the draft explanatory materials and the prior government announcement both refer to the application for income years starting on and after 1 July 2023.

To enable time for both tax authorities and taxpayers to be ready and to align the publication date with the EU Directive, the commencement date should be deferred so as to apply to the first accounting periods commencing on or after 22 June 2024 at the earliest. The current implementation timeline makes it impossible for MNEs to comply with an appropriate level of detail and accuracy.

The proposed timelines for completion and the requirement for amendment of the disclosures result in a near certainty that these reports will be revised repeatedly. In other contexts, such as Pillar Two, tax authorities have appropriately included changes related to prior years in current year disclosures rather than proposing amended filings, which could continue ad infinitum. At a minimum, there should be a high materiality threshold required for an amended filing.

The start date for the EU Directive will apply to the first financial year starting on or after 22 June 2024. For U.S. MNEs with a calendar financial year, this EU measure will first apply to calendar year 2025 with reporting due in late 2026. The proposed CbCR in the Exposure Draft, on the other hand, would potentially commence in 2023 with the first reports required in 2024. NFTC recommends that Australia align the timing of the proposal to at the least conform with the EU Directive in 2024 and limit detailed reporting to Australian entities. The Australia proposal should align with these other measures and go into effect on the same timeline.

The criteria under the Exposure Draft makes the publication of the Australia CbCR an obligation of the parent company (which may or may not file currently in Australia). As such, guidance for the implementation timeline is requested on how such entities will comply. This should also include details as to the format of the reporting, e.g., when a U.S. Parent does not have an Australian tax identification number or Australian address.

NFTC respectfully requests that companies have the option to publish the CbC report on their own website. Many companies will want to provide additional context around the data or include the data within a wider ESG report. Additionally, clarification on the details of the Maintenance of information on the Australian government website would be helpful. For example, the legislation should make clear how long the data will be maintained on the website. The EU rules provide for a five-year visibility period at which point the data can be removed. We recommend Australia adopt a similar approach.

Finally, clarity is requested on whether penalties for lack of compliance are criminal or civil and who is ultimately responsible. Specifically further information is sought on the responsibility of the Public Officer in Australia and how that responsibility differs from the CbC reporting parent. No local subsidiary directors should be subject to personal (either criminal or civil) penalties. These individuals cannot compel a parent company located outside of Australia to provide data relating to non- Australian operations and it would be inappropriate to subject them to a penalty

in Australia as a result. Additionally, clarity is needed on the application of penalties for non-compliance. The Exposure Draft does not specify how this applies to MNEs who are Significant Global Entities. While our members aspire to comply with all requirements of each country in which they operate, it is imperative that they understand the consequences of failing to comply with any provision or regulation.

Conclusion

NFTC has previously expressed its concerns with publicly available CbCR data. Notwithstanding our previously expressed concerns, if Australia chooses to pursue public CbC reporting as suggested by the Exposure Draft, we recommend a more limited and proportional approach to disclosure that closely aligns with international standards, including the EU's Public CbCR Directive and OECD. We recommend that the materiality thresholds be adopted, requirements to list tangible and intangible assets be removed, safeguards against commercially sensitive data be adopted, and exemptions for certain industries, such as the defense industry, where such exemptions should apply given national security and intelligence concerns, be granted. Lastly, we recommend that the commencement date be aligned with the EU Public CbCR Directive. NFTC appreciates the opportunity to provide comments on the Exposure Draft and looks forward to continuing opportunities for constructive engagement.