International taxation – global and domestic minimum tax – primary legislation

KPMG submission

KPMG Australia, April 2024

KPMG.com.au

Contents

Executive summary

As a leading professional services firm, KPMG Australia (**KPMG**) is committed to meeting the requirements of all our stakeholders – not only the organisations we audit and advise, but also employees, governments, regulators and the wider community. We welcome the opportunity to provide a submission on the primary legislation exposure draft materials and interactions with other Australian tax laws consultation paper in relation to the Australian implementation of Pillar Two, released by Treasury on 21 March 2024.

Our submission recommends an implementation of the Australian Pillar Two rules in a way that maximises efficiency and simplicity, and seeks to minimise the compliace burden on in-scope groups.

KPMG is supportive of the implementation of the Pillar Two Global Anti-Base Erosion (**GloBE**) rules in Australia, including a domestic minimum top-up tax (**DMT**).

We commend the efforts made to date to provide a robust legislative framework and rules that seek to provide certainty for Australian purposes while also aligning with the OECD Model Rules. In order to continue to attract and retain multinational business, Australia's implementation of these rules should focus on maximising efficiency, simplicity and reducing compliance costs for in-scope businesses, and many of our recommendations are focused on this.

It is also critical that the draft legislation and forthcoming Australian Tax Office (**ATO**) guidance reflect a provisional approach to penalties for the initial years of the application of the Australian GloBE rules, when in-scope groups are becoming more familiar with these new and comprehensive requirements.

With the introduction of the GloBE rules both in Australia and internationally, consideration should be given to scaling back domestic tax integrity measures which are duplicative, with a view to mitigating double tax outcomes and reducing complexity. In this regard, global consistency at the OECD level in relation to the interactions between the GloBE rules and domestic integrity rules should be prioritised. This is particularly the case for the hybrid mismatch rules.

KPMG looks forward to continued engagement with the Australian Government as it progresses further with implementation of these rules over the coming months.

Yours sincerely,

Alia Lum

Partner, Tax Policy and Regulatory Engagement Lead

KPMG Australia

©2024 KPMG, an Australian partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organisation.

Liability limited by a scheme approved under Professional Standards Legislation.

Background

About KPMG

KPMG is a global organisation of independent professional firms, providing a full range of services to organisations across a wide range of industries, governments and not-for-profit sectors. We operate in 146 countries and territories and have more than 227,000 people working in member firms around the world. In Australia, KPMG has a long tradition of professionalism and integrity combined with our dynamic approach to advising clients in a digital-driven world.

KPMG has also contributed to and adopted the *Australian Tax advisory firm governance, best practice principles* which aim to enhance public understanding of the large advisory firms and further build community confidence and trust in the taxation system. The principles have been developed in consultation with the ATO, the Tax Practitioners Board and the largest tax advisory firms.

©2024 KPMG, an Australian partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organisation.

Liability limited by a scheme approved under Professional Standards Legislation.

Section 1:
KPMG recommendations

RECOMMENDATION 1:

In finalising the primary and secondary legislation, Australia should strive to minimise the number of provisions that are worded differently to the corresponding Model Rules, particularly where they could be seen as giving rise to different outcomes. This results in in-scope groups having to navigate and address divergences, creating complexity and uncertainty. Australia's principal efforts where there is uncertainty in the Model Rules should be aimed at achieving clarity and consensus on these issues at the OECD level.

RECOMMENDATION 2:

It would be helpful for guidance to be provided to confirm where existing Australian tax concepts are relevant to definitions within the Australian GloBE rules. Existing tax concepts are well understood and applied by in-scope groups and hence guidance would reduce complexity and the work required for in-scope groups to determine whether they satisfy new definitions within the Australian GloBE rules.

RECOMMENDATION 3:

The introductory penalty relief from the OECD common understanding on penalties should be specifically legislated, rather than relying on existing powers of the Commissioner of Taxation. This ensures a clear and consistent approach for in-scope groups in the early years of implementation when they are still becoming familiar with these new rules.

RECOMMENDATION 4:

The rules relating to the filing of Australian GloBE Tax Returns and DMT Returns should be updated to allow for a Designated Local Entity to file one return which aggregates jurisdictional data with the other Constituent Entities (**CEs**) that are required to file these returns. The rules as drafted indicate that returns for each of the CEs are required to be filed on a stand-alone basis.

RECOMMENDATION 5:

The Australian GloBE Tax Returns and DMT Return forms should be streamlined and disclosures kept to a minimum, with no substantive additional information required beyond that required by the Global Information Return (**GIR**).

RECOMMENDATION 6:

The general policy approach in the consultation paper should reassess the need for certain integrity rules to subsist in the Australian tax law. Where integrity concerns are dealt with by the GloBE rules, domestic rules should be removed or scaled back in line with OECD recommendations. The financing integrity measure in the hybrid mismatch rules should be amended so that top-up tax is regarded for the purpose of determining whether the 10 percent threshold is met. In relation to the other parts of the hybrid mismatch rules, resolution of effective double tax outcomes should be prioritised at the OECD level.

©2024 KPMG, an Australian partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organisation.

Liability limited by a scheme approved under Professional Standards Legislation.

Section 2:
KPMG insights

Assessment Bill and Consequential Amendments

Assessment Bill

Consistency with Model Rules

We acknowledge the Government's efforts to draft the Australian GloBE rules with detail and specificity that may not be included in the Model Rules in order to provide certainty to in-scope groups.

However, this must be balanced with prioritising true consistency with Model Rules and ensuring the greatest levels of clarity and simplicity possible. In finalising the primary and secondary legislation, Australia should strive to minimise the number of provisions that are worded differently to the corresponding OECD rules, particularly where they could be seen as giving rise to different outcomes. We consider that rather than providing certainty, this results in in-scope groups having to navigate and address multiple divergences by the Australian rules and so, in fact, has the opposite effect. This issue of diverging views is then compounded where other jurisdictions also deviate from the wording of the Model Rules.

As such, rather than focusing on creating Australian specific GloBE rules, Australia's principal efforts where there is uncertainty in the Model Rules should be aimed at achieving clarity and consensus on these issues at the OECD level. For example, the Ownership Interest definitions are more prescriptive in the Australian GloBE rules (section 31) which risks the Australian GloBE rules being applied differently to the Model Rules (albeit the approach is broadly consistent with the Commentary). See also some examples in the "Miscellaneous" section below.

In addition, it would be helpful to in-scope groups and advisors for a matrix to accompany the legislation, which maps the Australian GloBE rules against the Model Rules. This would be consistent with guidance material published by HMRC for the UK GloBE rules[1].

Existing Australian tax concepts

There are many existing concepts and defined terms in Australian tax law that are well understood, tested and applied by in-scope groups. Given the terms and phrases in the Australian GloBE rules are derived from the Model Rules, and are therefore generally different to existing Australian tax concepts, in-scope groups will commonly encounter instances where there is uncertainty as to the relevance of their satisfaction of existing Australian tax concepts for Australian GloBE rules purposes.

As such, to reduce complexity for in-scope groups, it would be helpful for guidance to be provided in the explanatory memorandum (**EM**) to explicitly link or connect existing Australian tax concepts to definitions within the Australian GloBE rules where appropriate (i.e. confirmation that the domestic concepts falls within the corresponding GloBE rules concept and therefore existing guidance on the domestic tax law can be used in interpreting the GloBE rules). While this is important for terms throughout the Australian GloBE rules, we highlight some examples from section 16 Excluded Entities for illustrative purposes:

- Governmental Entity (section 27) and 'government entity'/ 'government related entity'[2].
- Non-Profit Organisation and the various entities exempt from income tax[3].
- Pension Fund and 'superannuation entity'[4].
- Paragraph (c) of the definition of Real Estate Investment Vehicle, which requires that the entity be 'widely held', however this is an undefined term. There are various

[1] Multinational-top-up-tax-draft-guidance (publishing.service.gov.uk), page 25.
[2] Defined in *A New Tax System (Goods and Services Tax) Act 1999*.
[3] Under Division 50 of the *Income Tax Assessment Act 1997*.
[4] Defined in *Superannuation Industry (Supervision) Act 1993*.

©2024 KPMG, an Australian partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organisation.

Liability limited by a scheme approved under Professional Standards Legislation.

'widely held' concepts in the Australian tax law which could be leveraged for this purpose[5].

If not appropriate to include in the EM, then we would recommend ATO guidance be issued to confirm the extent to which the local concepts align with the GloBE definitions.

Record keeping

We understand that CEs are required to keep records that are necessary for the collection and recovery of GloBE top-up tax and Domestic top-up tax (section 26). CEs are required to keep records that fully explain whether the CE of the Applicable MNE Group has complied with the Assessment Bill. The requirement to keep records applies to CEs located in Australia, notwithstanding that the GIR may be lodged overseas and then exchanged with the Commissioner of Taxation (**Commissioner**). Further, records must be kept until the end of 8 years after those records were prepared or obtained, or the completion of the transactions or acts to which those records relate, whichever is the later.

We consider that the requirement on Australian CEs to keep records for 8 years, particularly when the GIR may be lodged overseas, provides an unnecessary compliance burden on in-scope groups. While the Canadian rules include an 8 year record keeping requirement, the period starts after the end of the fiscal year to which the records relate. Hence, the Australian rules are more onerous, requiring retention for an 8 year period that starts after the records were prepared or obtained or the completion of the relevant transactions or acts (whichever is later).

We recommend that the record keeping requirement is reduced from 8 to 5 years (after the records were prepared or obtained, or the completion of the transactions or acts to which those records relate, whichever is the later). This is consistent with the existing record keeping rules in subsection 262A(4) of the *Income Tax Assessment Act 1936* and broadly in line with the timing of the general period of review for an amount of GloBE top-up tax or Domestic top-up tax (being 4 years from the date of lodgement of the relevant return).

Failure to keep records

We understand that the failure to keep records is an offence of strict liability with no discretion for remission (subsection 26(4)).

This is at odds with the OECD common understanding on penalties[6] and hence this provision should be modified so that it does not apply to the Transition Period[7].

Interpretation of the Assessment Act

The Illustrative Examples[8] report (14 March 2022) should be added to the list of OECD materials listed in section 3, given the report provides illustrative guidance regarding the application of the GloBE rules.

Consequential Amendments

Penalties

The implementation of the GloBE rules is a fundamental change to Australia's tax framework and hence it is important that a pragmatic approach is adopted in relation to the administration of the rules on a consistent basis.

We understand that penalty relief for the Transition Period is to be governed by existing tax legislation. However, in our experience, we generally observe inconsistencies in the approach to remission of penalties across taxpayers. To remove uncertainty, we recommend that the circumstances in which transitional penalty relief will apply is specifically legislated, in line with the OECD's common understanding on penalties[9]. We note the Canadian GloBE rules include such legislative provisions.

The ATO should also prioritise guidance as to when it will consider that an MNE Group has taken "reasonable measures", including the circumstances when it would consider that an MNE Group has acted in good faith to understand and comply with the GloBE rules and the DMT.

Tax secrecy

The tax secrecy provisions under Division 355 in Schedule 1 to the *Tax Administration Act 1953* are proposed to be amended to allow taxation officers to disclose protected information about one CE to another CE of the same Applicable MNE Group for the purposes of administering

[5] For example, 'widely held company' definition and widely held requirements in Managed Investment Trust rules in Income Tax Assessment Act 1997.
[6] Safe Harbours and Penalty Relief: Global Anti-Base Erosion Rules (Pillar Two) (oecd.org) (Chapter 3).
[7] Defined as any Fiscal Year beginning on or before 31 December 2026 but not including a Fiscal Year that ends after 30 June 2028 (per OECD common understanding on penalties).
[8] Tax Challenges Arising from the Digitalisation of the Economy – Global Anti-Base Erosion Model Rules (Pillar Two) Examples (oecd.org)
[9] Safe Harbours and Penalty Relief: Global Anti-Base Erosion Rules (Pillar Two) (oecd.org) (Chapter 3).

©2024 KPMG, an Australian partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organisation.

Liability limited by a scheme approved under Professional Standards Legislation.

the Assessment Bill. The proposed amendments also allow taxation officers to disclose protected information about a JV or JV Subsidiary to a CE, trustee or a partner that holds a direct ownership in that JV or JV Subsidiary.

Practically, we understand that this means that taxation officers may disclose protected information:

- Between entities that are consolidated for accounting purposes on a line by line basis in a global parent's consolidated financial statements (i.e. within the same Applicable MNE Group); or
- About a JV or JV Subsidiary to a CE that is covered by subsection 6(5) in relation to that JV or JV Subsidiary.

The ATO's confidentiality obligations are critical to maintaining the integrity of the tax system, and the ATO would need to carefully consider the need to disclose protected information to separate legal entities in the manner noted above. At present, there are no other types of specific tax obligations included in section 355-25(2) and any such amendment to start to include specific items should be carefully considered (and in particular, whether the outcomes sought can be achieved using existing powers).

If it is concluded such an amendment must be included, we would recommend narrowing the type of information that can be disclosed, to that which relates to the determination of a GloBE or DMT liability.

We also recommend a practice statement is prepared by the ATO to provide guidance to ATO staff in relation to the circumstances in which protected information should be disclosed pursuant to this amendment.

Franking credits and debits

We consider that the strike-through text should be retained in the amendments to sections 205-15 and 205-30 regarding franking credits and debits. This wording is tied to the concept of a franking entity, which is defined under section 202-15 'at a particular time'. As such, in order to test the franking entity definition, a specific point in time, or period of time, is required in sections 205-15 and 205-30.

Filing of the GIR

Where a GIR is filed in a foreign jurisdiction, the EM states at paragraph 3.32 that a CE is required to notify the Commissioner of the identity of the UPE or Designated Filing Entity that has lodged the GIR and the foreign jurisdiction in which that filing entity is located. This notification requirement should be stipulated by the legislation (i.e. there is a mismatch between the legislation and EM).

In relation to the proposal to require a CE to lodge the GIR within 21 days after the Commissioner provides a notice that the GIR has not been received from the foreign government agency (EM at paragraph 3.33), we consider this to be reasonable, although the Commissioner should have the discretion to extend this timeframe. We consider the imposition of penalties for failure to comply with this notice to be reasonable, subject to our comments above regarding penalty relief in the Transition Period.

In due course, a list of the foreign countries which have Qualifying Competent Authority Agreements with Australia should be made publicly available.

Australian GloBE Tax Return

Subsections 127-10(4) and 127-10(5) allow a Designated Local Entity to file returns on behalf of other CEs in the MNE Group. The drafting of this provision indicates that the Designated Local Entity is required to file multiple Australian GloBE Tax Returns (i.e. for each CE), rather than one aggregated jurisdictional Australian GloBE Tax Return.

While this may not be a practical issue for CEs applying an Income Inclusion Rule (**IIR**) as it is limited to GloBE Parent Entities, it is likely to become a practical issue if the requirement is also to apply to a CE with a potential GloBE Top-up Tax Amount under the Undertaxed Profits Rule (**UTPR**) (see below).

It would reduce the compliance burden and streamline the filing process if only one Australian GloBE Tax Return was required to be filed. Hence the legislation should be updated, and ATO should ensure this return includes disclosures reflecting the different ways a CE may file an Australian GloBE Tax Return (i.e. single entity v jurisdictional data).

It is not clear from the legislation or EM whether CEs are required to notify the Commissioner of the appointment of a Designated Local Entity. This should be confirmed.

The ATO should ensure the form for the Australian GloBE Tax Return is streamlined and disclosures kept to a minimum, with no duplication of information across the return and the GIR. The focus should be on allowing the final tax liability to be collected on a self-assessed basis. The ATO should also consult with stakeholders in relation to the return, including releasing draft versions for public comment.

©2024 KPMG, an Australian partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organisation.

Liability limited by a scheme approved under Professional Standards Legislation.

While not an immediate matter, it appears that the Australian GloBE Tax Return only relates to the assessment of the IIR, and not the UTPR. This is because the requirement to file this return only applies to CEs that are GloBE Parent Entities. The limitation to the IIR is also reflected in the EM at paragraph 3.35. This should be clarified.

DMT Return

Our comments above regarding Designated Local Entity filing (subsections 127-10(4) and 127-10(5)) also apply to DMT Returns given the drafting of subsections 127-15(4) and 127-15(5). That is, the Designated Local Entity should be filing one aggregated DMT Return on behalf of each CE, as it would seem to be an unnecessary compliance burden to require individual filings given that ETR and top-up tax calculations are prepared on a jurisdictional basis.

We note also the 'transitional simplified jurisdictional reporting framework' approach allowed in the draft GIR[10], which allows MNE Groups to disclose jurisdictional level data only (rather than entity by entity level data) for the first five years of the regime, where no top-up tax arises; or it arises but does not need to be allocated on a CE-by-CE basis. This transitional administrative relief should also be provided for disclosures in DMT Returns.

If this recommendation to allow for a Designated Local Entity to file one aggregated DMT Return on behalf of each CE is not agreed to, then as an alternative an Australian tax consolidated group should only be required to prepare a single aggregated DMT return.

Consistent with our comments regarding the Australian GloBE Tax Return, the ATO should ensure the disclosures in the DMT Return are streamlined and kept to a minimum, with no substantive additional information required beyond that required by the GIR. A draft version should be released for public comment.

In relation to the request in the EM at paragraph 3.41 for stakeholder comment in relation to whether there are circumstances in which lodgment of the DMT Return by a CE might not be warranted, we consider that this should be sufficiently addressed where the recommendation to allow aggregated DMT Returns is legislated. In any event, an administrative approach should be provided for, whereby the Commissioner can determine that a CE or group of CEs are exempt from filing DMT Return(s). The ATO should publish guidance in relation to factors that will be relevant to this discretion (e.g. the CE is a dormant entity).

GloBE consolidated groups

Our understanding is that these amendments are a collection mechanism only and do not impose joint and several liability on members of the GloBE consolidated group. This should be made explicit in the EM, particularly given differing approaches between jurisdictions to joint and several liability for top-up taxes.

Miscellaneous

We provide the following additional comments, which primarily relate to differences between the drafting of the definitions in the Australian GloBE rules and the Model Rules which we consider may have unintended consequences:

- The definition of Joint Venture in subsection 17(2)(c) appears narrower than the Model Rules definition (in (c)), given it links to the Excluded Entity definition which in turn prescribes ownership thresholds (i.e. 95 or 85 percent per subsections 16(2)(g) and (h)). These ownership thresholds are not in the Model Rules definitions.
- The definition of JV Subsidiary is missing part of the definition from Chapter 10 of the Model Rules which states 'A Permanent Establishment whose Main Entity is the Joint Venture or a JV Subsidiary shall be treated as a separate JV Subsidiary' (we note it may be possible to achieve this outcome through the operation of other provisions, however, it would be simpler to match the wording of the Model Rules).
- The definition of Governmental Entity (in (b)(ii) is missing part of the definition from Chapter 10 of the Model Rules, which states 'managing or investing that government's or jurisdiction's assets through the making and holding of investments, asset management, and related investment activities for that government's or jurisdiction's assets'. We consider that this narrows the definition and may unintentionally impact some foreign governmental entities due to the manner in which they are set up.
- Given the activities of an Excluded Service Entity relate to holding of assets or investment funds rather than provision of services (subsection 16(3)), the definitional name of this entity should be renamed as the word 'Service' may cause confusion.

[10] Tax Challenges Arising from the Digitalisation of the Economy – GloBE Information Return (Pillar Two) (oecd.org).

©2024 KPMG, an Australian partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organisation.

Liability limited by a scheme approved under Professional Standards Legislation.

- Page 6 of the EM should read as follows for clarity:

  ’Domestic top-up tax and IIR top-up tax apply for Fiscal Years beginning on or after 1 January 2024. UTPR top-up tax applies for Fiscal Years beginning on or after 1 January 2025.’

©2024 KPMG, an Australian partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organisation.

Liability limited by a scheme approved under Professional Standards Legislation.

Interactions with other Australian tax laws: Consultation paper

1 Do you agree with the proposed policy positions? If not, please propose an alternative and the reasons why.

2 Do you agree with the approaches outlined? If not, please indicate your suggested approach.

General policy approach

We agree with the general policy approach to interactions with Australian tax laws as outlined in the consultation paper. Notwithstanding, the general policy approach should also reassess the need for certain integrity rules to subsist in the Australian law where the GloBE rules effectively deal with integrity concerns in relation to inappropriate tax outcomes such as non-inclusion of income or the inappropriate use of low-tax jurisdictions. Where integrity concerns are effectively dealt with by the GloBE rules, we consider that government should assess whether domestic rules should be removed or scaled back. The purpose of this is to:

- Reduce any double tax (or effective double tax) outcomes that may arise where there is simultaneous GloBE top-up tax and Australian income tax; and
- Reduce the complexity that exists due to the multiple integrity and avoidance rules already in operation in the Australian tax law that target BEPS activities.

This approach is consistent with the OECD's recommendation that, against the backdrop of the Two-Pillar Solution, countries should eliminate or modify existing rules and measures addressing essentially similar risks which have become duplicative[11].

Further, where the domestic tax measures being considered in the consultation paper are also common features of other jurisdiction tax regimes (e.g. controlled foreign company (**CFC**) and foreign income tax offset (**FITO**) rules), Australia should strive to obtain global consistency in relation to the interaction between the GloBE rules and domestic integrity rules at the OECD level. This is particularly the case for rules such as the hybrid mismatch (**HMM**) rules (discussed further below) which originate from the OECD/G20 BEPS Project.

HMM rules

In relation to the targeted integrity rule in Subdivision 832-J, there is a strong case for amending this measure. This measure targets arrangements that involve financing into Australia via an entity located in a no- or low-tax (10 percent or less) jurisdiction, and hence specifically addresses low-taxed income in a multinational group. The 'subject to foreign income tax' test for Subdivision 832-J purposes should be updated so that GloBE and QDMTT top-up tax is regarded for the purpose of determining whether the 10 percent threshold is met. This would be consistent with the policy of that section which allows for Australian and foreign CFC taxes to be considered in

[11] Tax Co-operation for the 21st Century: OECD Report for the G7 Finance Ministers and Central Bank Governors, May 2022.

©2024 KPMG, an Australian partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organisation.

Liability limited by a scheme approved under Professional Standards Legislation.

determining whether an amount is 'subject to foreign income tax'.

In relation to the remaining components of the HMM rules, we acknowledge that the HMM rules and GloBE rules have differing aims, however effective double tax outcomes can arise if the GloBE rules are overlayed without allowances to address interaction issues. In particular, whether an amount of income is considered to be 'subject to foreign income tax' as defined in section 832-130 of the *Income Tax Assessment Act 1997* if it is subject to either a QDMTT or the IIR at a UPE level.

To illustrate the double tax outcomes using a simplified example which is adapted from Example 3 of Draft Taxation Determination TD 2024/D1:

- The HMM rules currently deny a tax deduction to Company C, a hybrid entity, given a deduction/ non-inclusion mismatch arises in relation to a payment made by Company C (an Australian tax resident) to Company B (a non-hybrid entity resident in a low tax jurisdiction and not subject to tax on the payment from Company C).
- Company B and Company C are wholly owned subsidiaries of Company A.
- Company A is resident in a jurisdiction with an IIR regime. Under the IIR, Company A would be required to pay top-up tax in respect of Company B's low-taxed profits (being the income received from Company C).
- The Company A global group has therefore paid top-up tax in relation to Company B's profits (at 15 percent) and has also had the corresponding deduction denied under the HMM rules (at the 30 percent Australian income tax rate).

We consider that where top-up tax is paid by Company A under the IIR, a double tax outcome would arise if the top-up tax paid under the IIR does not cause the income derived by Company B to be subject to foreign income tax. In our view, an outcome in such a situation would be punitive to MNE Groups and goes beyond the original intent of these rules.

To deal with these double tax outcomes in the Australian domestic legislation in a way that does not undermine the broader intent of the HMM rules is complex. Given the HMM are an OECD BEPS initiative (which a number of other countries have adopted), ideally any solution should be dealt with in a globally consistent way (either through the HMM rules or the GloBE Model Rules).

Accordingly, Australia should prioritise resolution of this double tax issue at the OECD level.

Foreign hybrid, FITO and CFC rules

We agree with the proposed policy positions regarding the interaction between the GloBE rule and these regimes.

In particular, we note the approach to recognise top-up tax paid under a foreign jurisdiction's qualifying domestic minimum top-up tax (**QDMTT**) (but not the IIR or UTPR) for CFC and FITO purposes is aligned with the positions adopted by other jurisdictions including New Zealand and Ireland.

In relation to the specific amendments proposed to the income tax legislation, we broadly agree subject to the following:

- The FITO rules should be amended to expressly allow for a foreign jurisdiction's QDMTT to be a 'foreign income tax'. Similarly, the CFC rules should be amended to expressly allow a notional allowable deduction for top-up tax paid under a foreign jurisdiction's QDMTT. While we accept a natural reading of the existing provisions allows for these positions, amendments should be provided for certainty and to avoid disputes. To do otherwise would also be at odds with the overall drafting approach to prescriptively deal with GloBE and DMT top-up taxes throughout the income tax legislation.
- Section 770-135 of the *Income Tax Assessment Act 1997* (which provides a FITO for an attributable taxpayer in respect of foreign tax paid by a CFC) should be amended to ensure an attributable taxpayer is able to obtain a FITO where top-up tax is paid by a CFC under a foreign jurisdiction's QDMTT on a jurisdictional basis.

  As the CFC rules operate on an entity-by-entity basis (rather than a jurisdictional basis), where an Australian taxpayer has multiple CFCs in a particular jurisdiction, it is possible that the entity which pays top-up tax under a foreign country's QDMTT may not be the same entity which has sufficient attributable income to enable the Australian attributable taxpayer to obtain a FITO for the foreign tax paid. If left uncorrected, this could result in the Australian attributable taxpayer being subject to economic double taxation where one CFC in a particular jurisdiction pays the top-up tax on behalf of all the CFCs in that jurisdiction, but does not itself have sufficient attributable income in order for the Australian attributable taxpayer

©2024 KPMG, an Australian partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organisation.

Liability limited by a scheme approved under Professional Standards Legislation.

to obtain a full FITO (whereas other CFCs located in that jurisdiction do have attributable income but have not paid the top-up tax).

This may be addressed by amending section 770-135 to specifically enable an attributable taxpayer to obtain a FITO in respect of its CFCs in a particular jurisdiction where top-up tax is paid by one CFC but, on an aggregate basis, all CFCs in that jurisdiction have sufficient attributable income to cover the amount of top-up tax paid.

- In relation to the safeguarding for future jurisdictional responses, we consider it too early to amend Division 770 to deal with such future jurisdictional responses. The policy response in Australia should be determined having regard to the precise form and mechanics of any future jurisdictional responses, as well as any future OECD guidance. Hence, a regulation making power is a sufficient and balanced option at this juncture.

Other issues

In relation to the 'subject to tax' definition in section 324, we consider that from a policy perspective the approach should follow that taken for the CFC and FITO rules. That is, the definition should be modified to recognise a foreign jurisdiction QDMTT but not an IIR or UTPR. For example, where a CFC resident in a listed country derives income that is subject to top-up tax under the listed country's QDMTT, the CFC rules should operate to exclude the income from attribution in Australia.

3 Do you consider there are any other significant interactions that should be considered? If so, how should they be addressed?

There are several other significant interactions that should be considered, as outlined below.

Diverted Profits Tax (**DPT**)

The DPT 'sufficient foreign tax' condition should be updated to ensure foreign GloBE and QDMTT top-up tax is appropriately regarded with no effective double tax outcomes.

General anti-avoidance law

Australia's general anti-avoidance laws (Part IVA) should be extended to cover GloBE and DMT top-up tax. This is consistent with the approach taken by other jurisdictions including Canada and the UK.

Conduit foreign income (**CFI**)

The CFI provisions in Division 802 of the *Income Tax Assessment Act 1997* broadly operate so that foreign income ultimately received by a foreign resident through an interposed Australian taxpayer is not subject to Australian tax. We recommend that CFI rules be updated to explicitly confirm that amounts of foreign income derived by an Australian taxpayer that have been subject to Australian top-up tax under the IIR should continue to be characterised as CFI (e.g. dividends received by an Australian UPE from a foreign Low Taxed Constituent Entity which is not located in a jurisdiction with a QDMTT).

This would make it clear that such foreign sourced income is able to be paid to foreign resident shareholders of an Australian corporate tax entity free from withholding tax, on the basis that the income has not been subject to Australian income tax (notwithstanding the Australian entity may have paid IIR top-up tax).

This would provide certainty for Australian corporate entities and their non-resident shareholders and allow alignment with the current tax law outcome where foreign sourced income is not subject to Australian corporate tax. It would also be aligned with the approach taken in relation to top-up taxes and the imputation system, which does not provide franking credits in relation to IIR top-up tax.

©2024 KPMG, an Australian partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organisation.

Liability limited by a scheme approved under Professional Standards Legislation.

Key authors and contacts

Alia Lum
Partner, Tax Policy & Regulatory Engagement Lead

Peter Oliver
Partner, International Tax

Denis Larkin
Partner, International Tax

Kristie Schubert
Partner, KPMG Law

Amanda Maguire
Director, Tax Policy

Luke Imbriano
Director, KPMG Law

KPMG.com.au

The information contained in this document is of a general nature and is not intended to address the objectives, financial situation or needs of any particular individual or entity. It is provided for information purposes only and does not constitute, nor should it be regarded in any manner whatsoever, as advice and is not intended to influence a person in making a decision, including, if applicable, in relation to any financial product or an interest in a financial product. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the situation.

To the extent permissible by law, KPMG and its associated entities shall not be liable for any errors, omissions, defects or misrepresentations in the information or for any loss or damage suffered by persons who use or rely on such information (including for reasons of negligence, negligent misstatement or otherwise).

©2024 KPMG, an Australian partnership and a member firm of the KPMG global organisation of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.

The KPMG name and logo are trademarks used under license by the independent member firms of the KPMG global organisation.

Liability limited by a scheme approved under Professional Standards Legislation.