2 September 2022

Assistant Secretary
Corporate & International Tax Division
The Treasury
Langton Crescent
PARKES ACT 2600

Via email: MNETaxintegrity@treasury.gov.au

Dear Treasury

Multinational Tax Integrity and Enhanced Tax Transparency

The Australian Financial Markets Association (AFMA) represents the interests of over 120 participants in Australia's financial markets. Our members include Australian and foreign-owned banks, securities companies, treasury corporations, traders across a wide range of markets and industry service providers. They are the major providers of wholesale banking and financial market services to Australian businesses and investors.

We are pleased to lodge a submission on the Treasury Consultation Paper addressing the Government's Election Commitments in relation to Multinational Tax Integrity and Enhanced Tax Transparency (**the Consultation Paper**).

Executive Summary

The key aspects of AFMA's submission to the Consultation Paper are as follows:

- The proposed MNE Interest Limitation Rules should have no application to financial or ADI entities and that the Government should explicitly state this policy position;
- No changes to the thin capitalisation rules for financial or ADI entities are warranted;
- Any determination of a "low or no tax" jurisdiction should be aligned to the OECD consensus on Pillar 2 and exclude any jurisdiction with whom Australia has concluded a Double Tax Agreement;
- Any measure to deny deductions for payments relating to intangibles/royalties paid to low or no tax jurisdictions should not be extended to transactions between unrelated parties;

Australian Financial Markets Association
ABN 69 793 968 987
Level 25, 123 Pitt Street GPO Box 3655 Sydney NSW 2001
Tel: +612 9776 7955 Fax: +61 2 9776 4488
Email: info@afma.com.au Web: www.afma.com.au

- Any measure to require the mandatory disclosure of CbC information should be aligned to the EU Directive, both in terms of information to be disclosed and the timeline for disclosure;
- The adoption of any mandatory transparency regime should cause the cessation of the Tax Transparency Report; and
- The determination of "material tax risk" for the purpose of reporting to shareholders should not be made with reference to any ATO publication, particularly Practical Compliance Guides.

MNE Interest Limitation Rules

Many of AFMA's members that are subject to the existing thin capitalisation rules are classified as either ADI entities or financial entities under Division 820 of the *Income Tax Assessment Act* 1997 (**the 1997 Act)**. In this regard, AFMA notes with approval the comment in the Consultation Paper that:

> "the fixed ratio rule will target 'general entities' as defined in the current thin capitalisation legislation. Financial entities and authorised deposit-taking institutions would, in the interim, continue to be subject to the existing thin capitalisation rules. In this regard, the OECD acknowledges that the fixed ratio rule is unlikely to be effective for these types of entities – partly because they are net lenders and are subject to regulatory capital rules. As such, they can be excluded from the fixed ratio rule."

The only point of clarification from an AFMA perspective is the presence of the words "in the interim" in the paragraph above. Our policy position is that, for the reasons articulated, there is no basis for the inclusion of ADI entities or financial entities within scope for the fixed ratio rule and such application would either have no effect (as many ADI and financial entities are likely to be net interest income recipients) or would disproportionately deny interest deductions for such entities. To the extent that it can be confirmed that the Government has no plans to include entities classified as financial or ADI for thin capitalisation purposes as within scope for the interest limitation rules, then AFMA has no further comment on the proposal.

Consultation Question 5 in the Consultation Paper seeks information regarding whether there should be any changes to the existing thin capitalisation rules applicable to financial entities and ADI entities. AFMA's comment is that, while members and the ATO continue to work through operational aspects of thin capitalisation compliance for such entities, from a legislative perspective, the thin capitalisation rules applicable to financial entities and ADI entities are fit for purpose and no changes are required.

Denying MNEs Deductions for Payments Relating to Intangibles/Royalties Paid to Low or No Tax Jurisdictions

The vast majority of AFMA members that operate in multiple jurisdictions are subject to prudential regulation in the jurisdictions in which they operate. Such regulation significantly reduces the ability of firms to hold intangible assets in jurisdictions in which they do not undertake significant operations without regulatory capital. Accordingly, the proposed measures will have little impact on AFMA members.

We make the following comments in relation to questions posed in the Consultation Paper:

- In terms of determining jurisdictions that meet the “low or no tax” criterion, AFMA would support an approach where this determination was aligned to the Pillar 2 rate of 15%. The consensus achieved through the announcement by multiple jurisdictions (including Australia) of what is an appropriate minimum rate of tax to apply to income should inform Australia’s domestic law. Adoption of this approach would be of assistance in other context where the phrase “low or no tax” is used without specificity, such as the work being undertaken by the OECD Forum on Harmful Tax Practices. Additionally, AFMA would support the exclusion of a country that has concluded a Double Tax Agreement with Australia from not being considered to be a low or no tax jurisdiction for the purpose of the rules;
- There does not appear to be a compelling case for the measures applying to non-related party transactions. While the Consultation Paper states that “nothing prevents unrelated entities from acting in concert to achieve a tax benefit,” it would appear in practice that there would need to be significant collaboration between unrelated parties to achieve an outcome to which the proposed measures would apply, with the Commissioner holding existing powers to address a scheme that was entered into by unrelated parties designed to achieve a tax benefit. The compliance burden associated with determining whether a payment to an unrelated party includes a payment referable to intangibles would be disproportionate to the risk of collusion between unrelated parties to achieve a tax benefit, particularly in circumstances where the proposed measures were to apply to embedded royalties.

Multinational Tax Transparency

General Comments

AFMA acknowledges the role of tax transparency in combatting the more egregious forms of tax avoidance, particularly transparency of information between revenue authorities. The majority of AFMA members that operate in multiple jurisdictions are subject to Country-by-Country (**CbC**) reporting requirements and while the compliance burden associated with the reporting requirement is significant, the ability for revenue authorities to be able to understand the taxation profile of companies from a global perspective is noted as a laudable objective. As noted in the Consultation Paper, information contained in CbC reporting is currently confidential in Australia.

Many AFMA members are also within the population of entities about whom information is published in the Corporate Tax Transparency Report. While AFMA agrees with the comment in the Consultation Paper that the information disclosed in the Corporate Tax Transparency Report does not provide a complete picture of a particular entity’s tax performance in Australia, it is also our view that public interest in the Transparency Report has waned significantly since the Transparency Report’s initial release. This highlights the need to ensure that any mandatory transparency initiatives are properly calibrated such that they both succeed in better informing the public’s assessment of MNE tax performance and also minimise the compliance costs associated with such transparency, particularly through alignment with other reporting regimes that multinational entities may need to comply with.

It is not the case that enhanced tax transparency can only arise through mandatory measures. As stakeholders look to ensure that large entities continue to adhere to expectations around Environment, Social and Governance (**ESG**) factors, it is becoming increasingly incumbent on

entities to enhance transparency in respect of their taxation affairs even without a legislative compulsion to do so. This should further influence the Government in prioritising the reduction of compliance costs in implementing any mandatory transparency regime.

Alignment with EU Public CbC Reporting Requirements

Noting the above, of the options canvassed in the Consultation Paper, AFMA would support any disclosure of CbC information from an Australian perspective to align with the EU public CbC reporting requirements, both in terms of the nature of information disclosed and the timetable for disclosure. To this end, and in response to Consultation Question 5, AFMA would not endorse additional disclosures above that required under the EU reporting requirements.

It is noted that such an approach would not hinder the ability of companies to make additional disclosures in line with their own governance frameworks, including potential disclosures aligned to the GRI Tax Standard, to meet growing stakeholder expectations with respect to ESG. However, in terms of mandatory disclosure, alignment to the EU requirements strikes the appropriate balance between providing public transparency in a consistent format that is applied in multiple jurisdictions and imposing an additional compliance burden on affected entities.

In terms of timing, under the EU Directive, member states are required to enact legislation to give effect to the directive by June 2023, with the first reporting to occur in relation to income years starting on or after 22 June 2024 (at the latest). Entities caught by the reporting requirements are then provided with twelve months from year end to report the required information. AFMA supports alignment in terms of timing to the EU requirements.

AFMA's position is that, to the extent that the Government implements its commitment to enhance transparency requirements through the mandatory reporting of CbC information, this should obviate the need for making the Voluntary Tax Transparency Code mandatory. Similarly, the implementation of any mandatory transparency regime should result in the cessation of the Tax Transparency Report; noting the comment in the Consultation Paper that the existing structure of the report "can hinder the general community's understanding of the tax affairs or corporate tax entities."

Mandatory Reporting of Material Tax Risk to Shareholders

AFMA understands that the scope of any proposal to require disclosure of material tax risk to shareholders is only in respect of Australian-headquartered entities that are listed on an approved securities exchange in Australia. This would appear to be an appropriate calibration of entities to whom the reporting requirements would apply.

AFMA expresses significant concern about any proposal to determine material tax risk with respect to assessment against Practical Compliance Guides (**PCG**) issued by the ATO - or indeed with reference to any ATO publication. A PCG is not the law, nor does it represent the ATO's interpretation of the law, but rather may be considered, at best, to be a guide to allow entities to determine the likelihood of further interaction with the ATO on a particular area. PCGs are not bonding on the Commissioner and the rigour through which PCGs are subjected prior to publication is significantly less than other ATO products, such as Public Rulings.

Although not canvassed in the Consultation Paper, AFMA would not support any proposals for mandatory disclosure of ratings under the ATO's Justified Trust review program, as these ratings are often influenced by factors outside of the control of the taxpayer and have ability of appeal/review.

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Thank you for the opportunity to the Consultation Paper. Please contact me on (02) 9776 7996 or at rcolquhoun@afma.com.au to discuss any of the matters that we have raised in this submission.

Yours sincerely,

Rob Colquhoun
Director, Policy