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TaxTalk Monthly

Keeping you up to date on the latest Australian and international tax developments

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Corporate Tax Update

Voluntary Tax Transparency Code notification to ATO

The Australian Taxation Office (ATO) has issued guidance on the Voluntary Tax Transparency Code. The Tax Transparency Code, developed by the Board of Taxation, is a set of principles and minimum standards to guide medium and large corporate businesses on public disclosure of tax information. The guidance also details how businesses can notify the ATO once the public disclosures have been made.

The ATO is responsible for administering the Code and compiling a list of published Tax Transparency reports provided by businesses that have adopted the Code. The list for 2015-16 is currently being compiled as the ATO progressively receives published reports from businesses.

General purpose financial statements for significant global entities

The ATO has commenced consultation on the administrative arrangements relating to the legislative requirement for a corporate entity that is a 'significant global entity' to lodge general purpose financial statements with the ATO, if they are not required to lodge them with the Australian Securities and Investment Commission (ASIC).

In broad terms, a significant global entity is an entity with annual global income of at least AUD 1 billion or that is part of a group with annual global income of at least AUD 1 billion. The new financial reporting requirement applies to years beginning on or after 1 July 2016.

In the ATO's consultation paper, a number of issues are raised, including:

- the interpretation of key concepts, such as general purpose financial statements and the applicable accounting standards required for their preparation; what constitutes "commercially accepted principles relating to accounting" for purposes of preparing general purpose financial statements and the evidence required to demonstrate this fact
- how an affected entity can give their general purpose financial statements to the ATO and
- practical guidance to assist affected entities to comply.

The ATO is seeking comments on its discussion paper until 30 September 2016. If you would like to discuss this further or have comments to share, contact Peter Collins on +61 (3) 8603 6247 or at peter.collins@pwc.com or Regina Fikkers on +61 (2) 8266 8350 or at regina.fikkers@pwc.com.

Let's talk

For a deeper discussion of how these issues might affect your business, please contact:

Tom Seymour, Managing Partner
+61 (7) 3257 8623
tom.seymour@pwc.com

Murray Evans, Newcastle
+61 (2) 4925 1139
murray.evans@pwc.com

Kirsten Arblaster, Melbourne
+61 (3) 8603 6120
kirsten.arblaster@pwc.com

Jason Karametos, Melbourne
+61 (3) 8603 6233
jason.karametos@pwc.com

Alistair Hutson, Adelaide
+61 (8) 8218 7467
alistair.hutson@pwc.com

Rob Bentley, Perth
+61 (8) 9238 5202
robert.k.bentley@pwc.com

Warren Dick, Sydney
+61 (2) 8266 2935
warren.dick@pwc.com

David Ireland, Sydney
+61 (2) 8266 2883
david.ireland@pwc.com

Julian Myers, Brisbane
+61 (7) 3257 8722
julian.myers@pwc.com

Employment Taxes Update

Payroll Tax Rebate for apprentices and trainees (Qld)

The Queensland Government has announced that it will double the payroll tax rebate for employing apprentices or trainees from 25 per cent to 50 per cent for 12 months with effect from 1 July 2016. This rebate will be calculated automatically when an employer with apprentice or trainee wages in Queensland lodges their payroll tax return.

PAYG Withholding – Failure to Withhold Penalty (Cth)

In *T T Lam and HT Ngo v Commissioner of Taxation [2016] AATA 552* the taxpayer appealed the imposition of a 50 per cent penalty by the Commissioner in respect of a failure to remit PAYG withholding to the ATO under a labour hire arrangement. The PAYG withholding underpayments were originally identified by the ATO under audit, however, as part of the audit process, the Commissioner had reduced the penalty to 75 per cent on the basis that the failure to withhold had resulted from an intentional disregard of the taxpayer's PAYG withholding obligations.

The taxpayer subsequently objected against this penalty and the objection was allowed in part by the Commissioner, further reducing the failure to withhold penalty down to 50 per cent of the PAYG withholding underpayment, having determined that the taxpayer was reckless with regard to its PAYG withholding obligations.

Ultimately, the Tribunal found that the taxpayer did not present any evidence which would allow the failure to withhold penalty to be further reduced.

This case serves as a reminder that the ATO will impose failure to withhold penalties where it is determined that a taxpayer has not complied with their PAYG withholding obligations. Where an employer has failed to meet its PAYG withholding obligations, it is important to take a pro-active approach with respect to disclosure in order minimise penalties imposed by the ATO.

Payroll Tax Exemption – Charitable bodies (WA)

In *Association of Mining & Exploration Companies Inc v Commissioner of State Revenue [2016] WASCA 131* the taxpayer appealed to the Supreme Court of Western Australia against a decision by the State Administrative Tribunal that the Commissioner was allowed to limit the taxpayer's payroll tax exemption to a prospective period commencing on 1 July 2012.

In December 2012, the taxpayer applied to the Commissioner for an exemption from pay¬roll tax on the grounds that it was a 'charitable body or organisation'. In granting this exemption, the Commissioner specified that the exemption only came into operation on 1 July 2012. The taxpayer formally objected against this decision, on the grounds that the exemption should apply for a period of at least five years prior to the date the exemption was granted. This objection was disallowed in full by the Commissioner. The State Administrative Tribunal then dismissed the taxpayer's application for a review of the Commissioner's decision before the taxpayer appealed against this decision to the Supreme Court of Western Australia.

The taxpayer contended that the Commissioner was required to specify the operative date of the payroll tax exemption as 1 July 2007, on the basis that the taxpayer had been a charitable organisation throughout the period. In contrast, the Commissioner's view was that the power to specify a date before the exemption application was made was not required to be exercised solely because the taxpayer was a charitable organisation before that time.

In rejecting the arguments of both parties, the Court found that the Commissioner's discretionary powers neither required the Commissioner to specify 1 July 2007, nor prohibited the Commissioner from specifying that day, as the date on which the exemption came into operation. As such, the Court accepted the taxpayer's submissions that the Tribunal had erred in law by misinterpreting the nature and scope of the statutory discretionary power which the Commissioner was exercising and set aside the former decision by the Tribunal. The matter was sent back to the Tribunal for reconsideration.

Working holiday maker visa review

The Federal Government has commenced its review of a range of issues affecting the supply and taxation

of labour performed by working holiday maker visa holders, including the 2015-16 Federal Budget proposal to increase the tax on people temporarily in Australia for a working holiday ('backpacker tax'). The terms of reference and a summary of the review has been released. The Government plans to announce the review's outcomes before 1 January 2017. Submissions can be made to the review by 2 September 2016.

Draft Taxation Determination on indeterminate rights and employee share schemes (ESS)

An 'ESS interest' in a company, as defined, includes a beneficial interest in a right to acquire a beneficial interest in a share in the company. The ATO has issued Draft Taxation Determination TD 2016/D3 which deals with the circumstances in which a contractual right, subject to the satisfaction of a condition, becomes a right to acquire a beneficial interest in a share under section 83A-340(1) of the *Income Tax Assessment Act 1997*. Comments are due by 16 September 2016.

Let's talk

For a deeper discussion of how these issues might affect your business, please contact:

Greg Kent, Melbourne
+61 (3) 8603 3149
greg.kent@pwc.com

Maria Ravese, Adelaide
+61 (8) 8218 7494
maria.a.ravese@pwc.com

Norah Seddon, Sydney
+61 (2) 8266 5864
norah.seddon@pwc.com

Rohan Geddes, Sydney
+61 (2) 8266 7261
rohan.geddes@pwc.com

Paula Shannon, Brisbane
+61 (7) 3257 5751
paula.shannon@pwc.com

Stephanie Males, Canberra
+61 (2) 6271 3414
stephanie.males@pwc.com

Ross Thorpe, Perth
+61 (8) 9238 3117
ross.thorpe@pwc.com

Global Tax Update

Latest news from international tax and transfer pricing

ATO continues its focus on international tax issues

The Australian Taxation Office (ATO) has issued three new Taxpayer Alerts (TA), continuing the trend of highlighting issues for multinational groups. These are:

- TA 2016/7, which identifies arrangements involving Australian income tax consolidated groups with subsidiaries that operate through offshore permanent establishments (PEs) that have entered into intra-group transactions. The ATO is concerned the consolidated group in Australia is not returning the right amount of taxable income. In particular, that the amount of taxable income returned does not reflect the economic substance and significance of the operations carried on in and between Australia and the offshore jurisdiction in a manner that is consistent with the arm's length principle.

- TA 2016/8, which discusses the ATO's review of arrangements entered into in response to the Multinational Anti-Avoidance Law (MAAL). Further to this, the ATO is considering the Goods and Services Tax (GST) consequences of the arrangements involving the distribution of intangible products and services into Australia, as they are deemed to be inconsistent with the policy intent of both the MAAL and GST Act. Under this arrangement, it is purported that while an Australian entity contracts with Australian customers to avoid the application of the MAAL, no GST is payable on the supplies on the basis the supplies are not made through an enterprise carried on in the indirect tax zone. An addendum was also made to GST Ruling GSTR 2000/31 which indicates the Commissioner of

Taxation's view that any supply made by an entity in the course or furtherance of an enterprise it carries on through a PE in Australia is connected with Australia even if the supply can also be said to be connected with a place of business in another country.

- TA 2016/9, which identifies arrangements where taxpayers have excluded the value of a 'debt interest' that has been treated wholly or partly as equity for accounting purposes from their 'debt capital' for the purposes of the thin capitalisation regime. The ATO is concerned that this treatment results in inappropriate debt deduction claims. The ATO's approach is that the sum of the accounting value of the equity component and the accounting value of the liability component of the debt interest on issue must be used in calculating the average value of debt capital. The Alert also states that the ATO will also generally take into account all relevant accounting entries, such as distributions to holders, such that the full face value of the debt interest will be used in the calculation of adjusted average debt. Furthermore, the Alert indicates that if the Commissioner determines that a taxpayer has undervalued its debt capital, the Commissioner may apply section 820-690 of the *Income Tax Assessment Act 1997* (*ITAA 1997*) to substitute an appropriate value having regard to the accounting standards and the thin capitalisation regime, or may apply the general anti-avoidance provisions (Part IVA).

Additionally, the ATO has also released a draft Practical Compliance Guideline (PCG) (in the form of a discussion paper) in relation to transfer pricing issues related to the location and relocation of centralised operating models involving procurement, marketing, sales and distribution function (i.e. offshore hubs).

The purpose of this PCG is to establish a framework for taxpayers to:

- assess whether hub arrangements pose a transfer pricing risk and how that risk can be mitigated
- understand when the ATO may take a closer look at hub arrangements and the documentation and evidence the ATO expect to be prepared and readily available and
- understand disclosure obligations in relation to marketing hubs.

Comments on the draft PCG can be made until 30 September 2016. Refer to our feature article, Australia: offshore marketing hubs – ATO releases draft discussion paper, for further information.

The ATO also plans to issue guidance in relation to other hubs, as hubs remain a concern for ongoing ATO compliance activity.

Draft Taxation Determination limits foreign hybrid limited partnership election

On 10 August 2016, the ATO issued Draft Taxation Determination TD 2016/D2 (the Draft Determination) which sets out the Commissioner of Taxation's preliminary view that a foreign resident cannot elect to treat their interest in a limited partnership as an interest in a foreign hybrid limited partnership under paragraph 830-10(2)(b) of the *ITAA 1997*. The following key points are made in the Draft Determination:

- Generally, limited partnerships are taxed as companies for Australian income tax purposes, subject to the application of the foreign hybrid rules in Division 830 of the *ITAA 1997*, where an entity that qualifies as a 'foreign hybrid' is treated as a partnership.
- When addressing the question of whether or not a foreign resident can elect to have their interest in a foreign investment fund (FIF) that is a corporate limited partnership to be an interest in a foreign hybrid limited partnership, the Explanation provided in the Draft Determination states that statutory interpretation principles require that the relevant sections be considered in context, having regard to the existing state of the law, the position under the former FIF rules, the amendments made to repeal the FIF rules and the mischief the statute was intended to remedy.
- The Explanation in the Draft Determination states that under the former FIF rules, the election available under section 485AA of the *Income Tax Assessment Act 1936* (*ITAA 1936*) was limited to Part XI Australian residents who would otherwise be subject to the operation of the FIF rules. As a foreign resident was not subject to the FIF rules it could not make that election. The amendments to Division 830 of the *ITAA 1997* made at the time the FIF rules were repealed did not broaden the scope of the election – the conditions required to make an election under paragraph 830-10(2)(b) of the *ITAA 1997* are the same as those under former section 485AA of the *ITAA 1936*. Accordingly, an election for foreign hybrid treatment is only available to partners who are Australian residents.

- Appendix 2 of the Draft Determination contains an alternative view based on a literal approach to interpreting the relevant sections, noting that the plain and ordinary meaning of the text in subsections 830-10(2) and (4) of the *ITAA 1997* does not contain any limitation that would preclude a foreign resident from electing to treat their interest in a limited partnership as an interest in a foreign hybrid. The only requirement in subsection 830-10(4) of the *ITAA 1997* is that the partner has an 'interest in a FIF' as defined in former Part XI of the *ITAA 1936*, and there is no requirement that the holder is an Australian resident. As such, a foreign resident can have an interest in a FIF, even though it may not have been an interest to which Part XI applied. The Commissioner does not accept this alternative view.

Comments on the Draft Determination can be made until 9 September 2016.

OECD and BEPS developments

In the Communique from the G20 Finance Ministers and Central Bank Governors Meeting held in Chengdu, China on 23-24 July 2016, G20 Finance Ministers welcomed continued progress on the implementation of the Base Erosion and Profit Shifting (BEPS) package. They also endorsed proposals made by the Organisation for Economic Co-operation and Development (OECD), working with G20 members on objective criteria to identify non-cooperative jurisdictions with respect to tax transparency. The G20 has asked the OECD to report back on the progress made by jurisdictions on tax transparency, noting that 'defensive measures' will be considered against jurisdictions that have not sufficiently progressed towards a satisfactory level of implementation of the agreed international standards on tax transparency by the time of the July 2017 G20 Leaders Summit.

The OECD Secretary-General released a Report to the G20 Finance Ministers regarding the OECD/G20 BEPS Project; tax transparency; tax policy tools to support sustainable and inclusive growth; and tax and development. The Report also included an updated progress report by the Global Forum on Transparency and Exchange of Information to the G20.

The OECD has released the Tax Design for Inclusive Economic Growth paper for discussion and submits that Governments should use tax systems to drive an inclusive growth agenda. The OECD also released the Report by the Platform for Collaboration on Tax to the G20: Enhancing the Effectiveness of External Support in Building Tax Capacity in Developing Countries.

In addition, the OECD has undertaken further work to progress specific BEPS implementation plans, including:

- a discussion draft on interest deductions in banking and insurance sectors. The draft document provides a more detailed consideration of the BEPS risks posed by banks and insurance companies and those posed by entities in a group with a bank or insurance company, such as holding companies, group service companies and companies engaged in non-regulated financial or non-financial activities. Comments are due by 8 September 2016. For further information, see PwC Tax Policy Bulletin.

- a discussion draft on branch mismatch structures under Action 2 (neutralising the effects of hybrid mismatch arrangements) of the BEPS Action Plan. The discussion draft identifies five basic types of branch mismatch arrangements and sets out preliminary recommendations for domestic rules which would neutralise the resulting mismatch in tax outcomes. Comments can be made until 19 September 2016. For further information, see our feature article, OECD releases discussion draft on branch mismatch structures.

Refer to PwC Tax Insights from Transfer Pricing for further information on the recent OECD announcements which provide both an update and insight into the progress of anticipated areas of future work.

China's State Administration of Taxation issues new transfer pricing compliance requirements

China's State Administration of Taxation (SAT) on 29 June 2016 issued a public notice Regarding Refining the Reporting of Related-party transactions and the Administration of Transfer Pricing documentation (SAT Public Notice 42). The public notice provides new transfer pricing compliance requirements in China, including annual reporting forms for related party transactions, country-by-country (CbC) reporting, and transfer pricing documentation, all of which are substantial changes to the existing rules. See PwC Tax Insights for further information.

Austria implements transfer pricing documentation and CbC reporting requirements

The Austrian Parliament has enacted legislation that introduces mandatory transfer pricing documentation requirements as defined in Action 13 of the OECD's Action plan on BEPS. The legislation follows the three-tiered approach to transfer pricing documentation requiring multinational enterprises to prepare a Master File, a Local File, and a CbC Report. See PwC Tax Insights for further information.

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Luxembourg proposes new corporate tax measures

On 26 July 2016, the Luxembourg Government introduced a bill with proposed tax measures for corporations to take effect from the 2017 tax year. The proposed changes, which include a reduced corporate income tax rate, are in line with the announcements made by the government earlier this year. See PwC Tax Insights for further information.

Let's talk

For a deeper discussion of how these issues might affect your business, please contact:

Peter Collins, Melbourne
+61 (3) 8603 6247
peter.collins@pwc.com

Robert Hines, Sydney
+61 (2) 8266 0281
robert.hines@pwc.com

Paul McNab, Sydney
+61 (2) 8266 5640
paul.mcnab@pwc.com

Michael Taylor, Melbourne
+61 (8) 8603 4091
michael.taylor@pwc.com

Nick Houseman, Sydney
+61 (2) 8266 4647
nick.p.houseman@pwc.com

Eddy Moussa, Sydney
+61 (2) 8266 9156
eddy.moussa@pwc.com

Greg Weickhardt, Melbourne
+61 (3) 8603 2547
greg.weickhardt@pwc.com

Michael Bona, Brisbane
+61 (7) 3257 5015
michael.bona@pwc.com

Superannuation update

Australian Taxation Office Tax Risk Management Update

In July 2015, the Australian Taxation Office (ATO) published the Tax Risk Management and Governance Review Guide to assist large taxpayers in understanding what the ATO considered to be better tax risk management and corporate governance practices.

Since that time, the ATO has been working with relevant stakeholders to develop two documents:

1 Director's handbook to the ATO's Tax Risk Management and Governance Review Guide; and

2 Tax Risk Management and Governance Self-Assessment Procedures.

From the drafts of these documents released for consultation, it is clear that the ATO intends a significantly more evidence and enterprise based risk management focus on the tax management function of large taxpayers and seeking, through the release of the Director's handbook, to increase the attention of Boards in this area.

There is a strong link between the ATO's view of a taxpayer's tax risk management and governance, and the risk rating it applies to that taxpayer. Funds that have not yet reviewed their policies and procedures in light of the ATO's guide should note that this is clearly an increasing focus for the ATO.

Ten questions to ask your investment manager and custodian on tax

This PwC publication looks at tax-efficient management of Australian equity portfolios, and what questions Trustees should be asking of their managers and custodians to ensure that members are getting the best possible after tax outcome. Tax efficiency gains have a real and consistent effect on returns for members. Read the full paper here.

Legislation expected for Federal Budget Measures

On 17 August, Prime Minister Malcolm Turnbull indicated that in the upcoming sittings of the new parliament, the Government will introduce an Omnibus Bill that puts together all the Government's savings measures that it is understood from the election campaign the Labor Party is prepared to support. Labor has expressed support for the Coalition's superannuation policies which target tax concessions. However, this position has not been finalised and is subject to further stakeholder consultation. Labor maintains that it will oppose the $500,000 lifetime non-concessional contributions cap.

Foreign residents CGT withholding

A reminder that the new 10 per cent non-final withholding tax on the acquisition of certain direct or indirect Australian real property interests from foreign residents applies to contracts entered into on or after 1 July 2016. The new rule imposes various obligations on vendors such as certifying their status as an Australian resident in the case of a sale of real property, or providing a declaration that an asset is not an indirect real property interest. Otherwise the purchaser may have a tax withholding obligation on the purchase price. This would require the purchaser to pay an amount of the purchase price to the ATO instead of the vendor.

Funds should note these new rules to ensure compliance with the law when dealing with property assets.

Property Commission Report

The Productivity Commissioner has released its draft report outlining how it proposes to assess the competitiveness and efficiency of Australia's superannuation system. Whilst the report does not have a specific tax focus, tax is considered an important element in some contexts of assessing the efficiency of the system, eg products available to members in the transition and retirement phases. The report is available here.

Treasury's new Tax Framework Division

Treasury has announced the establishment of a new policy division which is tasked with cross-tax system issues in the economy, including monitoring international tax developments and the tax simplification agenda. This new division will consult widely, and we expect that it will be concerned with many tax issues important to superannuation funds.

Let's talk

For a deeper discussion of how these issues might affect your business, please contact:

David Ireland, Sydney
+61 (2) 8266 2883
david.ireland@pwc.com

Marco Feltrin, Melbourne
+ 61 (3) 8603 6796
marco.feltrin@pwc.com

Abhi Aggarwal, Brisbane
+ 61 (7) 3257 5193
abhi.aggarwal@pwc.com

Alice Kase, Sydney
+ 61 (2) 8266 5506
alice.kase@pwc.com

Peter Kennedy, Sydney
+ 61 (2) 8266 3100
peter.kennedy@pwc.com

Jeff May, Melbourne
+ 61 (3) 8603 0729
jeffrey.may@pwc.com

Matthew Strauch, Melbourne
+ 61 (3) 8603 6952
matthew.strauch@pwc.com

Ken Woo, Sydney
+ 61 (2) 8266 2948
ken.woo@pwc.com

Other news

Final rulings on deductible expenditure

The ATO has also issued the following taxation determinations dealing with the deductibility of certain items of expenditure:

- TD 2016/14: A taxpayer who carries on a business is entitled to a deduction under s8-1 of the *ITAA 1997* for an outgoing incurred on a gift to a former or current client if the gift is characterised as being made for the purpose of producing future assessable income
- TD 2016/15: An employer is entitled to a deduction under s8-1 of the *ITAA 1997* for the annual fees incurred on an airport lounge membership for use by its employees where that membership is provided because of the employment relationship. However, annual fees will not be deductible to the extent they are incurred in relation to gaining or producing exempt income or non-assessable non-exempt income.

Let's talk

For a deeper discussion of how these issues might affect your business, please contact:

Tom Seymour, Managing Partner
+61 (7) 3257 8623
tom.seymour@pwc.com

Murray Evans, Newcastle
+61 (2) 4925 1139
murray.evans@au.pwc.com

Kirsten Arblaster, Melbourne
+61 (3) 8603 6120
kirsten.arblaster@pwc.com

Jason Karametos, Melbourne
+61 (3) 8603 6233
jason.karametos@pwc.com

Alistair Hutson, Adelaide
+61 (8) 8218 7467
alistair.hutson@pwc.com

Rob Bentley, Perth
+61 (8) 9238 5202
robert.k.bentley@pwc.com

Warren Dick, Sydney
+61 (2) 8266 2935
warren.dick@pwc.com

David Ireland, Sydney
+61 (2) 8266 2883
david.ireland@pwc.com

Julian Myers, Brisbane
+61 (7) 3257 8711
julian.myers@pwc.com