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21 September 2015

Committee Secretary
Senate Economics Legislation Committee
PO Box 6100
Parliament House
CANBERRA ACT 2600

Dear Committee members

INQUIRY INTO TAX AND SUPERANNUATION LAWS AMENDMENT (BETTER TARGETING THE INCOME TAX TRANSPARENCY LAWS) BILL 2015 ("BILL")

The Family Office Institute Australia Pty Limited (the Institute) has recently been created to represent, assist and promote Australian family owned companies. This issue before the Senate Economics Legislation Committee (the Committee) is one of the drivers for the creation of the Institute. Interest in the Institute by family offices has been significant and every family office we have spoken to has expressed concern about the current tax disclosure regime, for two main reasons:

1. It has the potential to breach the privacy and tax confidentiality of the affected taxpayer companies and their shareholders/family groups; and
2. It risks these family groups deploying their investments outside of Australia in order to escape the tax publication obligations, which in turn impacts on the Australian economy.

In a 2011 study on the contribution by family groups to the Australian economy, the total wealth of family groups in the "family office sector" was approximately \$226 billion[1]. The amount is likely to be significantly more in 2015. As such, the risks to Australia's investment by family offices in Australia should not be underestimated. A large proportion of family offices that set up corporate businesses in Australia are likely to exceed the \$100 million turnover threshold and therefore are subject to the current tax disclosure laws.

[1]http://www.familyofficeconnect.com.au/pdf/Family%20Office%20Connect%20-%20FOC%20-%20Executive%20Summary%202010.pdf

The Institute therefore supports the Bill and commends its passage by the Senate as it will protect family groups and their family offices. The submissions in support of the Bill are set out in detail in the attached document.

Should you have any questions or wish to discuss these submissions further, please contact Mr Richard Lie on .

Yours sincerely
Family Office Institute Australia Pty Limited

Submissions to Senate Committee inquiry into the Bill

The Institute fully supports the Bill and believes it is a positive step in protecting Australian private companies from the adverse consequences of the current tax disclosure laws.

1. Fundamental right to privacy should not be abrogated in respect of private companies

In debate on earlier taxation laws (the Tax Laws Amendment (Confidentiality of Taxpayer Information) Bill 2010) the Hon. Bernie Ripoll stated: *"People's tax affairs are very much between themselves, the Taxation Office and God. This Bill continues that spirit."* The Hon. Bill Shorten and the Hon. Wayne Swan also upheld a taxpayer's right to privacy of their personal taxation information during second reading speeches to that bill.

Whilst there is a longstanding fundamental principle that all taxpayers have a right to confidentiality of their tax affairs, the enactment of the tax publication laws in section 3C of the *Taxation Administration Act 1953* in 2013 sets out one exception to this – being publication of a part of the taxation information of specific large corporations on a premise of minimising aggressive tax avoidance practices.

The Commissioner of Taxation Chris Jordan noted in a recent media article that the tax publication law in section 3C was "really for multinational companies operating here, disclosing quite low revenue."[2] The tax publication laws were introduced against a backdrop of measures to target base erosion and profit shifting by multinational corporations, and arguably there may be merit in having specific laws to deter aggressive taxpayers who do not "pay their fair share of tax". The Government has recently introduced legislation into Parliament for that purpose.

Private companies the subject of section 3C are required to provide very detailed information to the Australian Taxation Office (ATO), setting out all items of income, type of income, expenses, deductions, exemptions, credits, overseas activities, transfer pricing details, restructures, capital gains and so on. What is provided to the ATO is the full picture of the company's tax affairs. The tax publication under section 3C will be a public disclosure of only very small and unconnected parts of that information: gross accounting turnover or income, net taxable income and tax payable. This comparison has been described by Treasury and the ATO themselves as "comparing an apple with an orange and not being about fruit"[3] as well as being confusing and misleading to the public.

It does not follow that the fundamental right to privacy of that taxpayer information should be abrogated in respect of large private companies and there has been no evidence to justify an exception to the principle for one targeted class of taxpayers. The ATO has itself noted that Australia's large private groups mostly pay their correct taxes and are generally compliant (Media Release 16 April 2015).

A perception of potential aggressive tax structures, particularly by multinationals, does not justify the means. That is, the perceived goal of deterring tax avoidance practices does not

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[2] http://www.smh.com.au/business/the-economy/atos-chris-jordan-says-tax-disclosure-laws-not-intended-for-private-companies-20150319-1m2r46.html

[3] Mr Rob Heferen, Executive Director Revenue Group of the Treasury, per Hansard, Estimates hearings, Economics Legislation Committee, 22 October 2014

justify abrogating a fundamental right to tax privacy that has been enshrined in Australian tax law, for a whole class of taxpayer entities regardless of their activities, particularly given that there has been no empirical evidence to indicate that Australian private companies have engaged in widespread aggressive tax avoidance practices.

2. Publication would discourage investment in Australia

Many successful Australian family groups that are currently subject to the disclosure laws have the flexibility to move their assets and investments to other jurisdictions. Family groups may be compelled to restructure their family office corporate businesses or deploy their assets overseas to avoid the unnecessary public exposure, and could do so with relatively little barriers, in order to remain below the $100 million Australian turnover threshold. Studies suggest that with favourable economic conditions, such as improved currency in other jurisdictions, there is a growing trend to move resources offshore and imposing public tax reporting obligations on family groups would only encourage this. The Institute anticipates that many family offices have already been obtaining advice to move their corporate affairs or significant investments offshore as a result of the current tax publication laws.

Ultimately the publication laws could lead to a situation where Australian family groups (or foreign investors, for that matter) invest less and less into the Australian economy and more in other jurisdictions, in order to minimise publication of their regulatory disclosure. This would negatively impact on Australia's economy and run counter to Australian taxation policy of encouraging Australian investment.

Whilst the costs of restructuring vary depending on the transactions undertaken, for many Australian family groups, this may be a relatively small price to pay in order to avoid the other adverse consequences of public tax disclosure.

3. Disclosure would incur additional costs to private companies

Companies are proper and legitimate entities to carry on substantial businesses. Successful private Australian companies which would be subjected to the tax publication if the Bill is not enacted, include substantial trading businesses which employ thousands of staff, invest heavily in infrastructure, skills, manufacturing, agriculture and other sectors, and contribute extensively to the indirect economy through supplies of goods and services, supply and delivery chains and so on.

In the Senate Economics References Committee Report *"Corporate Tax Avoidance"* released on 18 August 2015, it was observed that the private company sector had generally lower profits than public companies – private companies in Australia do not have the same access to capital as public companies, and usually do not have the scale and other resources. The fact that their expenses are greater, or the profitability lower, only shows the distinctly different nature of private and public companies.

Public companies, being public entities with disparate and anonymous shareholders, are accustomed and required as a private company to disclose financial information under the corporations law and listing rules. Often, large public companies have public relations and public media support and other measures in place to explain their financial positions and performances to their shareholders and other stakeholders.

On the other hand, private and family owned companies generally do not need to engage in the same level of stakeholder risk management. The current tax publication laws would cause those affected private companies to be subject to publication of their private accounting and tax information which, in the absence of further explanation or context, has the propensity to mislead. This could compel the private companies to do either of the following:

a) incur significant time and expenses in preparing information to its stakeholders and the public in general, to justify the tax liability of the company; or
b) restructure the private company's corporate affairs in order to keep below the $100 million reporting threshold.

In either case, private companies are burdened with additional costs and effort to undertake measures beyond the scope of their organisation, and this causes an inefficient use of resources which could otherwise be invested in the business.

In the case of potential restructuring to avoid the disclosure, this may take the form of groups operating under multiple companies rather than one head company, an increased use of opaque unit trusts or discretionary trusts to hold assets or operate businesses, and at worst, an increase in capital, investment and jobs being deployed in entities *outside* Australia to avoid the publication in Australia – as discussed above.

The Bill currently distinguishes between Australian-owned private companies and foreign-owned private companies. Whilst the Institute considers that the carve-out should apply to all private or family owned companies, it accepts that Australian-owned private companies may be more disadvantaged under the existing disclosure laws and for this reason, supports the Bill as currently drafted.

Australian shareholders of a private family company may have other Australian and outbound investments which are consolidated in the accounts of the corporate group, and the accounting income and tax liability of these investments may also be disclosed under the current tax disclosure laws. On the other hand, foreign owned Australian corporates, who may have other global investments not held through the Australian company, would only need to disclose the total income and tax liability of its Australian operations. This means that more of the business and investments of an Australian-owned private company may be exposed under the disclosure laws than a foreign-owned private company which may only effectively disclose the Australian operations of its global business. Such an increased exposure may not only translate to additional costs in having to provide explanatory materials to stakeholders and the public, but create commercial disadvantage or reputational risks, as discussed further below.

It is this prejudice against Australian-owned private companies that further justifies the need to carve-out Australian private companies from the existing disclosure laws.

4. Reporting private company information may create significant commercial risk and disadvantage

Very often, private Australian family companies specialise in the supply of a particular good or service rather than have a diversified business structure which is more common in public

companies. As such, the financial information of such a private company will reflect its whole and sole business whereas the financial information of a public company may reflect its diversified businesses with its various business lines and investments. If a private company only has one business line, the gross income and taxable income of that company could potentially be used to estimate the profit margins of that business.

The disclosure of gross turnover and sales income and the net taxable income under the current disclosure laws therefore presents significant commercial risk to private companies because stakeholders and competitors could potentially use such information to determine profit margins or other pricing information. This information could then be used to exert pressure or leverage when undertaking commercial negotiations with the private company, to target their now public total sales and undercut their perceived margin, or drive down prices to lower the net margin now published.

This argument was noted by the Commissioner of Taxation Chris Jordan when he stated:

> *"I understand, and this mainly what I've read in the media, that there's a lot of concerns about the private companies [being included] in these disclosures. [There are] personal reasons but also competitive reasons. People saying, well their [private companies'] margins might be looked at. If they're a major supplier to some of the major retailers there might be pressure on them to reduce their prices."*[4]

The result is that the private family company is at a commercial disadvantage because of the potential for its profits to be undercut or its market power undermined. On the other hand, competitors or stakeholders would benefit from such commercially sensitive information, however this would cause a misallocation of resources as they would not be operating within the typical market forces. Ultimately this will impact on the overall market in which the business operates as it may drive business growth downwards.

For a business which is currently below, and even 'just below', the disclosure threshold, or a business with more than $100m turnover but operated through a trust, partnership or other structure – they will not be subject to any of the publication of private tax information. That puts those other entities at a significant commercial advantage to an affected private company, which will usually have significant costs if endeavouring to avoid the disclosure.

Furthermore, the measure by which an entity is required to disclose is irrational and has no economic justification. Take for example a company with gross sales of $105 million and expenses of $100 million. The disclosures will show $105 million income and $5 million taxable income leading to the inevitable question as to why the disclosures do not show or explain expenses. On the other hand, another company with $90 million in sales and only $10 million expenses will have an $80 million profit with no requirement to disclose its tax information. It is this illogical outcome which would compel Australian private companies (and other affected taxpayers for that matter) to restructure their affairs to avoid the purview of the publication laws.

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[4] http://www.smh.com.au/business/the-economy/atos-chris-jordan-says-tax-disclosure-laws-not-intended-for-private-companies-20150319-1m2r46.html

The Hon. David Bushby in debate on the 2010 Taxpayer Confidentiality Bill referred to above, cited the Universal Declaration of Human Rights: *"No one shall be subject to arbitrary interference with his privacy, family, home or correspondence, nor attacks upon his honour and reputation."* Many successful private Australian family companies who now find themselves exposed to the publication of their tax affairs, without explanation or context, feel they are subject to such attacks only because they happen to have adopted a company structure and worked hard to be successful and contribute extensively to the Australian economy and revenue, in the process.

5. Privacy and personal safety concerns of shareholders of private companies

The publicly available ASIC records allow individuals shareholders or families behind private Australian companies to be identified. Private companies represent these individual shareholders or family groups and often the activities of the company reflect the activities of a family or group of individuals.

In the absence of a thorough understanding of Australian income tax, the disclosure of gross turnover and taxable income of a private company may incorrectly be interpreted as that of the individual shareholders or family group which it represents. In this sense, the privacy of such individuals is compromised and they would be exposed to not only media scrutiny, but such tax disclosures and media attention may adversely affect their relationships outside the family.

The consequence is that the individual shareholders and family groups of these private companies will likely be burdened by the public disclosure of their company's turnover and tax information. It would certainly be beyond public policy and public interest for such the tax disclosure laws to have such a reach.

The identification of those individuals in connection with successful business interests also exposes those persons to risks to their safety. Whilst this is not necessarily widespread in Australia today, there is a real and legitimate fear this may change, particularly for family members travelling overseas where such risks are more common.

Conclusion

The Institute believes that the Australian tax system should encourage Australian private companies to invest and develop their businesses rather than distract or impede the use of resources.

The Institute fully supports the Bill and believes that it should be enacted so as to protect Australian private companies from being burdened with the adverse consequences of public reporting of its turnover and tax information.

By removing these burdens, large Australian private companies can focus on developing and investing their businesses which will not only improve the Australian economy but also the Australian community.