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Mr Tim Bryant
Secretary
Senate Economics Committee
Parliament House
Canberra ACT 2600

Via e-mail: economics.sen@aph.gov.au

18 June 2012

Dear Mr Bryant

**Tax Laws Amendment (Cross Border Transfer Pricing) Bill (No. 1) 2012**

GE welcomes the opportunity to make submissions on the Tax Laws Amendment (Cross Border Transfer Pricing) Bill (No. 1) 2012 (the CBTP Bill), which, if enacted will insert Subdivision 815-A into tax law and effectively provide the Commissioner of Taxation (Commissioner) with a new, unjustified, retrospective, taxing power.

Having made a significant investment in Australia, employing over five thousand people across numerous industries and being one of many taxpayers affected, GE is strongly opposed to the CBTP Bill and is concerned that the Government has misrepresented and understated the implications and purpose of Subdivision 815-A.

To assist with its examination, GE would like to bring to the attention of the Senate Economics Committee (Committee) the following features of the CBTP Bill:

- Retrospective operation of Subdivision 815-A is unjustified;
- Subdivision 815-A is designed to impose retrospective taxation;
- Subdivision 815-A discriminates against Australia's major trading partners and does not apply to tax havens; and
- Subdivision 815-A is inconsistent with Australia's agreement with the United States under our tax treaty.

These issues are considered in more detail under the headings below.

**Retrospective operation of Subdivision 815-A is unjustified**

The Explanatory Memorandum to the CBTP Bill (CBTP EM) purports to justify the retrospective application of Subdivision 815-A on the basis that this "is consistent with Parliament's view that treaties provided a separate basis for making transfer pricing adjustments" and that there is "a real possibility" that the law already applies this way.

However, as evident from extensive and detailed submissions by the tax profession, industry bodies and other taxpayers in relation to the Consultation Paper and the Exposure Draft legislation leading up to the introduction of the CBTP Bill, there is very little foundation for this stated position.
Read in isolation, the CBTP EM appears to provide a comprehensive and compelling case for 1 July 2004 start date for Subdivision 815-A. However, when the true context is understood, it becomes clear that the arguments outlined in the EM are superficial and indeed are misleading by omission. Although a detailed analysis and rebuttal of the claims in the CBTP EM is beyond the scope of this submission, GE would like to bring the following to the attention of the Committee:

*Claim 1 – "Parliament's understanding"*

- Treating Australia's tax treaties as providing a separate basis for taxation marks a significant departure from international practice. GE's advisers have explained to us that none of Australia's major trading partners apply tax treaties in this way (e.g. Canada, China, Finland, France, Germany, Ireland, Italy, Japan, Netherlands, New Zealand, Sweden, the United Kingdom and the US).

- If Parliament had indeed assumed, intended or understood (the CBTP EM is inconsistent in its description of Parliament's position) that the operation of Australia's tax treaties depart from international practice, this would surely be noted in EMs to Australia's tax treaties – which is not the case.

  In fact, contrary to the position in the CBTP EM, EMs to Australia's tax treaties confirm that Parliament has assumed for a long time (and on each occasion when a tax treaty has been enacted into tax law) that Australia's tax treaties merely allocate taxing rights and do not provide a separate basis for taxation. The CBTP EM fails to address this point. For example, the EM to the 2003 tax treaty with the UK specifically provides:

  > *"What is the purpose of Australia's tax treaties?.... generally preserving the application of domestic law rules that are designed to address transfer pricing and other international avoidance practices ..."*

- The OECD transfer pricing country report for Australia (updated by the Commonwealth Treasury) dated November 2006[1] refers, in explaining Australia's transfer pricing rules, solely to Division 13 and makes no reference at all tax treaties as a basis for making transfer pricing adjustments. This commentary was updated as recently as 1 January 2012 and continues to refer solely to Australia's domestic transfer pricing rules[2]. In our view, it is impossible to reconcile the Government's consistent representations to the international community through the OECD (that its sole basis for making transfer pricing adjustments is Division 13) with the claims in the CBTP EM that it has always "assumed" that it could also make transfer pricing adjustments under Australia's tax treaties.

*Claim 2 - "Current law"*

- As highlighted by other submissions and journal articles on point, there is little basis for the position that Australia's "treaty transfer pricing rules apply alternatively to Division 13". GE and its tax advisors strongly disagree with this position and its purported rationale.

- The mere fact that the Commissioner has set out his view that tax treaties may be used in a way which imposes tax in tax rulings and speeches does not mean that this is correct or represents the law.

  A public ruling is merely an expression of the Commissioner's opinion about how a particular provision applies or may apply[3]. There are many examples where the Commissioner's longstanding views in a public ruling have been found to be incorrect by a court.

- In addition, it must be noted that the Commissioner has publicly acknowledged that his position that tax treaties could be used to make transfer pricing adjustments is uncertain. For example, in a speech given to The Tax Institute's Victorian State Convention in 2008, Jim Killaly, Deputy Commissioner states:

  > *"The constitutional and legislative standing of the Associated Enterprises Articles in Australia's treaties is not free from doubt and it seems clear that the debate around this issue could possibly continue until finally determined by the Courts. For its part the Tax Office will continue to reflect on the issue."* (emphasis added)

  More recently before the Senate Economics Legislation Committee Estimates on 30 May 2012[4], the Commissioner acknowledged that this remains "an open question".

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[1] http://www.oecd.org/dataoecd/1/6/44071214.pdf

[2] Refer OECD MULTI-COUNTRY ANALYSIS OF EXISTING TRANSFER PRICING SIMPLIFICATION MEASURES dated 10 June 2011. Available http://www.oecd.org/dataoecd/55/41/48131481.pdf

[3] TR 2006/10 (Public Rulings)

[4] Hansard at page 89 Also refer to *"In the best interests of Australia"*, Opening Speech by the Commissioner, Michael D'Ascenzo , Corporate Tax Association Convention, Melbourne, 15 June 2009

In light of the above, GE submit that there is no justification for the retrospective operation of Subdivision 815-A and that the true purpose of the CBTP Bill is to blatantly convert the Commissioner's previously expressed view (which is incorrect, or contentious at best) into law. This goes against the very spirit of the rule of law, the tax self-assessment regime and general trust in the administration of taxation in Australia.

### Subdivision 815-A is designed to impose retrospective taxation

The Government has refused to be transparent about the tax revenue at stake, claiming that there is no revenue impact as this is merely "a revenue protection measure".

However, subsequent to the release of the CBTP Bill, Mr Tony McDonald (General Manager, International Tax Treaties Division, The Treasury) appearing before the Senate Economics Legislation Committee on 30 May 2012, explained that the income tax at stake was in the billions[5]. A few days later at the Large Business Advisory Group (LBAG) in Canberra on 1 June 2102, Mr Mark Konza (Deputy Commissioner, Large Business & International) explained that Subdivision 815-A could affect 40 current tax audits and preserve $1.9 billion of taxes.

In summary, it is clear that Subdivision 815-A is designed to impose retrospective taxation targeted at open tax disputes.

### Subdivision 815-A discriminates against Australia's major trading partners and does not apply to tax havens

There is no dispute that subdivision 815-A will only apply to transactions with countries with which Australia has a tax treaty – essentially Australia's major trading partners, such as the United States.

Given that Subdivision 815-A will broaden the Commissioner's power to issue transfer pricing adjustments and will result in additional tax liabilities in the billions for affected taxpayers; it seems anomalous that dealings with countries that Australia does not have a tax treaty (eg Hong Kong and most countries considered to be "tax havens") will obtain preferential tax treatment.

This preferential treatment of tax havens is inconsistent with Australia being the Chair of the OECD Global Forum on Transparency and Exchange of Information for Tax Purposes – as Australia should be seen as discouraging (rather than encouraging) the use of tax havens for tax planning.

Although this anomalous result could possibly attract the operation of the non-discrimination articles in Australia's tax treaties, including Article 23 of the tax treaty with the United States, Treasury has failed to address this issue.

### Subdivision 815-A is inconsistent with Australia's obligations under the US tax treaty

Article 1(2) of the United States tax treaty provides that the treaty may not increase tax above the liability that would result under domestic law. Where domestic law provides a more favourable treatment than the treaty, the taxpayer may apply the provisions of domestic law.[6]

However, Subdivision 815-A creates a new domestic taxing provision designed to circumvent the clear spirit of the agreement between the Governments of Australian and the United States. Treasury has failed to address this issue.

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[5] Hansard at pages 88 and 89.

[6] Refer US Department of the Treasury Technical Explanation to the 1982 Australia-US tax treaty, available from the IRS website (http://www.irs.gov/businesses/international/article/0,,id=169499,00.html)

**Conclusion and recommendation**

GE kindly submits that the Committee should not support the CBTP Bill. Specifically, **the Committee should not support the retrospective operation of Subdivision 815-A from 1 July 2004** on the basis that this will result in:

- Significant, unjustified, retrospective taxation which is inconsistent with the rule of law, the tax self-assessment regime and the responsible administration of taxation in Australia;
- Discrimination against Australia's tax treaty partners;
- Promotion of tax havens; and
- A breach of by Australia of an international agreement with the United States Government.

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We are extremely keen to appear as a witness before the Committee to elaborate further on our submission.

If you have any questions or wish to contact us regarding the making of a presentation, please do not hesitate to contact me or Ardele Blignault, Vice President Government Relations or Amanda Leckie, Tax Manager . We will respond to any email within 24 hours.

We look forward to hearing from you regarding the details for appearing before the Senate Economics Committee.

Yours sincerely

Chris Vanderkley
Tax Director

Copies to:

- Steve Sargent - President & CEO, GE Australia and New Zealand