Question: aet 42

Topic: **Transfer Pricing**

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Senator JOYCE asked:

Senator JOYCE—Can you get back to me and explain how you are going to get transparency from foreign entities on transfer pricing of products from Australian entities overseas, because having worked for one I know you cannot do that?

Mr Murphy—There are rules on transfer pricing.

Senator JOYCE—Take it on notice.

Answer:

Australia applies transfer pricing rules to prevent profit shifting between associated companies located in different tax jurisdictions. Profit shifting can occur through manipulating the prices of goods or services transferred between associated companies, for example by reducing the price of goods sold to, or increasing the price of goods sold by a company located in a tax haven country. Australia’s transfer pricing rules ensure that taxable Australian profits are commensurate with the economic value added in Australia.

In order to ensure that profits are not deliberately manipulated, OECD countries have settled on a common set of rules to govern the setting of a “transfer price”, the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations. The object of these rules is to ensure that the price set between related companies in OECD member countries reflects the price which would have been paid between two unrelated entities, each seeking to maximise their own profitability. This price is commonly referred to as an “arm’s length price”; that is, the price that would have been set had the parties been dealing at arm’s length and is the basis for the transfer pricing rules in Australia's domestic tax legislation and its double tax treaties.

In practice, enforcing the transfer pricing rules requires a detailed comparison of the respective functions performed, assets used and risks assumed by the various related parties in contributing to the overall profits of the group. Australia’s transfer pricing rules are strictly enforced and transfer pricing audits are undertaken.

Australia’s tax treaties also help to ensure the transparency of multinational entities. All of Australia’s tax treaties contain provisions that enable tax authorities to exchange information on taxpayers for the purposes of preventing tax evasion and some of Australia's tax treaties contain further provisions that facilitate the cross-border collection of tax debts. Furthermore, the *International Tax Agreements Act 1953* facilitates the exchange of information in tax matters between Australia and tax havens under taxation information exchange agreements (TIEAs). The negotiation of TIEAs between Australia and tax havens are an important part of the Government's efforts in fighting cross-border tax evasion. To date, Australia has signed TIEAs with Bermuda, Antigua and Barbuda and the Netherlands Antilles.

In addition, the thin capitalisation regime ensures that multinational entities do not allocate an excessive amount of debt to their Australian operations to minimise their Australian tax, while Australia's rules regarding foreign source income ensure that Australian residents cannot accumulate income offshore and thereby defer, or even avoid, Australian tax.