AN ALERT FROM THE BDO INTERNATIONAL TAX PRACTICE

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INTERNATIONAL TAXATION

▶SUBJECT

EXPOSURE DRAFT LAW INTRODUCING NEW AUSTRALIAN TRANSFER PRICING RULES WITH SIGNIFICANT SELF-ASSESSMENT AND DOCUMENTATION REQUIREMENTS

▶INTRODUCTION

On November 22, 2012, the Australian Government released for consultation an exposure draft law of proposed amendments to reform Australia's transfer pricing rules. The proposed amendments will modernize Australia's transfer pricing regime, aligning Australia's domestic law with international best practice and improving the integrity and efficiency of the Australian tax system. The reforms will ensure that Australia's domestic laws better align with the internationally consistent transfer pricing approaches set forth by the Organization for Economic Cooperation and Development Guidelines ("the OECD Guidelines").

▶AFFECTING

Taxpayers residing in Australia involved in cross-border transaction(s), or businesses outside of Australia that engage in intercompany transaction(s) with a counter party located in Australia.

▶EFFECTIVE DATE

The exposure draft of the proposed amendments to Australia's transfer pricing rules was released for public commentary on November 22, 2012. Submissions on the exposure draft legislation closed on December 20, 2012. The legislation is proposed to come into effect once passed by Parliament.

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KEY IMPLICATIONS OF PROPOSED AMENDMENTS

The transfer pricing requirements have been brought effectively into the self-assessment regime. Entities are required to ensure that taxable income reported on the income tax return reflects arm's-length conditions in relation to international dealings. There are de minimis rules in relation to penalties, however these only allow for a shortfall of 1% of tax payable (or AUD 10,000 if greater).

Taxpayers will now be required to keep specified documentation to support their transfer pricing if they wish to argue that they have a Reasonably Arguable Position ("RAP"). The documentation must explain the way in which the new rules have been applied, and why the application best achieves consistency with the OECD Guidelines. A failure to keep documentation that meets the requirements in the draft legislation will mean the taxpayer will not have a RAP for penalty protection.

The new rules focus on profits and conditions, rather than transactions, which arguably strengthens the Australian Government's ability to apply transfer pricing rules to review the commerciality of taxpayers' arrangements. The Australian Government is expected to use the provision to scrutinize the international dealings of taxpayers that have:

- Business restructures, particularly where they involve the shift of profit-making functions offshore;
- Aggressive financing arrangements; and
- Poor profitability.

Positive implications of the draft law include (i) an eight-year limitation to the period in which an amended assessment can be made (compared to the current unlimited amendment period) and (ii) for permanent establishments, the attribution of income and expenses of the entity between its parts is reflective of an allocation that may be expected had the parts of the entity been separate entities transacting independently with each other; although the latter does not signal a change in the law, it supports the view that allocating expenditures and income is not inconsistent with a separate entity approach.

A full version of the exposure draft of the "Tax Laws Amendment (Cross-Border Transfer Pricing) Bill 2013: Modernisation of Transfer Pricing Rules" can be accessed at:

http://www.treasury.gov.au/~/media/Treasury/Consultations%20and%20Reviews/2012/Modernisation%20of%20transfer%20pricing%20rules/Key%20Documents/PDF/TPR_Exposure_Draft.ashx