

# Diverted Profits Tax

**Can you afford a forty percent tax on your profits?**

August 2018



Almost a year after the introduction of the Diverted Profits Tax (DPT) Bill into Parliament, the ATO has now released draft guidance to assist organisations in assessing their level of risk under the DPT.

The DPT is a new tax, aimed at arrangements that divert profits from Australia to a country where the effective tax rate is less than 24 percent and there is insufficient economic substance to justify those profits. A DPT liability is assessed at 40 percent of the diverted profits and is payable up-front.

The Government has stated that approximately 1,470 taxpayers are in scope of the DPT, with 130 estimated to be in the “high risk” category.

Once the ATO issues an assessment, the taxpayer has twelve months to provide information to the ATO to establish that the assessment is excessive. The matter will be referred to the General Anti-Avoidance Review (GAAR) Panel. The taxpayer cannot ‘object’ to the assessment, rather it must appeal to the Federal Court.

The ATO guidance provides ‘high risk’ and ‘low risk’ examples in indicative areas of focus, including the:

- migration of intellectual property (IP) by a pharmaceutical company to a low tax jurisdiction: where evidence indicates the Australian company continues to undertake manufacturing, commercialisation and functions to maintain, protect and exploit the IP;
- limited risk distributors (LRD): where, notwithstanding the contractual arrangements, evidence shows the Australian LRD is really a full risk distributor; and
- use of ‘marketing hubs’: this focuses on excessive profits allocated to the hub relative to functions undertaken.

## Questions to consider

- Is your organisation a significant global entity (SGE), being a member of a group with annual global income of AU\$1 billion or more?
- Have you assessed your DPT position and risk? How confident are you that DPT should not apply to your current or proposed arrangements?
- Can your organisation substantiate sufficient economic substance throughout your entire supply chain, by reference to Australian transfer pricing requirements?
- Has sufficient foreign tax (effectively over a 24 percent rate) been paid or imposed in all jurisdictions directly or indirectly relevant to the supply chain into Australia?
- Have you migrated ‘mobile’ IP rights (e.g. patents) to a low-taxed jurisdiction?
- How much profit is allocated to marketing or procurement hubs relative to the functions undertaken by those hubs?
- Can you demonstrate that the principal purpose of entering into a relevant arrangement was not to obtain a tax benefit?
- If you were to appeal to the Federal Court in relation to a DPT assessment, are you aware of the restrictions on what evidence might be admissible?

## How KPMG can help

KPMG has unique insights into the application of the DPT and the professional judgment to help SGEs in assessing their DPT risk levels for both current and future transactions. Our team includes dispute resolution specialists to assist taxpayers to appropriately evidence their position both before and after a DPT assessment issues, engage with the ATO and most effectively navigate the GAAR panel processes.

KPMG can help you develop a DPT Risk Management Roadmap, including undertaking:

- Review of the facts to fully understand the supply chains and intra-group flows that impact Australia and conduct further fact-gathering call/interviews where appropriate with key personnel;
- Identification of transaction streams (a) which are highest-risk and appropriate for focus and (b) which can be classed as low-risk with no further action;
- For highest-risk streams, assessment of whether the level of substance of entities in the scheme is sufficient to justify profits allocated, having regard to Australian transfer pricing principles;
- Documentation of review outcomes and provision of recommendations or next steps; and
- Approaching the ATO for a “comfort letter”, or remediating steps such as enhancing substance or restructuring.

# Contacts

## Liam Delahunty

### Director, International Tax

T: +61 2 9335 7648

E: [ldelahunty@kpmg.com.au](mailto:ldelahunty@kpmg.com.au)

## Kelly Chong

### Director, Tax Advisory Services

T: +61 2 9335 8404

E: [kellychong@kpmg.com.au](mailto:kellychong@kpmg.com.au)

**KPMG.com.au**

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August 2018. VIC N16640LOBS