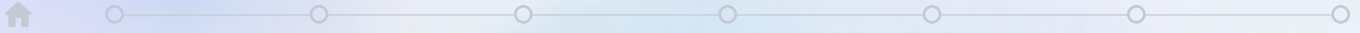


TAX DEVELOPMENTS IN LIFE SCIENCES

Navigating with Agility





INTRODUCTION



KELLY CHONG,
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In today's rapidly changing world, life sciences organisations need to be agile and proactively prepared to respond to the demands, needs and expectations of their stakeholders.

We are witnessing an increased focus on social and economic responsibility, demand for greater transparency and a myriad of complex compliance rules and regulations to navigate – both locally and globally. In this series, we take a closer look at recent developments impacting organisations in the life sciences sector – from utilising incentives to develop and hold intellectual property in Australia, to ensuring that your organisation is prepared to engage with the taxation authorities which are resuming rollout of their audit and review programs.

In addition, we consider the impact of new reporting requirements, namely the Payment Times Reporting Scheme, which aims to increase transparency over how large businesses deal with small business suppliers.

We also consider how customs duty and trade planning can be considered together when identifying cost-saving opportunities and managing trade compliance risks associated with supply chains and global trade operations.

Finally, we share how, in an unprecedented move, a globally co-ordinated approach to minimising profit shifting to low-tax jurisdictions will reshape the future of global taxation for large multinationals.

We hope you find this publication insightful in navigating new regulations, frameworks and legislation. Please reach out to the contacts listed throughout this report if you would like further information.



Should you hold intellectual property and other intangible assets in Australia?

The Australian government announced a number of proposed measures as part of the 2021-22 Federal Budget to improve the attractiveness of Australia as a location for R&D activities and to hold and develop intellectual property (IP) and other intangible assets. These measures are:

- A patent box tax regime to apply for income years commencing on or after 1 July 2022 for patented inventions in the medical and biotechnology sectors, but only in respect of eligible granted patents which were applied for after 11 May 2021 (the date of the Budget announcement); and
- The option to self-assess the period over which depreciation deductions may be claimed for eligible intangible depreciating assets acquired on or after 1 July 2023.

THE PATENT BOX TAX REGIME

Under the proposed patent box tax regime, corporate income derived from eligible Australian medical and biotechnology patents will be taxed at a concessional tax rate of 17% (compared to the current 30% corporate tax rate for large businesses and 25% for small to medium businesses). To qualify for the proposed patent box concession, a substantial activity requirement in respect of Australian R&D activities will need to be met.

Treasury released a Discussion Paper in July 2021 and is undertaking consultation and working through the design of the Australian patent box tax regime. In the design of the regime, the government will need to ensure that it accords with OECD guidelines and standards on patent boxes. At this time, no draft legislation has been released by the government.

ACCELERATED DEDUCTIONS FOR IP ASSETS

Under the current uniform capital allowances rules, depreciation deductions for eligible intangible depreciating assets are calculated based on prescribed statutory effective lives, which is 20 years for a standard patent, 8 years for an innovation patent and 6 years for a petty patent. The proposed changes will enable a taxpayer to self-assess the effective life of intangible depreciating assets, with the potential to accelerate the depreciation claims for IP. This will be particularly important for Australian businesses that have acquired significant IP assets through transactions and have substantial tax cost base in patents and other IP assets.

WHAT ACTION SHOULD MY ORGANISATION TAKE NOW?

Together, these two measures significantly improve the tax competitiveness of Australia as a jurisdiction to develop, hold and commercialise IP for the medical and biotechnology sectors.

Your organisation should:

- Review the group's IP investment and holding strategy and location of R&D activities, and assess potential eligibility for the patent box tax regime.
- Ensure processes are in place to capture information required to implement the proposed tax incentives.
- Monitor developments and participate in consultation on the development of the new rules.
- Be mindful of the ATO's framework in assessing the tax risk associated with intangibles arrangements.



— HOW CAN KPMG HELP?

We can assist companies:

- + Model the potential benefits of IP development and ownership in Australia under the proposed new patent box rules (and assess the benefits of the Australian regime to compare to regimes in other jurisdictions).
- + Assess eligibility for the patent box tax regime and potential accelerated depreciation claims for intangible assets.
- + Assess whether any proposed changes to the group's IP investment and holding strategy aligns with existing and proposed location of DEMPE functions (see section of this report *"Are you ready for the ATO to review your intangibles arrangements"*).
- + Manage revenue authority engagement, as any change to the IP investment and holding strategy of the group will likely impact a number of jurisdictions.
- + Facilitate participation in consultation with Government.

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Are you ready for the ATO to review your intangibles arrangements?

With investment in intangible assets surpassing investment in tangible assets across developed economies, intangible assets have become the key driver of value, innovation and growth for many companies.

The Australian Taxation Office (ATO), cognisant of this trend, has provided a framework to assist taxpayers in assessing their level of risk, with the release of its draft practical guideline associated with intangibles arrangements.

Taxpayers in the life sciences sector need to be proactive and prepared for ATO engagement, particularly given the importance of intangibles and associated cross border transactions between related parties such as patent licensing, clinical trials and research and development activities in this sector.

WHAT ACTION IS REQUIRED BY MY ORGANISATION?

Taxpayers will be asked by the ATO for a self-assessed risk rating, with the final risk rating then determining the level of ATO attention, with arrangements exhibiting high risk factors likely to attract an ATO review/audit.

Under the draft PCG, taxpayers first need to make a subjective and qualitative risk assessment of their arrangement against four key risk factors (set out further below). The 'High', 'Medium' or 'Low' risk ratings against each of these four factors will need to be determined by assessing whether existing documentation and evidence satisfies the ATO's exhaustive list of Documentation and Evidence Expectations, which are set out in the draft PCG. This PCG is yet another reminder of the importance of evidence for taxpayers to discharge their onus.

The fifth and final risk factor involves comparing the tested intangible arrangement to existing 'High', 'Medium' and 'Low' risk scenarios (set out below) which will be added to as and when the ATO become aware of new examples.

While the key focus is on the transfer pricing provisions, the draft PCG also covers other tax risks associated with intangibles arrangements, including withholding tax, capital gains tax and various anti-avoidance taxes, particularly where arrangements lack evidence of commercial rationale and/or substance.

Being prepared and undertaking a preliminary review of your key intangible arrangements to determine whether the level of documentation and evidence readily available is in line with the ATO's expectations is key. This should assist in gauging the initial risk rating of your intangibles arrangements and help identify gaps which require further action. Actions may include additional work to bolster existing documentation and evidence, revisiting the arrangements or developing strategies on mitigating risk, including proactive engagement with the ATO.



Risk assessment framework

ATO RISK FOCUS AREA	EXAMPLES OF EVIDENCE EXPECTED	EXAMPLE RATING
A Understanding and evidencing the commercial considerations and your decision making	<ul style="list-style-type: none"> Internal or independent reviews, cost-benefit analyses, forecasts, projections, modelling. Internal or external advice disclosing anticipated or potential Australian tax effects. Presentations, papers and minutes related to meetings around commercial objectives and consideration of intangible arrangements. Commercial, regulatory and tax advice obtained in connection to intangible arrangement. 	<div style="text-align: center;"> <div style="background-color: #ccc; padding: 2px; margin-bottom: 2px;">HIGH</div> <div style="background-color: #0070c0; color: white; padding: 2px; margin-bottom: 2px;">MED</div> <div style="background-color: #ccc; padding: 2px;">LOW</div> </div>
B Understanding the form of your Intangibles Arrangements	<ul style="list-style-type: none"> Legal agreements (asset purchase/sale, licensing / R&D agreements). Details of planning in connection with setting up legal arrangements. Transfer pricing documentation including any specific or supplementary analysis or valuation and/or other reports produced for transactions which form part of your Intangibles Arrangements. 	<div style="text-align: center;"> <div style="background-color: #ccc; padding: 2px; margin-bottom: 2px;">HIGH</div> <div style="background-color: #ccc; padding: 2px; margin-bottom: 2px;">MED</div> <div style="background-color: #00a651; color: white; padding: 2px;">LOW</div> </div>
C Identifying and evidencing the intangible assets and connected DEMPE activities of your Intangibles Arrangements	<ul style="list-style-type: none"> Intangible asset registers and registration documents. Organisational charts, roles and responsibilities of individuals involved in DEMPE activities. Correspondence (e.g. reports, approvals, authorisations and meeting minutes) of persons identified as involved in DEMPE activities. Contemporaneous valuation reports, working papers and associated documentation where intangible assets and relevant functions have been transferred offshore. 	<div style="text-align: center;"> <div style="background-color: #ccc; padding: 2px; margin-bottom: 2px;">HIGH</div> <div style="background-color: #0070c0; color: white; padding: 2px; margin-bottom: 2px;">MED</div> <div style="background-color: #ccc; padding: 2px;">LOW</div> </div>
D Analysing the tax and profit outcomes of your Intangibles Arrangements	<ul style="list-style-type: none"> Financial modelling or projections of anticipated tax impacts prepared internally or by external advisors. Analyses, data and briefing materials underlying any valuations or other connected advice obtained from internal or independent specialists. tax information for relevant domestic and offshore entities including foreign income tax returns, foreign notices of assessment, foreign tax receipts and notices of refund, foreign tax instalment notices and running balance accounts. Any advice or valuations obtained in relation to the potential tax consequences of proposed structures or transactions (including any approvals of tax holidays or other reductions in tax and relevant correspondence from foreign revenue agencies). 	<div style="text-align: center;"> <div style="background-color: #800080; color: white; padding: 2px; margin-bottom: 2px;">HIGH</div> <div style="background-color: #ccc; padding: 2px; margin-bottom: 2px;">MED</div> <div style="background-color: #ccc; padding: 2px;">LOW</div> </div>
E Understanding the type of example arrangements we consider to be high, medium or low risk	<ul style="list-style-type: none"> Example 1 – centralisation of intangible assets Example 2 – bifurcation of intangible assets Example 3 – non-recognition of Australian intangible assets and DEMPE activities Example 4 – migration of pre-commercialised intangible assets Example 5 – non-arm's length licence arrangements 	<div style="text-align: center;"> <div style="background-color: #800080; color: white; padding: 2px;">HIGH</div> </div>
	<ul style="list-style-type: none"> Example 6 – centralisation of intangible assets Example 7 – transfer of rights to intangible assets via a Licence Agreement Example 8 – contract research and development arrangement Example 9 – cost contribution arrangement 	<div style="text-align: center;"> <div style="background-color: #0070c0; color: white; padding: 2px;">MED</div> </div>
	<ul style="list-style-type: none"> Example 10 – centralisation of intangible assets Example 11 – contract research and development arrangement Example 12 – cost contribution arrangement 	<div style="text-align: center;"> <div style="background-color: #00a651; color: white; padding: 2px;">LOW</div> </div>



HOW CAN KPMG HELP?

- + If the draft PCG is finalised in its current form, taxpayers will face a significant compliance burden in gathering and preparing the required documents, evidence and analysis to apply the risk assessment framework.
- + This requires a KPMG multi-disciplinary perspective as the draft PCG crosses over transfer pricing, anti-avoidance and unique documentary and evidentiary requirements, including our KPMG transfer pricing specialists, international tax team and KPMG Law Tax Dispute Resolution & Controversy.
- + Together these teams can navigate clients through the complexities of the draft PCG, using our deep expertise in documenting and analysing cross border intangibles arrangements, and bringing our skills in evidence gathering and assisting taxpayers with strategies to proactively manage ATO engagement.
- + As organisations examine their intangible asset arrangements in light of the incentives proposed by the Australian government (see section of this report *"Should you hold intellectual property and other intangible assets in Australia"*), now is also a good time to consider whether their arrangements are tax compliant with the ATO's expectations (see section of this report *"Are you ready for the ATO to assess your tax governance?"*).

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Effective tax governance in life sciences

Are you ready for the ATO to assess your tax governance?

Tax authorities continue to expand their reach beyond their traditional role of collecting taxes and monitoring compliance with tax law.

There is a growing appetite for more transparency, and an increasing burden on large corporations, multinationals and tax authorities to disclose tax-related data and on taxpayers in general to demonstrate effective tax governance. The life sciences sector is not immune to this.

In Australia, the Australian Tax Office (ATO) continues to focus on the pharmaceutical industry due to its strategic significance to the Australian economy and tax base, with review of areas including tax performance and transfer pricing practices.

In late 2020, the ATO's Streamlined Assurance Review (SAR) program (which focused on Income Tax) was replaced by the Combined Assurance Review (CAR) program (covering both Income Tax and Goods and Services Tax) for top 1,000 organisations. The CAR program continues to encourage taxpayers to describe and evidence the effectiveness of their tax control framework.

The Top 1,000 Next Actions Program has also commenced for a selected group of taxpayers based on outcomes from their previous assurance review. These programs are part of the ATO's compliance activities, using its 'Justified Trust' methodology.

ALREADY BEEN THROUGH THE SAR?

The key for organisations who went through an earlier SAR is to demonstrate progress since the previous assurance review. This could mean addressing previous gaps identified, such as the development of documented procedures for key tax processes or undertaking design and operating effectiveness testing in accordance with a multi-year tax control test plan. The ATO's expectations on tax governance are increasing, so it is important that organisations continue their tax governance journey.



WHAT SHOULD I FOCUS ON?

For the life sciences sector, a number of whom operate in Australia as inbound groups and may not have an active board in Australia, it is important to clearly define and document the delegated oversight role to address the ATO's expectations on Board level controls.

For groups that have the baseline elements in place, they should also consider enhancing governance on tax areas that often attract ATO's attention such as transfer pricing and fixed assets.

We encourage taxpayers to take appropriate action as early as possible to prepare for review. If the ATO is not satisfied with the level of governance, this not only affects your ability to achieve an overall high assurance rating, it also increases the likelihood that the ATO will contact you again, resulting in higher compliance costs.

HOW DO I KNOW IF MY ORGANISATION IS PREPARED?

- Have you addressed the gaps from your first top 1,000 review to demonstrate improvements to the ATO in the next review?
- Do you have sufficient evidence to demonstrate to the ATO that your tax control framework is designed effectively covering income tax and GST?
- Do you have a documented commitment to testing and multi-year tax control test plan documenting your periodic testing program?
- Have you undertaken independent testing to demonstrate the tax control framework is operating in practice?
- Do you have procedures in place for the monitoring of transfer pricing policy implementation? (see section of this report *"Are you ready for the ATO to review your intangibles arrangements"*).
- Do you have procedures in place to manage the taxation risks surrounding tax fixed asset values?

If the answer to any of these questions is 'No' or 'Unsure', then consider: Are you ready to be assessed? Do you want to be selected for *Top 1,000 Next Actions Program*?

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HOW KPMG CAN HELP

- + KPMG has a dedicated tax governance team with extensive experience supporting both Top 100 and Top 1000 clients. Depending on your governance maturity level, we can assist in a range of activities, including assistance in submission of Combined Assurance Reviews, undertaking a Gap Analysis, development of your Tax Governance Framework, procedural documentation for key tax obligations and a multi-year testing plan. We also assist with testing of design and operating effectiveness of your tax control framework.
- + With our input, we are certain that we can provide a tailored approach to support you in your tax governance journey, designed to be cost effective, practical and fit for purpose.



Tax Controversy in life sciences

BE PREPARED TO RESPOND TO TAX OFFICE INFORMATION REQUESTS AND REVIEWS

The Australian Taxation Office (ATO) is resuming the rollout of its various audit and review programs, particularly for those matters that were put on hold in 2020 and 2021 due to COVID-19.

Taxpayers in the life sciences sector need to be proactive and prepared for further ATO engagement, arising from programs such as the Combined Assurance Reviews, Streamlined Assurance Reviews and the Next Action Reviews.

ATO reviews are broad ranging, covering all aspects of your income and indirect tax profile and affairs.

WHAT SHOULD I FOCUS ON?

For the life sciences sector, some of the current key focus areas that the ATO focus within these reviews include:

- Tax Corporate Governance (see section of this report *“Are you ready for the ATO to assess your tax governance?”*).
- Transfer Pricing, including related party debt funding, whether Australia is appropriately remunerated for the functions, assets and risks in Australia, intangibles (see section of this report *“Are you ready for the ATO to assess your tax governance?”*).
- Whether there is sufficient evidence to support Research and Development Tax Incentive claims.
- Significant transactions and restructures.
- Anti-avoidance and integrity issues arising from large restructures and transactions (inbound and outbound).

These reviews are the stage at which most tax ‘disputes’ commence, where the ATO will require large volumes of information, concerning complex historical tax and commercial matters relevant to your business. Importantly, the expectation is that taxpayers will have the evidence available to support the tax positions taken.

Being prepared and having experienced advisors to assist you to respond to these reviews (before they progress to an ATO Audit) is more important than ever. This is because, your responses to these reviews will play a significant role in determining what the ATO’s ‘risk hypothesis’ of your business will be.



ARE YOU READY FOR AN ATO REVIEW?

01.

Have you considered the advantages of proactively approaching the ATO to manage a tax risk?

02.

Do you have access to sufficient documents and/or oral evidence throughout the period under review or audit? Contemporaneous evidence is key.

03.

Have you considered the extent to which a tax risk will be required to be disclosed to the ATO in a streamlined assurance review or combined assurance review?

04.

Are relevant witnesses/personnel with knowledge available and willing to assist? Do you have all the documents readily available to provide to the ATO in a short timeframe during the ATO review?

05.

Have you obtained relevant tax technical advice and do you have a Reasonably Arguable Position (RAP) to mitigate penalties?

06.

Will you be able to respond within tight deadlines on request for information ensure audit readiness and the use of technology.

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HOW CAN KPMG HELP?

- + KPMG Law and the Tax Disputes & Controversy group have proven experience in assisting Australia's largest taxpayers to respond to significant and complex ATO Reviews and Audits.
- + Our approach focuses on providing reliable, commercial, and practical strategies to respond to ATO reviews, backed by our experience as expert tax controversy lawyers. We can assist you to mitigate risk, efficiently resolve disputes, engage effectively with the ATO and improve your position for any future disputes and tax risk.
- + It is never too early to consider engaging an experienced advisor to assist you to understand the types of issues that are likely to arise in an ATO review and to prepare to respond. Preparing early will save you time, cost and reduce risk for when the ATO do issue their first requests for information.



Payment Times Reporting Scheme

Time to refine before the next reporting deadline

As a key part of the Federal Government's commitment to improving cash flow and liquidity for small businesses, the Payment Times Reporting Scheme (**PTRS**) aims to increase transparency over how large businesses are dealing with small business suppliers and managing payments to them.

Given the public disclosure of data submitted to the Regulator and introduction of financial penalties from 1 January 2022 is it important for entities to have confidence in their approach, data, and metrics. With both compliance and reputational risk at stake – it's important to get this right!

WHAT IS THE PTRS?

From 1 January 2021, large businesses, and certain government entities with income of greater than \$100m are required to report on small business supplier payment terms and practices. Entities assessed as reporting entities will need to report bi-annually (timing based on their income years) and will then have three months at the end of every reporting period to lodge this information with the Regulator.

The first reports for many life science clients will have now been lodged. The data from certain first reports was made publicly available on 30 November 2021. The second report for reporting entities with 30 June and 31 December year-ends is due by 31 March 2021.

LESSONS LEARNED FROM ASSISTING LIFE SCIENCES CLIENTS WITH FIRST REPORTS

1. Input from various parts of the business is required – cross functional input and coordination is key.
2. Identifying and extracting required data, particularly for complex groups with multiple processes is difficult – system, internal controls and process changes are often required to assist in compliance with the PTRS.
3. Processes and procedures may need to be developed and refined to make this ongoing compliance obligation more efficient and increase levels of accuracy.
4. As with any new legislation there are several areas of uncertainty. This has been exacerbated by numerous rounds of updates to the guidance material in recent months. Given the wide-reaching nature of the legislation, we expect further changes to the guidance issued by the Regulator.
5. The impact of the PTRS needs to be considered in the context of acquisition and disposals of entities.

The above lessons need to be addressed as you refine your PTRS process prior to filing subsequent reports.

No matter where you are at on the Payment Times Reporting journey, KPMG can assist and we are happy to flex our approach to support your internal efforts.



HOW CAN KPMG HELP?

- + KPMG's specialist Payment Times Reporting team has assisted a number of life sciences clients navigate the new PTRS requirements and prepare submissions.
- + We can provide advice and guidance to identify which entities are reporting entities.
- + In addition, we have developed an approach which will help you analyse source data, assess it and prepare the information needed for submission.

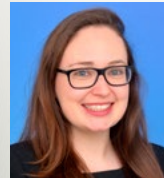
Specifically this can involve:

- + extracting your source data for reporting entities;
- + calculating and analysing your metrics in line with the latest guidance and legislation;
- + accessing insights on an interactive dashboard;
- + viewing metrics throughout the reporting period; and
- + creating detailed CFO & Board ready reporting.

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International trade risk management: Adopting a global approach

There are a number of unique indirect tax challenges for the life sciences sector when it comes to the cross-border movement of goods, which can increase a global organisation's risk of customs duty and GST/VAT leakage.

By design, the highly specialised, regulated and complex nature of this sector often results in illogical global supply chain decisions that "follow the science". The typical lifecycle journey of a drug product from starting materials through to secondary packaged goods can involve multiple national border crossings, which may expose each product-type to a host of indirect taxes and indirect tax compliance obligations.

As the after-shocks of COVID-19 continue, governments around the world are increasingly relying on indirect taxes to support revenue collection and economic growth.

Within this context, global organisations should be aware of the growing emphasis by government authorities on full compliance with their indirect tax obligations. In assessing risk in the supply chain from an indirect tax perspective, customs declarations and the data reported to national authorities can unduly expose an organisation to financial and non-financial risks where commercial documentation and data is not accurate.





WHAT DOES THIS MEAN FOR MY ORGANISATION?

Increasingly, national customs, health and tax authorities have scrutinised and relied upon, customs data to assess reporting obligations and pricing. Whilst the motivating drivers may be distinct – in that customs and tax authorities are focussed on compliance, tax avoidance and revenue collection, whereas health authorities may be focussed on reverse engineering pricing data to support reimbursement and renegotiation discussions – they share in the ability to form decisions based upon an organisation's trade data.

The importance of pricing cannot be ignored when determining a customs value at the time of importation as a value must be declared to customs. Specific customs valuation methods have been agreed within the World Trade Organization to properly determine the value of imported goods, which are globally applied. In most cases, the transaction value is used as the primary method of valuation (price actually paid or payable), with any adjustments required to be properly reported to customs authorities (e.g. transfer pricing adjustments, development costs, royalties). In the case of clinical trials, where there is no sale and goods are provided on a free-of-charge basis, the determination of a customs value can be fraught with risk from a tax and pricing exposure perspective (e.g. cost plus or resale minus).

To support financial and operational success, it is therefore crucial that life science organisations develop and implement robust trade compliance strategies that support the preservation of pricing and tax positions. Customs must be actively managed throughout the business if trade compliance strategies are to work with, not against, an organisation's strategic agenda. Various customs planning methods can be combined to reduce indirect tax liabilities by price unbundling certain non-taxable elements (e.g. buying commissions), whilst national customs policies can be leveraged to explore the art of the possible in reducing customs values (e.g. "first sale for export" or "last sale" in the case of Australia).

Effective management of customs duties and indirect taxes is essential to support growth, reduce costs and effectively manage risk. Without a robust strategy, global entities run the risk of increasing their compliance obligations, exposing their 'costs of goods' and incurring absolute indirect tax costs, which is true even where there is little or no customs duty.



WHAT ACTIONS SHOULD MY ORGANISATION FOCUS ON TO ENSURE WE ARE PREPARED?

- Identify and quantify the customs duties and indirect taxes paid.
- Identify customs supply chain optimisation opportunities.
- Assess whether the benefits of Free Trade Agreements and other customs duty concessions have been fully utilised.
- Map your physical and transactional supply chains for global alignment on key "triggers" for indirect taxes.
- Document clear best-practice strategies and policies around key trade compliance areas (customs valuation, origin, tariff classification).
- Implement a robust and scalable customs valuation strategy to support current and future growth.
- Align internally with key business units that are mutually dependable on business performance (pricing, valuations, supply chain, tax, finance).
- Outsource and co-source compliance and reporting functionalities to focus on high-risk/high reward focus areas.
- Assess the benefit of customs and trade facilitation programs to increase compliance and smooth the physical trade process.

HOW KPMG CAN HELP

KPMG Australia's Trade & Customs (T&C) team assists clients identify cost-saving opportunities and manage trade compliance risks associated with supply chains and global trade operations. Our team is part of a global network of 80 KPMG Trade & Customs team. We work with clients to deliver value and efficiency for their business, including:

- + Establishing and maintaining efficient cross-border operations keeping costs down to maintain strategic advantage, including using KPMG Data Analytics to identify costs savings and international trade risk.
- + Ensuring compliance with Australian laws and regulations associated with cross-border trade.
- + Customising trade processes and controls to a business unit, company, or industry.
- + Mitigating trade risk issues related to conducting cross-border business.
- + Assisting clients to become Australian Trusted Traders.
- + Advising on complex Free Trade Agreement matters in Australia and across the ASPAC region.
- + Advising on excise duties and excise compliance.

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What do the OECD's BEPS 2.0 changes mean for the Australian life sciences sector?

The OECD's Inclusive Framework ("IF") on Base Erosion and Profit Shifting ("BEPS 2.0") represents an historic and globally co-ordinated overhaul of existing international tax rules which will reshape the future of global taxation for large multinational enterprises ("MNEs").

The IF and the G20 have recently made clear statements committing to the implementation of these reforms, with changes due to begin coming into effect from 1 January 2023, so now is the time to take stock of how these rules will affect your business.

IN SUMMARY, THE BEPS 2.0 INITIATIVE ADOPTS A TWO PILLAR APPROACH TO REFORMS:

PILLAR ONE



Pillar One deals with the reallocation of profits between members of very large global MNEs (broadly, those with a world-wide turn-over greater than EUR20bn and profitability above 10%). Pillar One is a significant departure from the accepted basis of allocating profits between group members, moving from a reliance on physical presence to allocating a portion of profits to market jurisdictions.

PILLAR TWO



Pillar Two secures an unprecedented agreement on a global minimum level of taxation of 15% for the profits of MNEs, and applies to MNEs with revenues exceeding EUR750m.



WHAT SHOULD I FOCUS ON?

Given the turnover thresholds, it is expected that the main focus for Australian entities will be Pillar 2. As such, Australian life sciences organisations will need to consider the effective tax rates of its Australian and foreign operations, with a particular focus on whether tax incentives provided in Australia or foreign jurisdictions cause their effective tax rate in those jurisdictions to fall below the global minimum of 15%.

Whilst there are limited incentives in Australia below the likely global minimum rate of 15%, Australian outbound groups that claim tax incentives in other jurisdictions will need to carefully consider how these rules may neutralise the benefits of these incentives. Entities (inbound or outbound) will also need to consider the Subject to Tax Rule (top up withholding) when making payments to incentivised entities in their group that are taxed at a rate of less than 9% (for in-bound entities, this adds another foreign tax rate which needs to be considered when making payments to group companies, on top of the targeted integrity rule in Australia's hybrid mismatch rule and the diverted profits tax), although it remains to be seen which tax treaties that Australia has with other countries will be amended to give this rule effect. Importantly for the life sciences sector, royalties are caught within the list of payments covered by the Subject to Tax Rule.

HOW DO I KNOW WHETHER MY ORGANISATION IS PREPARED?

Consider the following questions:

- First and foremost, will Pillar One and / or Pillar 2 apply to our business based on the thresholds and any exclusions?
- How do we identify cashflow and financial statement impacts?
- Is our group structure and global supply chain structure still fit for purpose? Does it still make sense to operate in certain jurisdictions and claim incentives after these rules are implemented?
- Are our internal systems including data collection capability and jurisdictional reporting tools ready to deal with the disclosure and reporting obligations that will flow from BEPS 2.0? Linked with this, what will be the impact on tax compliance, reporting and payment obligations: are we ready to deal with the additional compliance and reporting obligations that will flow from these rules?
- What is happening in the rest of our group? Do we have the connectivity within our organisation to respond to the new rules and report to the ATO appropriately?





HOW CAN KPMG HELP?

- + KPMG has leveraged its global reach to develop an integrated multi-jurisdictional tax advisory team who can provide practical advice on the impacts of BEPS 2.0 on your business. We have developed a range of modelling and assessment tools to conduct risk assessments, highlight potential exposures and model tax outcomes to help you identify how the new global tax architecture might affect your business and model likely modifications to existing arrangements to manage the impact of BEPS 2.0.

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