



August 2015

Proposed Country by Country reporting measures increase compliance burden and transparency for large multinationals

On Thursday 6 August, the Australian Government released two further exposure drafts in relation to its multinational tax integrity measures.

In the 2015 Budget, the Government announced a package of measures to address multinational tax avoidance. As a part of these measures, the Government has released two new exposure drafts, which:

- Introduce new OECD Country by Country (CbC) reporting requirements;
- Adopt the new OECD standard on transfer pricing documentation (i.e. the Master File/Local File approach); and
- Double administrative penalties for multinational entities that are found to have entered into tax avoidance or profit shifting schemes.

The above measures apply to multinational groups with annual global revenue of A\$ 1 billion or more, whether they are Australian headquartered, or Australian subsidiaries of overseas headquartered groups of this size (collectively “affected taxpayers”).

Increased compliance obligations for multinationals

From periods beginning on or after 1 January 2016, affected taxpayers must provide a “statement” to the Commissioner on an annual basis. The statement must be provided within 12 months after the close of each income year (the “due date”). For example, 31 December balancers will be required to gather data from 1 January 2016, and file their first statement by 31 December 2017. This statement must be in an “approved form” which is yet to be determined by the Commissioner.

An entity may be required to include in its statement one or more of:

- A CbC report containing information on the location of the economic activity undertaken by the multinational group;
- A master file, which provides a high-level description of the multinational group’s business operations; and

Introduction

Increased compliance obligations for multinationals

Impact on inbound and outbound multinationals

Challenges faced in completing a CbC report

CbC reporting – undertaking a dry run

Australian documentation versus Master File and Local File

Penalty provisions

The transparency movement

Conclusion

Next steps

- A local file, which describes the Australian entity's operations and cross border related party transactions.

The filing of the statements will provide the Commissioner with relevant and reliable information to carry out transfer pricing risk assessments.

Impact on inbound and outbound multinationals

The statement that must be provided is expected to include:

	CbC	Master File	Local File
Australian headquartered MNE	✓	✓	✓
Australian Sub of overseas MNE	x ¹	✓	✓

¹ Expected to be obtained via automatic exchange of information

It is expected that the default will be that taxpayers are obligated to file the relevant documents, unless the Commissioner grants an exemption on application, or subsequent objection (for example where an affected taxpayer has insignificant cross border dealings). The measures do not contain a time frame for this process, however in the absence of an exemption being granted, administrative penalties will accrue from the due date for filing until the statement has been filed. Should an entity choose not to comply, the Public Officer may ultimately face criminal charges.

Further, it is unclear as to whether an exemption will be provided in the scenario where an overseas parent of an Australian subsidiary has not prepared a CbC report.

Challenges faced in completing a CbC report

Without a clear and consistent approach to gathering and interpreting data, the CbC report may contain materially misleading distortions or misrepresentations, leading to a picture of the company's global tax profile that may be misinterpreted by tax authorities. Some of the key challenges in this regard are highlighted below:

- There are clear definitional issues. For example in relation to income tax, a large multinational business may have over sixty direct taxes worldwide. Complexities will also arise when categorising taxes, for example the attribution of withholding taxes across entities worldwide can be complex and dependent on local rules;
- There are issues regarding scoping. Entities in scope may include companies, trust and partnerships, with tax jurisdiction defined as the place of residence, not incorporation. A clear view therefore needs to be taken on which structures and entities to include in the statement, with permanent establishments and branches being reported separately;
- There are issues regarding consistency. A consistent approach needs to be adopted across the multitude of systems in a large organisation as well as key differences between local and group accounting standards and management accounts. Further, language differences on a country by country basis can cause inconsistencies, and assurance requirements should be considered to combat this; and
- Broader engagement with the business is required around data gathering. For example, employee numbers may include independent contractors and must be reported on a whole FTE basis, requiring engagement with HR teams as well as finance teams.

Even once the data is obtained, reconciliation of the data to account for different business structures, jurisdictional divisions and currencies can be difficult to track. Further, there is no materiality threshold, meaning small, dormant and/or holding companies remain in scope regardless of accounting treatment and coverage.

As a result of these complexities, it is considered best practice for affected taxpayers to perform a 'dry run' of the CbC reporting process, in order to identify and address any issues with data collation and aggregation, as well as to identify any strategic concerns arising from how the data gathered is presented in the schedule.

The key considerations with regard to undertaking a CbC reporting dry run are outlined below.

CbC reporting – undertaking a dry run

The compliance requirements imposed on affected taxpayers by the measures will require attention well in advance of the due date. In particular, undertaking a dry run will ensure that data can be accurately captured in timely fashion, appropriate analysis of the results is performed, and strategies adopted as required to mitigate any disclosure related risks that may arise in relation to cross border dealings.

Our recommendations with regard to best practice in addressing the requirements under CbC typically utilise the following project framework:

- 1 Planning and strategy (feasibility study, scoping, project design, issue training, project management);
- 2 Data gathering (mapping, ERP/software assessments, templates, implementation training, dry-runs);
- 3 Assurance over data gathered (develop assurance framework, undertake assurance);
- 4 Analytics (transparency, sustainability, tax structuring and transfer pricing risk review);
- 5 Compliance/reporting (preparation of CbC Documentation, operationalise recommendations), linking in and reconciling to the local transfer pricing documentation, Master File and Local File, and reviewing prior to submission; and
- 6 Follow up (Redesign structures, proactive ATO engagement, drafting tax sustainability reports).

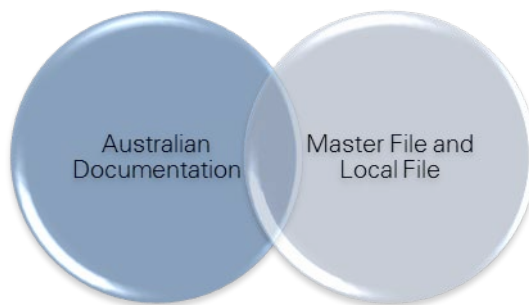
The more complex the entity, the greater the benefit that would be received from a CbC dry run.

Australian documentation versus Master File & Local File

Taxpayers should also consider how their existing transfer pricing documentation processes will be impacted as a result of the need to prepare and lodge the Master File and Local File.

There is substantial overlap between the documentation requirements under the OECD's Master File and Local File, and Australia's new transfer pricing documentation rules as contained in Subdivision 284-E. However, there are also differences between these documents in relation to timing, purpose and coverage.

- Required for a reasonably arguable position (“RAP”) and potential penalty mitigation.
- Prepared contemporaneously with tax return filing.
- Requires additional analysis (e.g. reconstruction provisions).
- Not required to be lodged with the ATO.



- Filed one year after end of financial period.
- Administrative penalties apply if not filed.
- Does not provide a reasonably arguable position and therefore penalty mitigation.

These differences will lead to administrative issues and uncertainty regarding what level of documentation to prepare, and when to prepare it. It is also unclear as to how the requirements under CbC reporting would impact Australian taxpayers with existing Advance Pricing Arrangements, or Australian subsidiaries of overseas headquartered multinationals who have adopted the simplified transfer pricing documentation measures.

The transparency movement

While it is currently not proposed by the authorities that the CbC report be made public, there is an increasingly large movement toward tax transparency that suggests it may become so in the future.

The ever changing landscape with respect to tax transparency means that multinationals should be pro-actively considering how their tax related information would appear in the public domain, as well as whether to voluntarily increase their level of public disclosure in relation to tax related matters.

Penalty provisions

In addition to the administrative penalties outlined above for late filing of a statement, the proposed amendments double the maximum administrative penalties for large companies that are found to have entered tax avoidance or profit shifting schemes, to 50 percent. These increased penalties only apply to companies with annual global revenue exceeding A\$1 billion who do not adopt a tax position that is reasonably arguable, and documented in accordance with Subdivision 284-E.

As a result, this places increased emphasis on the importance of preparing Australian compliant transfer pricing documentation, in addition to the requirement to submit a Master File and Local File, presenting an additional compliance burden to affected taxpayers.

Conclusion

Compliance with the CbC reporting measures will require a significant investment of time and effort by both inbound and outbound multinationals, with performance of a dry run recommended as best practice in order to identify and resolve any issues that may arise (either from a data gathering or from a strategic interpretation perspective) before completing the process live as part of the first reporting period.

The proposed measures also represent a significant change from a transfer pricing perspective as a result of the additional requirement for all affected taxpayers to provide the Master File and Local File to the Commissioner unless an exemption is granted. This effectively introduces a mandatory TP documentation requirement in Australia.

Furthermore, the doubling of penalties places additional pressure on the preparation of high quality documentation to support the transfer pricing or tax positions adopted, and a more onerous compliance regime on to those taxpayers who wish to obtain a RAP in relation to their transfer pricing or tax positions in order to mitigate the risk of additional penalties.

Finally, certain clarifications and changes to the exposure drafts will be required before the operation of the proposed rules can be properly implemented and understood, for example in relation to whether an Australian subsidiary of an overseas enterprise will be provided with an exemption from its obligations to file a CbC report if it has not been prepared elsewhere in the group.

Next steps

Interested parties are invited to comment on the exposure drafts and explanatory statements by Wednesday 2 September 2015. We invite your call to discuss any of the proposed measures.

Please contact the core CbC team below or your KPMG client service representative for assistance or further information.

Core CbC Team Contacts

Tax	GTPS	Tax Governance & Transparency	IT Data & Technology
Paul Sorrell +61 2 9335 8613 psorrell@kpmg.com.au	Jane Rolfe +61 3 9288 6341 janerolfe@kpmg.com.au	David Drummond +61 2 9335 8695 ddrummond@kpmg.com.au	Matt O'Keefe +61 3 9288 5430 mokeefe@kpmg.com.au
	Michael Smith +61 3 9288 5895 mnsmith@kpmg.com.au	Stephen Callahan +61 2 9335 7216 scallahan1@kpmg.com.au	

Or by email: CbC@kpmg.com.au

kpmg.com.au

KPMG's Tax practice is not licensed to provide financial product advice under the Corporations Act and taxation is only one of the matters that must be considered when making a decision on a financial product. You should consider taking advice from an Australian Financial Services Licence holder before making any decision on a financial product.

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act upon such information without appropriate professional advice after a thorough examination of the particular situation.