18 April 2024

Director
Pillar Two Unit
Corporate and International Tax Division
Treasury
Langton Cres
Parkes ACT 2600

By email: contact.internationaltax@treasury.gov.au

Dear Director,

International taxation – global and domestic minimum tax – primary legislation

The Tax Institute welcomes the opportunity to make a submission to the Treasury in respect of its consultation on the:

- exposure draft Taxation (Multinational – Global and Domestic Minimum Tax) Imposition Bill 2024 (**draft Imposition Bill**);
- exposure draft Taxation (Multinational – Global and Domestic Minimum Tax) Bill 2024 (**draft Assessment Bill**);
- exposure draft Treasury Laws Amendment (Multinational – Global and Domestic Minimum Tax) (Consequential) Bill 2024 (**draft Consequential Amendments Bill**);
- accompanying explanatory memorandum (**draft EM**); and
- consultation paper titled 'Global and domestic minimum taxes: Interactions with other Australian tax laws' (**Consultation Paper**).

In the development of this submission, we have closely consulted with members of The Tax Institute that have expertise in the area, including our National Large Business and International Technical Committee, and our Pillar Two Working Group, to prepare a considered response that represents the views of the broader membership of The Tax Institute.

The draft legislation package proposes to implement key aspects of Pillar Two of the Organisation for Economic Co-operation and Development's (**OECD's**) two-pillar solution as set out in the Global Anti-Base Erosion Rules (**GloBE**). In particular, the draft legislation package proposes to implement the Domestic Minimum Tax (**DMT**), Income Inclusion Rule (**IIR**), Undertaxed Payments Rule (**UTPR**), and domestic top-up tax. These changes, when legislated, will result in significant changes to the compliance obligations for impacted entities.

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Given the significance of this impact, we consider it important to ensure that the implementation of Pillar Two considers the cost of the additional compliance obligations on taxpayers, and seeks to minimise these costs where opportunities arise to reduce them. Examples include amalgamating the Australian Globe Tax Return (**AGTR**) and DMT returns into one form which are filed by one entity in the Applicable MNE Group (**AMG**), instead of by each Constituent Entity (**CE**).

Similarly, we consider that a CE's obligations in relation to the AGTR should be satisfied if it has been lodged with another foreign government agency. The Commissioner should rely on established information sharing protocols to obtain the needed information and provide other jurisdictions with the necessary information if they have been provided in Australia on behalf of other entities in the AMG. Requiring taxpayers to lodge multiple returns where the information is already accessible to the Commissioner is an unnecessary increase in compliance costs.

We also consider that the forms for the AGTR and DMT returns, or drafts of the proposed returns, should be provided to taxpayers at the earliest opportunity to give them sufficient notice of the information they will need to provide. This will assist taxpayers in making the necessary updates to their systems and processes, to enable them to lodge the relevant returns and meet any additional tax obligations.

The Tax Institute also considers that:

- further consideration and potentially, consultation is required regarding the interaction between Pillar Two and Australia's tax consolidation regime;
- further consideration should be given to whether entities that are subject to the top-up taxes should also be subject to the various integrity measures that form part of the Inclusive Framework on Base Erosion and Profit Shifting (**BEPS**) actions already in place in Australia;
- unintended timing issues with respect to the interactions between Pillar Two and the foreign income tax offset (**FITO**) rules should be rectified;
- the start date for Pillar Two should be delayed by at least 12 months to allow taxpayers reasonable time to understand and meet their tax liabilities;
- a prompt post implementation review of Pillar Two in Australia will be required to ensure that unforeseen issues are rectified in a timely manner;
- the approach to non-lodgment penalties should be reviewed, removing the unfair approach of potentially subjecting an AMG to multiple and significant penalties; and
- the definitions and terminology used in Australian legislation and the contents of information to be requested by the relevant compliance documents/returns should be consistent with the OECD's approach.

Our detailed response and recommendations to further improve the updated draft Bill and updated draft EM are contained in **Appendix A**.

The Tax Institute is the leading forum for the tax community in Australia. We are committed to shaping the future of the tax profession and the continuous improvement of the tax system for the benefit of all. In this regard, The Tax Institute seeks to influence tax and revenue policy at the highest level with a view to achieving a better Australian tax system for all.

If you would like to discuss any of the above, please contact The Tax Institute's Senior Counsel – Tax & Legal, Julie Abdalla, at (02) 8223 0058.

Yours faithfully,

Scott Treatt
Chief Executive Officer

Todd Want
President

APPENDIX A

We have set out below our detailed comments and observations for your consideration. Our comments broadly follow the consultation preamble contained on page 2 of the draft EM. Further, our response regarding the interaction with other taxation laws below incorporates our comments regarding the questions asked in the Consultation Paper.

Delayed exchange of the GloBE Information Return between jurisdictions

The proposed section 125-5 of Schedule 1 to *Taxation Administration Act 1953* (Cth) (**TAA**) requires a CE or a Designated Filing Entity (**DFE**) of an applicable MNE group to file a GloBE Information Return (**GIR**) with the tax administration of the jurisdiction where it is located. In this regard, the Consultation Preamble and paragraph 3.33 of the draft EM seek stakeholder feedback specifically regarding the delayed exchange of the GIR between jurisdictions.

As per subsections 125-5(6), 125-5(7) and 125-5(8), where a GIR is filed in a foreign jurisdiction by an ultimate parent entity (**UPE**) or a DFE, a CE's obligation to lodge a GIR is considered to have been met. Paragraph 4 of chapter 8 of the commentary on the Model GloBE Rules[1] explains that the rationale behind this is to enable either the UPE or DFE to submit a single GIR for all CEs within the MNE Group. This GIR can then be shared with tax administrations that have a CE located in their jurisdiction, using appropriate information exchange mechanisms.

Considering the above, The Tax Institute is of the view that the proposal to empower the Commissioner to demand a CE to lodge a GIR within 21 days through a written notice in case of a delay in receiving a GIR from the foreign government agency, with penalties for non-compliance, unreasonably shifts the onus and places disproportionate responsibility on the taxpayer. This also increases the compliance burden associated with GIR filing.

We consider that the Commissioner should be required to rely on existing information sharing protocols to obtain the relevant information in the GIR. Timing delays or the unavailability of GIRs from certain jurisdictions are likely to be indicative of a systemic issue that should be resolved. The Tax Institute supports funding for the Commissioner to ensure that he is able to receive information contained in a GIR from other jurisdictions, and provide the information contained in the AGTR to other jurisdictions, in a timely manner.

Lodgment of DMT returns

Proposed subsection 127-15(2) of Schedule 1 to the TAA broadly requires all Australian located CEs of an AMG to lodge DMT returns within the time period required for lodging the AGTR. A CE's obligation may be met by a Designated Local Entity who is permitted to file DMT returns for all CEs of an AMG.

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[1] *OECD (2022), Tax Challenges Arising from the Digitalisation of the Economy – Commentary to the Global Anti-Base Erosion Model Rules (Pillar Two), OECD, Paris*. Retrieved from: https://www.oecd.org/tax/beps/tax-challenges-arising-from-thedigitalisation-of-the-economy-global-anti-base-erosion-model-rules-pillar-two-commentary.pdf.

We consider that the AMG should be required to lodge one DMT return with the liability of all the Australian located CEs, along with any required supporting information to be included as separate items or schedules of the single return. We also consider that the DMT return should be amalgamated with the AGTR. We also refer to our comments below regarding the need to reduce reporting obligations under Australia's tax consolidation regime.

Streamlining the reporting obligations will reduce the compliance costs for impacted taxpayers, reducing the amount of duplicated information, while providing the Commissioner with the information needed to ensure there is an accurate assessment of the DMT.

Timing for franking credits

The Tax Institute is of the view that the words currently crossed out in the relevant items in proposed subsections 205-15(1) and 205-30(1) of the *Income Tax Assessment Act 1997* (Cth) (**ITAA 1997**) should not be crossed out. This would ensure that the approach is consistent with other areas of Australia's taxation legislation.

Interaction with other taxation laws

Tax consolidation

We consider that the interaction between Pillar Two and Australia's tax consolidation regime requires separate, detailed consultation in the context of ways to relieve potentially unnecessary compliance burdens. As currently drafted, the only nexus with the tax consolidation regime is the proposed Division 127-C of the ITAA 1997. The proposed Division has the effect of only making the head company of a tax consolidated group liable to pay to the Commissioner the total of all CEs' GloBE Top-Up Tax or Domestic Top-Up Tax amounts to the extent that those entities are members of the head company's tax consolidated group at the end of the fiscal year.

Furthermore, there is no provision to allow a GloBE or Domestic Top-Up Tax liability to be assessed to the head company of a tax consolidated group or for an AGTR or DMT return to be prepared on the basis of the 'single entity rule' (as applicable for head company or core entity purposes for income tax purposes). Each CE member of a tax consolidated group continues to have individual liabilities and filing obligations. Although a 'Designated Local Entity' may be appointed to lodge the CE's returns, this does not remove the need for each CE to lodge the relevant returns. Consideration should be given to the implications of having a single filing obligation on the basis that CEs of the same AMG are treated as part of the head company if so chosen.

The effect of the above in the context of the proposed Division 127-C of the ITAA 1997 would also appear to be that unless and until all of the group's liability is paid, each member of the GloBE consolidated group (**GCG**) would continue to be liable for a pro-rata share of the total unpaid amounts. This is regardless of whether the individual entity may have ensured that its actual share of the liability was discharged. Feedback from our members suggests that, if this is the underlying policy intent, this approach is likely to result practical and commercial tensions between group members.

Further, we note that there is no provision that treats each of the group members as being jointly and severally liable for the total GloBE consolidated group amount. That is, such taxes are not 'tax related liabilities', unlike income taxes pursuant to Division 721 of the ITAA 1997. This would mean that the current proposed regime would operate such that there should be no legislative basis for the need to have tax sharing agreements or allow a leaving subsidiary member to have clear exit in relation to any applicable outstanding GloBe Top-up Tax or Domestic Top-Up Tax amounts as all members would continue to remain liable until it is fully discharged. We consider that the legislation should clarify if this is the intended outcome.

We note that there appears to be no choice but for the head company of a GCG to have the liability for the GCG amount assigned to it. In practice this will mean that some form of funding agreements will need to be put in place to ensure that the liability can be met. To alleviate this, we consider that the legislation should allow an individual member to assign their liability to the head company of the GCG.

Interaction with other BEPS Actions

From a policy perspective there is an overlap between Pillar Two and other taxes that arose from the BEPS. Pillar Two broadly intended to:[2]

- ensure minimum taxation while avoiding double taxation or taxation where there is no economic profit;
- cope with different tax system designs by jurisdictions as well as different operating models by businesses;
- ensure transparency and a level playing field; and
- minimise administrative and compliance costs.

In part, these changes were seen to be necessary as the existing framework was not able to adapt or manage the challenges imposed by evolving business practices, particularly changes brought upon by the digital economy.[3] Although there is a detailed framework which provides a level of consistency across jurisdictions, each country is able to make simple tax policy rules to ensure the principles above are met.[4]

In this context, we consider that there is policy overlap between Pillar Two and several aspects of our existing taxation system. These include the:

- hybrid mismatch rules;
- controlled foreign company regime (**CFC**); and
- proposed measure to deny deductions for expenses relating to intangible assets held in overseas jurisdictions.

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2 OECD (2020*), Tax Challenges Arising from Digitalisation – Report on Pillar Two Blueprint: Inclusive Framework on BEPS, OECD/G20 Base Erosion and Profit Shifting Project*, OECD Publishing, Paris, https://doi.org/10.1787/abb4c3d1-en, paragraph 8.

3 Ibid, paragraph 3.

4 Ibid, paragraph 4.

From a policy perspective, we consider that entities that are subject to a top-up tax under Pillar Two should not be subject to a tax liability under the taxation regimes listed above in respect of the same amounts. This is because the various regimes seek to effectively tax the same aspects that will also be a fundamental part of a top-up tax under Pillar Two. We note that these taxes will still have a role in our tax system for entities that are not subject to a top-up tax under Pillar Two.

The Tax Institute does not agree with the proposed approach in the Consultation Paper for Australia's hybrid mismatch rules to continue operating even if a foreign jurisdiction imposes global or domestic minimum taxes. This is because it will give rise to an inequitable outcome for taxpayers in the form of double taxation as Australia will look to neutralise a mismatch at the same time as top-up tax being paid under Pillar 2 with respect to the same payment. The potential for double taxation is demonstrated in the example below.

> An Australian resident company Parent Co has two subsidiaries. Sub A is located in Australia (the same as Parent Co) and Sub B is located in Jurisdiction B. Jurisdiction B is a low-tax jurisdiction. Sub A and Sub B enter into a financial instrument. The financial instrument is treated for tax purposes as debt in Australia and equity in Jurisdiction B. The payment of interest on the debt is deductible in Australia and not be included in the foreign recipient's income, giving rise to a hybrid financial instrument mismatch. Under Australia's hybrid mismatch rules, the Australian payment will not be deductible to the extent that the paid amount is not included in the non-resident recipient's income. Given Jurisdiction B is also a low-tax jurisdiction under the Pillar 2 rules, top-up tax will be payable by Parent Co under Australia's IIR. As a result, the same payment will be taxed twice – both under the hybrid mismatch rules (in the form of deduction denial) and under Pillar 2 (in the form of top-up tax).

Foreign income tax offsets

The Tax Institute generally supports Treasury's position that a foreign income tax offset (**FITO**) should be available for top-up taxes imposed under a foreign jurisdiction's qualifying domestic minimum tax (**QDMT**), including where the income is subject to tax in Australia through our CFC regime. However, we consider that there is a general timing issue that results from an unintended consequence. A FITO is only available under Division 770 of the ITAA 1997 if foreign tax has been 'paid'. However, the QDMT liability in a foreign jurisdiction may not be payable until sometime after the relevant income year. Timing differences may be exacerbated due to other factors, such as delayed audits in other jurisdictions that result in the amount 'paid' only being known after the Australian amendment period has ended.

We consider that taxpayers should be able to claim the FITO for tax paid, in relation to the year it was paid, if the amount is only known at a later date as in such circumstances. The legislation should provide for the relevant mechanisms and powers to make this an efficient process, reducing compliance costs for the taxpayer and administration costs for the Commissioner.

Other comments

Proposed start date

The DMT is proposed to apply to fiscal years commencing after 1 January 2024. Despite the start date, the legislation is still at the exposure draft stage with an unknown but potentially lengthy period of time before it receives Royal Assent. We consider that the Government should give priority to having the relevant legislation finalised well before 31 December 2024 which is the most common end of the first fiscal year for which these rules will apply in an Australian context.

Following Royal Assent, taxpayers will need await finalisation from the Commissioner regarding the information needed to complete the DMT return and AGTR, and calculate their liability to any top-up tax. Although the relevant returns are proposed to be due up to 18 months after the end of the relevant fiscal year,[5] there is a real risk that taxpayers will not have sufficient time if the passage of the legislation is delayed, or if there are uncertain key issues where further guidance is needed. For this reason, we also consider that the Government should be open to the potential for further refinement or revision to the law if necessary.

It is also imperative for the Commissioner to provide taxpayer guidance (both technical and administrative) on the measures as soon as practicable. Noting the likely implementation challenges facing taxpayers during the transitional years, the Commissioner should adopt a reasonable approach in relation to administering the new law during the transitional period, especially when it comes to the potential imposition of penalties for shortfalls or for late lodgment of the relevant returns.

If the above is not realistically achievable, we consider that the commencement date should be delayed by at least 12 months, applying to fiscal years commencing no earlier than 1 January 2025. This will ensure that taxpayers have sufficient time to update their systems and processes to allow them to calculate their tax liabilities and lodge the relevant returns.

Delaying the commencement of the primary legislation until the same time as the secondary legislation will also reduce the likelihood of discrepancies that may arise from the staggered implementation. Given the underlying complexity of Pillar Two, there are likely to be unforeseen or unintended consequences that arise. Alternatively, we consider that the Government should work with the Australian Accounting Standard Board (**AASB**) and the Commissioner to ensure that guidance is issued to provide financial reporting certainty for impacted taxpayers in the case of any unintended discrepancies.

Availability of draft returns

We consider that the contents of and information requested in the DMT return and the AGTR should be made available at the earliest possible opportunity. Doing so will better inform taxpayers and allow them to begin preparing their systems to capture the information needed to complete the returns. If a final return is not possible due to other delays, such as the passage of legislation, releasing draft versions will also greatly assist impacted taxpayers. Also, it is crucial that the contents/information requested are consistent with and do not extend beyond what is required by the OECD rules.

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5 Proposed subsection 127-20(1) and (2) of Schedule 1 to the TAA.

Non–lodgment penalties

As stated in paragraph 3.19 of the draft EM, an administrative penalty will apply for each return a CE does not lodge on time, with the base penalty amount to be multiplied by a factor of 500.[6] We note that the amount of a penalty unit is expected to increase to $330,[7] resulting in CEs being subject to a penalty amount between $165,000 and $825,000 per late DMT return or AGTR. This could result in a single AMG or tax consolidated group being subject to multiple and significant failure to lodge penalties if a few entities (or simply the designated local entity) are late with their lodgment.

The Tax Institute is of the view that this is an excessive outcome that unfairly penalises taxpayers for late lodgment of a complex return. Taxpayers need time to understand the implications of the new reporting obligations, with further time to ensure that their systems and processes are updated to gather the relevant information needed to accurately complete the relevant returns. Further, and as noted above, we consider that the various reporting obligations should be capable of being amalgamated into one return. Efficiently imposing multiple penalties for an inefficiency resulting from legislative or administrative design is an inequitable outcome for impacted taxpayers. For these reasons, we consider that the failure to lodge penalty should be applied to each AMG instead of each CE.

As noted above, The Tax Institute is of the view that a reasonable approach should be taken with regards to penalties during the transitional period. The scope of the Pillar Two changes, combined with the associated changes needed to reporting systems and infrastructure, increase the likelihood of unintended delays in reporting obligations or accidental mistakes. Lowering the penalty rates and providing a broader discretion to the Commissioner to reduce penalty amounts during the transitional period will assist taxpayers until the systems are developed and finalised.

Consistency with OECD definitions

We consider that the terminology and definitions used in the draft legislation should be consistent with the approach proposed by the OECD. This will reduce potential confusion and better ensure that the DMT and UTPR are imposed as intended, reducing the likelihood of unintended consequences arising.

Post implementation review

The draft legislation package, including the subordinate legislation, is a large and complex framework. The concepts and implementation of Pillar Two are a new and untested area for taxpayers, tax practitioners and the Commissioner. Although consultation has been undertaken throughout the design of the implementation of Pillar Two in Australia, there are likely to be a number of issues that are only able to be identified once taxpayers are required to comply with the new obligations in practice.

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6 Proposed subsection 286-80(4B) of Schedule 1 to the TAA.

7 See Schedule 3 to the Crimes and Other Legislation Amendment (Omnibus No. 1) Bill 2024.

As a result, we consider that a post implementation review of Pillar Two will be required. Noting the complexity and lengthy period of time before concepts can be tested, multiple contemporaneous reviews may need to be undertaken. To facilitate ongoing review, The Tax Institute supports the creation of a working group consisting of stakeholders from Treasury, the ATO, industry experts and professional organisations, to regularly meet, discuss and address issues as they arise.