

Transfer Pricing Country Summary

Australia

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1. Introduction

Australia is not a member of EU, but a member of OECD. It basically follows OECD TP Guidelines and adopted local file, master file and local files. Apart from that, Australia also has special forms for certain documentations.

2. Laws & Regulations

a) References to OECD/EU/Local Rules

Legislation pertaining to transfer pricing for income years starting after 29 June 2013 is contained in Subdivisions 815-B (companies), 815-C (branches and permanent establishments), and 815-D (partnerships and trusts) of the Income Tax Assessment Act 1997 (ITAA97) and Subdivision 284-E of Schedule 1 of the Taxation Administration Act 1953 (TTA) (penalty provisions and documentation), and is supplemented by relevant provisions of Double Tax Treaties scheduled to the International Tax Agreements Act 1953, and Taxation Rulings issued by the Australian Taxation Office (ATO) after 29 June 2013, and Guidance provided by the OECD on transfer pricing and the Arm's Length Principle. However, some transfer pricing rulings still have effect despite being issued prior to this date.

Before 29 June 2013, Division 13 of the Income Tax Assessment Act 1936, Double Tax Treaties and various Taxation Rulings issued by the ATO applied, (the most significant Taxation Rulings were TR1997/20 (arm's length methodologies), TR 1998/11 (documentation expectations) and TR 1999/1 (intra-group services)).

A transitional provision contained in Subdivision 815-A of ITAA97 applied to income years starting from 1 July 2004 and ending 30 June 2013 regarding entities dealing with related parties in countries covered by a Double Tax Treaty. Entities with dealings with non-treaty countries continued to be covered by Division 13 of the Income Tax Assessment Act 1936 (ITAA 36) in the transitional year (the income year ending 30 June 2013). Division 13 covered all entities before this. The main objective of 815-A was to allow taxpayers to rely on and enforce the articles in the Double Tax Agreements – otherwise, there was no legislation to support this.

In the 2015–16 Budget, the government announced implementing the OECD's new transfer pricing documentation standards (commonly referred to as Country-by-Country (CbC) reporting) which later on came into force for the first income tax year beginning on or after 1 January 2016. The implementation includes a master file, local file and CbC report. The standard was recommended under Action Item 13 of the G20/OECD Base Erosion and Profit Shifting Action Plan.

These new reporting requirements apply to entities with an annual global income of AUD 1 billion or more. These entities are referred to as "Significant Global Entities". They are required to file the documents with the ATO within 12 months of their income tax year-end.

Also, the ATO has issued its final Taxation Ruling TR 2020/4 and Practical Compliance Guideline PCG 2020/7. Ruling 2020/4 takes the place of TR 2003/1 and regulates a thin capitalisation rule, and addresses crucial legal technical problems, such as record-keeping obligations and the arm's length

debt test for transfer pricing regulations. The ATO's compliance approach is outlined in PCG 2020/7, which should be read in combination with TR 2020/4. The ruling requires taxpayers to show that their notional debt levels address all the quantitative and qualitative measures of an arm's-length debt amount by referencing comparable entities, taking into account the reconstructed balance sheet, profit and loss statement, cash flows, and credit rating. The instruction contains an example calculation as well as references to certain financial ratios that the ATO considers satisfy the "relevant criteria" stipulated in the statute.

b) Definition of Related Party

Related parties are not defined in Australia's transfer pricing legislation. Regardless of whether the parties are related, Australia's transfer pricing statute applies if an Australian corporation receives a tax benefit in Australia due to non-length arm's cross-border conditions. While there is no definition in the legislation, the Taxation Officer's guidance on their website defines an international related party as those with interest in equity, voting rights, or income distribution of 20% or greater.

However, the ATO's instructions for filling out the Foreign Dealings Schedule include a definition of "International Related Parties" (IDS). When a taxpayer engages in specific international activities or agreements, an IDS must be lodged accordingly.

According to the IDS instructions, the term includes:

- any overseas entity or person who engages directly or indirectly in your management, control, or capital; any foreign entity or person in whose management, control, or capital you participate directly or indirectly;
- any overseas entity or person in whose management, control, or capital you participate directly or indirectly;
- any overseas entity or person in respect of which persons who participate directly or indirectly in its management, control or capital are the same persons who participate directly or indirectly in your management, control or capital.

c) Nature of Transfer Pricing Documentation

The ATO requires an International Dealings Schedule to be filed with each tax return where the aggregate amount of transactions or dealings with "International Related Parties", both revenue and capital in nature, is greater than AUD 2 million. Information disclosed on the International Dealings Schedule includes:

- Countries with which the taxpayer has international related party transactions;
- International related party transaction types and quantum,
- The percentage of transactions covered by contemporaneous documentation that satisfies TR 2014/8 (e.g., royalties, intercompany loans, services, etc.);

- Transfer pricing methodologies selected and applied for each international related party transaction type;
- Details of restructuring events involving “International Related Parties”;
- Dealings with branch operations;
- Interests in foreign companies or foreign trusts;
- Whether the simplifying transfer pricing record-keeping elections have been adopted,
- Debt deductions denied for taxpayers that are highly geared, known as the Thin Capitalisation rules.

d) Tax Havens & Blacklists

Australia adopts the OECD’s definition of a tax haven. Accordingly, OECD is taken as a reference to determine the list of Tax Havens.

e) Advance Pricing Agreement (APA)

APA’s have been available since 1991 and are actively promoted by the ATO with a preference for larger and more complex cases where there is significant uncertainty or risk of double taxation. APA’s (including renewals) have been concluded as unilateral, bilateral and multilateral agreements between the ATO and the taxpayer and, where applicable, other tax authorities normally cover an advance 3- or 5-year period. APAs are typically negotiated in a cooperative environment with a taxpayer, with unilateral APAs taking approximately 12 to 24 months to conclude and bilateral 24 months and upwards (with time limitations provided for in some double tax treaties).

f) Audit Practice

Australia is a high risk of transfer pricing audit jurisdiction. The focus of audit activity is contained in an annual Compliance Programs report issued by the ATO.

Recent focus has been on restructurings of Australian-based operations to shift functions, assets, and risks offshore on a non-arm’s length basis, complex or novel financial arrangements that are not supported by a business need, international shipping operations, payment of excessive royalties, interest, guarantee and other fees, provision of services by Australian-headquartered companies to overseas subsidiaries at no charge, improper use of tax havens and bank secrecy provisions, and use and structuring of intragroup loans.

The ATO is actively involved in joint tax authority audits of large multinational groups and expects this program to expand as the OECD BEPS review progresses. Specific industries such as oil and gas, motor vehicles, pharmaceuticals, distributors, banking and insurance, and e-Commerce-based trade are at higher risk than others. Under restrictive provisions, distributors are offered a safe harbour

option if annual Australian group turnover is less than AUD 50 million (weighted 3-year average of turnover as disclosed in tax returns).

Small taxpayers are offered a safe harbour election under restrictive provisions if the annual Australian group turnover is less than AUD 25 million.

The ATO will review transfer pricing as part of a taxpayer's general tax audit or conduct a specific transfer pricing risk review.

From 29 June 2013, potential penalties may be reduced if transfer pricing documentation covers specific matters referred to in Subdivision 284-E of TAA 53 and that documentation represents the legal concept of a "reasonably arguable position". Taxation Ruling 2014/8 has been issued to give guidance on this issue.

The ATO issued practice Statement Law Administration PSLA 2014/3 to limit audit exposure for entities entitled to elect Simplified Transfer Pricing Record Keeping for 2014 and the following 3 years. Effective, safe harbours are in place, but the rules permitting their election by taxpayers is complex. Start-ups established in Australia by foreign groups with annual income under AUD 25 million may receive administrative assistance (very low risk of audit). The Australian Taxation Office then extended the application of the simplified transfer pricing rules in Practical Compliance Guideline 2017/2 with no expiration date and has extended the application of these rules for seven various options.

3. Transfer Pricing Documentation

a) Level of Documentation

The ATO recommends in TR 2014/8 an extensive list of issues to be covered in documentation to evidence a RAP that documents a transfer pricing treatment. Five key questions are recommended by the ATO, to be considered and covered in the documentation as follows:

- 1) What are the actual conditions (in connection with the form and substance of commercial or financial dealings that operate between tested entities) relevant to the matter or matters?
- 2) What are the comparable circumstances relevant to identifying the arm's length conditions (that would operate between independent entities dealing with protecting their economic interests in comparable circumstances - noting comparability factors for pricing methodologies set out in section 815-125(3) of ITAA97)?
- 3) What are the particulars of the methods to identify the arm's length conditions (explain why the applied pricing method is the most appropriate and reliable – and should consider relevant factors described in section 815-125(2) of ITAA97)?
- 4) What are the arm's length conditions, and is/was the transfer pricing treatment appropriate (determine if a transfer pricing benefit is present and adjusted under the tax return's self-assessment lodging)?
- 5) Have any material changes and updates been identified and documented (from previous years treatments)?

Under the new documentation standards, the ATO will receive the following information on large companies that operate in Australia:

- Country-by-Country Report showing information on the global activities of the multinational, including the location of its income and taxes paid;
- a Master File containing an overview of the multinational's global business, its organisational structure and its transfer pricing policies; and
- a Local File provides detailed information about the local taxpayer's intercompany transactions and agreements.

Together these reports will provide the ATO with a global picture of how multinational entities operate, assisting it in identifying multinational tax avoidance. The CbC report will contain specific information on the global activities of the entity, including the location of its income and taxes paid. The Master File will provide an overview of the entity's entire business, its organisational structure, and transfer pricing policies. The Local File will contain detailed information about the local entity's intercompany transactions.

Note: a taxpayer can't have a RAP in the absence of appropriate transfer pricing documentation concluded and in the hands of the public officer (signing the tax return) at the date of lodgement. A taxpayer that does not have a RAP will not be protected from any transfer pricing penalty.

b) Industry Analysis

By identifying value drivers for the relevant industry, a first indication of the level of profitability common in the industry is being given.

c) Company Analysis

A description of the management structure of the local entity, a local organisation chart, and a description of the individuals to whom local management reports and the country(ies) in which such individuals maintain their principal offices.

A detailed description of the business and business strategy pursued by the local entity, including an indication of whether the local entity has been involved in or affected by business restructurings or intangibles transfers in the present or immediately past year and an explanation of those aspects of such transactions affecting the local entity.

d) Functional Analysis

In conducting a functional analysis, an assessment is made of the significant activities and responsibilities that are performed by the related parties relevant to the Intercompany Transactions under review, the tangible and intangible assets that are employed and the risks that are borne in

undertaking the business activities. Such an assessment is consistent with the recommendations that have been made in the OECD Guidelines in paragraph 1.51.

e) Choice of Transfer Pricing Method

Concerning the transactions between related parties, Australia's regulations do not define any specific procedure to be employed. "In identifying the arms-length conditions, use the method or combination of methods that are the most appropriate and reliable having regard to all relevant factors," says paragraph 815-125 (2) of the Income Tax Assessment Act 1997 (ITAA 1997). The paragraph mentions that possible approaches include those outlined in section 815-135 ITAA1997 documents, such as the OECD Transfer Pricing Guidelines. As a result, the OECD TPG's methods are employed. The transfer pricing methods given in Subdivision 815 are the same as in the OECD TP Guidelines:

- Comparable uncontrolled price (CUP) method;
- Resale price method;
- Cost-plus method;
- Profit-split method;
- Transactional net margin (TNMM) method.

The ATO expects the most appropriate method to be applied, although more than one method may be applied to confirm the application of a primary method. Under certain circumstances, broader methods may also be acceptable.

Australia's legislation states, "In identifying the arm's length conditions, use the method, or the combination of methods, that is the most appropriate and reliable, having regard to all relevant factors, including the following:

- the respective strengths and weaknesses of the possible methods in their application to the actual conditions;
- the circumstances, including the functions performed, assets used and risks borne by the entities;
- the availability of reliable information required to apply a particular method;
- the degree of comparability between the actual circumstances and the comparable circumstances, including the reliability of any adjustments to eliminate the effect of material differences between those circumstances.

f) Economic Analysis – Benchmark Study

Australia largely adopts the guidance on comparability analysis outlined in Chapter III of OECD TPG in its transfer pricing legislation. The legislation states in Division 815 of the Income Tax Assessment Act 1997: "In identifying comparable circumstances for the purpose of this section, regard must be had to all relevant factors, including the following:

- the functions performed, assets used and risks borne by the entities;

- the characteristics of any property or services transferred;
- the terms of any relevant contracts between the entities;
- the economic circumstances;
- the business strategies of the entities.

Where the tested party is located in Australia, comparables should ideally be from the Australian market. Detailed information and data on Australian companies are available from several databases (such as OSIRIS/ORIANA from Bureau van Dijk or the Thompson Reuters Onesource TP documenter database). If Australian comparables are weak, the ATO prefers functional comparables from overseas markets such as the US, UK and Canada. The ATO has no preferred database.

g) Inter-company (IC) Legal Agreement

Although an Inter-company legal agreement formalises the business and financial relationship between group entities, the legal agreements have a lower ranking since the OECD 2017 Guidelines made the “conduct of parties” the prevailing concept.

h) Financial Statements

Financial statement may be required to include related-party statement.

i) Production Process for TP Relevant Returns, Documents, Forms and Financials

In the chart below, the existence of the filing requirements with the details of which format is used, the latest filing date, notification requirement and its deadline, thresholds to be applied in case it exists, and the required languages are demonstrated. This information can be seen respectively for CIT, master file, local file, CbCR, local forms, annual accounts and segmented P&L documentations.

	Prepare or File?	Format	Deadline	Notification Deadline*	Threshold* (Yes/No)	Local Language (Yes/No)*(If “No”, it can be filed in English)
Corporate Income Tax	File	AASB Standards	Before the due date for the filing of the corporate income tax return for penalty protection purposes	N/A	No	Yes

Master File	File	OECD Guidelines 2017	Within 12 months after the end of the reporting period for which they relate	N/A	Yes	Yes
Local File	File	OECD Guidelines 2017	Within 12 months after the end of the reporting period for which they relate	N/A	Yes	Yes
CbCR	File	OECD Guidelines 2017	Within 12 months after the end of the reporting period for which they relate	Within 12 months following the last day of the fiscal year of the local entity	Yes	Yes
IDS	File	Special format	6 months and 15 days after the end of the income tax year	N/A	Yes	Yes
RTP	Prepare	Special format	Upon request	N/A	Yes	Yes
Annual Accounts	N/A	N/A	N/A	N/A	N/A	N/A
Segmented P&L	N/A	N/A	N/A	N/A	N/A	N/A
<p>* Australia has signed the MCAA agreement for the filing of CBCR. There is simplified transfer pricing rule relating to "Small and Medium-sized Enterprises".</p>						

In 2014, a simplified transfer pricing record keeping safe harbour was made available to SMEs (at the option of the taxpayer) by the ATO covering Small Taxpayers, Distributors, Intra-group services, and Low-level loans (inbound only). However, in practice, it is of relatively limited availability as restrictive conditions apply. The ATO recognises that the amount and complexity of the documentation should be in line with the tax at risk and the size of the international related party transactions.

The ATO simplification measures apply to low-risk taxpayers, namely:

- Small taxpayers with turnover between \$0 and \$25 million;
- Small distributors with turnover between \$0 and \$50 million.

In addition, "safe harbour" type arrangements also apply where taxpayers have:

- Certain intra-group service fee arrangements; and
- Inbound loans of up to \$50 million in Australian dollars.

To gain penalty protection, documentation establishing a RAP must exist as a final document at the date of lodgment of the tax return. The deadline for filing a corporate tax return is 15 July. For practical purposes, it must be in the hands of the person signing the tax return – the Public Officer – either as a hard copy or electronically in a format that can be presented to the ATO if and when requested, with clear evidence of its creation date.

All CbC reporting statements, along with the master file, local file, and CbC report, must be filed within 12 months after the end of the reporting period. The statements must be sent online in the form of an XML Schema. The International Dealings Schedule is attached to the income tax return and must be filed with the income tax return when it is due. Additionally, taxpayers may voluntarily create transfer pricing documentation (including details of comparables and transfer pricing policies) to show their compliance with the arm's length principle beyond the basic statutory requirements.

Documentation is generally only required to be submitted to ATO following the notification of an ATO transfer pricing documentation review, which precedes a possible audit. When the ATO requests TP documentation, the taxpayer is normally required to submit it within 28 days. Although the ATO has the authority to extend this deadline, based on recent practice, the ATO is unlikely to do so unless clear, compelling reasons support the request.

The statute of limitations on the assessment of transfer pricing adjustments is 7 years. There was no statute of limitations for TP modifications before 2013. Under Division 13, the Commissioner is particularly empowered by the tax legislation to make changes on assessments regarding financial years beginning before 1 July 2013. As a result, years before 1 July 2013 are subject to dispute indefinitely. Some double tax treaties may limit adjustment to a lesser period.

j) Mandatory Language

Documentation must be in English or easily converted into English when requested by the ATO. The original finalised document may be in a foreign language at the date of lodging of the tax return. Still, it must be capable of translation to English within a reasonable time if requested.

k) Notification Requirement

Each constituent entity of a multinational group that is tax resident in Australia must include in the Master File/Local File the name and tax residence of the ultimate CbC parent and, if different, the name and tax residence of the parent CbC entity.

l) Record Keeping

Transfer pricing documentation based on the form and substance of dealings between associated parties, compared to arm's length party commercial or financial condition norms, is strongly recommended to be in existence at the date of lodgment of a relevant year tax return.

m) Penalties and Interest Charges

Penalties for not providing enough information (which only apply for CbCr), for not filing or non-timely filing range from AUD 111,000 for offences committed on or after July 1, 2020 (AUD 105,000 for offences committed before July 1, 2020) for each delay period of 28 days or portion of a 28-day period to AUD 555,000 for offences committed on or after July 11, 2020 (AUD 525,000 for offences committed before July 1, 2020) for a maximum of 5 delay periods.

For incomplete or incorrect filing, the penalties can be AUD 26,640, 17,760 and 8,880 in different situations.